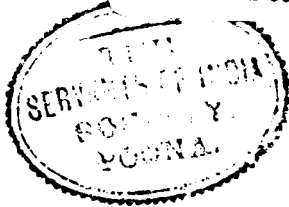


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COMMITTEE ON FINANCE & INDUSTRY

REPORT

*Presented to Parliament by the Financial Secretary to the
Treasury by Command of His Majesty
June, 1931.*

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**REPORT OF THE COMMITTEE ON FINANCE
AND INDUSTRY.**

TABLE OF CONTENTS.

	PAGE.
MINUTE OF APPOINTMENT	vi.

PART I.

HISTORICAL AND DESCRIPTIVE.

CHAPTER I.—INTRODUCTORY	2
CHAPTER II.—GENERAL CHARACTERISTICS OF MONETARY SYSTEMS	10
CHAPTER III.—THE INTERNATIONAL GOLD STANDARD ...	18
CHAPTER IV.—THE MONETARY SYSTEM OF GREAT BRITAIN :	
1. The Bank of England	25
2. The Joint Stock Banks	33
3. The Accepting Houses and the Discount Market ...	40
CHAPTER V.—THE SPECIAL PROBLEMS OF GREAT BRITAIN ...	46
CHAPTER VI.—THE DISEQUILIBRIUM BETWEEN DEMAND AND SUPPLY	55
CHAPTER VII.—GOLD AND ITS DISTRIBUTION	63
CHAPTER VIII.—THE SEQUENCE OF EVENTS SINCE 1925 ...	69
CHAPTER IX.—THE COURSE OF INTERNATIONAL INVESTMENT	79
CHAPTER X.—THE FALL OF INTERNATIONAL PRICES AND ITS CONSEQUENCES	84
CHAPTER XI.—THE INFLUENCE OF MONETARY POLICY ON THE PRICE LEVEL :	
1. Monetary and Non-monetary Factors	92
2. The Task of the Monetary System	94
3. The Functions of Bank Rate	95
4. The Supply of Credit to Business and Enterprise ...	99

	Page.
5. The Influence of the Banking System on Investment	102
6. International Limitations	105

PART II.

CONCLUSIONS AND RECOMMENDATIONS.

CHAPTER I.—THE MAIN OBJECTIVES OF THE MONETARY SYSTEM :

I. The Gold Standard :

1. The Recent Working of the Gold Standard ...	106
2. The Question of an International Standard ...	108
3. Devaluation	110
4. The Prospects of the Gold Standard	111

II. The International Price Level :

1. The immediate Necessity to raise Prices above their Present Level	114
2. The long-period Stability of the Price Level ...	117

III. International Currency Management

IV. Domestic Currency Management

CHAPTER II.—PROPOSALS RELATING TO INTERNATIONAL MONETARY POLICY :

I. Proposals of a Permanent Character :

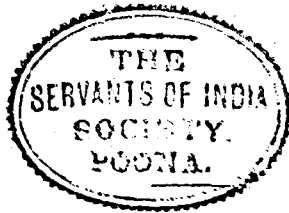
1. Main objective of Central Banks to Maintain Stability	121
2. Use of Central Bank Reserves	121
3. Post-war Changes in Gold Standard	124
4. Obstacles facing Central Banks	126
5. Central Bank control over the Volume and Terms of Bank Credit	129
6. Conclusions	131

II. Proposals to meet the Present Emergency

CHAPTER III.—PROPOSALS RELATING TO DOMESTIC MONETARY POLICY :

1. The Note Issue	137
2. The Resources of the Bank of England ...	147
3. The day-to-day Policy of the Bank of England ...	152
4. The Relations of the Bank of England with the Joint Stock Banks	155

	Page.
CHAPTER IV.—PROPOSALS RELATING TO THE CAPITAL MARKET FOR HOME INVESTMENT	161
CHAPTER V.—PROPOSALS RELATING TO INFORMATION AND STATISTICS	174
CONCLUDING NOTE	185
—	
LIST OF WITNESSES APPEARING BEFORE THE COMMITTEE ...	187
—	
ADDENDUM I	190
RESERVATION TO ADDENDUM I	209
ADDENDUM II	210
ADDENDUM III	217
ADDENDUM IV	237
RESERVATION BY SIR T. ALLEN AND MR. BEVIN.	239
RESERVATION BY MR. LUBBOCK	241
RESERVATION BY MR. NEWBOLD	241
RESERVATION BY SIR W. RAINE	257
MEMORANDUM OF DISSENT BY LORD BRADBURY	263
—	
APPENDICES : TABLE OF CONTENTS	282
INDEX	315



COMMITTEE ON FINANCE AND INDUSTRY.

MINUTE OF APPOINTMENT.

Treasury Minute dated 5th November, 1929.

The Chancellor of the Exchequer states to the Board that he proposes to appoint a Committee to inquire into banking, finance and credit, paying regard to the factors both internal and international which govern their operation, and to make recommendations calculated to enable these agencies to promote the development of trade and commerce and the employment of labour.

The Chancellor further proposes that the Committee should be constituted as follows :—

THE RT. HON. H. P. MACMILLAN, K.C.,* *Chairman.*

SIR THOMAS ALLEN.

MR. ERNEST BEVIN.

THE RT. HON. LORD BRADBURY, G.C.B.

THE HON. R. H. BRAND, C.M.G.

PROFESSOR T. E. GREGORY, D.Sc.

MR. J. M. KEYNES, C.B.

MR. LENNOX B. LEE.

MR. CECIL LUBBOCK.

THE RT. HON. REGINALD MCKENNA.

MR. J. T. WALTON NEWBOLD.

SIR WALTER RAINE.

MR. J. FRATER TAYLOR.

MR. A. A. G. TULLOCH,

with MR. G. ISMAY of the Treasury as Secretary.

The Chancellor proposes that the services of MR. F. W. LEITH-ROSS, C.B., † Deputy-Controller of Finance in the Treasury, should be made available at all times to the Committee in order to afford it such assistance as it may desire.

My Lords concur.

* Now Lord Macmillan.

† Now Sir Frederick Leith-Ross, K.C.M.G., C.B.

Report of the Committee on Finance and Industry.

TO THE LORDS COMMISSIONERS OF HIS MAJESTY'S TREASURY.

MY LORDS,

1. We, the undersigned Members of the Committee appointed by Treasury Minute of 5th November, 1929—

“ to inquire into banking, finance and credit, paying regard to the factors both internal and international which govern their operation, and to make recommendations calculated to enable these agencies to promote the development of trade and commerce and the employment of labour,”

have now the honour to submit our Report.

2. We held a preliminary meeting on 21st November, 1929, at which our terms of reference and the general lines on which our inquiry should proceed were discussed. Thereafter we at once began the hearing of oral evidence for which purpose we held 49 meetings. In all we examined 57 witnesses, several of whom attended on more than one occasion. The evidence which we have received was in many cases representative of the corporate opinion of economic organisations and industrial bodies, but we have also had the advantage of hearing the personal views of numerous witnesses specially qualified to deal with the more technical aspects of the problems before us. A list of the witnesses examined will be found at the end of our Report and will be seen to include a wide and varied range of representatives of banking and finance, both in this country and in the United States and Germany, as well as of industry and commerce from the point of view both of employers and of employed, while members of the Universities and the Civil Service and eminent economists of diverse schools have also lent their assistance. We have, in addition, received many written communications from individuals and from institutions and bodies interested in the various aspects of our inquiry. A list of these contributions is also given at the end of our Report. Apart from the meetings at which evidence was taken, we have met on many occasions for the purpose of hearing and discussing the views which certain of our members possessing expert qualifications desired to place before us. We also appointed Sub-Committees to deal with the preparation of statistics and the drafting of our Report, which held a number of meetings and by their labours materially lightened our task. We should add that, through the good offices of the Bank of England, the Bankers' Clearing House and others, we have had placed at our disposal a large amount of statistical material hitherto unpublished and inaccessible.

To all those who have thus assisted us we desire to express our great indebtedness.

3. To our Secretary, Mr. George Ismay, we find it difficult to express adequately our sense of obligation. He has done much more than discharge with zeal the ordinary, if arduous, duties which fall to the lot of a secretary of a Departmental Committee; he has also placed ungrudgingly at our disposal the remarkable and detailed knowledge which he possesses of our highly technical subject and has thus rendered us assistance of quite exceptional value.

PART I.—HISTORICAL AND DESCRIPTIVE.

CHAPTER I.—INTRODUCTORY.

SOME GENERAL OBSERVATIONS.

4. In addressing ourselves to the subject matter of our inquiry we desire to make a few general observations by way of preface. It would be difficult to conceive a more far-reaching investigation than that upon which we have been asked to embark, for the problems of finance underlie the whole field of human activities. Merely to deal in the abstract with the technique of the existing financial system, domestic and international, without relating it to the actual economic circumstances of the moment, would serve little purpose. If our inquiry is to render any public service we have to concern ourselves, as indeed our terms of reference exhort us to do, with practical matters. But this at once leads us into highly controversial regions. No doubt the duty of the members of such a Committee as ours is to approach their task entirely dispassionately, but when the problems confronting them are found to be intimately related to the political and economic topics of the day, on which convictions and prepossessions, in some cases already publicly expressed, are ardently entertained, the roles of judge and advocate are apt to become confused and the difficulty of reaching conclusions acceptable to all becomes manifest.

5. Another difficulty besetting our task has been due to the complexity, not to say mystery, in which the problems of finance are involved. Every citizen is dimly aware that in some way his daily business is affected by the operations of the monetary system but he is quite unable to appreciate how it is so affected. It is no exaggeration to say that to the vast majority even of intelligent people the principles of finance and the theory of money are a closed book. When we turn to the experts for enlightenment we find that they fall into two classes. On the one hand we have those who are engaged in the practical business of banking and finance and daily operate the elaborate system of adjustments of which

the financial mechanism is composed. On the other hand we have the theoretical economists who as observers and critics endeavour to expound the rationale of that system. Between these two classes of experts—the practical financiers and the theoretical political economists—a certain antagonism is inevitable. The theorist seeks to rationalise the processes which he observes and to construct a scientific edifice of principles. The practical man finds in his office that he has to deal with a world ruled not by principles but by compromises and is impatient of the formulas of the study which he generally fails to comprehend. Indeed the epithets “academic,” “theoretical,” “doctrinaire,” commonly applied to the philosophic thinker, have acquired a derogatory innuendo in the parlance of a nation which prides itself on its practical common sense and has an innate distrust of intellectual cleverness. The truth, as usual, lies midway. It is as foolish to disregard the analyses and generalisations of the scientific observer as it would be to believe that the world of finance could be successfully conducted by university professors. Each class has its contribution to make and it has been our endeavour to extract from the contributions of both such guidance as we could.

6. In view of the generally uninstructed state of the public on matters of finance we have from the outset recognised that not the least important service we might render would be to act as interpreters of the working of the monetary system and to make its main principles intelligible to the ordinary mind. Indeed, if our recommendations are to commend themselves to the public to whom they are addressed, they must be preceded by an intelligent appreciation of the problems to be solved. But this is an aspiration which we have not found it easy to realise. The subject is peculiarly intractable to handle from the popular point of view. The economic experts have evolved a highly technical vocabulary of their own and in their zeal for precision are distrustful, if not derisive, of any attempts to popularise their science. Moreover, agreement among the professors of the science is, as we have experienced, even harder to find than it generally is among experts and in their anxiety to avoid controversy they tend to avoid committing themselves to any definite conclusions. The difficulty of exposition really arises from the inherent nature of the subject matter. Political economy, like law, is not an exact science. It is concerned with a realm in which the incalculable elements of human psychology play a large part and the interplay of forces is extraordinarily complicated, and where, therefore, the exhaustive ascertainment of cause and effect is unattainable. But, as will be seen in the sequel, we have not been deterred from attempting to describe in some detail the nature of our financial mechanism and the method of its working, not indeed seeking to expound its more intricate refinements but confining ourselves to a general account of the system.

7. A period of economic depression such as that which the nation is now experiencing is a testing time for all our institutions, political, social and economic. Systems which in periods of prosperity have worked satisfactorily enough may at such times be found incapable of sustaining the stresses and strains of adversity and may disclose defects hitherto unsuspected. Machinery designed to work within a given range may jam when that range is exceeded. Moreover, there is a natural tendency on the part of the public to seek a scapegoat for any distress which may befall it and preferably to attribute that distress to any cause rather than its own shortcomings. In the search for a cause which should absolve itself from blame the public in the present instance has not been indisposed to find it in our financial system, none the less readily that refutations of the accusation are little likely to be appreciated. Accusation is always easy; defence even though well founded is often difficult. And what is least understood is apt to be most suspected. It has been our main task to examine the available evidence in order to ascertain to what extent, if any, the attribution of the present distress to monetary causes is justifiable, and then, so far as possible, to suggest remedies for any defects in the system we may have discovered.

8. If there is one characteristic of our times more conspicuous than another it is the recent growth among us of a spirit of self-consciousness. In the development of every civilisation there comes a stage when reflection awakens. While a nation is in the making it is so preoccupied with the practical business of gaining its livelihood and establishing its position that it has no time to bethink itself. Of our own nation pre-eminently it may be said that it has attained its great position not by the pursuit of any preconceived plan, but by a process of almost haphazard evolution based on trial and error and aided by the practical aptitudes and instincts of our race, as well as by certain fortunate accidents in the way of natural resources and geographical position. There has been little conscious direction of the national activities to definite ends. The policy compendiously known as "laissez faire" has prevailed. To this trust in the operation of natural causes we owe the development of our great political, financial and social institutions and the amazing growth of our industrial activities. But we also owe to it in part many of our deficiencies, such as our industrial instability, our social maladjustments, our slums. The most distinctive indication of the change of outlook of the government of this country in recent times has been its growing preoccupation, irrespective of party, with the management of the life of the people. A study of the Statute Book will show how profoundly the conception of the function of government has altered. Parliament finds itself increasingly engaged in legislation which has for its conscious aim the regulation of the day-to-day affairs of the community and now intervenes in matters

formerly thought to be entirely outside its scope. This new orientation has its dangers as well as its merits. Between liberty and government there is an age-long conflict. It is of vital importance that the new policy, while truly promoting liberty by securing better conditions of life for the people of this country should not, in its zeal for interference, deprive them of their initiative and independence which are the nation's most valuable assets.

9. The lesson of all this for our present purpose is that in the case of our financial, as in the case of our political and social institutions we may well have reached the stage when an era of conscious and deliberate management must succeed the era of undirected natural evolution. There are, as we shall see, already signs that the necessity for such a change of outlook is coming to be realised. The foundations of our financial system are being re-examined. Dogmas hitherto regarded as canonical are being questioned. The feeling is growing that our former easy-going ways will no longer ensure our prosperity in a crowded and increasingly competitive world. We are, indeed, at the parting of the ways and our future depends on whether we choose the right way. Hence the need for a careful study of the economic map. We must now choose our path deliberately and consciously. In other words we stand in need as never before of a definite national policy in our financial dispositions.

10. But the same admonition applies here as in the case of our political and social management. Financial policy must not be so imposed as to thwart the energies of enterprise. It should rather be so devised as to assist and give the freest play to those qualities which have won for us the premier financial position in the world. We have to deal with a system of peculiar delicacy. In no department of our affairs is caution more necessary, for the consequences of a false step may be incalculable. But the need for courage is no less than the need for caution.

11. An important thing to bear in mind is that financial policy can only be carried into effect by those whose business it is. We have in this country a great financial and banking organisation with great experience and great traditions. It is through and with that organisation that we have to work, for they alone are the repositories of the skill and knowledge and they alone possess the equipment necessary for the management of our financial affairs. Their views and opinions, however they may fail to commend themselves to enthusiastic reformers, are factors to be reckoned with just as much as the views and opinions of trade unions have to be reckoned with on questions of wages and working conditions.

) THE ECONOMIC SITUATION.

As it existed at the time of the Committee's appointment and as it has since developed.

12. We recognise that the present inquiry was instituted in consequence of the abnormal industrial depression and extensive unemployment prevailing at the time of our appointment, and in the hope that we might be able, as the result of our examination of the financial aspect of the problems involved, to devise if not remedies at least aids to recovery. The situation in the closing months of 1929 was already sufficiently grave. But the difficulties with which we were then faced were to a great extent peculiar to this country and were not shared by the world at large. Since the date of our appointment, however, the position has changed both in kind and in degree, and there have supervened upon our domestic difficulties grave disturbances of the economic world as a whole. This change of circumstances has necessarily altered the focus of our inquiry, as the domestic problem has tended to be overshadowed by the international situation. Nevertheless, however much we may attribute the aggravation of our industrial depression and unemployment to what it has now become popular to call "world causes," there remain in the background those domestic causes which at the time of our appointment had already brought about the grave result of over a million unemployed and which, if not remedied, will continue to operate in our own case even if those "world causes" are redressed.

13. If we turn first to the position existing when we were appointed, we apprehend that the tendency then, and since, to attribute the prevalent distress to monetary policy was largely due to an impression that the return of this country to the gold standard in April, 1925—itself one of the turning points in the post-war economic history of the world—had impeded instead of promoting our economic recovery from the consequences of the War, and to a suspicion that there had been a failure to utilise to the full such opportunities to expand credit as were still available notwithstanding the unchallengeable fact that our standard of value had once again become an international one. Not only was the adequacy of the volume of credit created called in question, but the efficacy of the means of its distribution was also the subject of adverse discussion. It may, indeed, be said that at no time since the termination of the historic disputes which followed the Napoleonic Wars and which led to the passing of the Bank Act of 1844 has the monetary organisation of our country been the subject of so much criticism as in recent times.

14. Apart from the development of this critical attitude, the economic position of this country during the five years succeeding the return to the gold standard was such as of itself to render

indispensable an examination of the facts and forces at work. We are far from suggesting that equilibrium had been attained before the return to the gold standard was effected. Indeed in the last year preceding that step, with an insured population between the ages of 16 and 64 of some 11.1 millions, unemployment never fell below a million and for the greater part of the year exceeded 10 per cent., while during the five succeeding years to the end of 1929 the volume of unemployment showed no substantial diminution. However caused, the existence in our midst of this great mass of unemployed persons profoundly disturbed the public mind, representing, as it does, a form of economic waste by its very nature irrecoverable. If the net output per worker be taken as in the neighbourhood of £200 per annum, the national loss from the unemployment of a million men over a period of five years may be estimated at a thousand million pounds. But this was not the only alarming phenomenon. Our export trade, although not completely stagnant, failed, even after making all allowance for changing price levels, to maintain its progress and lost ground in comparison with our competitors; the wholesale price index showed a continually falling trend; and the Bank of England found itself frequently resisting a tendency to lose gold. Meantime our population continued to increase, taxation was maintained at a level higher than in any other country, the national expenditure, with the consequent burden on industry, was being constantly added to by the policy of successive governments, and as a result of the fall in the price of imports the general standard of consumption remained substantially unaffected notwithstanding the economic depression.

15. These features of the period immediately preceding our appointment were sufficiently ominous to cause grave anxiety among those who appreciated their tendency. But it so happened that our appointment coincided in point of time with the beginning of a series of further economic events of an unprecedented character, leading to a state of world depression which shows at this moment few signs of coming to an end. It will suffice here to summarise these occurrences under the following main heads:—

(i) The heavy and rapid fall in wholesale prices affecting all countries alike. Within 15 months from June, 1929, wholesale prices fell 13 per cent. in the United States, 15 per cent. in the United Kingdom, 14 per cent. in France, 9 per cent. in Germany, 11 per cent. in Italy, 15 per cent. in Australia, 11 per cent. in Canada, and 20 per cent. in British India.

(ii) The general spread of unemployment to nearly all the other countries of the world. In three countries alone, Great Britain, Germany and the United States, there were at the end of 1930 probably from twelve to fourteen million persons wholly or partly unemployed.

(iii) The diminution of international long-term lending which may be regarded as partly a cause and partly an effect of the visible deterioration in the position of the raw material producing countries. Interacting with the fall in wholesale prices this has sharpened the severity of the crisis through which the debtor nations have been passing.

(iv) The abandonment of the gold standard in one country after another, e.g., Australia and Argentina, following upon the financial crisis, with the result of increasing the unwillingness to lend to those countries.

(v) The restriction of the process of investment, and consequently of enterprise, due to depreciation of securities and the uncertainty of the outlook, which has had the effect of causing resources to be held as far as possible in liquid form.

These events have been accompanied in many countries by serious political and social unrest which has in turn aggravated the crisis by diminishing their credit and deterring lenders. They have been unfolding themselves throughout the period of our meetings and we refer to them here only for the purpose of showing the far-reaching character of the phenomena with which we have been confronted and the complexity of the situation with which we have had to deal. We shall, of course, return to a detailed examination of them in subsequent chapters.

16. Not the least difficult part of our task has been to endeavour to ascertain how far the crisis through which we are passing is due to monetary causes and how far to other causes. Unfortunately there are no general principles universally accepted as to the mode in which monetary institutions and activities affect the economic situation, still less as to the precise degree of their importance as compared with other causes. Indeed we have been presented with a range of opinion which at one end attributed the whole trouble to monetary causes and at the other entirely absolved them, a divergence of view no doubt attributable in part to varying conceptions of what are monetary causes. Among the non-monetary causes their relative importance *inter se* is itself a subject of acute controversy upon which it is not necessary for our purpose to pronounce. It may well be, however, that in many instances the complaints which have been directed against our monetary system have been occasioned by the fact that it has been asked to perform feats quite beyond its compass. In the case of nations, as in the case of individuals, no financial system, however devised, can work miracles nor can it cope with all the problems which may be presented to it by an unsound national policy, whether internal or external. The financier is not to blame if the politician sets him problems which no financial expedients

can solve. If our budgetary position is unsound, and if our industries, owing to the level of their costs, or for other reasons, are unable successfully to compete, as they used to do, in the markets of the world, no management of the terms and quantity of credit will be able to maintain our national prosperity.

17. While the non-monetary causes which have contributed to the present distress, strictly speaking, fall outside the scope of our inquiry, we have found it impossible to avoid some discussion of them, for it is only by estimating their effect that we can arrive at some delimitation of the sphere of action of monetary causes properly so-called. We have, therefore, attempted in a series of chapters to describe and analyse the principal events and forces, both monetary and non-monetary, which appear to us to have a direct bearing upon our investigations.

CHAPTER II.—GENERAL CHARACTERISTICS OF MONETARY SYSTEMS.

18. Some common unit of value in terms of which transactions can be expressed is necessary, if only as a satisfactory measure for comparing the value of one thing with that of another. With the growth of contractual obligations, involving the conception of deferred payments, a time element was imported into transactions which rendered it even more essential to have a common unit of value as the basis on which to fix the amount of payments to be made at a postponed date. When a community, in order to meet this requirement, selects a particular commodity such as gold to serve as its common denominator of value, or, in other words, as its money, that commodity is used not only for the actual settlement of debts but is also naturally adopted as the unit for the measurement of those debts. It becomes what is termed the money of account, e.g., the pound, the dollar, the franc. But the person entitled to a future payment fixed in terms of the money of account may find, if there is instability in the purchasing power of money due to fluctuations of prices, that the value of his contractual right has substantially changed when he comes to receive payment. The importance of stability in the value of money, that is, in its purchasing power, thus becomes at once apparent if transactions are to be entered into with any degree of confidence.

19. It is important to realise the wide range of contractual obligations which are now affected by fluctuations in the value of money. The policy of modern States has greatly added to their number by the institution of social services which all involve future payments on a predetermined scale. Old Age Pensions, Insurance Allowances and other forms of assistance are all fixed by the Legislature in terms of money which, when it comes to be paid, may represent something quite different in value from what it represented when it was originally prescribed. The growth both of joint stock enterprise and of Government debts has also in the course of the past century enormously increased the number of fixed future money payments. Rights and interests in fact all tend to become more and more divorced from the underlying substratum of real things and are not merely expressed in terms of money but are actually constituted by the right to receive money payments. It is thus obvious that changes in the value of money may give rise to important changes in the distribution of the national income. We return in Chapter X to some of the difficulties thus occasioned.

20. The nature of the changes which the monetary system itself has been undergoing cannot be better illustrated than by the alteration in the emphasis placed by economic science upon the two functions which money is traditionally regarded as fulfilling—the

function of acting as a medium of exchange and the function of acting as a standard of value, or, as it used to be put, as a common denominator of value. Victorian economic theory emphasised the first, modern theory emphasises the second, of these functions. This is significant of more than a mere change of academic fashion. Whereas in the nineteenth century, the symbols (pound sterling, dollar, etc.), which expressed values corresponded to coins actually in circulation, this is not often the case in the modern world. To an ever-increasing extent, paper representatives of the monetary unit constitute the hand-to-hand currency in circulation. The symbolic character of the monetary unit has emerged into the foreground while its relation to some actual physical material has receded.

21. Moreover, in the course of the past and the present century, the importance of hand-to-hand currency has been steadily diminishing. Although its absolute amount grew with the trade and population of the world, its relative importance as the means of settling debts of all kinds at the same time declined. For international payments, even from a very early period, metallic money was little used, and credit instruments in the shape of bills of exchange were largely employed in its place. Before the development of modern banking institutions, indeed, internal remittances were largely effected by means of bills, whilst in the course of the eighteenth and nineteenth centuries the bank note and Government paper money became increasingly important. But, contemporaneously with the development of paper money as a circulating medium, there also developed methods of economising cash either by means of "giro" transactions in the books of banks established for this very purpose at great commercial centres such as Amsterdam and Hamburg, or by the use of written transferable orders on bankers, i.e., cheques drawn against "running cash," the English equivalent of the Continental "giro" system. In the modern world payments are effected by cheques or similar means to a far greater extent than by cash, though the extent to which substitutes for cash are employed varies in different countries. Thus the mass of purchasing power in a modern community is still further removed from the physical objects with which it is linked through the monetary unit.

22. The devices mentioned above are very important in that they have given great elasticity to the volume of purchasing power. When the reserves of purchasing power of each individual were held separately in the shape of current coin, what amounted in the aggregate to a large amount of money was necessarily withheld from active use. Under modern banking conditions, such reserves are entrusted to the banks, and it is the function of the banker to employ in granting loans the amounts which experience teaches him are not likely to be demanded immediately by their

owners. If no additional in-payments were made by customers and there were no withdrawals in cash, the volume of deposits of a single banker would fluctuate only with the volume of the loans he himself made, and the limit of his loans would therefore be fixed by the size of the cash reserve he deemed it necessary to keep. When the lending powers of the banking system as a whole are being considered, however, allowance has to be made for the circumstance that individual banks lose cash, not only to their customers in consequence of demands over the counter for wage and other payments usually made in that form, but to one another, if the cheques drawn on them by their customers in favour of customers of other banks are in excess of the cheques drawn on other banks in favour of their customers. The cash reserves of the banks take the form largely of deposits at the Central Bank, and if the different banks make a point of maintaining a constant ratio between their deposits and their cash reserves (whatever that ratio may be) then the additional lending capacity of a single bank, due to a greater proportion of the aggregate cash reserves passing to it in consequence of favourable clearing balances, will be offset by the smaller lending capacity of all those banks which have been losing cash to it through the clearing. If, however, the aggregate of cash reserves is increased, or if all the banks together decide to reduce the proportion of their cash reserves simultaneously, increased lending will thereby be made possible; though the additional loans thereby justified will only assume their ultimate form gradually. An increase in the deposits of a single bank, accompanied by an increase in its cash reserve due to gold imports or to an increase in the volume of bankers' cash through credit operations of the Central Bank designed to have this effect, will, in the first instance, lead, through adverse clearing house balances, to part of the additional reserve passing into the hands of other banks. As they in turn expand their loans, again part of the additional reserves which they have previously gained will pass over to other banks, until, in the end, the increased reserves are spread over the system as a whole, supporting a larger volume of loans and deposits. Again, a single bank which voluntarily lowers the proportion of its reserve to its deposits will impart an upward movement to the volume of credit by *not* restricting credit as it loses cash through the operations of the clearing. The volume of bankers' loans is elastic, and so therefore is the mass of purchasing power, but there is a time lag involved before the factors which lead to an expansion exercise their full influence.

23. The banking system thus forms the vital link between the two aspects of the complex structure with which we have to deal. For it relates the problems of the price level with the problems of finance, since the price level is undoubtedly influenced by the

mass of purchasing power which the banking system creates and controls, and by the structure of credit which it builds upon the basis of available supplies of gold. Thus, questions relating to the volume of purchasing power and questions relating to the distribution of purchasing power find a common focus in the banking system.

24. If the money income of the community were constant in amount, stability of individual prices would be assured only if all goods and services were being produced in forms exactly corresponding to the way in which the owners of income were disposing of this income. Even the stability of average prices would imply equilibrium between consumers' goods and the instrumental goods necessary for their production. But in addition to these factors affecting the stability of prices, the money-income of the community is itself a variable quantity. If Governments pursue an inflationary policy, i.e., meet expenditure not out of revenue or loans, but by the issue of paper money; or if there is an increased output of gold from the mines, adding to the incomes of gold producers and to the lending powers of the banking system; or if, finally, the banks pursue an easier credit policy and lend more freely to the business community, forces are set in motion increasing profits and wages, and therefore the possibility of additional spending arises. The effects upon the price level are complicated by the fact that the distribution of money-incomes may be altered and the rapidity with which they are spent. Thus, apart from an absolute rise in the price level, relative prices may be distorted and a new direction given to the mechanism of production. In short, an expansion of credit and of currency, however arising, has a complex effect upon the price level.

25. The characteristic modern feature of great banks of deposit, investing their funds largely in short-dated commercial loans is historically recent. Before joint stock banking arose the field was already occupied (i) by the private banker, dealing in international bills of exchange, handling bullion and foreign exchange transactions, and issuing Government and other loans to the public, the predecessor of the modern "merchant banking" firms; (ii) by institutions created with special powers and privileges granted in return for loans to Government, the prototypes of our modern Central Banks; (iii) by the old country banks mostly possessing the right of note issue; and (iv) in certain countries by special banks intended to facilitate mercantile transactions in an age of great currency disorganisation, the "giro" banks of the great commercial cities. It was not until the middle of the last century that joint stock organisations for deposit banking, discounting, or the handling of securities began to come into existence.

26. But underneath the diversity of functions assigned to the various classes of financial institutions, there may be discerned certain general features which may be summarised as follows:—

(i) Every advanced financial organisation possesses a market in which funds available only for very short periods are lent out. This is designated the call-loan market. The immediate effect of an increase in the supply of credit is usually an increased flow of funds to this market, whether, as in New York, it is primarily associated with the Stock Exchange, or whether, as in London, it is primarily associated with the market in bills of exchange, i.e., the discount market.

(ii) Every organised system possesses a market in which the supply of and the demand for short-period loans is balanced. To bring short-period lending into relation with short-period demands for accommodation is the primary function of commercial banks.

(iii) Every organised system includes a market for the adjustment of the supply of and the demand for new long-period capital. This is the capital market in the ordinary sense of the term, which prepares and offers new securities to those seeking opportunities for investment.

(iv) In addition, and as an inevitable accompaniment of the capital market, there must be an organisation capable of transferring ownership rights in already existing securities. This organisation is the Stock Exchange.

(v) There are usually special organisations dealing with the supply of savings of a special character, or linking up the flow of savings with the demand for savings for special purposes. Into this category fall the insurance companies, the savings banks, agricultural mortgage banks and other analogous institutions.

27. If the multifarious character of these functions, and of the agencies which perform them, is borne in mind the question of co-ordination naturally arises. How is it possible to attain equilibrium between forces of so diverse a character? In the first instance, of course, equilibrium is attained, as in every market, through the medium of rate or price; if the whole system is in equilibrium, then there will be a definite relationship between the rates of interest or the price of loans in every one of these markets, and between these rates and the expected return on long-period capital. Moreover, since the financial structure of every country influences, and is influenced by, the financial structure of other countries, the whole system of money markets will be in a position of mutually determined equilibrium. Since under an international gold standard international prices tend to a common level; since, further, price movements are influenced by events in the money markets, and the money market is influenced by price

movements, a self-determining equilibrium of all the factors, national and international, is attainable, given a sufficiently long period of time, and the absence of disturbing causes. Thus variations in the rate of interest charged appear to be the appropriate instrument to bring about harmony.

28. Considerations such as these lay at the back of the long-drawn controversies between the supporters and opponents of what used to be called "Free Trade in Banking" in the middle of the nineteenth century. By that time, however, it had already become clear that there resided in the financial structure a tendency not only to harmony but also to disharmony. The necessity for some agency, capable of acting as a brake upon the system, was gradually recognised. The institution called upon to keep the financial structure upon an even keel is the Central Bank: in this country the Bank of England. Historically the principles of central banking were established empirically long before they received theoretical formulation. That there is a distinction between the code of behaviour appropriate to a commercial bank and that appropriate to a Central Bank was recognised as early as 1797, was a bone of contention between practical authorities for nearly three-quarters of a century thereafter, and was finally established with unanswerable brilliance and cogency by Walter Bagehot in 1873. We mention this long struggle to show how recent, even in the case of Great Britain, is the full realisation of all that is involved in the theory of central banking.

Functions of a Central Bank.

29. Since freedom of issue of paper money may easily, under the stimulus of the desire to make profit, lead each issuer to expand until the total amount in circulation is inconsistent with the retention of a sufficient reserve of gold, it is clear that the Central Bank should possess a monopoly of note issue, and this is indeed the almost universal practice of the modern world. But this does not of itself secure to the Central Bank control over the volume of credit, the modern substitute for hand-to-hand currency. This came about in our country through the following causes. It is to the interest of every commercial banker that, in the short run, his reserves should be as small as possible consistently with safety. It is equally to the advantage of each banker that there should be one institution carrying a large reserve available for the use of all in moments of emergency, provided that this institution is willing to utilise its reserve for the common safety when the emergency does arise. Hence the one-reserve system, the foundation of all central banking practice, arose in this country to meet a practical need and found its organ in the Bank of England. The immense importance of this system has had to be recognised, in newer areas in which commercial banks preceded the institution of central banking, by the system of compulsory reserve-deposits

at the Central Bank. Once the commercial banks of a country hold their reserves in the shape of deposits at the Central Bank, the possibility of control by the Central Bank arises. For an expansion of credit by the Central Bank has the effect of increasing the reserve-deposits of the commercial banks at the Central Bank, and a restriction of credit by the Central Bank decreases these reserve-deposits. In the first case the commercial banks can expand, in the second they are sooner or later forced to contract, their own loans. These results follow whether or not the expansion or contraction of credit is effected by the Central Bank through operations in the money market, or through operations in connection with the commercial banks themselves, i.e., whether the Central Bank acts by means of "open market operations" or by means of "re-discounting" for the commercial banks.

30. The Central Bank should, therefore, possess four rights: the right of note issue, the right to hold the reserves of the commercial banks, the right to buy and sell securities, and the right to discount. In return, it must so manage its operations as to be able at all times to meet the demands which may be made upon it, that is, it must be able to safeguard its cash reserve.

In practice the tasks which have been imposed upon the Central Bank make it imperative that it should hold the account of the Government, for the financial operations of Government are conducted on a scale so great as seriously to derange the money market unless special measures are taken to counteract the inconveniences which result from the inflow of revenue or the temporary easiness which results from interest and dividend payments. This task ought to devolve upon the Central Bank in virtue of its general function as guardian of the money market, and does in fact devolve upon it when it carries the Government account.

31. It follows that the functions of a Central Bank and the obligations resting upon it are of a very special character, calling for skill, experience and judgment of a kind different from those which must be possessed by commercial bankers. No banker can neglect the rules of prudence and of safety, but the object of a commercial banker is to make a profit. The situation of the Central Bank is such that it must often undertake operations which are not only not profitable, but result in losses. Its aim must be the safety of the financial system and the economic welfare of the country.

32. These differences of standpoint and function are reflected not only in the powers, but also in the constitution, of the Central Bank. The frame-work of its scheme of government, the general powers conferred upon it, as well as the standards to which, in the exercise of its powers, it is expected to work, are usually embodied in legislation, which in addition to setting a time limit to the privileges conferred upon the Bank, normally subjects the institution to some special limitation upon the disposition of its profits,

either by directing that they shall be used in specified ways, or by limiting the total amount which may be distributed, or by combining directions such as these with appropriation of profits in part by the State.

33. In the sphere of Central Bank legislation two tendencies may be observed. The first concerns the degree of elaboration of the constitutional code by which the Bank is to be governed. There are what may be called the British and the Continental traditions in these matters: the first leaving the Bank much more free to develop its constitution in accordance with changing circumstance, and limiting the degree of State interference to a minimum: the second regulating machinery in detail, emphasising the subordination of the Bank to the organs of the State, and admitting some, in certain cases much, State participation in the affairs of the Bank itself. Such detailed regulation is explicable in many cases on the ground that the Bank has been set up in an environment generally favourable to State paternalism or under circumstances, such as a disorganisation of the currency, which made detailed regulation appear advisable. Nevertheless, rational consideration of the problem will show that a Central Bank which is able to adjust itself to new necessities and exigencies without requiring an amendment of its constitution or powers on every occasion when innovation is considered desirable possesses the inherent advantages which an elastic structure has over a rigid one.

34. The other tendency to which allusion must be made refers to the reserve requirements of modern Central Banks. In the earlier bank constitutions, in so far as a statutory cash reserve was provided for, it was against the volume of the note issue that the reserve was to be held. The magnitude of the reserve was either to be the same as the outstanding volume of notes (subject to a certain minimum of notes which need not be covered) or was to be a certain minimum percentage of the notes outstanding, whilst the reserve itself was to be composed of gold bar or gold coin actually in vault. The deposits of the Central Bank were not subject to regulation. Contrasting the present with the former situation, we note some significant differences: (i) whilst the tendency to insist upon a minimum ratio (generally 35 per cent. or 40 per cent.) still exists, there is a tendency to assimilate deposits to notes for reserve purposes, (ii) the reserve need no longer consist exclusively of gold bar or gold coin in vault, but may consist, to a greater or less extent, also of gold bars or coins ear-marked and held at some other Central Bank and of foreign bills of exchange or bank deposits, payable in gold or held in some country upon a gold standard, (iii) where notes and deposits are statutorily convertible upon demand, the Central Bank is no longer obliged to meet these demands in gold coin, but in gold bars or foreign exchange, and in minimum amounts sufficiently large to prevent a frivolous use being

made of the power of conversion. The effect of these measures may be shortly summed up. In so far as notes and deposits have both to be protected by a statutory reserve, the net amount of reserve to be kept increases. In so far as substitutes for gold, instead of gold itself, can be kept in reserve, the net demand for gold for reserve purposes can diminish if Central Banks in practice make full use of the opportunities of the reserve regulations. Finally, experience has shown that, where a Central Bank is required to maintain its reserves at a certain minimum percentage figure of its outstanding liabilities, the maintenance of such a minimum ratio offers no adequate barrier to a rapid growth of its liabilities in periods of expansion, whilst, at the same time, if it is found necessary subsequently to contract credit, the degree of contraction required, in order to comply with the law, is greater than would have been the case if no fixed relation between cash reserve and liabilities had existed. These provisions have therefore an important relation to the question of the economy of gold which we discuss elsewhere in our Report.

CHAPTER III.—THE INTERNATIONAL GOLD STANDARD.

35. To restore gold to its old position as an international standard of value was the avowed aim of currency policy for a period of six or seven years after the cessation of hostilities. This aim was endorsed by two International Conferences, that of Brussels (1920) and Genoa (1922). Since the restoration of the gold standard the main preoccupation of currency authorities has been with the manner in which it has worked and the extent to which, under the conditions actually experienced, it has been responsible for the present degree of international disequilibrium.

36. By an international gold standard is to be understood not identity of the currency arrangements of all the countries comprising the gold standard group but the possession by all of them of one attribute in common, namely that the monetary unit (i.e. pound sterling, dollar, franc, mark and so on) should possess a gold value prescribed by law, or, rather, a gold value within the limits of the buying and selling price of gold of the local Central Bank. In almost all countries gold coin has now been withdrawn from circulation and its place taken by paper representatives of the gold. The gold price of the paper representatives of gold is determined by the limits at which the Central Banks will give gold for paper, or paper for gold. Thus in Great Britain an ounce of standard gold, containing eleven parts of gold to one part of alloy, is legally equivalent to £3 17s. 10½d. This is the price at which the

Bank of England must sell gold in exchange for its own notes : the minimum price at which it must give its own notes in exchange for gold is £3 17s. 9d.

37. The legal determination by each of a group of countries of the gold equivalent of the monetary unit, though an essential, is not the only condition of an effective international gold standard. Something more is necessary ; namely, the right freely to import gold and to tender it in unlimited quantities to the Central Bank ; and the converse right, freely and in unlimited quantities, to draw gold from the Central Bank and to export the gold so obtained. During and immediately after the War there were countries which, though nominally, were not actually, on the gold standard because the rights in question did not exist. Thus in Great Britain, although the holder of Bank of England or of Currency notes was legally entitled to obtain gold in exchange for notes, he was, under war conditions, unable in practice to export gold and was later by statute prohibited from exporting it except under licence. Again, in Sweden, gold importers were not free to tender gold in unlimited quantities to the Central Bank : the Swedish krona therefore possessed a value superior to the weight of gold which it nominally represented.

38. The right to demand gold in exchange for local purchasing power, or local purchasing power in exchange for gold, is not, however, the only guarantee of the effective working of the gold standard. It is sufficient if the local currency is exchangeable for another currency which is itself convertible into gold. It is possible indeed to classify currency systems based upon the gold standard by the extent to which the relationship between the local monetary unit and gold is proximate or remote. First there are the systems in which the monetary unit is itself a gold coin ; then come currency systems in which conversion takes the form of the exchange by the Central Bank of gold bars into local currency or vice versa ; more remote still is the connection when the conversion right takes the form of an exchange of local purchasing power into foreign currency which is itself convertible into gold bars or gold coin. Nor is it absolutely necessary that the right to convert should be conferred by statute ; it suffices if the currency authority never refuses to give gold or the equivalent at a fixed rate for the local currency, and vice versa.

Primary Objective of the Gold Standard.

39. The primary object of the international gold standard is to maintain a parity of the foreign exchanges within narrow limits ; this has the effect of securing a certain measure of correspondence in the levels of prices ruling all over the gold standard area. Incidentally it provides an objective test of the correspondence of local currency policy with that of the rest of the world, whilst

under it the currency mechanism itself provides the resources by which, in the event of temporary disequilibrium in the relation of one currency to another, equilibrium can be restored. But although so long as an international gold standard exists, the currency authority of any gold standard country has always a simple test of the effect of its policy constantly before it, the disequilibrium between the local currency in relation to the rest of the world leading to a loss of gold may be due to deep-seated causes which, if not corrected by measures involving a definite change in values in the country in question, would result in a permanent drain of gold, or alternatively it may be due to a merely temporary deficiency in the balance of payments, not in itself due to deep-seated currency derangements. A sudden check to exports due to the failure of a crop in an exporting country, or a sudden weakening of markets in an importing country, or pressure on the foreign exchange market due to a demand for remittance in consequence of a rush of new long-term issues in the capital market, or the withdrawal of short-term balances from a money market in consequence of political unrest in the borrowing or lending country, or indeed, in any part of the world, are instances in point. What is necessary is the possession of some one exportable commodity, the value of which will not fall, i.e., for which the short-period price is not subject to change. Gold is such a commodity; so also is the exchange represented by a draft on a bank of the creditor country. Gold and foreign exchange reserves are easily mobilisable assets which are available at moments of emergency, when perhaps nothing else is available. Thus, under the international gold standard, the currency system itself provides the resources by means of which equilibrium can be restored, so long as the causes by which disequilibrium has been brought about are only temporary in character, and so long as the international gold standard is itself maintained.

40. The fact that a state of temporary disequilibrium can be adjusted by flows of gold or foreign exchange does not remove from the currency authority the necessity of caution and of interpreting the situation in the light of its fundamental duty of safeguarding the international standard. What appears at first sight to be a case of purely temporary disequilibrium may prove to be a symptom of a more deep-seated lack of adjustment. Whilst gold exports need not be followed by more drastic remedial measures if the disequilibrium is temporary, they are always a warning both to the money market and to the Central Bank itself that further action may later be necessary. Thus, whenever gold is lost, the Central Bank is provided with an "automatic" signal of the emergence of conditions which may make positive action necessary. The ultimate aim—the restoration of the international value of the currency—is clear, but the action to be taken, and the precise moment at which it should be taken, remain in the sphere of

discretion and judgment, in a word with "management". That the sphere of "management" in this sense is wide and responsible is beyond doubt. For if the wrong action is taken, the state of disequilibrium which the monetary authority designs to correct may be accentuated or perpetuated. If, in a state of temporary disequilibrium, the monetary authority takes action resulting in a change in the level of values here, a new state of disequilibrium may be unnecessarily created. The sense in which the gold standard can be said to be automatic is thus very limited; it is automatic only as an indicator of the need for action and of the end to be achieved.

Secondary Objectives of the Gold Standard.

41. It may be considered a secondary object of the international gold standard to preserve a reasonable stability of international prices. The mere existence of an effective international gold standard does not, however, guarantee stability of prices as a whole either over space or over time. In the nineteenth century, indeed, price movements in different gold standard countries showed a marked tendency to move together, but the absolute level of prices showed a considerable degree of long-period instability. And in the post-war period the sympathetic movement of prices over space is subject to a much greater degree of interference than was the case before the War, whilst the trend of prices over time has shown a very marked degree of instability. These circumstances call for investigation.

42. If prices are to be kept in approximate equality over space, two sets of conditions, which must be present simultaneously, are necessary. In the first place, countries which are losing gold must be prepared to act on a policy which will have the effect of lowering prices, and countries which are receiving gold must be prepared to act on a policy which will have the effect of raising prices. In the second place, the economic structure (as distinct from the currency structure) must be sufficiently organic and sufficiently elastic to allow these policies to attain their objective. The first condition concerns central banking policy: the second limiting condition is not a question of monetary policy, but of the actual economic conditions in which such policy has to work. In practice, it may easily happen that where the first condition is present, the second is absent, and vice versa.

43. The nineteenth century philosophy of the gold standard was based on the assumptions that (a) an increase or decrease of gold in the vaults of Central Banks would imply respectively a "cheap" or a "dear" money policy, and (b) that a "cheap" or a "dear" money policy would affect the entire price structure and the level of money-incomes in the country concerned. But, in the modern post-war world, neither of these assumptions is invariably valid. The

growth of the practice of Central Banks, by which gold inflows or outflows are offset by the withdrawal or creation of bank credit—the movement of gold not being allowed to produce any effect on monetary conditions—involves not the absence of policy, but a policy inconsistent with the rapid adjustment of relative money-incomes and prices. Thus, if at a time when gold flows freely to the United States the Federal Reserve System offsets gold imports by sales of securities, thereby preventing credit expansion, the level of American money-incomes and prices will not rise. If, at the same time, the levels of European money-incomes and prices are already higher than international equilibrium justifies, the whole burden of re-adjustment will be thrust exclusively on Europe. Again, if the level of British costs is out of line with international conditions, but gold exports are offset by the creation of fresh credit by the Bank of England, the maladjustment will continue. Both the failure of American incomes and prices to rise, and the failure of British incomes and prices to fall, may be deliberately intended, but in that case a policy of stabilising local values has been, implicitly or explicitly, substituted for a policy of maintaining a level of values consistent with international equilibrium.

44. Moreover, the effect of the policy of a Central Bank is uncertain when the general economic structure is itself rigid, and more particularly so when the object of that policy is to reduce the price level and the income structure. Pressure can be brought to bear upon the users of credit by a restriction of credit or the raising of bank rate, but that pressure cannot be directly brought to bear upon the costs of production. If the economic structure is rigid, then the effect may be to depress wholesale prices but to leave other prices unchanged, and the process of restoring incomes and prices to an equilibrium level through gold flows and associated bank policy may be interrupted or long delayed or even completely obstructed.

45. The degree to which the price level remains stable over a period of time is again profoundly influenced by policy. If gold were the only form of currency, if there were no alternative uses for gold, and if no stocks of gold were held by Central Banks, the price level would be directly affected by the habits of the community on the one hand and the output of gold on the other. Actually, in the modern world, gold plays in the main only an indirect rôle in the determination of the price level, because the circulating media consist overwhelmingly of paper money and bank deposits; it is this volume of purchasing power which directly affects the price level and not the amount of gold which may be held in reserve. Gold itself affects the price level mainly through the decisions of the holders of gold reserves as to the amount of purchasing power which they will allow to be outstanding against a given holding of gold. Central Banks and currency authorities as a whole can increase their total reserves only to the extent of the new gold supplies available each year for currency purposes. An

acute competition for gold in order to increase reserve ratios tends to a reduction of the aggregate amount of purchasing power against which the gold is held, and to a fall in prices additional to the fall which would in any case have taken place if, in a period of falling supplies of gold, a rigid relationship between gold supplies and additional supplies of purchasing power had been maintained, i.e., if reserve ratios had been left unchanged. In a period of expanding trade production and population, a decreased gold supply, unless accompanied by a similar movement of reserve ratios, lowers prices. If, in addition, certain countries take steps to obtain gold solely for the purpose of increasing the ratio of their gold to their liabilities, the price level must fall still more. It falls more because the countries successful in the struggle do not allow their additional supplies of gold to affect their prices, and because the countries which are threatened by a loss of gold take steps to resist the loss which have the effect of lowering their prices.

Conditions necessary for the working of the Gold Standard.

46. The international gold standard is intended to subserve the general ideal of stability—as regards the relations between currencies, and price relationships over space and time—but it does not, in and of itself, guarantee that this ideal will be realised. The international gold standard can, under appropriate conditions, enable both exchange stability and a considerable degree of price stability to be attained simultaneously, over a wide area, but, the mere fact that the standard is gold, and that it is international, will not under all conceivable conditions and varieties of policy, automatically bring about these results. In other words, there are “rules of the game,” which, if not observed, will make the standard work with undesirable, rather than beneficial, consequences.

47. It is difficult to define in precise terms what is implied by the “rules of the game.” The management of an international standard is an art and not a science, and no one would suggest that it is possible to draw up a formal code of action, admitting of no exceptions and qualifications, adherence to which is obligatory on peril of wrecking the whole structure. Much must necessarily be left to time and circumstance. Central Banks, in whose hands the working of the international gold standard has been vested, no doubt largely recognise that in many respects the purely traditional and empirical rules by which their conduct was guided in pre-war days are no longer adequate as guides of action in present day conditions, and we consider that the following principles would be generally accepted:—

(i) The international gold standard system involves a common agreement as to the ends for which it exists.

(ii) It should be an object of policy to secure that the international gold standard should bring with it stability of prices as well as that it should guarantee stability of exchange.

(iii) Action by individual Central Banks which, by repercussions on the policy of the others, imperils the stability of the price level should, as far as possible, be avoided.

48. The direct influence of Central Banks upon the price level is exerted through an alteration of the volume of purchasing power brought about by changes in bank rate or by variations in the volume of assets held by them. But there is also an indirect influence exerted by Central Banks to which considerable importance must be attributed. Changes in the level of bank rate affect the price, and therefore the yield, of investment securities. In periods of low bank rate the price of fixed-interest-bearing securities tends to rise, and their yield to fall. The supply of such securities is therefore gradually encouraged because the cost of borrowing is lower whilst at the same time the demand for them is increased once confidence has returned in any degree. Long-terms funds are thereby placed at the disposal of Governments and entrepreneurs and the process of real capital formation is stimulated, with the result that a rise of general prices is engendered. It may even be held that the indirect effect of easier conditions in the money market is more important as an intermediate link in the chain of events which leads from acute depression to the gradual restoration of confidence than the direct effect of attempting an expansion of the volume of purchasing power. For a Central Bank has no assurance that the net amount of purchasing power in existence will in fact be increased by the steps which it may take to that end. Its own operations in the market, through purchases of securities, may for instance lead to a repayment to it of loans previously made by way of discounts; the net amount of purchasing power would then perhaps remain unchanged. The investment market, and particularly the international investment market, thus occupies a place of great importance among the agencies determining price changes.

CHAPTER IV.—THE MONETARY SYSTEM OF GREAT BRITAIN.

49. In Chapter II we indicated that the Central Bank of the country must possess four rights :—

- (a) the right of note issue ;
- (b) the right to hold the reserves of the commercial banks ;
- (c) the right to buy and sell securities ; and
- (d) the right to discount.

In giving a brief description of the monetary system of this country, it is mainly on those rights, and the machinery through which they are exercised, that we shall concentrate.

1. THE BANK OF ENGLAND.

50. The Bank of England is almost unique as a Central Bank in that it is a private institution practically independent of any form of legal control save in regard to its powers of issuing bank notes and granting loans to the State. Its foundation in 1694 arose out of the difficulties of the Government of the day in securing subscriptions to State loans. Its primary purpose was to raise and lend money to the State and in consideration of this service it received under its Charter and various Acts of Parliament, certain privileges of issuing bank notes. The corporation commenced with an assured life of twelve years after which the Government had the right to annul its Charter on giving one year's notice. Subsequent extensions of this period coincided generally with the grant of additional loans to the State. Finally by the Bank Act of 1844 the privileges of the Bank were continued subject to termination by twelve months' notice and subject to the repayment of the debt amounting to £11,015,100 due to the Bank by the State.

51. Apart from statutory provisions regulating the issue of notes, the grant of loans to the State and the publication of a weekly account, Sir Ernest Harvey informed us that "the Bank of England is practically free to do whatever it likes with one exception There is only one real prohibition that is imposed upon the Bank, and that is in the Tonnage Act of 1694, which says that in order not to oppress His Majesty's subjects the Bank is to be debarred for all time from using any of its funds in dealing in merchandise or wares of any description." (Q. 62). "The restrictions, so far as there are restrictions, under which the Bank works in its operations are restrictions which the Bank has imposed upon itself and which, of course, it has the power to alter." (Q. 71).

The Note Issue.

52. For many years subsequent to 1694, the Bank of England remained the sole banking institution in England and Wales with more than six partners possessing the legal right to issue notes. The Bank gradually acquired an effective (though not a legal) monopoly of the note issue in London, and through its relations with Government, a privileged position in conducting deposit banking. Not until 1826 was legislation passed permitting the formation of other banks of issue with more than six partners, but this relaxation was subject to the restriction that such banks should not be established, or issue notes, within a distance of 65 miles from London. In 1833 the notes of the Bank of England were given the status of legal tender: by the same Act it was declared that companies, although consisting of more than six persons, might carry on the business of banking in London and the surrounding area, but

such companies were debarred from issuing notes payable on demand. Finally the Bank Act of 1844 for the first time brought the note-issuing powers of all banks under complete legal control.

53. Under the Act of 1844 it was provided that the issue of notes by the Bank of England should be kept wholly distinct from the banking business of the Bank. The amount of notes allowed to be issued was fixed at £14 millions to be covered by securities (i.e., the fiduciary issue), and such further amount as might be covered by gold coin, gold bullion, or, to a limited extent, silver bullion. At the same time the powers of note issue of the country banks were restricted to those banks already possessing the right of issue, and the volume of notes which they might issue was limited to the average amount actually in circulation over a stated period of twelve weeks. Further, it was provided that the right of issue possessed by those banks should lapse in certain contingencies, such as amalgamation with a non-issuing joint stock bank or an increase in the number of partners above six. Upon such a lapse the Bank of England was entitled to increase its fiduciary issue by two-thirds of the amount of the lapsed issue. By 1921 the whole of the private issues had in fact lapsed with the result that the fiduciary issue of the Bank of England was eventually (in 1923) raised to £19,750,000.

54. In connection with the separation of the note issue business from the banking business, the Act of 1844 directed that there should be transferred, appropriated and set apart to the Issue Department securities to the value of £14 millions (of which the debt due by the State to the Bank was to be deemed a part) and so much of the gold coin and gold and silver bullion then held by the Bank as was not required by the Banking Department. The Issue Department was required to deliver to the Banking Department such an amount of Bank of England notes as, together with bank notes then in circulation, was equal to the aggregate amount of securities, coin and bullion transferred, and the whole of the note issue was deemed to be issued on the credit of the securities, coin and bullion so appropriated and set apart to the Issue Department. Apart from the minor provisions regarding the lapsing of private issues, the Bank had thus no power to increase the volume of notes in any way but by the acquisition of further gold. In emergencies, when the demand for cash exceeded the Bank's powers of payment, the course which was adopted was for the Prime Minister and the Chancellor of the Exchequer to communicate with the Bank promising to lay proposals before Parliament for authorising an excess note issue should the Bank find it necessary to go beyond the statutory limits of issue.

55. The currency in circulation and in bank reserves thus consisted, except for the fiduciary issue of the Bank of England and the issues of the private and country joint stock banks in England,

together with those of certain Scottish and Irish banks of issue (which were not legal tender), entirely of gold and subsidiary coin or of notes backed by gold. Thus legal tender currency could only be increased by the acquisition of additional gold. In the early stages after 1844 the use for the settlement of transactions of means of payment other than legal tender currency was relatively limited, but the rapid growth of the joint stock banking system led to the development of the cheque drawn against sums deposited in, or loans granted by, a joint stock bank. The mechanism under which those banks made credit available to customers and the limitations on the volume created will be described later; it is sufficient here to indicate that the use of the cheque introduced into the monetary system the possibility of greatly expanding the amount of the country's purchasing media, legal tender currency being required in the main only for the payment of wages and retail transactions, for pocket money, and for such part of the joint stock banks' cash reserves as they hold in their own custody.

56. During the War the Currency and Bank Notes Act of 1914 authorised the issue of Bank of England notes in excess of the limits fixed by law to such extent as might be temporarily authorised by the Treasury and subject to any conditions attached to that authority. But the important change in practice was that during the War and for ten years afterwards currency notes for £1 and 10s. were issued by the Treasury, the amount and manner of the issues being entirely within the discretion of that department.

57. It is unnecessary to trace here the processes by which during the War both the deposits in the joint stock banks and the currency note issue were greatly expanded; these matters are dealt with in the Report of the Cunliffe Committee which enquired into Currency and Foreign Exchanges after the War (Cd. 9182 of 1918). So far as concerns the note issue that Committee considered it to be imperative that the issue of fiduciary notes should, as soon as practicable, be once more limited by law, and the currency notes and Bank of England notes amalgamated into a single Bank of England issue. They favoured the principle of a fixed fiduciary issue embodied in the Act of 1844, subject to the continuance of the provisions of the Act of 1914, under which the Bank of England could, with the consent of the Treasury, temporarily issue notes in excess of the statutory limit.

58. As regards the amount of the fiduciary issue the Cunliffe Committee recommended that, as a temporary expedient, pending final arrangements, the actual maximum fiduciary circulation in any year should become the legal maximum for the following year. The Committee considered that without further experience it would be dangerous to lay down a precise figure for the fiduciary issue and

recommended a review of the position when the foreign exchanges had been working normally for a period of at least a year on the basis of a minimum gold reserve of £150 millions. These recommendations were accepted generally by successive Governments, and following the report of the Committee on the Currency and Bank of England Note Issues, 1925, there was enacted the Currency and Bank Notes Act, 1928, whereby the note issues were amalgamated as one issue under the control of the Bank of England. By this Act the new fiduciary issue was fixed at £260 millions, this figure being approximately the amount of the actual maximum fiduciary issue of Bank of England and Treasury notes for 1927, subject to a small deduction in respect of the circulation in the Irish Free State which was being replaced by a Free State issue of notes.

59. While the Act of 1928 maintained the principle of the fixed fiduciary issue of the 1844 Act, it at the same time gave power to the Treasury, on the application of the Bank of England, to assent to an increase or reduction of the amount of the fiduciary issue, subject, in the case of an increase, to the conditions that any such authority (i) should run for a period not exceeding 6 months and (ii) might be renewed or varied on the representation of the Bank but not so as to remain in force (with or without variation) for more than two years without the sanction of Parliament. Any authority for an increase of the fiduciary issue was directed to be laid before Parliament.

60. The eight Scottish joint stock banks still possess powers of note issue. They may issue notes pound for pound against legal tender cover held at two approved offices or held by the Bank of England on their account, and in addition each bank has a fiduciary issue of fixed amount. The total authorised fiduciary circulation for the Scottish banks is £2,676,350 while the average circulation is usually somewhat over £20,000,000. A similar position exists in regard to certain banks in Northern Ireland for which the fiduciary circulation was fixed by the Bankers (Northern Ireland) Act, 1928, at £1,634,000 (subject to a period for the reduction of the previously existing fiduciary issues to that level). We were informed by Sir Ernest Harvey that at the time of his evidence (November, 1929) the average amount of Bank of England notes set aside as cover to the note issues of banks in Scotland and Northern Ireland was about £24,500,000 (Q. 132).

61. Apart from these small issues, the Bank of England is at the present time the sole note issuing authority of the country, subject to the legal requirement that notes in excess of £260 millions require to be covered pound for pound by gold. Against the fiduciary issue the Bank is required to hold securities to an amount sufficient in value to cover it. These securities may include silver coin to an amount not exceeding £5½ millions; apart

from this, they are interest-bearing securities. From the income yielded by the securities held against the fiduciary issue there have to be met the expenses of printing, issuing and cancelling notes and the general expenses of management; the amount of the net profit, ascertained in such manner as may be agreed between the Bank and the Treasury, is payable to the Treasury as public revenue. In practice this allows for the appreciation or depreciation of the values of the securities held. The nature of the securities held by the Issue Department is left to the decision of the Bank of England.

62. The Act of 1928, although it greatly enlarged the amount of the Bank of England's fiduciary issue, and imported a measure of elasticity into the issue through the power conferred on the Treasury to authorise a temporary increase in the fiduciary issue, confirmed as a normal arrangement the essential provision of the Act of 1844 by which variations in the amount of the note issue depend upon the stock of gold held by the Bank, the amount being increased or decreased as gold flows in or flows out. Practically all the gold held by the Bank is concentrated in the Issue Department and notes are issued up to the full amount of the assets of that department. Notes so issued but not actually in circulation are held in the Banking Department of the Bank and the amount of those notes together with the coin is the measure of the cash held against the liabilities of that department to the public.

The Banking Department.

63. The Issue Department is thus concerned solely with the issue of bank notes up to the legal maximum. The Banking Department on the other hand, is a bank of deposit, the position of which can be best understood by a brief reference to the nature of the liabilities and assets of the department. Its liabilities comprise the Proprietors' Capital of £14,553,000; the Rest (or undistributed profits), which is not normally allowed to fall below a figure of £3,000,000; and the liabilities of the Bank to its clients which are shown under the heads of Public Deposits, Other Deposits (subdivided into Bankers' Deposits and Other Accounts), and a small amount of seven day and other bills.

64. The Public Deposits include all balances of the British Government held at the head office and branches of the Bank, including the Exchequer Account, the Paymaster General's account from which supplies are issued to the spending departments and many accounts in connection with the National Debt, the collection of taxation and Government funds of various types.

65. The Bankers' Deposits relate exclusively to British banks whose main business is conducted in this country. The balances of other banks, such as British banks operating in the main in the

Dominions (including the Bank of Ireland) and in foreign countries fall into the "Other Accounts." The latter head also includes balances maintained by foreign Central Banks, Colonial Banks, merchant banks and financial houses, Indian and Colonial Governments, and the dividend accounts of stocks managed by the Bank other than the direct obligations of the British Government.

66. Against these liabilities the Bank holds assets consisting of—

(i) "Government Securities" under which fall only direct obligations of the British Government, including Treasury Bills acquired on the initiative of the Bank and not presented to it for discount, and any temporary Ways and Means Advances made to the Exchequer.

(ii) "Other Securities" divided under two heads, viz. :—

(a) "Discounts and Advances," which comprises bills of exchange and Treasury bills brought to the Bank for discount, and advances made by the Bank to the bill market and to private clients, and

(b) "Securities," which may include stocks guaranteed by the British Government, Indian, Colonial or foreign securities, miscellaneous securities, and commercial bills purchased by the Bank on its own initiative.

(iii) Bank notes issued by the Issue Department but not in circulation. The notes in circulation include not only notes actually in the hands of the public but also notes in the tills and reserves of other banks, and notes set aside as cover for the note issues of banks in Scotland and Northern Ireland to the extent to which those issues exceed limits prescribed by Parliament. The average amount of Bank of England notes so set aside is normally about £23,000,000 to £24,000,000.

(v) Gold and Silver Coin which consists almost entirely of silver coin.

The ratio which the Bank of England notes held in the Banking Department, together with coin, bears to the total of Public and Other Deposits and post bills is generally known as "the Proportion".

67. The reserve of notes in the Banking Department is in effect the measure of the maximum amount of gold which the Bank could part with in the absence of a change in the volume of notes in circulation, unless the powers of extending the fiduciary issue are used. In practice, of course, it could not be allowed to sink to zero. If for any reason there is a drain of gold from the country the Bank must therefore take steps to correct the situation which has given rise to that drain before its gold stock is too seriously affected. As regards the stock of gold which the Bank might desire at any time to hold, Sir Ernest Harvey said in evidence before us :—

"I think it is fair to say that the Bank of England do not carry any fixed figure in their mind as at all times an adequate figure of

gold. It must be obvious that the sufficiency of the gold held must depend upon the changing circumstances of the moment—what is the period of the year?—is it a period of the year when we may be subject to considerable withdrawals from abroad?—what are the liabilities which we know to lie ahead of us?—what, so far as we can measure, are the claims upon us by foreign countries which they might enforce at any moment? We have never considered, I think, that the Cunliffe Committee, in mentioning £150,000,000, did more than consider a figure which in normal circumstances and having regard to the fact that gold in the pockets of the people had been replaced by notes would be a fair average figure, may I say. It is obvious that at one moment £150,000,000 might be sufficient, whereas at another moment it might be insufficient. We are not wedded to the figure of £150,000,000 in the least. I think there is good evidence of that in the fact that we have allowed the figure to be brought down. There is, however, one fact which must always be borne in mind. Whatever the figure named as the minimum below which we should not fall, the lower you put it the less our power of resistance in case of any crisis. The lower, therefore, you allow the figure to fall the more necessary it may be at times to take rather drastic measures for the curtailment of credit—for the maintenance of a comparatively high, or at any rate effective, rate. But we are not wedded to any figure. We judge the figure according to the circumstances of the moment, and in our judgment so far as we were able to estimate the circumstances of the time we considered that it was not unreasonable to allow that figure of £150,000,000 to be reduced to the figure at which it now stands." (Q. 152).

68. If, however, circumstances arise such as to call for positive action by the Bank to prevent a drain of gold, or to encourage the importation of gold, the means which the Bank has at its disposal is an alteration in the level of the bank rate—the minimum rate of discount at which the Bank will discount certain types of bills for the discount market—in combination, if necessary, with open market operations, i.e., the purchase or sale of securities by the Banking Department, or it may be only with an alteration in the types of securities so held without alteration in their total amount.

69. As regards the circumstances in which one of these methods might be employed in preference to the others, Sir Ernest Harvey stated: "I find it rather difficult to attach in general any order of importance to those methods. As regards the first . . . the mere movement of the rate, the exact effect cannot be determined beforehand—at least it is very difficult to do so with any certainty. You know that if you put up the Rate one per cent. you will produce a certain effect upon rates. But the extent of the effect and whether it will hold or not depends upon a great many other circumstances. The relative importance of the different methods is entirely dependent upon the circumstances existing at the

moment. . . . The mechanism of tightening up rates by a market operation of some kind would be the natural method to use, if, in our view, the existing Bank Rate which, if effective, would be high enough, had for some reason or other become ineffective." (Q. 7519). As regards the use of the two types of market operation, " I think our first operation would normally be to reduce the volume of credit by the sale of bills." (Q. 7520). " Unless we had clear evidence that there was a margin of credit which could only find employment in the short loan market, we should not necessarily effect any reduction in the volume of credit. If we do reduce the volume of credit in order to make the rate effective, it is only because we are satisfied that the reason for the weakness of the market rate is an excess of money which cannot find employment elsewhere than in the short market." (Q. 7521).

70. We discuss in Chapter XI the consequences which follow from Bank policy as exercised through the bank rate and open market transactions; here we are concerned only with the mechanism. An alteration in the level of bank rate may, as we have already indicated, be made for the purpose of correcting an outflow of gold due to a temporary disequilibrium in the balance of international payments. In such a case it may produce the desired result by its effect on international movements of short-term capital without any marked effect upon the internal position of this country. Or it may be designed to correct deep-rooted disparities in the price level in this country as compared with other countries, in which case it may have to be continued until the altered price for the use of money restrains or expands demand as the case may be. The mechanism by which this effect is transmitted is that by custom the clearing banks vary certain rates of interest, charged or allowed, by reference to the level of bank rate. While these normal rates are subject to many exceptions in practice, the general position (with occasional deviations) is that :—

(a) the rate of interest allowed by the clearing banks on London deposits repayable at short notice is 2 per cent. below bank rate ;

(b) the rate of interest charged on loans and overdrafts is $\frac{1}{2}$ per cent. to 1 per cent. above bank rate, with an agreed minimum of commonly 4 to 5 per cent. ;

(c) the rate of interest charged by the clearing banks on call money to the discount market is somewhat above the rate paid on London deposits.

Thus an increase of bank rate brings with it an increase in the rates both for short money and for bank loans. It works both on the international position by attracting funds to this country or preventing funds from moving outwards, and on the internal position by discouraging borrowing from the commercial banks and so tending to a reduction of their deposits.

71. But the Bank also holds at command the power directly to increase or decrease the amount of purchasing media in the country by open market operations. If the Bank purchases securities in the market the transaction is settled by crediting the drawing account of the broker or other party through whom they are purchased. This eventually leads to an increase in the balances of the joint stock banks at the Bank of England. The Bank's holdings of securities will of course have been increased by the same operation. The deposits of the joint stock banks at the Bank are the equivalent of cash and the banks thus find themselves with more than their usual proportion of cash to deposits and are in a position to grant further loans to their customers or otherwise to create additional credit. Since the banks as a whole maintain a cash proportion to deposits of from 10 per cent. to 11 per cent. they are in fact able to increase their deposits by some 10 times the cash created by the Bank of England. By the opposite process a sale of securities by the Bank of England or the calling in of a loan will reduce the cash of the joint stock banks and entail a reduction of their deposits. The Bank of England is thus in a position (provided that it has knowledge of the variations in the note holdings of the joint stock banks) to exercise almost complete control over the amount of bankers' cash in the country, and thus, given the conventions which govern the transactions of the joint stock banks, over the total volume of deposits within such limits as are set by the existence of the international gold standard. The bankers' cash may, of course, be reinforced by gold imports without action on the part of the Bank of England but it is within the power of the Bank to take steps to offset any expansion in deposits which might thus arise.

72. There are normally no direct borrowing or lending transactions between the Bank of England and the joint stock banks. The connection is established through the discount market, which we consider later. That market employs funds lent to it by the joint stock banks (as well as other institutions, British and foreign) at call or short notice. If a joint stock bank or other lender finds its cash position is below normal, it withdraws call money from the discount market. That market, if it cannot supply itself with necessary funds from other banks or other sources, brings bills to the Bank of England for discount or borrows from the Bank on the security of bills or Government securities, thus again increasing the cash basis.

2. THE JOINT STOCK BANKS.

73. The joint stock banks, or deposit banks, are the banks with which the public in general deal. They carry out many familiar services for their customers but we are concerned mainly with their functions as recipients of deposits and as lenders to trade and industry, the financial market and other borrowers, and the mechanism which governs generally their operations.

74. It is not unnatural to think of the deposits of a bank as being created by the public through the deposit of cash representing either savings or amounts which are not for the time being required to meet expenditure. But the bulk of the deposits arise out of the action of the banks themselves, for by granting loans, allowing money to be drawn on an overdraft or purchasing securities a bank creates a credit in its books, which is the equivalent of a deposit. A simple illustration, in which it will be convenient to assume that all banking is concentrated in one bank, will make this clear. Let us suppose that a customer has paid into the bank £1,000 in cash and that it is judged from experience that only the equivalent of 10 per cent. of the bank deposit need be held actually in cash to meet the demands of customers; then the £1,000 cash received will obviously support deposits amounting to £10,000. Suppose that the bank then grants a loan of £900; it will open a credit of £900 for its customer, and when the customer draws a cheque for £900 upon the credit so opened that cheque will, on our hypothesis, be paid into the account of another of the bank's customers. The bank now holds both the original deposit of £1,000 and the £900 paid in by the second customer. Deposits have thus increased to £1,900 and the bank holds against its liability to pay out this sum (a) the original £1,000 of cash deposited and (b) the obligation of a customer to repay the loan of £900. The same result follows if the bank, instead of lending £900 to a customer, purchases an investment of that amount. The cheque which it draws upon itself in payment for the investment is paid into the seller's bank account and creates a deposit of that amount in his name. The bank, in this latter case, holds against its total liability for £1,900 (a) the original £1,000 of cash and (b) the investment which it has purchased. The bank can carry on the process of lending, or purchasing investments, until such time as the credits created, or investments purchased, represent nine times the amount of the original deposit of £1,000 in cash.

75. The process is much the same when we remove the assumption that there is only one bank. The credit granted by one bank may reach the accounts of customers in another bank. There is thus established a claim by the second bank upon the first for cash, and the ability of the second bank to grant loans is improved in so far as that of the first bank is reduced. Over the banking system as a whole therefore, loans and investments made by the banks increase their deposits. There is, however, a limitation on this process. A bank which is actively creating deposits in this way will naturally find that a considerable part of the cheques drawn against them will be in favour of other banks. It will thus lose part of its cash reserve to those banks and must proceed to limit its loan operations if its normal cash ratio is to be maintained. In practice, therefore, no one bank can afford to pursue a policy

of creating deposits by making loans or investments which is much out of line with the policies of other banks.

76. The cash which the banks hold is partly in the form of bank notes and coin maintained in tills and reserves to meet current demands by customers and for exigencies, and partly in the form of a deposit with the Bank of England—the bank of the bankers. The latter credit affords first the means of settling day to day balances between banks and secondly the means of obtaining any further supplies of notes or coin that they may need for current use. A further cash item is represented by balances with other banks and cheques on other banks in course of collection. These claims on other banks, which are settled within a day or two, usually amount to about $3\frac{1}{2}$ per cent. of the deposits, varying of course with the amount of business done by the bank.

77. For the ten London clearing banks, the division between the cash in hand and the balance at the Bank of England was as follows for the years 1919 to 1930. The figures are the annual averages of the monthly figures supplied to us by the banks :

	£ mills.		Proportion to Current and Deposit Accounts* (average for year.)		
	Cash in Hand.	Balance at Bank of England.	Cash in Hand.	Balance at Bank.	Total Cash.
1919	112.4	103.9	7.4	6.9	14.3
1920	105.8	83.7	6.2	4.9	11.1
1921	110.7	96.1	6.3	5.5	11.8
1922	107.5	92.9	6.3	5.4	11.7
1923	103.8	87.3	6.4	5.4	11.8
1924	103.8	88.3	6.4	5.5	11.9
1925	103.7	86.2	6.5	5.4	11.9
1926	103.1	86.1	6.4	5.4	11.8
1927	105.1	85.3	6.3	5.1	11.4
1928	104.5	83.6	6.1	4.9	11.0
1929	104.4	82.9	6.0	4.8	10.8
1930	103.6	84.5	5.9	4.9	10.8

* These percentages differ somewhat from those shown by the published monthly statements of the Clearing Banks for the reasons stated in the notes to Appendix I.

78. The figures included in the monthly statements are the average of the aggregates of the figures of each bank on its weekly "make-up" day. There are in fact four different days of the week on which the banks compile their weekly balance. Thus if one bank improves its cash position on the make-up day at the expense of the cash position of the remaining banks, it follows that

the monthly statement would not reflect the true daily cash position of the banks as a whole. Since the end of 1928 the Bank of England has shown separately in its weekly account the actual Bankers' Balances as on Wednesday of each week and a comparison of the two returns throws considerable light upon the true cash position.

79. The Bank of England figure covers a wider group of banks than the ten clearing banks whose figures are shown above. Nevertheless, if we exclude the larger balances maintained at the end of each half year, it shows that for 1929 the Bankers' Balances averaged on each Wednesday about £62 millions and for 1930 about £63 millions. If we take the clearing banks' figures (excluding the half yearly figures) the average balance at the Bank of England works out at about £77 millions for 1929 and £78 millions for 1930. It is evident, therefore, that the clearing banks do not maintain from day to day so high a proportion of cash as is shown by the monthly statements, and although we have not available all the data required to make an exact calculation, it seems probable that the balance maintained by those banks (excluding the half yearly periods) is appreciably below £60 millions or less than $3\frac{1}{2}$ per cent. of deposits. It is probable therefore that the total cash reserve kept (apart from balances with other banks and items in transit), is over all about $9\frac{1}{2}$ per cent, against the published figure of nearly 11 per cent.

80. Behind the actual cash reserves the banks maintain a volume of assets which are readily realisable in case of need to meet withdrawals. In order of liquidity these are :—money at call and short notice lent to the bill market and to a small extent the Stock Exchange, usually about 7 per cent. or 8 per cent. of deposits; bills of exchange and Treasury bills, usually about 13 per cent. to 15 per cent. of deposits; and investments consisting mainly of a mixture of short-dated and long-dated bonds and stocks (largely British Government securities), usually about 16 per cent. of deposits. The remaining large item on the assets side consists of the debts of the customers of the banks in respect of the loans and advances granted to them by the banks, the normal percentage of which varies for different banks between 50 and 55 per cent. of deposits.

81. The following table of the percentages which the various assets (other than cash) bore to deposits in the years since 1919 shows how closely these percentages have been adhered to by the banks as a whole; though it may be that minor accounting changes conceal or account for small variations. As between individual banks, there are, however, fairly substantial variations in the proportions in which their assets are divided. The percentages are calculated from the annual averages of the monthly figures given in Appendix I.

Proportions to Current and Deposit Accounts.

—	Money at Call.	Money at Short Notice.	Bills.	Investments.	Advances.
1919	1.5	7.2	17.6	23.3	38.4
1920	1.4	4.4	15.1	21.4	48.4
1921	1.6	4.2	20.4	19.9	45.1
1922	1.7	4.8	18.8	24.6	41.7
1923	1.5	5.2	16.5	23.4	45.2
1924	1.5	4.9	14.3	22.6	47.9
1925	1.5	5.7	13.6	19.1	51.3
1926	1.6	5.9	13.0	17.7	53.3
1927	1.5	6.9	12.7	16.4	54.2
1928	1.7	7.3	13.2	16.1	54.0
1929	1.7	6.9	12.7	15.8	55.5
1930	1.9	6.2	14.7	16.2	53.6

We add a further table showing the total deposits of the ten clearing banks in each year since 1919 and the division of this total into current accounts payable on demand and deposit accounts payable after date or notice, together with the proportions of each to total deposits.

—	Total Deposits.	Current Accounts.	Deposit Accounts.	Proportion of Current Accounts to total.	Proportion of Deposit Accounts to total.
	£ mill.	£ mill.	£ mill.		
1919	1510.7	1015.9	494.8	67.2	32.8
1920	1719.7	1097.6	622.1	63.8	36.2
1921	1753.6	1024.7	728.9	58.4	41.6
1922	1707.4	998.3	709.1	58.5	41.5
1923	1614.1	965.6	648.5	59.8	40.2
1924	1615.7	950.0	665.7	58.8	41.2
1925	1602.7	922.5	680.2	57.6	42.4
1926	1608.9	921.4	687.5	57.3	42.7
1927	1658.6	932.1	726.5	56.2	43.8
1928	1708.9	953.7	755.2	55.8	44.2
1929	1738.0	940.1	797.9	54.1	45.9
1930	1740.8	920.8	820.0	52.9	47.1

82. On the general question of the proportions in which the banks normally divide their assets we may quote from the evidence given by Mr. Hyde :—

“ We must bear in mind that our deposits are in a very considerable part payable on demand, and even those deposits that are fixed for a period may be payable on demand by arrangement with the depositor ” (Q. 866). This puts the banker under an obligation to keep available an amount of cash “ which is very

much more than sufficient to meet any demand that may be made upon us " (Q. 867). " After we have allowed for the £40,000,000 of cash that we keep in absolutely ready form to meet withdrawals we have then to consider how we shall spread the rest of our assets, bearing in mind two principles. First, that we must keep still a large proportion of our assets very liquid so that if there are withdrawals from our cash owing to the shrinkage in our deposits, we can replenish the cash and still maintain very large liquid resources " (Q. 869). " Then the second point is that we have to earn a profit. You can quite well understand that our expenses are heavy . . . therefore we have to see that we use the remainder of our assets as well as we can in making profits. For that reason we distribute our assets over a variety of different forms of employment so as to secure two objects, first of all, liquidity, and, secondly, profits " (Q. 870).

83. With regard to the particular increase which has taken place in the percentage of advances, Mr. Hyde said that while some part of the addition over the normal ratio of the Midland Bank represented their desire to accommodate customers, " part of it represents the fact that at some time in the past our deposits were on a higher plane and we let out part of them to trade and we cannot now, without putting trade to considerable difficulty and inconvenience, get it back from trade immediately. It has got to be a slow process " (Q. 906). Mr. Goodenough attributed the increase largely to the inability of industries which had obtained credit to repay their liabilities (Q. 624).

84. Despite the small variations, the figures we have quoted show a remarkable adherence to the conventional distribution of assets over a period of years, and this feature has to be kept in mind in considering the position of the commercial banks as the distributive agents for credit throughout the commercial, industrial and financial world. Given the maintenance of a certain cash base the banks will always in time expand their deposits to a figure of some nine or ten times that base, but it does not necessarily follow that they can distribute their assets immediately in the proportions at which they normally aim. In certain circumstances it may be, indeed, that the efforts of the bankers to employ their cash remuneratively will set in motion forces which will themselves bring about a reduction of their deposits. The general process may be summed up briefly as follows.

85. A bank has each day to take a view of its general cash position. Loans and advances are constantly being granted and repaid, bills mature every day and investments are being repaid at intervals. If the result of these day to day changes is to show an increase in the cash balance relative to deposits, the bank has to find means of employing its surplus resources at a profit.

Its aim ultimately is to distribute its assets in the normal proportions, but it cannot, for example, at once expand advances to its customers, since it is dependent upon the volume and quality of applications made by would-be borrowers. In the first place, therefore, the bank finds an outlet for its surplus cash, either by lending money to the market or by buying bills or investments. The choice will be dependent largely upon the view taken by the bank as to the liquidity of its position, the nature of the demands which it anticipates in the early future, and the relative profitability of each type of transaction. The natural outlet in the first instance is, however, the grant of additional loans to the bill market. That market has then an increased volume of funds seeking remunerative employment while nothing has affected the supply of bills for discount. Competition for bills may force the rate of discount down, and though some bills may be attracted to London for discount from other markets, the weakening of the rate may be such as to lead to the possibility of an outflow of gold and thus entail restrictive measures by the Bank of England. It is possible, therefore, that in certain circumstances the cash base may have to be contracted before the banks have had the opportunity of employing their resources in loans to industrial or other borrowers.

86. If, however, such conditions do not arise and the cash base remains unaffected, the general policy of the commercial banks will be to restore the normal distribution of their assets. As and when the demand for advances increases they will be ready to withdraw accommodation from the money market. How far this readiness may affect the actual demand for advances is a matter upon which the views of our witnesses appear to differ. In one case we have been told that the demands for advances for industrial purposes are continually in excess of the ability of the bank to lend; in most cases the evidence we have received is to the effect that the banks have not been compelled, by reason of their cash position, to reject any application for an industrial loan which they regarded as a desirable loan to grant.

87. In general, however, it is clear that the ability of the commercial banks to grant loans to their customers ultimately depends, under existing joint stock banking practice, upon the provision of the necessary cash base by the Bank of England. If the commercial banks have made loans up to that percentage of their deposits which they have adopted as a working basis, either they must cease to grant new loans except to the extent that existing loans are reduced, or the cash base must be expanded by the Bank of England. The determination of what is an adequate supply of credit rests ultimately therefore with the Central Bank. As to the factors upon which the Bank frames its judgment we quote from Sir Ernest Harvey's evidence :—“ It is to the joint stock banks that we have

to look for guidance as to the needs of industry for an increased volume of credit or for signs that the volume of credit is in excess of requirements. . . . The barometer to which we look is the volume of money that is seeking investment in the short market, presumably for the reason that, except in so far as additional short assets may be necessary for the restoration of bankers' proportions, the funds in question cannot find employment elsewhere than in the short market We have to look to the volume of the private deposits considered in conjunction with conditions in the money market, and we have to measure on that basis the adequacy of the volume of credit—always, of course, having regard to the external position, the state of our reserve, the position and trend of the exchanges " (Q. 8848).

3. THE ACCEPTING HOUSES AND THE DISCOUNT MARKET.

88. In the British monetary system, these organisations play an important part. In contrast with most other countries, the function of accepting and discounting bills of exchange is very largely performed in this country by highly specialised firms and companies instead of by the commercial banks, although the latter do a not unimportant share of the business. It is unnecessary to enter into a detailed account of the work of these organisations since we are concerned particularly with the manner in which one of them, namely the discount market, as an intermediary between the Bank of England and the commercial banks, acts as the principal user of the short-term funds of the latter.

89. International trade is largely financed by bills of exchange drawn on banks or banking houses. The process may be briefly described by an example. A British importer wishing to import goods from a foreign country will go, say, to his accepting house and ask them to open a confirmed credit in favour of the foreign exporter through some bank in the exporter's country. The exporter, on exporting the goods and obtaining the ship's bill of lading, will attach the latter together with an invoice, insurance policy and any other relevant documents to a draft for the sum due to him drawn on the London accepting house and ask the local bank to discount the bill so that he may receive his money at once. Relying on the confirmed letter of credit and the first-class standing of the accepting house the bank will be ready to do this. It will then send the draft and the documents to its London agent with orders to present it to the accepting house for its acceptance. The draft being accepted, the agent can either hold it for collection till maturity, or discount it at once in the discount market and recoup his principal abroad. The exporter therefore receives his money at once; the importer secures credit for a period; the discounter of the bill abroad obtains an instrument freely negotiable, and the accepting house receives an acceptance commission for the use of its name on the bill, either retaining

the documents until the bill is repaid or, as is often done, parting with them at once to the importer. The risk run by the accepting house is therefore the insolvency of the importer.

90. The details of the transaction will vary with the particular case. The accepting house may stipulate that the importer must give security, either in the form of the relative documents (such as bills of lading, &c.) or some other form, or it will often give a blank credit to a client who is well-known and financially strong. The importer must place the accepting house in funds in time to meet the payment of the bill on its due date. The accepting house does not, therefore, actually provide cash in respect of its acceptances, though it must always be ready to "take up" its acceptances whether or not funds have been received to cover them. Its function is to guarantee due payment of the bill and in this way to make it one which will be readily discounted by banks or by the discount market. For this guarantee it makes a charge which in general varies from one to two per cent. per annum according to the credit of the customer and the character of the risk.

91. We have given as an example the case of imports into this country. But the same system of acceptance may apply to exports from this country or to imports and exports between any two foreign countries. The variations in the type of transactions financed by sterling acceptances are indeed exceedingly numerous. It is very common too—almost a rule, in fact, where a joint stock bank accepts—for the facilities given to be granted by the London acceptor not directly to the foreign client but through the channel and under the guarantee of a foreign bank. A German bank for instance is given by an English bank or accepting house a certain limit of credit which it is free to use for the re-imbusement business of its clients. These clients then finance themselves by drawing sterling bills on London.

92. The world-wide standing of the London accepting houses, in combination with the discounting facilities available and the maintenance of a free gold market, has led to the use of the sterling bill for international transactions in all parts of the world and not only for transactions in which this country is concerned either as importer or exporter. While the mere acceptance of a bill does not involve the immediate financing of trade in cash, bills always tend to be discounted in the market in which they are accepted. If there were no counterbalancing factor the existence of the accepting business would mean that the resources of London were being applied to the financing of a large part of the world's trade. In fact, however, the accepting houses and the joint stock banks hold substantial deposits of foreign money. Sir Robert Kindersley in evidence before us said of his own firm:—
" My foreign deposits which I lend to the discount market, or

invest in Treasury bills, or use otherwise are equal to the bills drawn upon me, and therefore I get a commission and London is not asked to produce any money for it because the foreign deposits which I have are sufficient to finance the bills" (Q. 1157). He thought also that a very large proportion of those deposits would not be made were it not for the acceptance business (Q. 1158). In his view also this position was likely to be typical of all accepting houses (Q. 1232). On a similar point Mr. Hyde, giving evidence for the Midland Bank, said:—"The total of the deposits that we have from foreign banks, the total money that is placed in London, that can be used in London, is more than twice the total of all our advances and all our acceptances to foreign banks put together. So on balance we get a considerable sum that is being used in advances to home trade—home customers" (Q. 953). These extracts explain one source of the funds which reach the Discount Market.

93. Since this evidence was given we have received from the clearing and certain other banks and from the accepting houses figures showing their total acceptances on foreign account and the amount of foreign money deposited with them or held by them in sterling bills on foreign account. These figures, while not complete, throw considerable light on the position. They will be found in detail in Appendix I (with some notes on their composition) but we reproduce the main items here:

I.—Deposits and Sterling Bills held in London on foreign account.

£ mills.

	30th June, 1927.	31st Dec., 1927.	30th June, 1928.	31st Dec., 1928.	30th June, 1929.	31st Dec., 1929.	30th June, 1930.	31st Dec., 1930.	31st March 1931.
Held through Bank of England, Clearing Banks, and Scottish Banks.									
Deposits ...	123·2	116·8	132·0	139·4	126·4	118·3	171·4	164·6	146·2
Sterling Bills	129·0	161·6	158·5	195·3	190·0	200·2	147·8	144·7	136·8
Held through Accepting Houses, etc.									
Deposits ...	76·1	89·3	96·4	104·3	86·4	79·2	86·5	82·1	81·0
Sterling Bills	9·4	13·1	9·1	16·9	14·5	19·4	8·6	8·0	7·4
Advances to Discount Market by certain foreign banks, etc.									
Advances ...	38·3	38·4	47·3	47·0	36·5	34·0	42·3	35·1	35·7
Aggregate of Deposits, Bills, etc. ...	376·0	419·2	443·3	502·9	453·8	451·1	456·6	434·5	407·1

II.—Sterling Bills accepted on foreign account.

	30th June, 1927.	31st Dec., 1927.	30th June, 1928.	31st Dec., 1928.	30th June, 1929.	31st Dec., 1929.	30th June, 1930.	31st Dec., 1930.	31st March 1931.
By Clearing Banks and Scottish Banks ...	31·4	31·7	38·5	51·3	51·6	40·0	43·2	35·7	32·3
By Accepting Houses, etc.	91·5	108·0	126·9	149·2	150·9	135·7	132·1	125·3	120·6
Total	122·9	139·7	165·4	200·5	202·5	175·7	175·3	161·0	152·9

94. The Discount market in London consists of three public companies, with capital and reserves amounting to about £6,215,000, four private companies with a capital of £1,625,000, 17 private firms and 8 running brokers (who act as intermediaries only) with a capital of roughly £8,000,000. For the most part this capital is invested in securities which are used as a guarantee for loans granted by the banks and others. For the bulk of its resources actually employed in discounting bills, the market relies mainly upon direct borrowing from the clearing and other banks, and from accepting houses and other financial institutions, but partly upon deposits made by the public, for which generally interest is paid at $\frac{1}{2}$ to $\frac{1}{2}$ per cent. above the rates paid on deposits by the banks.

95. The loans and advances made by the joint stock banks to the market constitute their second line of liquid assets. For money at call or short notice the banks normally charge a rate of interest somewhat above that paid on bank deposits, but in addition they lend overnight at a lower rate any surplus money which they have in hand as a result of day to day changes in their balance sheet. The discount market is in the first instance therefore largely dependent for its resources upon the volume of the funds which the clearing and other banks and accepting houses have available for use in this way. Should the market be short of money—by the calling in of loans by the banks or by an increase in the volume of bills for discount—it is able to apply to the Bank of England for accommodation. On this aspect we may quote from the evidence of Sir Ernest Harvey:—“At the Bank, our regulations as regards the bills we accept, though they are not governed by any statutes or anything of that kind, are, in fact quite definite, and have been taken more or less as a model by most foreign Central Banks. They are, that the bills should bear at least two good British names, one of which must be the acceptor. The discount market knows that. Of course, the bills may represent, let us say, a sale of cotton by the United States to Great Britain; they

may represent movement of produce from the East to Great Britain; they may also represent movement of produce between two foreign countries which is financed by credit obtained from a British house, and where they accept the bill, although the bill relates to a movement of goods abroad, it is a British acceptor. The market knows that it can always get its accommodation at a price. Of course, I do not mean to say that any member of the discount market can come in and get accommodation to an unlimited extent. The relations between the Bank and the discount market are exceedingly intimate. Seeing the sort of obligation that the Bank accepts towards the discount market, we claim the right to be kept fully informed regarding their position, if need be, to see their balance sheets, and the right—of course in the strictest confidence—to the very fullest information (Q. 365). . . The rate paid by discount houses to banks for short money, call money, of course, has nothing to do with us at the Bank; that is a matter for the banks themselves. . . . It is generally understood that they charge a minimum of about one per cent. below bank rate (Q. 370). . . . There is a lot of other money that is lent on call. What the proportions are it is difficult to say. I have often asked people and I should estimate—I may be quite wrong—that the bankers' call money is probably about 50 or 60 per cent. of the call money in the market. The other call money is call money in the hands of private lenders and if they cannot get such a rate as the bankers will expect to get . . . they will cut the rate at once . . . and that is the call money which may act as a depressing factor on discount rates. But, of course, that is a factor over which we really have no control. . . . The rate at which the discount house can generally sell its bills to the Bank is what is known as bank rate. . . . Advances to the discount market are usually made for periods of a week and at a rate of one-half per cent. over the bank rate. I say usually. There is no rule that absolutely governs it, but that is the usual practice" (Q. 371).

96. From this brief review of the mechanism of our monetary system we may now see the machine as a whole. The Bank of England, as the Central Bank, is in complete control of the creation of the cash base of the country, subject to such limitations as result from the statutory restrictions upon the issue of legal tender money and the obligation to meet demands for the export of gold. As regards the former, however, the provisions of the Act of 1928 permit of the expansion of the note issue by an increase of the fiduciary portion.

↓ 97. By its control over the cash base the Bank of England is in a position to regulate the volume of bank deposits, so long

as the joint stock banks adhere to their normal practices in regard to the distribution of their assets, or indeed to offset any change which might be made in those practices. The volume of deposits, in turn, is the approximate measure of the amounts which the commercial banks are prepared to employ in various ways and more particularly, from the point of view of our inquiry, the amount which they are ready to lend to trade and industry if the demand for accommodation is forthcoming. Money so lent and actively employed in production is disbursed in wages and other payments and becomes the incomes of those who will purchase commodities. It is through this relationship that the creation of credit affects the level of prices.

98. The link between the Bank and the commercial banks is established through the discount market which is the first outlet of any surplus funds held by the banks and from which funds are withdrawn when the banks find it necessary to replenish their reserves. If the withdrawal causes a shortage of funds in the market, the market borrows in one form or another from the Bank of England and the accommodation given by the Bank provides the means of replenishing the cash resources of the commercial banks.

CHAPTER V.—THE SPECIAL PROBLEMS OF GREAT BRITAIN.

99. At the time of our appointment the outstanding feature of the trade and industry of this country was that they were not merely depressed, but that they were depressed in relation to the state of the rest of the world. The world-wide depression has since obscured the special characteristics of the British situation, but it is nevertheless an essential part of our task to review the economic condition of this country as it stood during the earlier period.

100. In the first place we must recall the chief characteristics of our economy. We are a small island, crowded with a population of 46,000,000, of whom about 80 per cent. live in towns or urban districts. We have under existing conditions to import 60 per cent. of our food, and, in fact, in 1930 imported altogether articles of the value of £958 millions (excluding re-exports) or £20 17s. Od. per head, a figure high in comparison with most countries. We are enabled to pay for these imports partly because we are a great industrial and exporting country, but—since our commodity exports alone would be insufficient—very largely because, as a great commercial, financial, shipping and entrepôt nation, we draw an income of some £195 millions from the rest of the world in banking, insurance and other commissions, and in shipping freights, and because, by the investment of our past savings abroad, we have built up large foreign assets, from which we draw each year in interest about £270 millions.* We are thus the antithesis of what the economists term a "closed system." We are dependent on very large imports to maintain our standard of living and on very large exports to maintain employment; but to pay for those imports we have become largely dependent on our interest from our foreign investments, and on our profits as international bankers, merchants and so forth. Since 1913 our net imports have increased from £659 millions to £958 millions in 1930, though, as prices have risen and the territory covered has changed, the volume of imports into Great Britain and Northern Ireland increased by 18 per cent. only; our domestic exports, while increasing in value from £525 millions in 1913 to £571 millions in 1930 owing to higher prices, have in volume decreased by about 32 per cent. if changes in the quality of goods are left out of account. While the increase in imports of food and raw materials has helped to maintain our standard of living, the decrease in exports and the increase in imports of manufactured goods have caused much of our unemployment.

101. Before the War we managed to combine, with a standard of living higher than that of almost any other country in the world,

* These figures relate to the year 1929. For 1930 the income from commissions, shipping, etc. is estimated at £160 millions and the income from overseas investments at £235 millions. The figures do not include sinking fund repayments estimated to be of the order of £30 millions per annum.

a flourishing and growing export trade. Although our costs were higher than in most other countries, we were still able to compete, though under a growing pressure from our rivals. We owed this favourable position to the advantage of being the first in the field, of having long had an established position, and of the world evincing a keen demand for our special products. Moreover, we were assisted greatly by the vast sums we lent abroad which were used by the borrowers largely in making purchases in this country.

102. Since the War the situation has greatly changed. We have had of recent years a large and continuous amount of unemployment, heavy direct taxation and a diminishing volume of exports. On the other hand, the standard of living of the employed in certain industries has not only been maintained but considerably raised.

103. This change in our situation took place before the world recession in trade. It cannot, therefore, be attributed to causes affecting the world as a whole, although that is not to say that the causes may not to some extent have been external to this country. The outstanding fact is that up to 1929 we suffered from trade depression in many of our great industries, accompanied by a more or less steady figure of 1,000,000 unemployed, at a time when other countries were enjoying a considerable degree of prosperity. It is not, of course, to be inferred that this mass of unemployment represented continuous unemployment week after week of the same persons. The fluctuations in the composition of the total are large; in 1930, for instance, out of 12 million workpeople insured, nearly 8 millions drew no unemployment benefit at all; and of the remaining 4 millions, the benefit drawn by about 2 millions in no single case exceeded 100 days in all.

104. The fluctuations in the percentage of unemployment in recent years are shown by the following figures (which relate to Great Britain only) compiled by the Ministry of Labour:—

				<i>Total number of insured persons aged 16 to 64. (1st July) (000).</i>	<i>Mean of monthly percentages of unemployed.</i>
1922	...	...	...	10,855	14.1
1923	...	...	...	10,903	11.6
1924	...	...	...	11,061	10.2
1925	...	...	...	11,271	11.0
1926	...	...	...	11,422	12.3*
1927	...	...	...	11,526	9.6
1928	...	...	...	11,629	10.7
1929	...	...	...	11,834	10.3
1930	...	...	...	12,138	15.9

* Affected by general mining stoppage; the figure excludes, however, persons disqualified for benefit by reason of trade disputes.

105. The percentages of unemployment in the principal industries in Great Britain and Northern Ireland for the years 1924 to 1930 published in Statistical Tables relating to British and Foreign Trade (Cmd. 3737) throw up clearly the heavy and continuous unemployment in certain of the basic industries, despite, in some cases, a large reduction in the insured population engaged in those industries. In general engineering, steel-smelting and iron and steel rolling mills, and ship-building—the industries which had been greatly expanded during the War—the insured population, if represented by 100 in 1923, had fallen by July, 1930, to 92.3, 88.7 and 78.6 respectively. Yet, even so, throughout the period unemployment remained much above the average. Coal prospered up to 1924 by the damage to the French and Belgian mines and subsequently by the occupation of the Ruhr. But for the six years 1925 to 1930 this industry, representing about one-tenth of the insured population, has been responsible for about one-sixth of the total unemployment despite a contraction in the insured population in the industry of about 128,000. In later years, cotton (in which the insured population has remained almost constant) and to some extent wool, began to affect the position seriously. Among other industries which show a high average of unemployment are docks, shipping, public works contracting, and building, but in the latter two at any rate the cause is probably mainly the intermittence of employment and short-term fluctuations, accompanied by a substantial expansion in the insured population.*

On the other hand the severity of unemployment has not been very marked in the distributive services, despite an expansion of some 43 per cent. in their insured population since 1923; nor in electrical engineering, printing, or banking and finance.

106. These statistics tend to show that the real unemployment problem in this country is that of continuous depression in some areas and in some industries, which are in fact those in which the economic development of this country has been mainly exhibited in the past. Over a large part of the insured population, certainly more than two-thirds, and probably three-quarters, employment between 1921 and 1930, with the exception of the interruption caused by the coal dispute in 1926, has either been entirely regular, or subject to such slight intermittence that it can be regarded as regular by pre-war standards.†

107. An examination of the position from another angle, that of employment, fortifies this conclusion. Estimates of the number of insured workpeople aged 16 to 64 in employment in Great Britain show the following result.‡

* See Evidence before the Royal Commission on Unemployment Insurance pp. 117-8.

† Ibid, p. 119.

‡ Ibid, p. 116.

Estimated number of insured persons in Employment in Great Britain (excluding persons sick or directly involved in trade disputes).

—		1924	1925	1926	1927	1928	1929	1930
		(Thousands)						
1st Quarter	...	9,360	9,560	9,800	9,840	10,010	10,030	10,020
2nd Quarter	...	9,620	9,610	8,890	10,080	10,050	10,270	9,870
3rd Quarter	...	9,530	9,510	8,460	10,060	9,970	10,300	9,690
4th Quarter	...	9,550	9,710	9,050	10,030	9,990	10,230	9,480

Thus, although there were 900,000 more unemployed at July, 1930, than at March, 1924, there were actually over 300,000 more insured workpeople employed in the third quarter of 1930 than in the first quarter of 1924, and the position throughout 1929 was from this aspect markedly better than 1924. Nevertheless, even in that year, the increase in employment did not keep pace with the increase in the numbers of the insured population.

108. It must, of course, be recognised that the complicated rules which determine what is an unemployed person on the live register of unemployed, and the variations in qualifications for benefit which have from time to time affected the numbers on the register, make it impossible to draw detailed conclusions from this brief sketch of the unemployment position. But, from the aspect of our inquiry, it is important to establish the fact that the mass of unemployment has been, and is, mainly concentrated in the heavy industries, and latterly in certain of the textile trades, all of which figure largely in our export business.

109. The broad inference is that, as Professor Clay put it in evidence before us, the post-war unemployment problem in this country up to 1929 included an element amounting to perhaps 7 per cent. of the insured population which was new and not attributable to the causes which explained pre-war unemployment. This mass of unemployment is attributable directly or indirectly to the War and the disturbance in economic conditions it created by, first, the excessive expansion of the metal, engineering and explosives industries in relation to any probable peace-time demand; second, the interruption of our export trade, dislocating the foreign exchanges and stimulating competitive industries abroad, to the permanent injury of our export industries; and third, the discontinuance, up to the close of the post-war boom period, of the normal and necessary adjustments of industry to the continuous technical, commercial and competitive changes that would have gone on if there had been no war.

110. It is not, of course, to be denied that substantial headway has been made towards the readjustment necessary to meet the changed situation in several directions. Indeed, as the figures of insured workers show, contraction in the coal industry and in several others has already gone far, and war-expanded industries have been relieved of a large part of the excess labour they had absorbed. Essentially, however, throughout the whole period there has been a large problem of labour adjustment to peace-time conditions which in the main was independent of monetary conditions and in itself insoluble by monetary means.

111. In addition to this problem of internal adaptation of war-distended industries to peace-time conditions, certain general changes in world economic conditions, to which we need only refer briefly, have borne heavily upon this country. Pre-war Britain was essentially adapted to supply the world in particular with coal, textile goods and other manufactured articles. But since the War she has had to face the development of the cotton industry in the East; the substitution in a substantial degree of oil and hydro-electric power for coal; the generally less favourable terms on which the agricultural countries of the world have been able to sell their products, affecting not only the demand for our manufactures but also bringing a reduction in domestic agricultural prices; the disorganisation of trade with China and India and many other countries resulting from political and other forms of disturbance, and to a large extent from the fall in the value of silver; the currency disorders in various European countries followed at a later date in some cases by stabilisation of the currencies on a basis which gave a substantial temporary stimulus to their export trades; the growth of tariffs and alterations in tariff policies; and a great development of nationalism.

112. It is beyond question that such a concentration of disturbances, of widely varying type, must impose a great strain on any economic system. They fall obviously with peculiar severity upon a country such as ours of which the economic structure has for many generations been especially developed to support a large volume of international trade, and to conduct, with substantial profit to itself, a major proportion of the world's financial business. Unemployment is inevitably created in some industries. Even in favourable circumstances it can only be absorbed in the more prosperous or in new industries over a period of time during which production is dislocated, and it will only be so absorbed if, in fact, those industries themselves offer to the business man an expectation of profit from his enterprise.

113. Unfortunately, the conditions in this country have not been favourable either to the maintenance of the output of the basic industries at what might reasonably have been expected to be its post-war level or to the development of the less exposed or new

industries. From a period commencing some time after the War, the currency policy of the country was directed to the reduction of the inflated price level of the War and immediate post-war period preparatory to the return to gold. This necessarily involved a reduction of money costs of production. It is probable that equilibrium had not been achieved even prior to the return to gold, and there was, moreover, a marked difference between the behaviour of costs in the so-called sheltered and unsheltered industries. But the return to gold in 1925 itself required the reduction of sterling prices and, consequently, of money costs of production to an extent which is variously estimated. At any rate, the actual situation which was disclosed in the years following the return to gold marks that step as the beginning of a new series of difficulties for our trade and industry. Whatever the disequilibrium between costs and prices which still existed in 1924, it was seriously accentuated by the adjustment of sterling prices to gold prices. If gold prices had continued to rise, as they had been rising just previously, those difficulties would have largely vanished; as it was gold prices fell and the hopes then entertained in that respect were disappointed.

114. It is naturally very difficult to assess our disadvantages in costs of production, and the situation can only be tested by examination from more than one aspect. If it be looked at from the position of wages, which constitute so large a part of the costs of most manufactured products, the Ministry of Labour statistics show that over the whole period 1924 to 1929 money wage rates have remained practically unchanged at 170 to 175 per cent. of the pre-war level. In the period 1st January, 1925, to 1st January, 1930, the cost of living index fell from 180 to 166, or 8 per cent., while wholesale prices fell from 100 in 1924 to 82 in 1929, a fall of 18 per cent. Real wages, as measured by the cost of living index, rose by $8\frac{1}{2}$ per cent.

115. Measured over the period 1924 to April, 1931, the fall in the cost of living index has been 18 per cent., that in the wholesale index 38 per cent., and the rise in real wage rates about 20 per cent. The rates of wages do not, of course, take account of overtime, short time or unemployment; in addition, the wage-earners have throughout this period had the benefit of the increased social services and shortened hours. For those in employment Professor Bowley's index of earnings shows a fall of about 1 per cent. from December, 1924, to December, 1929, in comparison with a fall in the cost of living index of 8 per cent. in that period.

116. These figures are, however, averages, which conceal a wide diversity in the relative positions of workers in different industries and occupations. Although the average weekly rate of wages is

still some 70 per cent. above the 1914 level, the increase in many industries exposed to foreign competition is much below the average, and in some cases is substantially below the increase in the cost of living index. On the other side, this fall is, of course, balanced by a relative improvement in the wage rates of industries and occupations not directly exposed to foreign competition.

117. It would be misleading to infer from so brief a statement as we have given that the relative positions of wage-earners are to be judged by a comparison of rates at two points of time. Account must necessarily be taken of the state of adjustment of wages in different industries at the datum line. But such refinements are unnecessary for our purpose, which is merely that of forming a judgment on broad lines of the factors which may have impeded industrial recovery. With the absolute level of wages and with the question whether the standard of living which can be maintained on a given rate is a desirable or undesirable standard, we have nothing to do. But the very existence of the unemployment problem demonstrates that there is a disparity between prices and costs of production, which has the result of diminishing or eliminating profits and damping down all incentive to the expansion of output.

118. If Great Britain were a closed system, having no trading relations with the outside world, both diagnosis and remedy would be less difficult. For, provided that the disparity was not due to money wages and other costs rising faster than physical efficiency, it would presumably be the result of a failure of the purchasing power, paid out by entrepreneurs to meet their costs of production, to return to them in its entirety in the shape of the selling proceeds of their output. The right policy in these circumstances would therefore be for the banking system to stimulate investment by reducing the cost of borrowing, increasing the supply of purchasing power and discouraging the hoarding of balances.

119. But for a country which adheres to an international gold standard and in the economic life of which foreign trade plays a large part, a disequilibrium associated with unemployment may arise in any of three ways:—(i) it may be due to a domestic situation of the kind just described in which entrepreneurs as a whole are failing to receive back as sale proceeds the equivalent of what they have paid out as costs of production, (ii) it may be due to a situation of a similar character, but existing in the world as a whole, or (iii) it may be due to domestic costs having risen relatively to those of foreign competitors. Moreover, even if the trouble had arisen mainly under the first head, some of the remedies which would be appropriate in a closed system may be injudicious or impracticable, because of their tendency to cause excessive foreign lending, short or long.

120. The unemployment which existed at the time of our appointment was probably due, in the main, to the first and third factors. While we have been sitting, it is evident that the second factor has supervened in an aggravated degree, so that the present situation is highly complex. The remedy of the first factor still remains to some extent within our own control, but the difficulties and dangers of applying a remedy are much increased in an adverse international environment. To remedy the second factor, international co-operation is necessary.

121. On the question of the relative costs of production here and abroad we require to examine the position in some detail. An adverse change in our effective costs of production compared with those elsewhere might be due to any of the following causes :—

(i) Our technical efficiency of production might be declining, or increasing less rapidly, than that of our foreign competitors. It is extremely difficult to obtain a satisfactory statistical test of this. Doubtless our technical efficiency is not what it might be—but that is usually so; nor is a falling short of the highest a peculiarly British characteristic. It is true also that several of Great Britain's most important traditional industries are not amongst those which have been showing, of late years, the most rapid technical progress, and that we may have been somewhat slow, partly for reasons arising out of the War, in applying ourselves on an adequate scale to some of the newer industries.

On the whole, however, we incline to the view that the shortcomings of this country in technical efficiency as distinct from organisation may not have been so great or have played so large a part in producing our present difficulties as is sometimes supposed. This view is based on an examination of the relevant statistics relating to the year 1929; we take this year rather than 1930, partly because detailed statistics for 1930 are not yet available, but chiefly because for purposes of comparison with foreign countries the figures for 1930 are much confused by the effects of the world depression, an influence which has to be excluded for the purposes of the statistical test which we are trying to make.

In 1929 our exports of manufactured goods, though declining, were still greater than those of any other country in the world. At the same time our real wages, whilst comparing unfavourably with those in the United States (which country, however, is unable to compete with us in world markets in our principal staple exports such as coal or textiles and many iron and steel products) were much higher than those paid by any of our chief European

competitors, as shown in the following table (for January, 1930) based on hourly time-rates of wages :—

Great Britain	...	...	...	...	...	...	100
Holland	...	...	...	...	...	...	87
Germany	...	...	...	...	...	...	77
France	...	...	...	...	...	...	58
Italy	...	...	...	...	...	...	43

If we could retain so substantial an export trade in spite of so great a disparity of wage-rates, it would seem unlikely that our technical efficiency can have been much inferior to that of our competitors.

The figures for the increase in output per head per hour given in Appendix VI confirm this conclusion. Those figures suggest that hourly output per head in 1929 may have been quite 10 per cent. greater than in 1924 and 33 per cent. greater than in 1907. To take particular industries, the output per worker increased between 1924 and 1929 by 27 per cent. in the case of coal, 20 per cent. in iron and steel, and 15 per cent. in engineering and ship-building, though the extreme depression in the volume of sales caused a decline in textiles. Indeed, it could scarcely have been possible for British employers to have paid in 1929 real wages ten per cent. higher than in 1924 for hours 10 per cent. less than before the War, if they had not been making great technical progress, or if they had been falling seriously behind their competitors in technical efficiency.

122.—(ii) Access to our established markets may be made much more difficult by reason of increases of tariffs in those markets, or analogous measures, and our relative costs may require to be reduced if we are to be in the same position as before relative to competitors working under the protection of the tariffs. It is well known that this factor has played an important part, particularly in the case of textiles. Striking evidence of the increase of tariff rates will be found in Section IV of Statistical Tables relating to British and Foreign Trade and Industry (1924-1930) (Cmd. 3737).

123.—(iii) An adverse change in our position may take place owing to a change in the relative values of the national moneys in which the costs of production are paid without a corresponding change in the amounts of these costs expressed in terms of the national moneys.

It is here that we find the major part of the explanation of the adverse change in our costs of production compared with those elsewhere. The process of raising the gold-value of sterling, which culminated in the return to the gold standard at the pre-war parity, necessarily involved an increase in our costs of production in terms of gold unless these costs were being reduced *pari passu* in terms of sterling, which has not been the case.

Furthermore, the difficulties which this brought on our manufacturers were seriously aggravated by the fact that shortly afterwards several of our most serious competitors, in particular France, Belgium and Germany, suffered changes in the gold-value of their national moneys of precisely the opposite kind. That is to say, the rates at which they stabilised their currencies in terms of gold had the effect of decreasing their gold-costs of production, except in so far as these costs expressed in the national currency were tending to rise, which was only partially the case. It is difficult, or impossible, to obtain an exact statistical measurement of the competitive handicap which the relative over-valuation of sterling and under-valuation of certain other countries have imposed on our exporting manufacturers. But it is certainly substantial.

124. We must, therefore, attribute the difficulties of those of our industries which are either substantially dependent on exports or which are exposed to the competition of foreign imports largely to the fact that sterling costs did not prove adjustable to the change in the value of sterling necessary as a consequence of the return to gold at the pre-war parity; and still more so to the heavy fall in world prices which has since occurred.

125. This lack of adjustment has not, however, been a phenomenon working uniformly in all types of industry. The industries which have to sell their products at world prices in the face of foreign competition have in fact made substantial reductions in cost of production; indeed wage rates are low in comparison with other occupations. But the export industries require the services of transport and other occupations in which wage rates have been substantially improved as compared with the pre-war level and must therefore carry in their costs of production some part of the increase in the more sheltered industries. In these circumstances the export industries are driven, if they are to be successful in competition, to force their own costs yet lower in so far as the position is not met by increased efficiency in the transport and other occupations above mentioned. At the same time the cost of living is in part held high in relation to wholesale prices by the very fact that costs in the home services have been maintained, and the burden on the wage-earner in the export industries is thus intensified.

CHAPTER VI. — THE DISEQUILIBRIUM BETWEEN DEMAND AND SUPPLY.

126. The difficulties of this country which we have surveyed in the preceding Chapter have been added to by the course of events in the world at large. The period since 1925 has been at the same time one of rapid economic development and adjustment and one of great instability. Not only the monetary policies of other nations

but also the changes in the volume and the nature of production have had their reactions on this country. Pressure has come from many directions and in many forms. The total situation is complex, and we think it desirable, therefore, to review at some length such of the factors in it as are relevant to our conclusions on the monetary aspects of the problems presented.

127. If we survey the world as a whole, a distinction needs for some purposes to be drawn between Europe and other Continents. For though the disorganisation of currencies and the one-sided development of production in response to war demands extended beyond Europe, the weight of destruction, disorganisation and social and economic disintegration operated with special intensity in that Continent. Broadly speaking whilst the rest of the world progressed, in some areas with great intensity, throughout the whole of the period under survey—until the equilibrium of production was everywhere shattered by the international crisis through which we are still passing—in Europe, before absolute progress could be registered, a period of recovery had to take place. The first phase of recovery was completed by 1925. Up to that time, it was not suggested that currency reform and economic reconstruction stood in any sort of opposition to one another. Industrial recovery depended upon the restoration of order in the sphere of currency, for the instability of the currency was not only depriving the countries affected of the assistance of foreign capital, but was undermining the whole foundation of the social and economic structure.

128. The years which have elapsed since 1925, when Great Britain's return to the gold standard definitely ended the period of currency experimentation which had begun in 1914, fall into two sharply divergent phases; the first sub-period ending with the year 1928; the second commencing with the accentuated Wall Street boom of the spring and summer of 1929. In the first sub-period the circumstances and the technique employed in working the gold standard itself were on balance favourable to economic progress and to the re-establishment of the prestige of the standard. It is true that in Great Britain the return to gold was followed by industrial disputes in 1926, and, in consequence, by a marked decline in production for the time being. But the coal dispute and general stoppage, which might have been expected to produce serious difficulties in maintaining the international parity of the pound sterling, did not in fact lead to any such result, in consequence, no doubt, of the "flight from the franc" which preceded the *de facto* stabilisation of that currency at the end of the year 1926. In other respects the European situation during those years was improving. The Dawes Plan had put the Reparations question upon a reasonable basis in 1924, and the Dawes Loan had enabled the Reichsbank to accumulate the necessary funds for the rehabilitation of the German currency. The recession of German

business in 1926 was successfully overcome. The work of financial reconstruction undertaken by the League of Nations in Austria, Hungary, Greece and Bulgaria, the stabilisation of the franc, the lira and the belga, together with the settlement of the Reparations question and the more friendly political relations between France and Germany, created an atmosphere favourable to investment and economic enterprise. In the sphere of central banking also, conditions were propitious. Friendly understanding existed between the Central Banks of the United States, Germany and this country. It appeared not impossible then that these banks might, in conjunction with the Bank of France, inaugurate a new era of successful and intimate co-operation. Prices were indeed falling in the earlier part of this period, but not at such a rate as seriously to impair equilibrium at a time when rationalisation was beginning markedly to affect costs.

The Production of Raw Materials and Foodstuffs.

129. Inadequate and unsatisfactory as the statistical material may be, there can be no question that the tendency towards an increasing return from human effort and a growing command over the resources of nature persists and has persisted in recent years. Thus it appears from the data collected by the Economic Section of the League of Nations* that, in comparison with the position in 1913, the world's population had by 1925 increased by some 5 per cent., whilst the general index of production had risen by 18 per cent. Excluding cereals and other foodstuffs, the index of production had risen by no less than 25 per cent. In other words, the command over the sources of well-being—in so far as these are measured by the growth in the volume of materials available for working up into more finished forms—had increased, even by 1925, much faster than the population.

130. If comparisons are made, not between 1913 and 1925, but between 1913 and 1928, much the same impression is received, with the significant difference that by 1928 the position of Europe relatively to the rest of the world had greatly improved. Between 1913 and 1928, the population of the world increased by 10 per cent., the production of foodstuffs and raw materials together by 25 per cent. Foodstuffs taken alone had increased by 16 per cent., raw materials by no less than 40 per cent. Moreover, to quote from the League of Nations Memorandum, "The apparently very rapid and substantial progress achieved by Europe in the period given represented, until 1925, a recovery of lost ground. In that year, the European index on the base of 1913 stood at 103. The indices of all the other Continental groups were very substantially higher. . . ."

* The following figures (unless otherwise stated) are obtained from the *Preliminary Memorandum on Production and Trade* and the *Memorandum on Production and Trade 1928 to 1928/29*, issued by the Economic and Financial Section of the League of Nations.

In 1923 . . . all the indices except that for Europe, which stood at 85, were well above the pre-war level. The rising figures for these Continents, therefore, during the whole period 1923 to 1928 represent rather normal progress than recovery. . . . In Europe the rate of growth since 1923 has averaged some 5.8 per cent. per annum, while in the rest of the world it was only 2.4 per cent. According to the preliminary information available, this differentiation in the rate of progress continued during 1929. If the U.S.S.R. were excluded from Europe, the differences would be still greater.**

The Growth of International Trade.

131. From the standpoint of international trade, the growth has not been quite so marked, whether as regards Europe or the world as a whole. If 1913 be taken as base, the quantum of international trade increased up to 1928 by some 24 per cent.; more rapidly, that is to say, than the growth in the volume of foodstuffs production; less rapidly, on the other hand, than the growth in the production of raw materials. Nevertheless, the rate of growth was more rapid than the growth of world population—24 per cent. against 10 per cent. As regards Europe alone, the population growth (including Russia) of eight per cent. contrasts with a rate of growth in the quantum of international trade of some seven per cent. The divergence in the movement of the index of production of materials and foodstuffs and of the quantum of foreign trade is natural. For with the growth of population in the raw material and foodstuffs producing countries, a larger proportion of the local produce is necessarily consumed locally; international trade does not consist merely in a transfer of foodstuffs and raw materials, but of an exchange of these goods for manufactured articles, and the terms of interchange have altered to the disadvantage of the raw material producing areas; lastly, international trade is greatly affected by the volume of capital issues, the quantum of which depends upon circumstances having little direct connection with the conditions affecting production. Taken all in all, however, the statistics so far adduced prove that the general conditions have been favourable to a growth of material welfare throughout the world.

The Growth of Production generally.

132. This favourable impression is strengthened if the indices of production which are now available for various countries are drawn into the picture. Production as a whole—still more production as represented by official indices which do not pretend to cover the entire area—is subject to the vicissitudes of cyclical and other influences and is therefore liable to unequal growth from year to year. A recent foreign survey of the ground shows the position as follows:—

* *Memorandum on Production, etc., 1923 to 1928-9, pp. 16-17.*

*Industrial Production in Various Countries.***Monthly Average 1929 = 100.*

Monthly Average	England	Germany	U.S.A.	France	Sweden	Austria	Poland
1925	—	81·8	88·2	77·4	78·5†	—	72·7
1926	—	77·6	90·8	90·3	80·7	76·4	71·3
1927	96·2	98·4	89·0	78·8	85·2	89·6	88·7
1928	94·3	98·3	93·3	91·0	81·5†	100·5	100·3
1929	100·0	100·0	100·0	100·0	100·0	100·0	100·0
1930 1st Quarter	99·2	92·4	87·4	103·0	110·3	87·5	84·8
„ 2nd „	92·2	89·4	87·4	103·1	99·3†	89·3	80·0
„ 3rd „	89·0	80·8	76·5	99·6	93·3	79·7	82·3

The general impression given by the statistics is one of fairly continuous improvement up to 1929, followed by sharp declines in 1930. The same impression is derived from an inspection of the figures given in a recent British official publication:—

Base Period.	U.K.	Canada.	U.S.A.	Germany.	France.
	1924=100	1919-24= 100	1923-25= 100	1928=100	1913=100
1924	100	116	95	69	108
1925	—	125	104	83	107
1926	—	146	108	79	124
1927	107	156	106	100	109
1928	106	173	111	100	127
1929	112	193	118	102	139
1930—1st Quarter	111	173	105	94	144
„ 2nd „	103	175	103	91	144
„ 3rd „	100	158	92	82	139

The Effects of Increased Production in relation to Demand.

133. It is not difficult to find an explanation of the forces which made for increased production during this period. In consequence of the situation during the War, when demand was great and labour scarce, the standardisation of industrial methods and the introduction of labour-saving machinery necessarily received a great impetus. At the same time, the advantages to be gained by an integration of works and the building up of horizontal and vertical combinations in industry were very substantial. These forces did not cease to operate after the War was over. In some

* *Deutschlands Wirtschaftliche Lage an der Jahreswende 1930/31*, published by the Reichskreditgesellschaft, Berlin, p. 3.

† Influenced by labour troubles.

‡ *Tables relating to British and Foreign Trade and Industry*. [Cmd. 3737], p. 375.

countries, as in the United States, the growth of new needs and wants made it easier in the industries supplying those wants to organise production upon an ever vaster scale, and thus to obtain the well-recognised economies of large-scale production. In other countries, such as Germany, the pressure of heavy international debt payments, and the consciousness that the productive machine had been allowed to fall behind, combined to stimulate a process of reorganisation. What prosperity and the demand for still greater well-being achieved in the one case was enforced in the other by the pressure of want and scarcity. Thus the many-sided movement known as rationalisation has exerted a steady influence, making towards a reduction of costs, in all industrial countries, though the impetus thereto differs from case to case.

134. Had the technical changes in question been confined to manufacturing industry, a situation similar to one which has before occurred in the world's history might have repeated itself. Industry might have been reducing its costs, whilst the cost per unit of agricultural output might have been rising, thus altering the terms of exchange in favour of the agricultural countries. The actual development has been very different. For agriculture also has become subject to the influence of the technical advances of recent years, with the result that the absolute volume of agricultural production has greatly expanded, without a corresponding rise in the cost of production. On the contrary, recent mechanical inventions have created a problem of surplus labour in the agricultural regions of the world, at a time when technical changes were tending to reduce the chances of employment in industry, and when simultaneously the substitution of artificial products (for example, of artificial silk for cotton) was narrowing the market for, at least, some agricultural products.

135. Technical changes and the partial substitution of artificial for natural products, combined with a relative decline in the growth of population, thus created a situation of some danger even before the depression of 1929-30 occurred. The danger presented was that of the relative over-production of certain kinds of foodstuffs and raw materials and of a consequent fall in the prices of those products below the general level of prices. Moreover, if the general price level is falling the situation of producers of articles in over-supply is much aggravated. Industry tends to be depressed generally, and the demand falls away much more rapidly, relatively to the supply forthcoming, than it would in times of stable or rising prices.

136. It is beyond doubt that the rapid increase of production of, e.g., wheat, rubber, coffee was a factor making for instability of economic conditions in the countries largely dependent for their prosperity upon these products, even before the general dislocation of the price level occurred. In such a state of over-

production of particular commodities the natural remedy is a restriction of the supply. The process by which the weaker producer is eliminated is necessarily one accompanied by much hardship and—especially if the article is largely produced by small cultivators or small units—it takes considerable time to produce its effects. Attempts to rationalise, not only the costs of production but the conditions of supply, whether by attempting to control the output, or the quantity allowed to come upon the market, in the effort to achieve a fair measure of price stability and a guarantee both of profit and permanent employment to the producing unit, are therefore perfectly understandable and cannot be condemned out of hand. In fact, a variety of stabilisation schemes have been adopted in recent years and have been applied, either in particular areas or over the whole of the world, to rubber, sugar, zinc, coffee, nitrate, copper, iron and steel, tin, wheat, cotton. The majority of these schemes designed to secure orderly conditions of production, marketing and price have in practice failed to achieve their object. It is beyond our province to investigate the causes of failure. We are concerned rather with the results, and from that aspect it is clear that such schemes, when they do come to grief, are themselves a further cause of price instability. Especially is this the case where the temporary success of the scheme evokes a further addition to the supply or where a substantial part of the current output has been held off from the market. For, as the Federal Farm Board of the U.S.A. remark in their First Report—“the accumulation of a substantial volume, the most of which necessarily must be in the visible supply, has a somewhat depressing effect upon prices. Announcement that such accumulation will not be sold is not sufficient to reassure buyers unless the quantity thus held renders difficult the purchase of supplies adequate to the demand. Even then the demand is curtailed or limited to immediate requirements, and forward buying in anticipation of future needs is lessened.”

137. The position of the raw material producing countries has thus been an extraordinarily difficult one. High prices during and immediately after the War stimulated production, and by increasing the national income and financial strength of the producing countries made it easy to obtain capital loans; and this situation encouraged the consumption of additional imports and a postponement of the pressure on the national economy of the interest payments on capital loans. The very increase in production helped to bring about lower prices, and these lower prices led to the adoption of various schemes to prevent prices from depreciating further. The partial or complete failure of these schemes forced prices still lower, and discouraged capital imports, thus increasing the pressure towards a forced sale of exports to meet external payments of interest and for other purposes.

Changes in the Rate of Growth of Demand.

138. If, in certain cases, the most conspicuous feature in the situation threatening a rupture of the economic equilibrium of supply and demand has been an over-stimulus to supply from changing conditions of technology and price, in others rupture has been produced by a definite falling off in the rate of growth of demand. In these latter cases, it has not been a positive increase in the volume produced so much as the existence of a permanent excess capacity to produce; relatively to the changing demand situation, which has caused depression and dislocation. A distinction should be drawn, in other words, between such a case as artificial silk, where temporary depression has been due to a great increase in world-demand leading to an even greater increase in world-supply, and the case, e.g., of coal, which has had to meet the competition of oil and water-power with the result that the coal industry has been depressed throughout the world. The coal industry and the cotton industry—to some extent the woollen industry also—are indeed the leading examples of industries in this class; for, although the older centres of the cotton industry have found their situation aggravated by an increase in manufacturing capacity in newer centres, it is clear, to quote from the Memorandum on Production issued by the League of Nations, that the "generality of the depression through which the cotton industry is passing can be judged by the figures showing the number of weeks of forty-eight hours during which the total number of spindles from which returns were received were stopped." These figures, which relate to the half-years ending January 31 for the years 1926 to 1929 show a considerable degree of depression even before the onset of the crisis in 1929.* Or, as the same authority elsewhere points out, "During the last three years the amount of cotton consumed has been practically stationary. But this is due to the fact that during this period the takings of the Russian mills have steadily increased, and there has been a similar increase in the use of cotton in some of the minor producing countries . . . If these two users (i.e. Russian and minor producing countries) of cotton be ignored, it will be found that the consumption in the year ending July 31st, 1929, was lower in all the Continental groups (excepting South America, where the change was slight) than it was in the commercial year 1926-27."†

The Effects of Tariffs, &c.

139. A further influence affecting the equilibrium of supply and demand throughout the post-war period has been the increase in the growth of restrictive policies in the shape of Tariffs and Subsidies, Import and Export Prohibitions, the exploitation of the administrative features of the tariff for protective purposes, and the

* See Table XXII in *Memorandum on Production, 1923—1928-9*. p. 56.

† *Ibid*, p. 54.

retention of the national market for local manufacturers by the exclusion of foreign firms from public works contracts. Moreover, the number of separate Customs areas has increased in consequence of the break-up of the old European Empires. One of the effects of these commercial policies consists in the tendency to increase surplus capacity. The break-up of Europe resulted in the old industrial organisation of countries like Austria-Hungary being parcelled out among the Succession States. If the spinning section of the cotton trade was mainly located in one State, and the weaving in another, efforts were directed in each, through the instrumentality of the State, to setting up a new weaving and spinning section respectively. The net effect was to increase the total world capacity beyond the point at which the total equipment could find employment. No doubt to some extent the commercial policies which permitted these developments merely anticipated the inevitable. The growing rationalisation of agriculture brings with it, for instance, the necessity of finding alternative methods of employment for the displaced agricultural population. But the attempt to solve the transfer problem so created by the unco-ordinated tariff activities of a large number of independent authorities may very well accentuate the transitional difficulties involved, by action which increases the duplication of productive capacity and the consequent wastage of capital.

CHAPTER VII.—GOLD AND ITS DISTRIBUTION.

140. The questions relating to the production and distribution of gold have recently been under consideration by a Delegation of the Financial Committee of the League of Nations which has already issued two interim reports.* In these circumstances we think it unnecessary to review these questions in the detail which might otherwise have been required.

141. With the departure of the majority of countries from the gold standard during the War, the distribution of the world's monetary stock of gold naturally underwent a vast change. In particular during the earlier years of the War gold flowed largely to the United States in exchange for the goods required by Europe. At a later date gold flowed to that country when instability of the currency in various European countries caused a flight of capital. Thus when the international gold standard was restored the European countries held only £741 millions, or 35 per cent. out of the then existing aggregate gold stock of £2,102 millions,

* First Interim Report, C. 375. M. 161, 1930, II; Second Interim Report, C. 75. M. 81., 1931, II.

in comparison with the £1,138 millions (or 63 per cent.) held in 1913 out of a total stock of £1,803 millions. On the other hand the North American holdings had risen from £429 millions in 1913 to £950 millions in 1925, or from 24 per cent. to 45 per cent. of the total stock.

142. The general return to the gold standard created an intensified demand for gold, especially in European countries, for the reconstitution of Central Bank reserves as and when currencies were stabilised. For some time the demand did not become acute owing to the adoption in several cases of the gold exchange standard, but following the stabilisation of the franc, a large demand for gold arose from France. During the period 1925 to 1928 European gold stocks increased by about £165 millions or some £18 millions more than the total addition to world stocks in that period. At the same time the gold holdings of South America increased substantially, the loss falling in the main on North America. Since then the main feature has been the flow of gold from the debtor countries to the creditor countries, and, in particular, France and the United States, accompanied by even more severe reductions in the foreign assets of the debtor countries. Thus, the American gold stock rose from £880 millions to £944 millions between December, 1929, and December, 1930; the French gold stock rose from £336 millions to £431 millions during the same period. A continued growth in the aggregate gold stock has in fact been accompanied by a growing concentration in a few countries. It has been estimated that the world's monetary stock of gold rose during 1930 from £2,301 millions to £2,407 millions.* Of these amounts eight countries (Germany, Great Britain, France, Italy, Spain, United States, Argentina, and Japan), held 80 per cent. and 82 per cent. at the two periods. Of the amount controlled by those eight countries, the United States, France and Great Britain controlled 74 per cent. and 78 per cent. at the beginning and end of the period.

143. These changes both in the amount of the gold stock and in its distribution have given rise to much discussion. On the first point it is argued that the stock of monetary gold is being added to at a slower rate than that at which the physical output of the world's industry and trade is increasing and that this goes some way to explain the fall in prices which has already taken place and in any case threatens a fall in the future. On the second point, it is argued that whether or not there is an absolute shortage of gold, the distribution of gold has itself been such as to bring about a fall in the world price level.

* Selected Documents on the Distribution of Gold submitted to the Gold Delegation. C. 102. M. 38, 1931, IIa.

The Output of and Demand for Gold.

144. So far as the absolute output of new gold is concerned the views of expert witnesses, both before our Committee and the Gold Delegation of the Financial Committee of the League of Nations, leave little room for doubt. The long-run tendency is for gold production to fall, though the rapidity of the decline in yearly output is differently assessed by different experts. Prospecting and mining for gold has now become a highly scientific and capitalised industry and as the world is more and more thoroughly surveyed the chances of discovering another field to take the place of the Transvaal, which now supplies about half the total world output, steadily diminish. Moreover, as Mr. Kitchin, whose own estimates are somewhat higher than the official estimates presented to the Geneva Committee,* stated in evidence before us, "If there is any important new discovery, it will (unless alluvial is concerned) reach appreciable figures only after many years' work. While it would not be reasonable to dismiss the possibility of considerable additions from new sources—the analogy of the history of gold itself and of other metals forbids that—it is not prudent to attempt to speculate on what is unknown and unassessable." (Statement, paragraph 18.)

145. Apart from new sources of supply, the possibility of a fuller exploitation of known supplies is afforded by future improvements in metallurgy and by the fact that a fall in mining cost—due to falling prices as distinct from additions to technical knowledge—leads to a more thorough utilisation of the gold-bearing ores. But, apart from the fact that an improvement in gold production through falling prices is analogous to curing one disease by inoculating a worse one, not very much reliance, we are given to understand, should be placed upon further improvements as an element in solving the problem. It must be concluded, therefore, that, so far as can be foreseen, the gold output of the world is likely to diminish. Mr. Kitchin, in fact, estimates that within a decade, the world's annual output of gold will have fallen from £83 millions to £76 millions. (Statement, paragraph 19.) A substantial part of this output is absorbed by industrial consumption and by hoarding in the East. Over the periods 1890-1914 and 1915-1929 it is estimated by Mr. Kitchin that about 42 per cent. of new production was required for these purposes. The Gold Delegation concluded on the available evidence that the non-monetary demand might amount to £37-41 millions a year.

146. There is no precise means of estimating the actual future needs of gold for monetary purposes. We reproduce in Appendix III an estimate of the monetary demand for the years 1930-1940 made by the Gold Delegation on alternative assumptions as

* The difference is not inappreciable, being of the order of six per cent. in the total production for 1930 to 1944.

to (a) the proportion of gold reserves to notes and sight liabilities maintained by Central Banks and (b) the annual rate of growth of world productivity. Apart from changes in existing currency regulations and practice, the Delegation concluded that the increment of new gold for monetary purposes would by 1934 fall short of the requirements of the price level assumed by the argument. The estimates of the Delegation took as their starting point the volume of the notes and sight deposits of Central Banks for the year 1928. Since that date there has of course taken place a heavy fall in world prices which, if it were to prove permanent, would be accompanied no doubt by a substantial reduction in the aggregate volume of notes and deposits. But this, as we have indicated, would represent an acceptance of the position rather than a remedy for it.

147. Whilst the available figures serve as a warning that, unless definite steps are taken to avoid the danger, a fall of prices due to insufficiency of gold will undoubtedly occur in the future, they by no means prove that the gold problem is one so closely linked with the physical facts of gold production as to make the outlook in any way a hopeless one. On the contrary it seems probable that, given good will and understanding on the part of the world's monetary authorities, the dangers threatening the price level can be postponed for a period of time sufficiently long to deprive the problem of practical importance.

148. In the first place, the maintenance of a stable price level is not bound up with an inevitable annual increment in the volume of the various forms of purchasing power held by the public—coin, notes and deposits in commercial banks. Changes in habits may alter substantially the amount of purchasing power which the public desire to hold in various forms and, as the world situation improves and confidence is restored, the holding of purchasing power in cash or liquid deposits may decline in importance. Thus even if a constant relation must be maintained between the growth of Central Banks' liabilities and the desire of the public to hold liquid resources, a rate of growth of the former less than that usually assumed as necessary will suffice. In the second place, the relation between total Central Bank liabilities and gold supplies is influenced by the form which those liabilities take. For in so far as the legislation governing Central Banks' reserve ratios requires a smaller (or no) reserve to be kept against deposit liabilities, a growth in these liabilities relative to total liabilities will diminish the pressure upon the available gold supplies. In the third place, it is not necessary that the volume of note issues should continue to be regulated, as it is now, by reference to the amount of gold held in reserve. If, as

we recommend in Part II of our Report, the principle is adopted that gold reserves should be held, not primarily against note issues, but to meet temporary deficiencies in the balance of international payments, there need be no obstacle to the creation of a much increased volume of purchasing power without any increase in the supply of monetary gold.

149. Some of the directions in which remedial measures might be found to avoid a future shortage in the supply of gold were indicated by the Gold Delegation as follows :—

(a) the concentration of all monetary gold in the reserves of Central Banks ;

(b) the economising of these reserves by the reduction of the current legal minimum reserve ratios, full recognition being given to the varying requirements of different countries in accordance with their economic circumstances ;

(c) a common understanding between Central Banks as to the reduction, as occasion demanded and circumstances permitted, of the proportion of total gold cover held in practice (i.e., the excess of cover over the legal minimum ratio).

150. These measures would all be helpful. We would only add to them the desirability of recognising the point which we have emphasised at the end of paragraph 148, namely, that there is no reason why the volume of purchasing power need be related in the rigid way which has characterised banking legislation hitherto with the volume of gold held in reserve.

The Distribution of Gold.

151. The present distribution of gold is very generally held to be unsatisfactory : a maldistribution to which is to be attributed a large measure of responsibility for the heavy fall in prices in recent years. It is necessary, however, to look beyond the statistical facts of the existing distribution and consider the causes which have brought that distribution about.

152. The fact that a substantial gold reserve is held by a Central Bank serves no doubt to create confidence in the credit structure of the country concerned. But now that, with small exceptions, gold coin has been withdrawn from circulation, an internal demand for gold cannot arise. The sole practical use of a gold reserve is to serve as a medium of meeting a deficit on the balance of international payments, until steps are taken to bring it again to equilibrium.

153. In the period since the return to gold the balance of international payments between gold standard countries has been affected by many circumstances of an abnormal character. The monetary policies adopted, the course of international trade, the erection of barriers against the free flow of commodities, and political instability have all played a part in contributing to the

movement of gold upon an unusual scale. Thus there has arisen in many countries a great stress on gold reserves. That pressure inevitably takes the form of a contraction of credit to prevent the undue depletion of gold reserves, with the result, if the strain is continued, of a diminution in business and investment activity and a fall in prices. It is to the instability of post-war international finance and especially to the irregularity of the flow of credit between debtor and creditor countries that the present distribution of gold and the pressure which the process of re-distribution has exerted on credit policies must be largely attributed. Amongst the causes of that instability the following are the most outstanding :—

(a) The burden of the War debts: the principal debtor, Germany, has until recently not been able to discharge her obligations by means of the delivery of goods but has been forced to adjust her situation by short and long borrowings from abroad.

(b) The entry of the United States into the group of the chief creditor countries has caused a dispersion of initiative and responsibility in the leadership of international finance.

(c) Many of the loans incurred since the War have been for non-productive purposes, having been of a political character or to balance budgets or to support the exchanges, or to build up currency reserves. Thus there have been many influences at work on the market rate of interest and on the movement of obligations in the international market which have had no close relation to the actual yield of new capital enterprise.

(d) The perils of the war and post-war period and the unfortunate currency experiences of many countries have led to a greatly increased preference for liquid assets as compared with long-term securities. Especially there has been a tendency on the part of many countries to pile up liquid claims in the leading financial centres, instead of embarking on foreign fixed investment or funded obligations. France, the third largest creditor country in the world, appears to have employed virtually the whole of her international surplus during the last three or four years in the purchase of gold and short-term liquid claims; whilst the attitude towards long-term foreign securities of the investors of the United States, which is now the second largest creditor country next after ourselves, has fluctuated violently. The effect on prices internationally of an increased preference for employing resources in the purchase of liquid claims, including gold, is the same as is that of hoarding in a primitive community. It is to this increased, and undue, preference for the employment of resources in a liquid form, rather than to the shortage of new supplies of gold, that the

fall of prices is to be attributed ; though of course it is the case that a suddenly increased rate of supply of new gold, if it could have occurred just at the right moment, would have increased the supply of liquid assets and would, therefore, have served to diminish the degree of tension set up and hence the fall of prices.

(e) Movements of gold have ceased of late to have what used to be considered their " normal " effect on the domestic credit policy of certain countries, notably France and the United States. In recent years it has been impossible to rely on action being taken by both the country losing gold and the country gaining gold to preserve international equilibrium, the one meeting the other half way, as we explain in paragraph 185.

154. We conclude that the important factor for consideration in the problem of the so-called maldistribution of gold lies in the removal or mitigation of the underlying causes which have led to the present concentration and we return to this aspect of the matter in our recommendations. Indeed, even a large increase in the current supplies of new gold would not do much good so long as the causes persist which have led to the present maldistribution of gold. For the additional supplies would soon find their way to the same destinations.

CHAPTER VIII.—THE SEQUENCE OF EVENTS SINCE 1925.

155. When in 1925 Great Britain took the decisive step of restoring the gold standard, the French, Belgian and Italian currencies were not yet stabilised ; in Germany the stability of the new currency had only been maintained by a drastic rationing of credit by the Central Bank in 1924 ; the future of Indian exchange was not yet determined ; and the Federal Reserve System had only recently developed in a deliberate manner its system of open market operations as an instrument of great flexibility in the control of credit conditions. The full implications of the technical changes taking place in industry were not by any means clear ; and, although in this country the volume of unemployment was already giving rise to grave concern, a general feeling was abroad that with the restoration of the gold standard and the settlement of the Reparations question the era of extreme instability had definitely passed away.

156. Outranging all these factors in ultimate importance, however, though influencing them and being in turn influenced by them,

was the development of the economic situation in the United States. For a century the United States had been borrowing heavily from Europe. America had freed herself from indebtedness to Europe during the War; and thereafter it appeared that the tide had definitely turned and that the United States, having undergone the transition from a largely agricultural to a predominantly manufacturing country was about to repeat the history of Great Britain and to emerge as an exporter of capital upon a vast scale. For some years after the end of the War, indeed, the growth of American capital exports was the indispensable means of recovery of economic conditions in the rest of the world. Issues of long-period securities in the United States reached their maximum in the four years 1925-1928, during which period the net amount offered on long period account aggregated \$4,789 millions, or nearly £1,000 millions—an amount twice as large as the volume of long-period capital issues (£482 millions) floated in London during the same period. At the same time, American concerns were also investing largely in foreign enterprises. Whilst the net amount advanced on long-term account by the United States was in reality somewhat less than these figures would seem to indicate, there can be no doubt either that American foreign investments assumed large proportions in these years or that they had striking effects upon the areas—Central and South America and Central Europe—where the investments were chiefly made.

157. To this movement many factors contributed—the desire of the great industries to safeguard their foreign markets; the sentimental attachment of American citizens of Central European origin to their original countries and the desire to aid them; the high rates of bond interest offered; the belief that the world was now once more politically and economically stable; the desire to assume a dominating role in Latin America; at times also (especially in 1927) a temporarily depressed condition of American business; a rate of per capita savings so large as to outstrip the possibilities of profitable investment at home in periods of business quiescence. But at a crucial moment one other factor intervened to accentuate the process. That factor was the policy of the Federal Reserve System in the second half of 1927.

158. Broadly speaking, the United States continued throughout the post-war period to gain gold, until by the middle of May, 1927, the gold stock of the U.S.A. reached its maximum figure of \$4,700 millions. It had been the avowed policy of the Federal Reserve Authorities to regard this gold stock as a trust fund, and therefore to prevent such an expansion of credit in the United States as would necessitate the permanent retention of the whole stock as a permanent reserve. The policy of gold sterilisation was the objective expression of this point of view. In 1927 the moment seemed to have arrived when the exigencies of the local credit situation coincided with the necessities of the outside world. In

the autumn of 1927 the Reserve System encouraged low money-rates in the New York market and thereby stimulated a boom in international securities. Gold flowed out, and by June, 1928, the United States had lost \$600 millions of gold, the gold stock on 23rd June, 1928, being \$4,099 millions against \$4,700 millions on 16th May, 1927.* The effect of these various incidents can be thus summed up. Easy credit conditions had more than restored the pre-war ratios between gold and the short-term liabilities of European Central Banks† and had, in conjunction with other circumstances, generated a period of world prosperity which, *inter alia*, enabled Great Britain to recover to some extent from the direct effects of the return to the gold standard and the industrial troubles which had followed upon it.

159. But the credit situation in the United States was now to change, and to change disastrously in its reactions upon the rest of the world. In the first place, cheap money in the United States strengthened the tendency, already present in spite of a relative ebb of business in 1927, to a rise in the price of common stocks. From 1925 to 1928 building and other construction in the United States was on an unprecedented scale, reaching the colossal aggregate of \$38,000,000,000‡ for the four years together (or about £160,000,000 a month), which was about double the value of the construction in the four years 1919 to 1922. The putting into circulation of this enormous volume of purchasing power, which was not directly associated with any corresponding increase in the production of immediately consumable goods, caused a huge growth of business profits, which culminated in 1928 and 1929. At the same time the market value of securities increased in an even greater proportion than profits, the process of the appreciation of securities being greatly assisted, apart altogether from the influence exerted by cheap money and business prosperity, by the belief that a "new era" had dawned in the United States due to mass production and rising money wages. The difficulty of determining what was a reasonable basis for capitalising the yield of securities made it possible for securities to sell at 30 to 40 years' purchase, or even more, without upsetting public opinion, and they did, in fact, sell at such values. With such glittering chances of stock appreciation before their eyes, it is not surprising that it began to be more and more difficult to float international loans in New York or to sell bonds to American investors, nor that the prices of already existing bond issues should decline. To the

* See Federal Reserve Bulletin, January, 1930—p. 2.

† Mr. Loveday's figures show that the ratio of Gold Reserves to notes and sight liabilities of Central Banks and demand deposits of commercial banks amounted (in Europe) to 14.0%, 13.2% and 15.2% respectively in 1913, 1927 and 1928. Memorandum on p. 103 of First Interim Report of the Gold Delegation of the Financial Committee of the League of Nations.

‡ Cf. "Planning and Control of Public Works" compiled by the National Bureau of Economic Research in New York.

bullish bond market of 1924-27 had succeeded the bullish stock market of 1928-29:

160. From the very beginning of the more spectacular stage of the boom the Federal Reserve Authorities watched the situation with misgiving. By three successive stages in 1928, the New York Reserve rate was raised from $3\frac{1}{2}$ per cent. to which figure it had been reduced in August, 1927, to 5 per cent. in July, 1928, and, at the same time, in an effort to get control of the market, securities held by the Reserve System were sold upon a large scale, whilst the volume of open market acceptances had fallen to a bare minimum of \$75 millions by July, 1929. These measures proved sufficient to prevent the demand for Reserve Bank credit from expanding by more than the amount required to offset gold movements but could not cope with other elements in the situation. As the Annual Report of the Federal Reserve Board for 1929 remarks, "The problem was to find suitable means by which the growing volume of security credit could be brought under orderly restraint without occasioning avoidable pressure on commercial credit and business. With the system portfolio of Government Securities practically exhausted by the sales made in the first half of the year 1928, the main reliance in a further firming of money conditions must have been further marking up of Federal reserve discount rates, unless some other expedient could be brought to bear in the situation."

161. The Reserve Board being unwilling to permit the Reserve Banks to raise the discount rate still further, the Reserve System tried to check the rising flood of speculation by moral suasion and by bringing pressure to bear upon the New York member banks, hoping thereby to cut off the supply of call-loan money to the Stock Exchange at the source. But though the supply of call-money from the New York Banks was successfully cut off, the total volume of call-money continued to rise. The effect was to raise the level of call rates to a figure which made investment in such funds highly attractive, and there was thus drawn into the vortex of American speculation a mass of short-money, not only from non-banking agencies in the United States, but from European countries as well, though as regards European funds the bulk came from deposits previously made in the United States. America exerted a double pull on the European monetary and financial situation. Capital was placed in American securities and contributed to their rise; the rise in price stimulated further speculation and demanded further amounts of call-money; the call rate rose and this, together with rises in other associated rates attracted further European money to the United States. But, more important, the rise of call-rates to highly attractive levels impeded investment by all those who thought the situation essentially unstable. By investing in call-money they kept their position liquid, and at the same time earned upon their funds at least as much as, if not more than, they would have obtained upon foreign investments, without any

risk at all. A further deterrent to foreign investment had thus arisen. The increase in the gold stock of the United States indicated the pressure on European and other money markets. Between June 23rd, 1928, and January 11th, 1929, the gold stock rose by 7 millions of dollars; between that date and October 25th, 1929, it increased by a further 282 millions. A general rise in European bank rates followed the gold drain to the United States, and was accompanied by a general stiffening up of open-market rates in the European money markets. Finally at the beginning of August, 1929, the New York bank rate was itself raised to six per cent. By that time the peak of production had already passed, and the business conditions which provided the justification for the boom were definitely at an end.

162. The effort to stop the boom in the United States, and the European attempt to resist the redistribution of gold, which followed upon the flow of funds to the United States, led everywhere to a policy of dear money, almost at the moment when economic conditions were becoming ripe for a policy of cheaper money. For the index of industrial production ceased to expand in the United States after June, 1929, when the Reserve Board's index reached a maximum (1923-25 = 100) of 126 (seasonal variations being eliminated). Moreover, by the middle of 1929 the construction boom in the United States had passed its peak.

163. Upon the influence of boom conditions and monetary policy in the United States on the working of the gold standard were superimposed the effects of French monetary policy. The stabilisation of the franc, though it had taken place at a rate much above the lowest to which the franc had fallen, had nevertheless left the French price level considerably below that of the outside world. Further, the period of stabilisation involved in France, as it had previously done in the case of Austria and Germany, a readjustment of the per capita holding of currency so as to bring the amount into line with normal needs. Thus, a stabilisation boom combined with an increased per capita demand for currency to swell the aggregate demand for francs which could only be supplied by the Bank of France. This shortage of currency was accentuated by the abnormally high figures of the French Treasury balances. The note circulation did in fact rise considerably. In 1927 the average yearly circulation had been 53.5 milliards. In the next three years the circulation rose (half-yearly averages) as follows:—59, 61.2, 63.1, 65.9, 70.4, and 73.8 milliards, the amount in the autumn of 1930 being affected by the discredit attaching to certain banking institutions, which led to a marked hoarding of currency. The importance of these developments from the standpoint of the international gold standard was that they involved an enormous inflow of gold into France.

164. These flows were rendered necessary primarily by the provisions of the law by which the Bank of France is governed. Preceding and during the period of *de facto* stabilisation a special Act had permitted the Bank of France to buy foreign exchange and to issue notes against such purchases. (Law of 7th August, 1926.) So long as the influx of French balances and the sale to the Bank of foreign assets could be carried out through a transfer of foreign exchange, no positive pressure was brought to bear on foreign money markets, though they continued to run the risk that gold might ultimately be taken. But the transition from *de facto* to *de jure* stabilisation was accomplished by means of a law (June, 1928) which did not incorporate any provision for making permanent the right to issue notes against foreign assets; on the contrary, the law of August, 1926, was repealed, and the resulting legal position of the Bank of France in regard to the purchase of foreign exchange has remained obscure. Moreover, the new law did not give the Bank power to buy even French Government securities in the open market, and thus to satisfy the demand for currency by purchases giving banks and holders of securities additional deposits at the Bank which they could take out in notes if they desired. The Bank of France was thus practically deprived of two important instruments of modern central banking technique—the right to issue currency not only against gold, but also against the equivalent of gold, and the right to increase the volume of credit and currency by operations in securities initiated by itself. These changes in the French situation coincided with that change in the American situation—the end of the period of cheap money in the United States—to which we have already referred. Currency was drawn in the first instance from the commercial banks leading to a reduction of their cash balances. In so far as the banks possessed assets, i.e., bills of exchange, which the Bank of France was prepared to rediscount, and to the extent that they were prepared to part with these bills, a replenishment of cash balances became possible. In so far as bills were not available, or, alternatively, to the extent that the banks did not desire to part with them, this method of meeting the situation failed. It was possible to satisfy the demand in another way, however. The banks could sell their foreign balances for francs, thus appreciating francs and bringing a flow of gold to France. The existence of these balances was due either to the original flight from the franc or to their replenishment owing to the failure to invest in the purchase of foreign securities the credit balance accruing to France on the current balance of indebtedness. Very great quantities of gold did, in fact, flow in. The net changes of the significant items are as follows :—*

* These figures are taken from a paper on French Monetary Policy read by Mr. R. G. Hawtrey before the Manchester Statistical Society in January, 1931.

*Changes between June 25th, 1928, and December 26th, 1930.**(Millions of francs.)*

Discounts and Advances	+6,467	Notes	+17,664
Gold	+24,643	Private Deposits	+5,954
Foreign Exchange	-382	Public Deposits	+5,611
	<hr/>		<hr/>
	+30,728		+29,229
	<hr/>		<hr/>

165. For a time, between June and December, 1928, the Bank allowed its foreign exchange holdings to increase to a total of 32,641 millions of francs. Thereupon up to May, 1929, exchange holdings fell by 6,132 millions and gold holdings increased by 4,485 millions and these changes must be presumed to reflect the deliberate intention of the Bank. But thereafter the Bank maintained a "passive" attitude—its holdings of foreign exchange hardly varied, but it allowed gold to reach it freely. Bank rate was indeed lowered to $3\frac{1}{2}$ per cent. in February, 1928, and to 3 per cent. in the same month a year later. But this was a situation which a lower bank rate could do little to correct. Before the Wall Street crash something could have been done to stimulate foreign investment and thus to turn the tide of gold away from France. But the universal depression thereafter was not a propitious moment at which to begin, and of the 25 milliards of gold acquired in these thirty months, over $14\frac{1}{2}$ milliards were acquired between September, 1929, and December, 1930, i.e. during the period of depression.

166. The burden of these gold movements was thrown upon two markets, London and New York, the position of which, of course, differed very much. Whilst in the calendar year 1929 gold exports from Great Britain to France amounted to £33 millions and in 1930 to £55.2 millions, the exports to France from the U.S.A. amounted during the same period to £28 millions—or less than one-half of those from this country. The period of heavy gold exports to France from America had taken place earlier; from May, 1927, to June, 1928, France had taken some £47 millions. Nor was the gold drain to France the only significant flow of gold from Great Britain—Germany took £18.4 millions in 1929 and £16.2 millions in 1930, whilst a heavy export of £7.9 millions took place to the United States in 1929. The pressure on the London money market is indicated by the average yearly stock of gold coin and bullion held by the Bank of England. This rose from £148.6 millions in 1926 to £150.1 millions in 1927, rose again to £162.6 millions in 1928, to fall sharply to £146.9 millions in 1929. And though in 1930 the average rose again to £155.1 millions, the explanation is only partly satisfactory since the gold inflow in that year was fed by "distress shipments" from Spain, Argentina,

Brazil and Australia which reflected the economic malaise of these areas. The pressure on the Bank is marked by the fact that, whilst in 1928 and 1929 of the bullion sold in the London market about one half was bought by the Bank, in 1930, of an amount of £43.91 millions sold, the Bank was able to buy only £1.41 millions.

167. The important issue from the standpoint of the working of the gold standard in this country is the reaction of Bank of England policy to the events we have outlined. Bank rate had been reduced to $4\frac{1}{2}$ per cent. in April, 1927, and remained unchanged till February, 1929, when it was raised to $5\frac{1}{2}$ per cent., the average gold stock having fallen from a maximum of £173 millions for the month of September, 1928, to £150.2 millions in February, 1929. Bank rate was not again raised until September 26th, 1929, when it went up another one per cent., the Bank having lost gold steadily after July, so that the average monthly figure for the gold stock stood at only £130.9 millions in October. If the figures of the Banking Department are studied for the two critical years under review, it will be found that the range of variation of the Bankers' Deposits was less than the variation in the Reserve. While there was some reduction in the volume of Bankers' Deposits, part of the fluctuations in the Reserve was offset by movements in the Securities, and this applies to an even greater extent to the quarterly movement than it does to the fluctuations over the two years taken in their entirety:—

	<i>Bankers' Deposits.</i>		<i>Reserve of Notes and Coin in Banking Department.</i>	
	(£ mills.)	Increase (+) or Decrease (—) (£ mills.)	(£ mills.)	Increase (+) or Decrease (—) (£ mills.)
1928 1st Quarter ...	66.9	—	41.2	—
2nd „ ...	62.9	—4.0	47.5	+6.3
3rd „ ...	68.6	+5.7	59.1	+11.6
4th „ ...	64.5	—4.1	46.6	—12.5
1929 1st „ ...	64.0	—0.5	54.3	+7.7
2nd „ ...	62.1	—1.9	58.7	+4.4
3rd „ ...	63.9	+1.8	35.4	—23.3
4th „ ...	61.5	—2.4	32.8	—2.6
	—	—5.4	—	—8.4

168. In the critical third quarter of 1929, whilst the Reserve of the Banking Department fell by over £23 millions, the Bankers' Deposits actually increased by nearly £2 millions. The gold movements were thus not allowed to affect the basis of credit at that

time, though over the period as a whole the loss of gold was allowed to reduce the credit basis to some extent. Stated positively, Bank policy in so far as it made use of the weapons of open market policy and of bank rate consisted, it would appear, in preventing the *full* rigour of the international gold movements from affecting the volume of credit except in so far as it might be directly influenced by rising bank rates : and the rise in bank rates to a really deterrent level was long postponed.

169. But it must not be overlooked that, throughout the whole period since the return to the gold standard, the economic structure of this country has been exposed to quite exceptional strain, and that business opinion has been in consequence exceptionally sensitive to movements in bank rate, with the result that a level of bank rate not in itself highly deterrent to enterprise so far as its influence upon the profitableness of business is concerned may nevertheless have had psychological repercussions out of all proportion to the absolute magnitude in the movements of the rate. Moreover, in estimating the net influence of Bank of England policy in recent years, and especially before the American collapse in the autumn of 1929, allowance has to be made for the circumstance that the Bank has at times brought its influence to bear in a manner, which, as in the instances of unofficial embargoes on the flotation of new capital issues, is incapable of measurement in quantitative terms, but which, nevertheless, has exercised, at particular moments, a considerable influence upon the movements of business.

170. Since 1925, Bank of England policy has had to adjust itself to four major episodes : the return to gold itself, the inauguration of a cheap money policy in the United States in 1927, the stock-market boom, and the French gold drain in 1928-29. The view has been expressed that on occasion throughout these years, the Bank, by pursuing a less restrictive or more expansionist policy might have induced a similar policy elsewhere. But in the early days of the return to the gold standard a Central Bank inheriting a certain body of experience, and faced in any case with relatively difficult and novel problems would naturally hesitate before inaugurating a policy the success of which was doubtful and the failure of which would be attended with grave results. In fact, the Bank attempted at this early stage, so far as possible, to stabilise the volume of credit which it placed at the disposal of the banking system, whilst keeping the level of rates sufficiently above those in other centres to ensure the retention of foreign balances here.

171. During the period of cheap money in the United States, which lasted from August, 1927, to February, 1928, the Bank maintained its rate unchanged at $4\frac{1}{2}$ per cent., whilst its gold stock and Reserve in the Banking Department increased, accompanied by a decline in the Securities, deposits remaining substantially unchanged. In view of the fact that American monetary policy

was intended, *inter alia*, to relieve the European situation, it remains an open question whether the Bank might not, at that time, have pursued a somewhat more venturesome policy without running any overwhelming risks. In any case, by the end of 1928 the Bank had again lost a substantial part of the gold it had acquired in the second and third quarters of the year.

172. During 1929 the Central Banks of the world were faced by a combination of circumstances of a most abnormal character. In so far as that situation, reviewed in the light of history, induced drains of gold either of a temporary character (the American boom) or of a kind not amenable to the usual instrument of banking policy (the French inflow), requiring therefore a policy of acquiescence rather than of active opposition, it can be said that Bank of England policy was of the kind appropriate to the problems presented by the unfolding phenomena of the time.

173. If the events of the last five years are passed in review with the object of determining what lessons are to be drawn from them to serve as guides to future action and policy, it is necessary to distinguish between the incidents which are capable of recurrence, and those which may fairly be deemed to be of a purely passing and evanescent character, however disturbing they may have been at the moment of their actual occurrence. The world is not likely to have again to experience the simultaneous pressure on the monetary machine of an American stock exchange boom of such exceptional dimensions and a drain of gold for restocking purposes of quite extraordinary magnitude. This unique conjunction of events which gave to the years 1928-9 their peculiar impress is not likely to recur. After all allowances for these unusual or novel manifestations of the world order have been made, it is clear, nevertheless, that the working of the international gold standard requires, in the modern world, a realisation that the forces making for disequilibrium are very powerful and that any mechanical application of the purely empirical rules derived from pre-war experience could easily lead to very grave and unsuspected results.

174. Among the causes which may make for disequilibrium two stand out most prominently. In the first place, the working of the gold standard may from time to time be seriously affected by the recurrence of boom conditions in American economic and financial conditions. In the second place, the gold standard is liable to be affected by the breakdown, after a period of expansion, of the process of international investment. The immense growth of the financial and economic power of the United States has altered the scale, if not the terms, of the problem of American-European economic relations, and thrown upon the European Central Banks—in the absence of any definite guarantee that the Federal Reserve Banks will be permitted by public opinion to co-operate at all times whole-heartedly with other Central Banks—a task of great

difficulty, which can only be solved by common understanding and action. The vast technical changes now manifesting themselves in the sphere of agricultural production are only one among a number of features which give to the flow of international funds a new social and political significance. The working of the gold standard must be adjusted to these striking changes in world conditions, and the task of adjustment must be entrusted to the Central Banks.

CHAPTER IX.—THE COURSE OF INTERNATIONAL INVESTMENT.

I.—THE PROCESS OF INTERNATIONAL INVESTMENT.

175. The substantial variations in the volume of international investment in recent years and especially the abrupt reduction in the last two years, have contributed largely to the troubles which have overtaken both the raw material producing areas of the world, such as Australia and Latin America, and (to a smaller extent) those Central and East European countries which, in consequence of the war and of the post-war inflation, have become impoverished and unable to provide for themselves the capital of which they stand in need.

176. The supply of capital to overseas areas is for some countries an indispensable element in their development and, in so far as it is itself subject to irregularity, imports irregularity also into their economic life. For it is largely through capital movements that these overseas areas are linked up with the ebb and flow of economic activity in other, and particularly the capital exporting, countries of the world. The processes by which these fluctuations are transmitted are briefly :—

(a) The borrowing countries use a part of the capital borrowed for the purchase of constructional goods from the industrial countries, and the purchasing power thus circulated in the industries producing those goods provides at least some part of the market for the raw materials of the borrowing countries.

(b) In part the capital borrowed is used in the employment of labour in constructing railways or other plant, and is thus expended in the borrowing country itself. The borrowing country has acquired, through the loans granted to it, purchasing power in the lending country which it wants to employ locally. There is thus a demand for remittances from the lending country to the borrowing country and the exchange moves in favour of the borrowing country, which in these circumstances can either allow credit to expand at once or

import gold to form a basis for expansion. In either case the local demand increases and imports are stimulated. The increase in employment in the borrowing country caused by the expenditure of the loan moneys provides the means of absorbing these additional imports.

(c) Moreover, the adjustment of interest payments on capital previously borrowed frequently requires that there should be a steady stream of loan-moneys flowing towards these areas, so that the sums borrowed can be used to prevent a weakening of the exchange rate if, for any reason, it is impossible to meet interest payments by means of an export of local produce. Ultimately it is to be expected that interest on loans should be met out of the increased production made possible by the loans. If the increased production takes the form of exportable raw materials, the drafts drawn against the exports furnish the means of meeting the interest payments; if the increased production is in the form of general development (roads, etc.) the interest should be provided by taxation, which would reduce local spending power and thus diminish imports which would otherwise have been consumed locally. But this process of transfer works with great friction because of the fluctuating character of all raw material production and the lack of diversity in the production of raw material countries. A bad harvest, or series of bad harvests, plays havoc with the mechanism. In the absence of fresh capital loans, the flotation of which depends in the main upon world credit conditions, the gold or foreign exchange reserves of the local banking system must be used. If these sink to a point which engenders lack of confidence in the stability of the local currency, or if a fear that they will be exhausted causes a flight from the local currency, there may be no alternative except a departure for the time being from the gold standard.

177. The recent history of the South American Republics well illustrates the practical aspects of the matter. During the years 1924 to 1929 the United States and this country, respectively, made loans to South America approximating \$1,200,000,000 and £50,000,000. Take, for example, the small Republic of Colombia which received over those years \$170,000,000. There was a great boom. Competitive railway building and other public works sent up wages by leaps and bounds; imports vastly increased; food was imported where before it had been produced locally. When the golden stream ceased there was a collapse. Imports ceased and Colombia thus added its small quota to depression in the industrial countries. Prices fell precipitously and Colombia is only now recovering gradually from its previous excess.

178. This example can be multiplied in Brazil, Peru, Chile and even perhaps the Argentine, and certainly in Australia. The United

States made loans to South America on an undesirable scale; Great Britain with equally good intentions had already shown the way in the case of Australia.

179. The economic position of Germany again has been much influenced by the ebb and flow in the tide of international investment. Germany's working capital, much reduced by the war, was enormously diminished by the subsequent vast inflation. Her needs in this direction, her Reparations burden, and the necessity to build up a gold reserve, all compelled her to borrow very largely. In addition to large amounts of long-dated capital taken up by States, municipalities and industries, estimated in the Final Report of the Agent-General for Reparation Payments to amount to £335 million for the period 1925 to the end of April, 1930, German banks and other borrowers have taken up a very great amount of short-dated capital. In the period following the stabilisation of the mark, and especially during the boom in the American bond market, the imports of capital into Germany resulted in checking exports, in raising the standards of expenditure by the public authorities, and in encouraging a generally higher standard of life among the population. The dangers of over-borrowing were regarded so seriously by the authorities of the Reichsbank as to lead to an official control of capital loans raised abroad for purposes not regarded as increasing German productivity, and short-period loans, in particular, were regarded with disfavour. Nevertheless, the net movement of capital inwards was on such a scale as to affect profoundly the rhythm of German economic life; and the partial cessation of the flow, as well as the uncertainty whether capital could be borrowed or not, which has been the result of events in America and elsewhere since 1929, has had the result of profoundly modifying the economic, and through it, the political situation in Germany. It has become steadily clearer that Germany's heavy debtor position has placed her at the mercy of her creditors; if she cannot continue to borrow she must, by any reduction in costs necessary, increase her exports and reduce her imports, thus affecting the equilibrium of other countries trading with her and her customers.

180. It is unfortunate that, in practice, a cessation of loans to raw material producing countries generally coincides with a period of lower prices for their products, and, conversely, large capital imports accompany higher raw material prices. This tendency is the natural outcome of the preferences of investors, who are much more likely to lend to a country when it is prosperous and enjoying prices for its crops which are high relatively to the general level of prices. Thus the alternations of prosperity and depression are likely to be particularly severe in those countries, for the national

income is in the one case inflated both by large sales at high prices and by the effects of the expenditure of loan proceeds, and in the other case deflated by the absence of loan expenditure and by small sales at low prices. Nor do borrowing countries—at any rate the raw material producing areas—possess means which might help to stabilise their balance of payments in time of bad harvests. For they do not, as a rule, draw large payments for services—such as shipping, insurance and merchant transactions—but on the contrary have to pay for such transactions carried out on their behalf. Generally also their foreign investments are small.

181. In certain cases, moreover, particularly in the case of Germany, the cessation of foreign lending has been accompanied by an increase in the export of capital, short or long, by her own nationals, the combined effect of these two movements being, of course, greatly to accentuate the difficulties of the local situation. The causes of this double pressure are clear: a lack of confidence in the economic and political outlook of the area concerned deters foreign investment and encourages a flight from the local money market. In so far as the direct effect of a cessation of capital imports and of an increase of capital exports is to increase the strain on the foreign exchanges, the two movements work in the same direction and accentuate one another.

182. Statistics relating to the movements of international capital supplies are notoriously difficult to interpret. The volume of *new* capital issues (issues for conversion or redemption being excluded) throw no light upon the movements of private investments and may be in part or in whole offset by the movements inwards of short-term or long-term funds for investment purposes. Nevertheless, the figures for public flotations on the one hand, and the figure for the excess of credit over debit items in the balance of indebtedness, i.e., the net balance on income transactions, throw some light upon the fluctuations in the capital flow, although they may not be an accurate guide to the volume of capital investment.* The tendency of the British and the American figures is not to compensate each other, but to reinforce one another; rising together (so far as issues are concerned) sharply between 1925 and 1928, and falling in 1929. Thus, between 1928 and 1929, the net capital movements outwards from the United States fell by 561 million dollars, or £115 millions, while the total overseas issues on the London market declined from £143 millions to £94 millions, a total decline of £164 millions, a figure not far short of one-half of the absolute amount of New York and London combined in the year 1928.

* See Appendix IV.

II.—INTERNATIONAL INVESTMENT AND INTERNATIONAL DISEQUILIBRIUM.

183. Apart from new loans and purchases of securities in other countries, a creditor nation's claims on the rest of the world show, each year, a net surplus. A debtor country on the other hand, which requires and borrows money from other countries for capital development, possesses current claims on the rest of the world which are normally less than its liabilities. If, for the time being, it cannot borrow, it must try to meet the deficiency, so far as it can, by the export of gold. It is roughly true, therefore, that, if creditor nations do not lend their surplus, that surplus, so long as all parties remain on the gold standard, can only be employed in increasing the gold reserves of the creditor and diminishing the gold reserves of the debtor nations, with the ultimate result of the former finally having all the gold and the latter none.

184. Since no country, not even a young and developing one, can borrow incessantly and largely without incurring an external debt greater than it can stand, debtor countries which wish to be able to maintain their surplus gold holdings must not depart too far from a balance between debts to and claims on the rest of the world on income account, while creditor countries must, unless they are ready to upset the economic conditions, first of the debtor countries and then of themselves, be prepared to lend back their surplus instead of taking it in gold. In other words, all must perform their part towards maintaining a reasonable equilibrium.

185. Formerly, it was assumed that the efflux and influx of gold itself produced a new equilibrium by altering the level of prices in the lending and receiving countries respectively and thus modifying, through an alteration in exports and imports and through the short money market, the debtor position of the first and the creditor position of the second. Gold standard countries were indeed supposed to meet each other half way, each altering its conditions sufficiently to produce the desired equilibrium. This result might be soon reached in normal and quiet times between highly developed countries, able rapidly to adjust their short-money position and their balance of payments, and willing to let the increase or decrease of gold if need be freely modify their economic conditions. But in actual fact to-day the position of debtor countries is apt to deteriorate rather than improve as a result of their having to export gold. For it is usually beyond their power to adjust their balance of payments so rapidly and completely as to permit a complete cessation of borrowing; yet, in so far as they export gold, their credit as borrowers suffers. Thus, having lost their gold and not being able to borrow, they are forced off the gold standard. And creditor countries, on the other hand, when they have accumulated more than their fair share of gold, far beyond their legal require-

ments; fearing to provoke an inflation by letting the new gold produce a rise in prices, try, in effect, to make themselves insensitive to further imports. Thus, when equilibrium is profoundly upset between creditor and debtor nations, the whole world suffers. The adjustments to be made are greater than can be accomplished by a movement of short-money funds or by a small alteration in prices. The debtor countries suffer a serious deflationary crisis and some of them, probably failing to meet their problems by drastic measures, may be forced off the gold standard; the creditor countries will be affected both by the depression in the debtor countries and by the influx of large quantities of gold. Here is, perhaps, the major part of the immediate explanation of the collapse of international prices which we describe in the next Chapter.

CHAPTER X.—THE FALL OF INTERNATIONAL PRICES AND ITS CONSEQUENCES.

186. The general effect of the world depression upon the price level of commodities at wholesale cannot be more strikingly summed up than by saying that during the course of the year 1930, the Board of Trade index number (base 1924=100) fell by 17 per cent.; that the Economist index number fell between February, 1930, and February, 1931, from 84.2 to 66.5 (base 1927=100) or by over 21 per cent.; that some commodities suffered a fall of price within the year of between 40 and 50 per cent. and that, by February, 1931, all the main groups of commodities, with one exception, as measured by the Economist index number (1913=100), were below their pre-war price, as the following table shows:—

(Average 1913=100)

Date.	Cereals and Meat.	Other Foods.	Textiles.	Min- erals.	Miscell- aneous.	Com- plete Index.
Average 1924 ...	159.9	169.9	210.6	145.2	131.5	159.3
" 1928 ...	145.0	149.4	161.7	111.9	119.8	135.1
" 1929 ...	135.6	136.8	141.9	116.2	112.7	127.2
" 1930 ...	113.4	122.9	99.1	101.6	101.5	106.8
End Feb.: 1930 ...	119.5	132.2	115.1	110.1	108.4	115.9
" Jan.: 1931 ...	94.3	110.8	75.8	91.5	90.4	91.3
" Feb.: 1931 ...	92.9	108.4	78.0	93.5	90.5	91.6

Within the period February, 1930 - February, 1931, the group Cereals and Meat fell by 22 per cent., the group Other Foods by 18 per cent., Textiles by as much as 32 per cent., Minerals by 15 per cent., and Miscellaneous by 16½ per cent.

187. When wholesale price movements are compared with movements in the cost of living index and with index numbers of average weekly wages, it is at once apparent that the fall in the former has been much greater than the fall in the other series:—

(Base 1924 = 100 in all cases).

	Wholesale Prices (Board of Trade).		Cost of Living Index (M/L).	Index No. of Average Weekly Wages.	Industrial Production (Board of Trade).
	All articles.	Total non-food.			
1924 1st Quarter...	99.9	100.5	101	100	100
2nd " ...	98.5	100.3	97		
3rd " ...	99.3	99.1	99		
4th " ...	102.3	100.1	103		
1928 1st " ...	84.6	81.1	94	100.2	109.3
2nd " ...	86.1	81.4	94	100.0	103.6
3rd " ...	83.8	80.5	94	99.7	100.2
4th " ...	83.1	79.9	96	99.5	108.4
1929 1st " ...	83.6	80.5	93	99.5	110.6
2nd " ...	82.2	79.7	92	99.5	112.0
3rd " ...	82.1	79.3	94	99.3	110.7
4th " ...	80.7	78.1	95	99.0	114.0
1930 1st " ...	76.9	74.8	92	98.8	111.0
2nd " ...	73.4	71.5	88	98.3	103.1
3rd " ...	70.7	68.1	89	98.3	99.5
4th " ...	67.0	64.5	89	98.3	99.0
1931 1st " ...	64.0	62.2	85	98.0	95.4

188. The fall in the wholesale price index number is, of course, in no way a phenomenon confined to this country. Indeed, since the articles comprised within the scope of a wholesale index number are largely internationally-traded commodities, the rate of fall of their prices must be much the same in all countries, allowance being made for differences of qualities and tariffs and the movements of freight rates. We publish in Appendix V a set of wholesale index numbers for various countries from which it will be seen that between January and December, 1930, the price fall in Japan has been 20 per cent.; in Canada 19 per cent.; in the Netherlands 18 per cent.; in the United States and Italy 16 per cent.; in France approximately 14 per cent.; and in Germany 11 per cent.

189. The same feature of a much sharper fall in the wholesale level of prices than in the level of the cost of living, which is characteristic of the position in Great Britain, is to be noted in other countries. Thus the ratio $\frac{\text{Cost of Living Index}}{\text{Wholesale Index}}$ stood at 126 in January, 1930, and at 142 in December; in Germany, for the same months, at 115 and 120; in France (1st Quarter 1930, compared with last Quarter) at 101 and 120. Thus, all over the world

the wholesale price index has been falling abruptly and the cost of living has nowhere completely adjusted itself to the fall in the level of wholesale prices.

Consequences of the Fall in Prices.

190. The consequences which follow from a fall in prices of the severe dimensions recently experienced are complex and react with unequal incidence upon different types of income. They may be briefly summarised as follows :—

(i) All incomes fixed in terms of money, such as interest on the National Debt, debentures and other fixed-interest securities, remain unaltered. Thus incomes derived from those sources are able to purchase an increased proportion of the national output at the lower price level now prevailing. On the other hand, such incomes will, of course, lose this advantage if the fall of prices proves to be temporary, and meanwhile the rate of interest on all new lending should fall.

(ii) Many other incomes, which are not contractual in the same way as is interest on the National Debt, are fixed by custom or by statute. In the latter category fall, for instance, many classes of pensions and unemployment relief. Unless and until measures are taken by Parliament to alter these charges, the recipients benefit in the same way as do holders of contractual incomes.

(iii) The proportion of the national output which can be purchased by these classes of recipients being increased, the amount left for distribution between the remaining sections of the community is reduced, with the result that so long as salaries and wages are unchanged the final residue available for profits is inadequate.

(iv) The attempt to effect an adjustment sets in train a series of consequences making for acute trade depression and unemployment.

(v) In the sphere of international debts also a large fall of prices greatly increases the real burden falling upon the debtor nations.

191. It is apparent from this summary that a severe fall in prices upsets the entire balance of every kind of money settlement. It works to the advantage of those whose incomes are protected by contract or otherwise and to the disadvantage, either in the form of reduced incomes or of unemployment, of those who receive the residue of the national income. It brings with it the problem of reducing costs. For the entrepreneur, faced with a fall in the

price of his commodity and the money receipts he derives therefrom, must seek to reduce his money costs of production whether in the form of wages or otherwise.

192. Thus when prices fall the first person upon whom the impact falls is the business man (unless the fall is due to an increase in efficiency). Nothing occurs automatically to change his costs of production save in a minority of cases where wages are regulated by changes in the cost of living or by sliding scales based on selling prices, and even here, whatever reduction takes place necessarily lags behind the fall of prices in articles of international trade. The result is, in the first instance, a narrowing of the margin between prices and costs, that is to say, a diminution of profit. The burden of reducing costs is thrown on business men to effect as best they can.

193. Some part of their costs, e.g., rates and taxes and interest charges, it is not in their power to diminish. As regards the rest, their first effort, naturally, is to increase efficiency. But an important increase may not be possible unless they have been failing to do their best previously. Moreover, it will not help them competitively unless they can increase their own efficiency faster than their rivals are increasing theirs. Next they will, no doubt, cut out various items of expense which were never justifiable on strictly business principles, but were due to kind-heartedness, old custom, and for the sake of the amenities of life. If this is not enough, there are various further measures which they can take gradually in greater or less degree. They will cut out some of their marginal and least profitable lines of business, which are not essential to the maintenance of their connections and their organisation—which will already have the effect of somewhat reducing employment. They will resist rises of salaries and wages, which otherwise they would have been inclined to grant. They will endeavour to adjust the conditions of labour so as to make it cost less without earnings being reduced. And finally they may be compelled to join issue with their men to seek a general reduction of wages.

194. But the pace at which these things will happen will tend to vary widely from industry to industry. Where fixed overhead costs are a small proportion of total costs, the employer will be brought much sooner to the point where he has to choose between closing down or seeking to lower wages. Moreover, such cases will largely coincide with the cases where labour costs are a large proportion of the whole, so that there is little room for reducing total costs except by reducing labour costs. On the other hand, there are also many industries where fixed overhead costs are large, so that it will be worth the employer's while to accept much less than a normal contribution towards interest, replacement, etc., before financial considerations will impel him to close down. Such a situation will preclude expansion or even the replacement of old

plant as it wears out, so that it may spell a slow, long drawn-out ruin for the industry without the trouble being brought to a head by a sudden crisis. Between the extremes there are industries and firms at every intermediate position.

195. This procedure for adjusting incomes to upward changes in the value of money works well enough if the changes are gradual and if they are moderate relatively to the rate of technical progress. For the pressure put upon the business world by the declining margin between prices and costs will be limited in its effect to putting a brake for the time being on the rate of expansion and on the upward movement of incomes corresponding to the increased efficiency due to technical progress. It may even be beneficial by enforcing those necessary minor economies which get forgotten in a period of wide margins between prices and costs, and by regulating the relative rates of progress as between different industries. Moreover, the higgling of the labour market between employers and trade unions may be healthy and of a tendency to produce a proper equilibrium between the advantages offered by different industries, without threatening serious loss or serious hardship to anyone.

196. But if the change in the value of money is large and rapid the result is chaotic. Extreme hardship and injustice will prevail, and great loss to the income and wealth and productive power of the whole community. For the individual members of the community can be ranged in a long line, according to the degree in which their incomes are susceptible to pressure, beginning with those whose incomes are protected by contract, such as the recipients of interest on the national debt, through workers in sheltered industries protected by powerful unions, to workers in unsheltered industries, where labour is a large part of the cost, as in the case of coal. The process of bringing about a reduction of incomes will be protracted and unequal in its incidence, and years may pass before the injustices as between different sets of individuals will have worked themselves out.

197. Thus, although a severe fall in prices, if permanent, in itself necessitates a reduction of costs if business is to continue on a profitable basis, the process of effecting adjustment involves great friction. That it has not been made in this country we show elsewhere. The result is that business, being unprofitable, is depressed, output is reduced and unemployment results. We think that the recent increase in unemployment in every part of the world, accompanied by a decline in production, can in the main be attributed to the fall in the level of prices, unaccompanied by a proportionate reduction of money costs, however brought about.

The Relation of Falling Prices to Investment.

198. In the modern world, where a willingness to assume risk is an essential element of economic life, the process of investment is

seriously affected by the reduction of profits due to a disparity between prices and costs of production. An inevitable accompaniment of sharply falling profits is a decline in the yield of ordinary share capital, and therefore a fall in its market price, as has indeed taken place. Under these conditions it becomes increasingly difficult to finance new enterprise by the issue of ordinary shares. And yet in a period of falling prices it may in many cases be imprudent to finance enterprise by means of fixed interest-bearing securities, for the further prices fall, the more onerous the capital taken up on fixed terms of interest becomes. It has for two generations been a subject for discussion and dispute among economists as to whether periods of rising or periods of falling prices are more fruitful of technological improvement. The truth would appear to be that whilst periods of falling prices afford the greater inducement to cut costs, they do not necessarily afford the greater opportunity to do so, if the capital necessary can only be obtained on terms which will increase the aggregate risks which the entrepreneur must run.

199. The deterrent effect upon the process of introducing improvements due to the uncertainties of the future may, it can be argued, be offset by the greater margin of saving available from recipients of fixed incomes and by the fact that they are obliged, because of the rise in the value of fixed-interest securities, which commonly occurs in periods of falling prices, to accept a lower yield in the shape of interest. It is through these falling yields, indeed, that the burden resting upon the entrepreneur may be reduced, though very gradually. And with an increased willingness on the part of the public to invest their money in long-dated securities, these results will be obtained and may be an indispensable part of the process of recovery. But, so long as the economic outlook is very uncertain, and the public are disinclined to venture their savings, the additional savings possible to certain classes when prices fall (even if the aggregate for all classes were the same, which is more than doubtful) may merely be hoarded for the time being. If the public choose to hold their savings in liquid form, this may hinder the process of re-equipping industry or lowering the yield of securities; and, in so far as this is the case, the process of industrial and economic recovery is held up. The reluctance to venture savings is, in fact, a marked feature of the present depression and as potent a cause prolonging and deepening it as is the reluctance of the entrepreneur, depressed by his heavy losses, to seek new loans for new construction or the extension of his enterprise.

The Effects upon Public Finance.

200. In the direction of public finance also, a large fall in prices produces serious reactions affecting the equilibrium of the National Budget by its operation both on the revenue and on the expenditure

of the State. We need only summarise briefly the directions in which pressure is felt :

(i) The revenue of the State tends to be affected unfavourably in all its branches. Business depression reduces the volume of profits (including dividends distributed) liable to Income Tax and Surtax; the valuation of estates liable to Estate Duties; the volume of transactions liable to Stamp duties; the yield of Customs and Excise duties by reason not only of a reduction in the volume of goods consumed but of a fall in values. Consequently, in so far as the State must meet charges fixed in terms of money, it must meet the situation by an increase in the level, or an extension of the field, of taxation.

(ii) At the same time, the circumstances of the time tend to swell expenditure in certain directions with a view to relieving the unemployment situation or providing for the unemployed.

(iii) A high proportion of State expenditure is contractual in the form of debt interest and can only be reduced by conversions, either voluntary or on maturity, in favourable circumstances. A further large block of expenditure is fixed in terms of money by Acts of Parliament (e.g. Pension Allowances of many kinds, contributions to Health and Unemployment Funds and other Social Services) and is not readily alterable when changes take place in the value of money.

201. Examined from the point of view of the total tax burden, the position is that nominal Imperial taxation fell between 1920/1 and 1929/30 from £22 per head to £14.8 while the burden of local taxation remained unchanged at £3.9 per head. Thus total taxation fell from £25.9 to £18.7 per head. But the change in prices in that period has meant that the commodity value has risen from about £18 to £20 (expressed in 1924 values on the basis of the cost of living index); a reduction of nearly one-third in the nominal value of the taxation imposed has yet left an increase in the real tax burden.

202. Whilst it is difficult to form an estimate of the contractual elements involved in the Budget in the shape of pensions and social services, there seems to be little doubt that, including debt interest, some 60 per cent. to 70 per cent. of the total ordinary expenditure (excluding self-balancing items) is of this nature. Thus with a falling price level, while revenue falls, a very large proportion of expenditure is more or less fixed in terms of money. There are some favourable influences to be set on the other side, such as the lower cost of the Floating Debt and the possibility of large-scale conversion operations. Nevertheless, it would appear as if a most important consideration for those in charge of the public revenue to bear in mind, so long as the future course of prices is uncertain, is the avoidance of any form of obligation involving a large addition to the contractual obligations of the State.

203. The budgetary problems referred to in the foregoing paragraphs are not, of course, peculiar to this country. The fact that the fall of prices is a world-wide phenomenon has meant a general increase in the burden of indebtedness. But the problem is particularly acute in this country in that the recent fall of prices was not preceded, as was the case in many other countries, by a period of intense inflation followed by devaluation of the currency and, consequently, the destruction to a greater or smaller extent of the original debt burden. Relief from the weight of internal indebtedness was obtained in this way over a large part of Continental Europe; most markedly in Germany, Austria and Hungary, but to a great extent also in France, Belgium and Italy. On the other hand it must not be overlooked that Great Britain is still on balance a great creditor nation on long-term account, so that the fall in the price level has increased the commodity value of the whole of her external assets in the shape of sterling investments; whilst for Germany, as a debtor both on long-term and short-term account, the price fall has resulted in a serious addition to the burden of external indebtedness, both Government and industrial. And what is true of Germany is also true of those overseas countries which stand in the relation of debtors to this country. Indeed, as these areas produce commodities which have felt the price decline most heavily, their economic situation has deteriorated the more seriously; since their national income is more closely dependent on the sale of a relatively restricted number of commodities. Areas like Brazil, Argentina, Malaya and Australia, dependent upon sales of coffee, wheat and maize, tin and rubber, wool and hides and wheat, have felt the shock of falling prices the most. The result has been that their budgetary position has become very difficult; their exchange position no less so. The efforts to maintain faith with their creditors have imperilled the stability of their Governments, and this in its turn, has made it more difficult for them to raise fresh loans in the international capital market—loans which are vital to their further economic development and the realisation of their political stability.

204. In many respects it is the social rather than the directly economic consequences of falling prices which are most serious. For price changes raise delicate issues of equity between different classes of the community, the resolution of which presents grave difficulties. The payments received by the factors of production ultimately constitute income, and income is received by men and women with standards of social justice, with ideas of settled expectation and with a natural reluctance to make the necessary sacrifices. The tensions so set up are paralleled by the tension between creditor and debtor nations. Thus violent price changes (for what we have said applies *mutatis mutandis* to rising as well as to falling prices) initiate social as well as economic disturbances which leave no part of the national or international order unaffected. But we

feel that the significance of what has been taking place in recent months is not always fully grasped. A study of history would, we believe, confirm the opinion that it is in the changes in the level of prices, and in the consequential alteration in the position of debtors and creditors, entrepreneurs and workers, peasants and the tax gatherer, that the main secret of social trouble is to be found. Looked at from this point of view the events of the last decade are of the most extraordinary kind. A very violent depreciation of money was sufficient in the immediate post-war period to destroy over a large part of the continent of Europe all rational economic calculation and all orderly social and economic development. This violent movement was followed in turn by a period of relative stability in which material well-being progressed markedly. This phase has now been followed by a violent down-turn of prices the effects of which upon political and social stability have already been very great. The problems thus raised transcend in importance any others of our time and generation and we have regarded it as our main task to expound their significance and to bring forward suggestions for their solution.

CHAPTER XI.—THE INFLUENCE OF MONETARY POLICY ON THE PRICE LEVEL.

1. MONETARY AND NON-MONETARY FACTORS.

205. Many of our witnesses can be divided into two groups according to the way in which they answer the question whether the fall of prices is primarily due to monetary causes. But this difference of opinion may have appeared greater than it really is owing to a confusion as to just what is meant by the question.

206. Those who assert that the fall of prices is primarily due to monetary causes may mean by this that the fall is due to a failure of the monetary machine throughout the world to adjust itself to general economic perturbations. Those who deny the same proposition may mean that the changes and disturbances which are ultimately responsible for the fall of prices are non-monetary in origin and character. But there is nothing necessarily inconsistent between these two statements, and both of them may be true. Or it may be that those who emphasise monetary causes do so because they believe that the monetary machine *could* have adjusted itself to the non-monetary changes and so have avoided the fall of prices, if this machine had been operated with greater knowledge and wisdom, whilst those who emphasise non-monetary causes may do so because they believe

that it has not been within the power of the monetary machine to offset the effect of non-monetary changes on prices, so that the fall of prices could only have been avoided, if at all, by bringing to bear on the non-monetary factors. Here there is indeed a difference of opinion, but it is one, probably, of degree and of practical judgment as to what is or is not feasible.

207. Obviously the general price level must be governed by the volume of purchasing power directed to the buying of current output relative to the volume of this output. Moreover the behaviour of the world's banking and monetary systems as a whole must have a considerable influence on the volume of such purchasing power. To this extent, at least, the general price level is rightly described as a monetary phenomenon; and the controversy turns on the degree to which in practice a monetary system can exert its influence to remove difficulties due to changes in the rate at which such purchasing power circulates or in the uses to which it is put.

208. On the other hand, it seems to us equally clear that the economic difficulties of the post-war decade are primarily due, not to any wanton misbehaviour on the part of the monetary factors themselves, but to unusually large and rapid changes on the part of what are rightly described as non-monetary phenomena, these non-monetary factors again themselves producing monetary changes. In particular, war and post-war non-monetary causes led to the great and unwanted flow of gold to the United States from which such vital consequences have ensued. For example, in the foregoing summary of events we have attributed great importance (i) to the unusual instability in the demand for capital resulting from the losses and interruptions consequent on the War, (ii) to the changes in the established relationships between debtor and creditor countries consequent on the War debts, (iii) to the rapidity of technical changes in manufacture and agriculture, (iv) to the shifting character of demand resulting in a want of balance between the demand and supply of services as against manufactured products, of new types of manufacture as against old, and of manufacture as a whole as against agriculture, (v) to the rigidity of wage-rates, (vi) to the growth of tariffs, (vii) to the embarrassments of Budgets, and (viii) to violent changes in speculative activity in New York and elsewhere.

209. Our view is, therefore, that the price level is the outcome of interaction between monetary and non-monetary factors, and that the recent world-wide fall of prices is best described as a monetary phenomenon which has occurred as the result of the monetary system failing to solve successfully a problem of unprecedented difficulty and complexity set it by a conjunction of highly intractable non-monetary phenomena. Whether the inter-

national monetary system *could* have solved its problem is a matter on which we should hesitate to express a dogmatic opinion. It is probable that the difficulty of our national problem was much increased by the relative over-valuation of the pound sterling and under-valuation of many other currencies. But the satisfactory handling of the international problem, even if it was theoretically practicable, might have required a degree of knowledge, experience and prescience which no one in fact possessed or could have been expected to possess.

210. It will be sufficient for our purpose, in putting forward our recommendations in Part II of this Report, to hold that it should be our object to *increase* the power to exercise deliberate control over the price level; that there is nothing inherently impracticable in this; that with the gradual growth of knowledge and experience, and particularly with the further development of suitable machinery for regular international co-operation, the possibilities of such deliberate control should steadily increase; and that we should forward these ends to the best of our powers by being ready to attempt the task and to gain experience by practice.

2. THE TASK OF THE MONETARY SYSTEM.

211. The task of the monetary system, as we see it, is, therefore, to balance, so far as it can, by changes in the quantity and terms of credit, the effect on the price level of certain fluctuating factors, which, whether we prefer to call them or their underlying causes monetary or non-monetary, are largely outside the *direct* control of the monetary system. The fluctuating factors in question are, principally, the three following:—

(i) The proportion of bank credit which is employed for financial purposes as distinct from the purposes of new current output;

(ii) The degree of preference felt by investors for the employment of their funds in more liquid or in less liquid forms;

(iii) The readiness of enterprise to embark on expansion of one kind or another, given the financial terms on which the necessary resources can be raised.

The greater the amount of bank credit which is being used for financial purposes, the greater the desire of investors to keep their funds liquid and the greater the reluctance of enterprise to move forward on given terms, correspondingly greater—generally speaking—will have to be the volume of bank credit and the easier the terms on which the banking system is ready to lend, in order to keep the price level from falling; and *vice versa* when it is a case of preventing a rise.

212. It is no doubt less difficult to check a boom than to stimulate activity during a slump; but the checking of a boom may well prevent the subsequent depression from being as deep as it would have been if the boom had been allowed to proceed unchecked. In certain extreme states of speculative excitement or of depression and general want of confidence, it may indeed be well-nigh impossible for the banking system to exercise sufficient restraint or to provide sufficient stimulus. But such states of excessive excitement or depression are generally reached as a result of the excitement or the depression having been allowed to feed on itself; and it does not follow that the banking system could not have prevented the aberration if it had acted soon enough and drastically enough. The fact that a motor car is not well-adapted for getting itself out of a ditch once it has fallen in does not prove that it is beyond the powers of good driving to keep it in the middle of the road.

213. We pass, therefore, to a brief consideration of the means at the disposal of the banking system for performing its task. It would take us much too far into a difficult and intricate subject if we were to attempt a full analysis of the causes operating on the price level. But some account of the way in which we conceive of the monetary system as exerting its influence is a necessary introduction to the recommendations which follow in Part II.

3. THE FUNCTIONS OF BANK RATE.

214. The methods by which a modern Central Bank controls the volume and terms of credit in its domestic monetary system consist, in the main, (i) in what are now known as "open market operations," that is to say the purchase or sale of assets in the market on the initiative of the Central Bank itself, and (ii) in varying the terms on which it will purchase assets on the initiative of the seller, which is conveniently summed up as "bank rate policy." The effects of the two methods are different in detail and in the rapidity of their influence on the various elements in the market rather than in essence. It will be sufficient for the purposes of this section if we discuss the general consequences of the tightening or relaxation of the volume and terms of credit, as the result of deliberate policy on the part of the Central Bank, under the general designation of "bank rate policy."

215. "Dear money" (and *mutatis mutandis* "cheap money") produces a long chain of consequences, some of which result quickly and some only in the long run. The most important are, in the order of their normal time of occurrence, the following:—

- (i) Dear money tends to diminish the net amount which a country lends abroad or to increase the amount which it borrows. Both short-term lending and long-term lending are

affected, though it is the former which feels a change soonest and most sensitively. Thus there is an immediate favourable effect on the country's balance of international payments and hence on its foreign exchanges and its gold reserves. This assumes that the change in bank rate is a change relatively to rates elsewhere and is not merely keeping pace with changes elsewhere.

(ii) Dear money tends to curtail enterprise at home and the volume of purchasing power which is put into circulation. Some part of the purchasing power which is thus curtailed would have been spent on imports or on home-produced goods which are now released for export. Thus dear money has a favourable effect on a country's "visible" balance of trade; which, again, has a favourable effect on the country's balance of international payments and hence on its foreign exchanges and on its gold reserves.

(iii) The curtailment of enterprise at home has the secondary effect (by its influence on demand relative to supply) of making it impossible for producers who are still continuing operations to sell their output at as high a price as before. Owing to the various difficulties in the way of closing down, especially if the trouble is expected to be of short duration, and since even a reduced price will generally show some margin over prime cost, some producers will—for a time at least—accept a lower price for their products. This, again, will help the country's "visible" balance of trade.

(iv) The fall of prices considered under (iii) is a fall of prices which is not accompanied by a corresponding fall of costs and is, therefore, at the expense of the producer. If such a fall continues for any length of time it necessarily puts a pressure on producers to reduce costs, including wages if necessary. When costs as well as prices have fallen, the help to the country's "visible" balance of trade resulting from the fall of prices will be on a more durable and reliable basis.

216. Now it is not to be assumed on every occasion on which bank rate is raised that the whole of this train of consequences is desired or intended, or will in fact ensue. It depends on how deep-seated is the cause of the disequilibrium in the country's balance of international payments. But it is the peculiar property of bank rate policy that it exercises a pressure in the right direction whether the problem is merely one of momentary short-period adjustment or whether it is of a more fundamental character.

217. Thus the Bank of England has felt in the past, as we have been told in evidence, that it will be pursuing the safest course if it keeps its eye primarily on the movements of the foreign exchanges as the indicator of the balance of international payments,

and then effects its changes in bank rate mainly in response to such movements. For whether it be a passing trouble or whether it be an occasion for a more fundamental readjustment, this will be the right remedy.

218. There can be no doubt, in our judgment, that "bank rate policy" is an absolute necessity for the sound management of a monetary system, and that it is a most delicate and beautiful instrument for the purpose. Nevertheless there are certain limitations to its usefulness, unless it is supplemented in certain ways. In particular:—

(i) The business world has found it difficult hitherto to interpret the meaning of a change of bank rate in any particular instance. They may be uncertain whether it merely represents an effort to correct a temporary maladjustment in the international short-loan position or whether it is the beginning of a contraction which will produce a curtailment of enterprise and business losses until the necessary adjustments have been effected. Thus a change of no great significance which is likely to be merely temporary or seasonal may cause undue alarm and may have a seriously unfavourable psychological reaction on business confidence. The only remedy for this is to be found, we suggest, in a diffusion of knowledge as to the relevant facts and a readiness on the part of the Bank of England to inform the money market, and the joint stock banks, whenever it can, as to its views of the situation. If the public was enabled to distinguish changes in bank rate intended merely to equalise supplies of short-term funds between different international markets from changes made necessary by excessive costs or excessive activity at home and intended to cause a contraction of domestic credit, some unnecessary disturbances to confidence might be avoided, and in course of time industry would learn to be more philosophical about changes made for non-industrial reasons. We make certain proposals concerning this in Part II of our Report.

219.—(ii) A policy which waits upon movements of gold may be too tardy. For these movements are often the last event in a situation which has been developing for a considerable time. If we had a more complete knowledge, both scientific and statistical, of what is going on in our economic system, it might be possible to act sooner with great advantage, to correct aberrations before they have gone too far and thus keep business and enterprise on a more level keel. It would be better (if it is possible) to develop greater powers of diagnosis and not to depend so much on a comparatively late-appearing symptom. Such a policy would require definitely to be less automatic and would thus undoubtedly place greater responsibility on the banking authorities.

220.—(iii) Bank rate policy, guided and governed by the tendency of gold to move, is a means of maintaining the stability of the exchanges rather than the stability of business. It is a means of

keeping us in step with the rest of the world ; of keeping us, not at a steady pace, but at the same pace as others. Indeed so far from preserving a stability of prices, profits and employment, the maintenance of stable exchanges has the effect of transmitting to our credit system any serious disturbances, of a cyclical character or otherwise, which may be affecting the rest of the world.

All this, of course, is inherent in belonging to an international standard and is not the fault of bank rate policy which will merely be carrying out successfully the duty laid upon it. Nevertheless these considerations serve to emphasise the importance of two matters to which we shall refer in Part II of our Report, namely, the expediency of international co-operation with a view to keeping a steady pace for the international system as a whole, and the desirability of protecting our own national system so far as we can from being unduly sensitive to international perturbations of a temporary character.

221.—(iv) Bank rate policy is quite a proper instrument, not only for the correction of temporary disequilibrium in the international loan market, but also for regulating the pace of expansion and enterprise at home and for putting pressure on costs to accommodate themselves to changes in our relative situation or in the international price level. But it is only adequate by itself for such purposes within certain limits. When substantial changes in the level of our industrial costs are necessary to correspond to substantial changes in the value of money, changes in bank rate alone cannot hope to achieve all that is necessary. In such a case, however necessary it may be that bank rate policy should be employed to maintain the international value of our currency, some other supplementary means must be found to restore equilibrium. For consider how bank rate policy works out in such a case. Its efficacy depends in the first instance on reducing the profits of business men. When in the effort to minimise this result, output and employment are contracted, it depends on decreasing the amount of business profits and increasing unemployment up to whatever figure is necessary to cause business men either to decrease their costs by additional economies or to insist on, and their workers to accept, a reduction of wages. But public opinion does not easily acquiesce in such a process. And the reduction, if and when effected, will fall unequally and unfairly on those sections of the community who are least protected by contract, least able to defend themselves, and often least able to afford the sacrifice.

Moreover, those who are in charge of our monetary system will—naturally and excusably—be reluctant to carry through so ruthless a policy to its proper conclusion, with the result that we may continue for a long period in a depressed condition with severe losses and severe unemployment and yet with not enough of both to compel by *force majeure* the necessary readjustment of incomes.

Moreover once such a condition of depression has become firmly established a policy of dear money will no longer be necessary to ensure its continuance; for it will contain within itself the seeds of its own perpetuation.

4. THE SUPPLY OF CREDIT TO BUSINESS AND ENTERPRISE.

222. We have seen that, apart from its immediate influence on the international short-loan market, bank rate policy—and the same is true of “ open market ” policy—operates, as a method of currency management, by its effect on the terms and the quantity of credit which the banking system as a whole is in a position to afford to business and enterprise. For in making an adequately high bill rate effective in the market, the Bank of England varies the amount of its assets, and hence of its deposits, to the necessary extent, which, in turn, has the effect of changing on a much larger scale the quantity of credit made available by the joint stock banks, since, when the banks' deposits at the Bank of England are increased by a given amount, these banks feel themselves free to increase their own assets by nine or ten times this amount.

223. It has been explained to us in evidence that when the action of the Bank of England impels the joint stock banks to increase or decrease the volume of their assets (and hence of their deposits), the first effect of the change is likely to fall on the banks' more liquid assets, namely, their bills and their loans to the money market, and next on their investments; whilst, if they are forced to curtail their advances, they will first of all cut down advances of a financial or personal character and will be most reluctant to refuse advances to their customers for normal business purposes.

224. Thus the effect of credit expansion or contraction on the amount of business advances will be mainly indirect. The expansion or contraction of the amount of credit made available by the banking system in other directions will, through a variety of channels, affect the ease of embarking on new investment propositions. This, in turn, will affect the volume and profitableness of business, and hence react in due course on the amount of accommodation required by industry from the banking system. Finally the diminished (or increased) profitableness of business will diminish (or increase) the desire to embark on new investment propositions. Thus what started as an alteration in the *supply* of credit ends up in the guise of an alteration in the *demand* for credit.

225. It is for this reason that controversy is apt to arise as to the connection between business depression (or the opposite) and the policy of the banking system in decreasing (or increasing) the volume of credit. For example, it has been put to us, on the one

hand, that the maintenance of the basis of bank credit, and therefore its volume, at the actual figures of recent years instead of at some higher figure, however inevitable it may have been, has had an important influence in depressing British business and in causing unemployment. On the other hand, there has been a decided preponderance of evidence from banking quarters to the effect that sound borrowers for purposes of a kind which it is suitable to finance by means of bank loans have seldom or never been refused adequate accommodation by their bankers. Broadly speaking, the evidence which we have received from business quarters has also supported this view. But these two views are, for the reasons just given, not necessarily inconsistent with one another. For it is a usual characteristic of a process of restriction to reduce business profits below normal, just as it is a usual characteristic of an inflationary process to swell them above normal; and the reduction of profit naturally diminishes the eagerness of the business world to expand the scale of production or to seek bank advances on a larger scale. Indeed, anyone would expect that a restriction of credit, once it was well under way, would greatly diminish the pressure on the banks for new advances for the purposes of business expansion. Thus it would be a mistake to conclude from the absence of such pressure that a restriction of credit has, therefore, had no adverse influence on the volume of output and employment.

226. Since, then, it is a rare event for the banks—except, quite properly, at the height of an inflationary boom—to restrict the accommodation required by their business customers for liquid employment in their own businesses, the banks regarding this as having the first claim on their resources, it follows that the effect of a restriction of credit on business activity operates, as we have said above, in a different way. We think it would be generally accepted, as a brief summary of the case, that a restriction of the volume of credit has to be associated with a higher market rate of interest than would rule if the volume of credit were greater, that an enhanced rate of interest operates in a variety of ways as a deterrent to new capital enterprise and the volume of current business, that the reduction of new enterprise has an all-round adverse effect on the level of profits, that the reduction of profits has an adverse repercussion on the volume of output, and so on.

227. This train of events is partly brought about in a direct and obvious way; but partly also in a more obscure manner through its effect on the prices of long-term securities and on the ease and comfort of the new-issue market. Two examples will illustrate the character of what occurs. If, at a time when the public is showing an increased relative preference for liquid assets, the banking system—which is the main creator of liquid assets—does not increase the available volume of such assets in the shape

of bank deposits, it is inevitable that the price of non-liquid assets should fall; for the increased desire to hold liquid assets must either be satisfied by an increased supply of such assets or held in check by the loss which has to be incurred in exchanging non-liquid assets for liquid assets. In the second place, the banks are themselves large holders of investments, as distinct from bills and advances; and for the banks to keep the supply of advances for productive business equal to the demand for them does not serve to dispel the adverse effects of credit restriction, if it has to be done at the expense of the banks' investments.

228. We may now consider in the light of the above, the actual figures of the leading banks of England and Scotland for the six years from the beginning of 1924 to the end of 1929 (see Appendix I). During these years the banks did indeed increase the volume of their commercial bills and advances by the very large amount of £222,000,000. But £205,000,000 of this was found by the sale of investments and Treasury bills and the net increase in the banks' earning assets was only £70,000,000. Moreover this was occurring at a time when the public was showing an increased disposition to hold money on deposit account, fixed deposits increasing during the same period by £132,000,000. Except in so far as this increase in fixed deposits was offset by an increase in the assets of the banks, the tendency (by reducing the velocity of circulation) was in the same direction as that of a contraction of credit.

229. Or we may look at it in another way. According to the best evidence we can obtain, industrial output per head increased over the period covered by the above figures (1924-1929) by 10 per cent., whilst the numbers seeking employment in the insured industries increased by 7 per cent. Thus the potential output of the country may have increased by somewhere between 15 and 20 per cent. If at such a time it is found that the active deposits are substantially unchanged or slightly reduced, it is evident that deflationary forces have been at work though they have taken the form primarily, not of a reduction in the basis of credit, but in a lower velocity of circulation for bank deposits as a whole, due to a larger proportion of them having been held on fixed deposit account. Further, the effect of such forces on enterprise, and employment is bound to be adverse so long as they last; an expectation with which the actual facts of the period from 1924 to 1929 are fully consistent.

230. We do not mean to imply by the above that it was within the power of the Bank of England to allow a larger basis of credit than it actually allowed. For it is arguable that, during the greater part of the period, the duty laid on the Bank by

Parliament to maintain the gold value of sterling at the figure to which it was restored in 1925 was incompatible with appreciably easier credit conditions than actually existed.

5. THE INFLUENCE OF THE BANKING SYSTEM ON INVESTMENT.

231. There can be no doubt as to the power of the banking system (subject to international limitations which we deal with below) to increase or decrease the volume of bank money. But what is not so certain is its power to control the volume of bank money which is actively employed. When it is a case of *contracting* the volume of bank money, the question is how drastic the contraction must be to produce an effect, rather than whether the banking system can achieve its purpose if it is sufficiently determined. For whilst a buoyant and optimistic market for investment and enterprise may contrive for a time to carry on the same volume of business with a diminished supply of credit, there are definite limitations to the possibilities of this. When, however, it is a case of expanding the volume of bank money with a view to stimulating active investment, the view is often expressed that the powers of the banking system may be altogether inadequate, since the additional bank money created may simply lie idle as an addition to liquid funds.

232. In discussing the power of the banking system to overcome this difficulty, we need to distinguish sharply between a more or less normal situation, and one of acute business depression at or near the bottom of a severe slump. In normal conditions we see no reason to doubt the capacity of the banking system to influence the volume of active investment by increasing the volume and reducing the cost of bank credit. For in ordinary circumstances the new-issue market is responsive to the ease of bank credit, and the additional real investment which ensues on a brisker new-issue market serves to increase profits generally and hence to stimulate enterprise in various directions. The effect of cheap and abundant credit on the willingness and ability of dealers and others to carry increased stocks, and hence to increase their orders to the manufacturer, is also important. Indeed it is more usual to emphasise the extreme ease of stimulating enterprise and investment in these ways, and hence the danger of inadvertent or excessive action, rather than the difficulty of providing by banking means a sufficient stimulus to produce a noticeable effect; and this view is obviously the right one.

233. Thus we consider that in any ordinary times the power of the banking system (subject of course as before to international limitations) to increase or diminish the active employment of money in enterprise and investment is indisputable; and it is equally indisputable that an increased activity of money in these

ways will tend to raise prices and that a decreased activity will tend to diminish them.

234. In the midst of an acute slump, however, a more difficult problem is presented. When conditions of extreme uncertainty and depression have developed, a mere change in the cost of short-term credit will not be sufficient by itself to attract borrowers for purposes of new enterprise who on other grounds are reluctant. Moreover, a limit is easily reached below which it is not practicable to reduce the cost of credit any further. An appreciable part of the charges made for loans by the joint stock banks represents, not pure interest, but their actual expenses in carrying on their business. Thus even if pure short-term interest, for transactions into which no element enters but pure interest, falls so low as to 1 per cent. per annum, the minimum rate which must be charged to the bulk of borrowers will nevertheless remain at an appreciably higher level than this. In fact the cost of short-term loans to most borrowers falls with the greatest difficulty below 4 per cent. Besides this fact, the extra inducement to borrowers of such a rate, compared with (say) 5 to 6 per cent., will not be very appreciable so long as prices are falling and profits small and precarious.

235. Some authorities have concluded from this that in such circumstances the monetary authority is largely impotent (although it does not follow that *earlier* action by the monetary authority might not have been efficacious) and cannot expect to promote a revival of confidence and of trade until its efforts are supplemented by some adventitious event bringing a stimulus from some other quarter.

236. As to the correctness or otherwise of this view, it is particularly difficult for us to dogmatise as there has not hitherto been any adequate opportunity for putting the opposite view to the test of experience. But we ourselves are inclined to the view that the monetary authority is not so powerless as is sometimes supposed and that the danger, if any, is rather in the direction of letting loose too strong a force, which it might be difficult to control later.

237. The preceding argument has dwelt, it will be noticed, on the cost of credit rather than on its quantity. What would be the result of the monetary authority largely increasing the quantity of bank credit in the circumstances supposed, whilst leaving the rate charged for loans to find its own level? For it will always be possible for the monetary authority to effect this by the purchase in the market of e.g., Government securities. It would seem safe to conclude that the price of Government securities would rise as a result both of the direct action of the Central Bank and also of the action of the rest of the banking system in endeavouring to find a use for the idle funds which the Central Bank would be thus placing at its disposal. A rise in the price of these securities must in due course be reflected to some extent in the price of other

securities of a less prime class. Conversion operations would be facilitated. And gradually the rise of price beginning with securities of the highest class will spread over wide classes of securities including most of those where the special risks of the slump are relatively unimportant. Moreover it may not need very drastic action on the part of the Central Bank to produce this result. For as soon as the course of prices for high-class securities has a markedly upward trend, it is likely that many persons who have hitherto preferred to keep their funds liquid will alter their preference in favour of securities.

238. So far, however, nothing will have happened except a rise in the market price of certain classes of fixed-interest securities. This in itself will not directly affect the prices of commodities or the volume of output and employment. But it will have affected by this time the cost of long-term borrowing by first-class borrowers; and there are, as a rule, various types of fixed investment such as house building and the expansion of public utility undertakings which are fairly sensitive to changes in the long-term rate of interest. There are many schemes, for example, which are not worth while at 5 per cent., but become profitable, on the best estimates which can be made, if long-term funds are obtainable at 4 per cent. Or again, a fall from 6 per cent. to $4\frac{1}{2}$ per cent. in the rate of interest on loans against houses is nearly as good as a fall of 25 per cent. in the cost of production, when it comes to calculating the minimum level of rent which will prove profitable; and there is reason to think that the demand for house-room is elastic.

When, therefore, this point has been reached, the effect of abundant credit on the long-term market will be to bring about an increase of actual new enterprise. The repercussions of this on business confidence and on the actual level of profits may then be expected to break the vicious circle.

239. It is not argued that this chain of events can be completed quickly. It may occupy a considerable time. The contention is that an increase in the basis of credit is a step which can be taken by the Central Bank in the supposed circumstances without any risk of untoward consequences—for at the worst the effect will be nugatory—whilst there is fair reason to expect that it may do something to set in train the course of events outlined above. Some of us take the view that, provided the policy was adopted by Central Banks generally, the most hopeful form of attack on the existing depression would be along these lines. The same method is one which could be, and ought to be, employed with great effect in the opposite circumstances, namely, in face of an incipient inflation. In such a case Central Banks should sell the securities which they had accumulated during the depression. Indeed they would have to be careful not to allow too large a basis of credit to

persist when once the vicious circle had been broken. The method proposed would in fact have the additional advantage that it would put the Central Banks in a stronger position for curbing the next tendency towards inflation, because they would have a larger volume of securities for open market operations.

6. INTERNATIONAL LIMITATIONS.

240. We have entirely neglected in the preceding section the limitations which are actually set to a policy on the lines considered by the duty of adhering to an international standard. It is evident that a Central Bank which belongs to an international system cannot afford to maintain credit conditions which are out of relation to those which obtain in the rest of the system. For otherwise the additional liquid funds made available in the domestic market will endeavour to find an outlet in foreign money markets where better terms are obtainable by lenders, with a resulting loss of gold.

241. It is necessary, therefore, in any policy, whether of expansion or contraction, which is adopted by a particular Central Bank that due attention should be paid to the relation of this policy to the policies which are being pursued by the other Central Banks. It is a condition of adherence to an international standard that a Central Bank must not get much out of step with the average movement of other Central Banks, under penalty of provoking large movements of gold. It is for this reason that we shall lay so much emphasis in what follows on the importance of international co-operation.

Part II.—Conclusions and Recommendations.

CHAPTER I.—THE MAIN OBJECTIVES OF THE MONETARY SYSTEM.

I.—THE GOLD STANDARD.

1. THE RECENT WORKING OF THE GOLD STANDARD.

242. Unfortunately, the anticipations of those who were responsible for our return to the gold standard in 1925 have to a large extent not been fulfilled. Whether these anticipations were justified at the time, and what other course was practically possible, are questions on which we do not all agree, but which it would be unfruitful now to discuss. The six years since that act of policy have, for the reasons stated below, proved to be of a very abnormal character and the sacrifices which a return to gold at the old parity involved have not been compensated by the advantages of international price stability which were anticipated.

243. The accomplished fact of the restoration of our currency to the pre-war gold parity and its maintenance there for a period of six years creates, however, an entirely new situation; and it by no means follows, even if the view be held, as it is by some of us, that a mistake was made in 1925, that the consequences can be repaired by a reversal of policy in 1931.

244. Apart from the more general considerations relating to the gold standard which we discuss below, there have been two sets of difficulties in the way of its working to advantage in recent years, one of which we may expect, and the other of which we may hope, to be temporary.

245. The first set of difficulties has been caused by the fact that the various gold-parities established by the countries returning to the gold standard did not bear by any means the same relation in each case to the existing levels of incomes and costs in terms of the national currency. For example, Great Britain established a gold-parity which meant that her existing level of sterling incomes and costs was relatively too high in terms of gold, so that, failing a downward adjustment, those of her industries which are subject to foreign competition were put at an artificial disadvantage. France and Belgium, on the other hand, somewhat later established a gold parity which, pending an upward adjustment of their wages and other costs in terms of francs, gave an artificial advantage to their export industries. Other countries provide examples of an intermediate character. Thus the distribution of foreign trade, which would correspond to the relative efficiencies of different countries for different purposes, has been seriously disturbed from the equilibrium position corresponding to the normal relations between their costs in terms of gold. This, however, has been a consequence of the manner in which the post-war world groped

its way back to gold, rather than of the permanent characteristics of the gold standard itself when once the equilibrium of relative costs has been re-established, though, even after six years, this is not yet the case.

246. The second set of difficulties has resulted from the international lending power of the creditor countries being re-distributed, favourably to two countries, France and the United States, which have used this power only spasmodically, and adversely to the country, Great Britain, which was formerly the leader in this field and has the most highly developed organisation for the purpose. This re-distribution of lending power has been largely due to the character of the final settlement of the War debts in which this country has acquiesced. For although Great Britain suffered during the War a diminution of her foreign assets of some hundreds of millions, she has agreed to a post-war settlement by which she has resigned her own net creditor claims, with the result, that on a balance of transactions, virtually the whole of the large annual sums due from Germany accrues to the credit of France and of the United States. This has naturally had the effect of greatly increasing the surplus of these two countries, both absolutely and relatively to the surplus of Great Britain. The diminution in Great Britain's international surplus, due to her war sacrifices remaining uncompensated by post-war advantages, has, however, been further aggravated recently by the adverse effect on her visible balance of trade of the first set of difficulties just mentioned, namely, the differing relationships between gold and domestic money-costs on which different countries returned to the gold standard.

247. This re-distribution of lending power need not, however, in itself have interfered with the working of the gold standard. The difficulties have arisen through the partial failure of the two recipients, during the last two or three years, to employ the receipts in the way in which Great Britain had always employed hers, namely, either in the purchase of additional imports or in making additional foreign loans on long-term. On the contrary, they have required payment of a large part of their annual surplus either in actual gold or in short-term liquid claims. This is a contingency which the normal working of the international gold standard does not contemplate and for which it does not provide.

248. But this set of difficulties, too, one may hope, though with less confidence, to be a temporary phenomenon. Should it not prove so, we can scarcely expect the international gold standard to survive in its present form. If for any reason, however plausible from its own point of view, a creditor country, after making all the purchases it desires, is unwilling to lend its remaining surplus to the rest of the world, there can be no solution except the ultimate

destruction of the export trade of the country in question through a relative reduction in the gold-costs of other countries. If there were no international standard, but each country had its own domestic currency subject to fluctuating exchanges, this solution would come about at once. For in this event the exchanges of France and the United States, for example, would by now have risen to so high a level relatively to the rest of the world that their exporters would have been driven out of business, so that their unlent surplus would have disappeared. According to the classical theory of the gold standard, the same result should ensue, though more slowly and painfully, as a result of movements of gold inflating costs in those countries and deflating costs elsewhere. But in the modern world, where, on the one hand, inflows of gold are liable to be sterilised and prevented from causing an expansion of credit, whilst on the other hand the deflation of credit set up elsewhere is prevented by social causes from transmitting its full effect to money-wages and other costs, it may be that the whole machine will crack before the reaction back to equilibrium has been brought about.

249. Unfortunately upon these two sets of abnormal difficulties there has supervened, starting in the United States, a business slump of a more normal type though of quite unusual dimensions, further aggravated, in the opinion of some, by being associated with the necessity for a transition from the high rates of interest appropriate to the War and post-war period back towards the lower rates which were typical before the War.

250. Naturally the total result leads some people to question the desirability of adhering to an international standard.

2. THE QUESTION OF AN INTERNATIONAL STANDARD.

251. This brings us to the question whether adherence to an international standard may involve the payment of too heavy a price in the shape of domestic instability. Many countries, both to-day and at former times, have found that such continued adherence involves a strain greater than they can bear. But these are generally debtor countries, the trade of which is concentrated on a narrow range of primary products subject to violent disturbances of prices. If we leave aside the position to-day, experience does not show that a creditor country with diversified trade is liable to suffer undue domestic strain merely as the result of adherence to an international standard. We are of opinion, therefore, that we should not be influenced merely by the exigencies of the moment, if there is reason to believe that there may be important counter-vailing advantages on a longer view. If we need emergency measures to relieve the immediate strain, we should seek them in some other direction.

252. In the particular case of Great Britain we believe that there are such advantages. One of our most valuable sources of income, indeed one of our most important export industries, is the practice of international banking and associated services. Along with our shipping and our staple export industries this has been for a long period past one of our main sources of wealth. It is by no means clear that the possible advantages to our export activities from the fact that a fluctuating exchange would automatically offset the rigidity of money-incomes would balance the unquestionable loss to the first named; and we might be a poorer country on balance. It is not necessary, in order to reach this conclusion, to exaggerate the benefits which accrue to us from our international financial business. They are not so enormous as to outweigh all other considerations. For example, it is not likely that they have gone even a fraction of the way towards compensating the losses of wealth through unemployment in recent years. It is not our case that industry should be sacrificed to finance. It is, rather, that the benefits to industry from a fluctuating exchange would be inadequate to compensate the losses in other directions. For whilst a fluctuating exchange would have undoubted advantages in certain conditions, it would often be merely substituting one form of instability for another. It would not be possible for a country so intricately concerned with the outside world as Great Britain is to escape so simply from the repercussions of instability elsewhere.

253. There is, moreover, a further reason which cannot easily be weighed merely in the balance of our own direct economic advantage and which weighs more heavily with us than any other. There is, perhaps, no more important object within the field of human technique than that the world as a whole should achieve a sound and scientific monetary system. But there can be little or no hope of progress at any early date for the monetary system of the world as a whole, except as the result of a process of evolution starting from the historic gold standard. If, therefore, this country were to cut adrift from the international system with the object of setting up a local standard with a sole regard to our domestic situation, we should be abandoning the larger problem—the solution of which is certainly necessary to a satisfactory solution of the purely domestic problem—just at the moment, maybe, when, if we were able to look a little further forward, the beginnings of general progress would be becoming visible.

254. We conclude, therefore, that we shall best serve the purpose for which we were set up, and have the greatest hope of securing a sufficient general agreement to lead to action, if we base our recommendations on the assumption, which we hold justified, that the next phase of monetary policy must consist of a wholehearted

attempt to make the existing international standard work more satisfactorily. It is possible—though we believe that hard experience will teach them otherwise—that some countries may be unable or may fail to work an international standard in a satisfactory way. But this is not yet proved, and it would be unwise for us, who have so much to gain by it, to give up the attempt to secure a sound international currency.

3. DEVALUATION.

255. It has been represented to us that, without in any way departing from the principle or the practice of adherence to an international standard, it is desirable for us in the national interest to do now what might have been accomplished with much less difficulty in 1925, namely, to revise the gold-parity of sterling. Such a step is urged on the ground that, if we diminished the gold equivalent of the £ sterling by 10 per cent. thereby reducing our gold-costs automatically by the same percentage, this would restore to our export industries and to the industries which compete with imported goods what they lost by the return to gold at a figure which was inappropriate to the then existing facts, and that it would also have the great advantage of affecting all sterling costs equally, whether or not they were protected by contract.

256. We have no hesitation in rejecting this course. It is no doubt true that an essential attribute of a sovereign state is a power at any time to alter the value of its currency for any reasons deemed to be in the national interest, and that legally, therefore, there is nothing to prevent the British Government and Parliament from taking such a step. The same may be said of a measure writing down all debts, including those owing by the State itself, by a prescribed percentage—an expedient which would in fact over a considerable field have precisely the same effect. But, while all things may be lawful, all things are not expedient, and in our opinion the devaluation by any Government of a currency standing at its par value suddenly and without notice (as must be the case to prevent foreign creditors removing their property) is emphatically one of those things which are not expedient. International trade, commerce and finance are based on confidence. One of the foundation stones on which that confidence reposes is the general belief that all countries will seek to maintain so far as lies in their power the value of their national currency as it has been fixed by law, and will only give legal recognition to its depreciation when that depreciation has already come about *de facto*. It has frequently been the case—we have numerous examples of recent years—that either through the misfortunes of war, or mistakes of policy, or

the collapse of prices, currencies have fallen so far below par that their restoration would involve either great social injustices or national efforts and sacrifices for which no adequate compensation can be expected. The view may be held that our own case in 1925 was of this character. The British currency had been depreciated for some years. It was obvious to the whole world that it was an open question whether its restoration to par was in the national interest and there is no doubt in our minds as to our absolute freedom at that time to fix it, if it suited us, at a lower par value corresponding to the then existing exchange. But it would be to adopt an entirely new principle, and one which would undoubtedly be an immense shock to the international financial world, if the Government of the greatest creditor nation were deliberately and by an act of positive policy to announce one morning that it had reduced by law the value of its currency from the par at which it was standing to some lower value.

257. Moreover, considering the matter from another point of view, in the environment of the present world slump the relief to be obtained from a 10 per cent. devaluation might prove to be disappointing. It is not certain that, with world demand at its present low ebb, such a measure would serve by itself to restore our export trades to their former position or to effect a radical cure of unemployment. On the contrary, in the atmosphere of crisis and distress which would inevitably surround such an extreme and sensational measure as the devaluation of sterling, we might well find that the state of affairs immediately ensuing on such an event would be worse than that which had preceded it.

4. THE PROSPECTS OF THE GOLD STANDARD.

258. The course of events in the last two years has had the effect of forcing a number of countries off the gold standard. But these are all debtor countries; and if matters continue as at present, it will be the debtor countries of the world, and not a creditor country such as Great Britain, which will be the first to find the strain unbearable. We consider that the leading creditor countries of the world should consult together to prevent matters from continuing as at present; and we deal at length with international co-operation in the next chapter. In order that Great Britain may speak with authority in such discussions, it is essential that her financial strength should be beyond criticism. This largely depends in the near future on an increase of her surplus available for new foreign lending.

259. In this connection it may be worth while to summarise the result of certain information which we have collected. For it is of

a reassuring character and goes some way to answer certain criticisms which have been made, or doubts which have been entertained, regarding one aspect of the financial position of this country. In view of the large volume of foreign issues which have been floated in recent years in London and of the common belief that, in addition, British investors have made large purchases in the United States, partly of foreign bonds initially issued in New York and partly of American securities, whilst at the same time our surplus for new foreign lending has been diminished, it has been surmised that Great Britain must have been financing some part of her new foreign investment on long-term by means of an increase, and perhaps a dangerous increase, in her short-term liabilities to foreign centres. We have accordingly made it our business to collect for the first time as full a summary as possible both of foreign liquid resources in London and of British acceptances on foreign account. We take this opportunity of thanking the Bank of England, which has done the detailed work on our behalf, and the numerous financial institutions which have willingly co-operated in supplying the information, since they have enabled us to fill what was perhaps the greatest gap in our previous knowledge of the financial commitments of this country. We cannot claim that our figures are complete and they could doubtless be improved with further experience; but we believe that they may cover, in quantity, nearly the whole field. The most important item about which we have no information is the total of sterling bills held in their own custody by foreign banks, and it may be that this item is a more fluctuating one than the items for which we have obtained figures. We were prepared to find that these totals might give some support to the fears expressed above, but in fact they are reassuring.

260. The figures are given in full in Appendix I (with some notes upon the items included therein) and may be summarised as follows:—

End of Year.	Deposits and Sterling Bills held in London on foreign account.*	Sterling Bills accepted on foreign account.	Net Liability of London.
	£	£	£
1927	419,000,000	140,000,000	279,000,000
1928	503,000,000	201,000,000	302,000,000
1929	451,000,000	176,000,000	275,000,000
1930	435,000,000	181,000,000	274,000,000
1931 (March)	407,000,000	153,000,000	254,000,000

* Exclusive of sterling bills held by foreign banks in their own custody.

261. We have not obtained figures prior to 1927. We think it probable that in the period between the return to the gold standard in 1925 and the end of 1927 London's net liability was increasing substantially, since the French balances abroad were mainly built up during that period. But these figures show that in the last three years so far from there having been a large increase in London's short-term liabilities, there has been a small decrease in their amount, so far as we have been able to ascertain it.† The preliminary figures which we have obtained for the first quarter of the present year indicate that this tendency has been continued.

262. We have not obtained figures of British balances abroad, i.e., of British short-term claims on foreign centres (which may be quite considerable in amount), or of various other items which would be required for a complete picture. It would be desirable to obtain these, as we recommend later in Chapter V.

263. It seems probable, therefore, that in spite of the reduction of our surplus, the whole of our *net* purchases of foreign securities have been paid for out of our currently accruing surplus on income account. It is possible, we think, that this surplus may be somewhat larger than the usual estimate.

264. As regards the immediate situation, it is also interesting to note that the trade returns, unsatisfactory though they are, bear

† It is interesting to compare these figures with the comparable items for the United States. (The American returns also include other figures reducing their total net liability, which we have not yet been able to collect for Great Britain.)

End of Year.	Deposits and Bills held in U.S.A. on foreign account.	Dollar Bills accepted on foreign account.	Net Liability of New York
	£	£	£
1927	637,000,000	83,000,000	554,000,000
1928	595,000,000	104,000,000	491,000,000
1929	632,000,000	171,000,000	461,000,000
1930	573,000,000	168,000,000	405,000,000

The figures of dollar acceptances are taken from the Annual Reports of the United States Department of Commerce on the Balance of International Payments of the United States and the New York Federal Reserve Bank Monthly Review. The figures issued by the American Acceptance Council are somewhat higher.

out the conclusion that the worst strain of a situation such as the present falls on the raw material countries. During the first quarter of this year the quantity of our exports fell off by more than 30 per cent., whereas the reduction in the quantity of our imports was only 6 per cent. Nevertheless, as a result of the catastrophic fall of raw material prices, the visible balance of trade has been actually less adverse to us than in recent years, the net position in terms of money moving £5 millions in our favour, so that less of our surplus under other heads (i.e., from foreign interest, shipping, etc.), is being required to-day to finance our imports than in 1930 or in 1929.

265. The same point can be strikingly illustrated by what has happened in the case of the single commodity wheat. At the price prevailing in December, 1930, the annual cost of our wheat imports would be about £30 millions less than it was in 1929, and £60 millions less than in 1925. It is obvious what a large contribution this single item represents to the national cost of supporting the present volume of unemployment. It is a great misfortune both for us and for the raw material countries that we should have a great volume of unemployment through their inability to purchase from us as a result of the fall in the price of their produce. But merely from the point of view of our balance of trade it is not to be overlooked that the latter fact not only balances the former but may even outweigh it. We conclude that the underlying financial facts are more favourable than had been supposed, and that Great Britain's position as a creditor country remains immensely strong.

II.—THE INTERNATIONAL PRICE LEVEL.

1. THE IMMEDIATE NECESSITY TO RAISE PRICES ABOVE THEIR PRESENT LEVEL.

266. We mean by the international price level in this context the composite price at wholesale of the principal foodstuffs and raw materials entering into international trade as measured by the best-known wholesale index numbers. We do not consider that a high degree of precision in the definition of this is necessary or practicable.

267. We are emphatically of the opinion that, even if a further fall of wholesale prices be avoided, their stabilisation at approximately the present level would be a serious disaster for all countries of the world alike; and that the avoidance of such an event should be a prime object of international statesmanship.

268. The losses which are now being incurred by nearly all categories of producers of average efficiency in nearly all countries

of the world are an overwhelming proof that the fall of commodity prices has gone far beyond the substantial reduction which might be justified in the case of many important commodities by the increases in productive efficiency which have been achieved in recent years. Consequently, even the continuance of the present price level—quite apart from a further fall—must prolong business losses and the unemployment which the attempt to avoid these losses necessarily brings with it, until a substantial downward readjustment of money-costs has been somehow brought about. This would mean a reduction of money-incomes except to the extent that efficiency can be increased yet further. But it is obvious that the reduction of money-incomes must encounter resistance. Each individual, whatever may be the ultimate effects upon his standard of life, resents the lowering of his salary or his wages by economic pressure, and cannot readily believe that this can be necessary at a time when the technique of production is making revolutionary strides forward. Governments and Central Banks will, justly or unjustly, be blamed for the misfortune. Social unrest will tend to make moderate and rational remedies more difficult the longer they are delayed.

269. The classes who have suffered by the fall are the shareholding class in general, the entrepreneurs and those thrown out of employment; they have suffered partly by a direct reduction in the national income, partly by the transfer of wealth from them to the rentier and the employed. If, on the other hand, an adjustment is brought about by a rise in prices, purchasing power will be transferred from the rentier and from those earning salaries and wages to the shareholder and entrepreneur in the shape of larger profits; though if, as a result of the adjustments, the national output is increased, the salaried and wage-earning class as a whole may easily gain more in increased employment than they lose in the purchasing power of their money earnings. The fact that an adjustment of all non-contractual incomes to the new level does not affect the rentier is of particular importance in Great Britain at the present time on account of the vast increase of national indebtedness contracted in terms of money as compared with Great Britain herself before the War and with most of her neighbours to-day who have by a depreciation of their currencies written down their war debts to a modest figure.

270. The increase in the burden of internal War debts ensuing on a rise in the value of gold money will present a most difficult problem if incomes generally become adjusted to the new lower level. But in addition to this, there is the intractable problem of international indebtedness. The internal obligations arising

out of the War contain to-day no provisions, such as were introduced into the Dawes Plan, for changes in the value of gold. Moreover, the fall in the prices of raw products is facing the debtor nations of the world, which are dependent on the sale of such products, with tasks of exceeding difficulty. Superficially the creditor countries may appear to obtain a corresponding advantage. But this may prove delusive. International credit is a fragile plant. The effect of the pressure of the present price level on the credit of debtor countries may, if it is long continued, prove so serious that their ability to contract new loans will be dangerously impaired. The vicious circle will then be complete. Creditor countries will find that the security of the loans which they have already made is evaporating. And the whole system of international loans, on which the trade and prosperity of the world and the development of its natural resources so largely depend, will be seriously affected.

271. Thus, a failure by the Central Banks of the world to attempt to redress the fall of prices, in our judgment, would endanger the principles on which modern economic society is founded, namely, the dependence of the productive process on the expectation of normal profit to individual concerns, and the sanctity of contract. For to allow prices to fall, whilst social forces maintain wage-costs, obliterates profit; and the attempt to reduce non-contractual incomes, without the power to abate contractual incomes immediately, jeopardises, both nationally and internationally, the sanctity of contract.

272. At the present time, the objective of raising the international price level would probably command widespread, though not universal, approval. When, however, it begins to rise again, a more widespread difference of opinion will soon emerge as to how far the recovery should be allowed to go. Beyond saying that a large rise towards the price level of 1928 is greatly to be desired, it is difficult for us at the present date to be very precise, because the exact answer will depend on the course of events in the meantime. To the extent that efficiency-earnings may have fallen in terms of money during the continuance of the slump, the first of our reasons, namely, the difficulty of effecting a change in the level of incomes will have spent its force. But the force of the second reason, namely, of the burden of indebtedness, will not have been weakened to an equal degree. Moreover, a point may come when the encouragement of a further rise, though desirable in itself, may be difficult or impossible without running the risk of setting loose uncontrollable forces which will generate an undesired inflation carrying the price level much beyond the equilibrium point, with the prospect of an injurious reaction, equally

uncontrollable, at a subsequent stage. Thus the decision in detail will have to be left to the exercise of practical judgment at a later date.

273. Nevertheless, we think it much more likely that attempts may be made to stop the revival prematurely than to allow it to proceed too far. We believe that this would be a great mistake. It is often argued, and it may well be true, that the power of the banking system to hold a business expansion in check is greater than its power to revive business when depression has set in. If, however, we are over-prompt to check every expansion, yet hesitant in the face of every depression, the net result will be a steady lowering of the price level with all the attendant evils of such a prospect. As soon as business begins to lift its head again, we may be sure that austere voices will be raised declaring that there is an incipient inflation of credit present which must be scotched, when, in fact, the existing deflation of prices will not yet have been redressed. After so severe a depression as the present one, when we have to travel such a long way to reach the most expedient position of equilibrium, it will be most important, in our judgment, to be slow to accept such advice.

2. THE LONG-PERIOD STABILITY OF THE PRICE LEVEL.

274. Yet whether or not the ultimate price level will be as high as we might have wished having regard to all the social expediences involved, a point will eventually come when, taking the world as a whole, international prices will have been restored to a level which is appropriate to the then existing levels of salaries and wages and to the burden of monetary indebtedness. When this point has been reached, monetary policy directed towards raising the price level further must, of course, cease, and there must be substituted for it a policy which has as its objective the stability of the international price level.

275. Thus our objective should be, so far as it lies within the power of this country to influence the international price level, first of all to raise prices a long way above the present level and then to maintain them at the level thus reached with as much stability as can be managed.

276. We recommend that this objective be accepted as the guiding aim of the monetary policy of this country. The acceptance of such an objective will represent in itself a great and notable change. For before the War scarcely anyone considered that the price level could or ought to be the care and preoccupation, far less a main objective of policy, on the part of the Bank of England or any other Central Bank.

III.—INTERNATIONAL CURRENCY MANAGEMENT.

277. We have concluded that a restoration of the international price level should be a prime object of international statesmanship. How far such a restoration of the international price level is in fact feasible is, however, a further question. We believe that the outcome is likely to depend in part on a complex conjunction of economic factors in the world at large of a kind which is not directly controllable at the centre. Nor can we give a confident answer to doubters in advance of an actual attempt to solve what is a practical problem. We can do no more than aim at this objective to the best of our powers and persevere with practical efforts along the lines to be suggested below, or in any other way which may commend itself.

278. At the same time we see no great reason to doubt the feasibility of attaining the objective of a higher price level in due course, provided that the Central Banks of the leading creditor countries will work together with this end in view. No one would doubt the ability of a closed monetary system to bring about a rise of prices; in fact it is only too easy. Thus the chief ground of hesitation is the difficulty of securing adequate co-operation among Central Banks, rather than any obstacle inherent in the nature of the problem. The subsequent maintenance of stability may prove more difficult but experience alone will supply a confident answer.

279. We have already investigated in the previous section the ways in which the banking system can expect to influence the price level. The question of the practical steps in the right direction which it is worth while to attempt at the present time we discuss in the next ensuing chapter.

IV.—DOMESTIC CURRENCY MANAGEMENT.

280.—(i) The monetary system of this country must be a Managed System.—It is not advisable, or indeed practicable, to regard our monetary system as an automatic system, grinding out the right result by the operation of natural forces aided by a few maxims of general application and some well-worn rules of thumb. The major objectives of a sound monetary policy—for example, the maintenance of the parity of the foreign exchanges without unnecessary disturbance to domestic business, the avoidance of the Credit Cycle, and the stability of the price level—cannot be attained except by the constant exercise of knowledge, judgment and authority, by individuals placed in a position of unchallengeable independence with great resources and every technical device at their disposition.

281.—(ii) The managing authority should be the Bank of England.—It is not necessary in this country, as it was in the United States before the War, to create a new organ for the centralised

control of the monetary system. For we have in the Bank of England an excellent instrument for the purpose; independent of political influences, yet functioning solely in the public interest; with long traditions and experience and clothed with vast prestige, yet not distrustful (as we have learnt in evidence) of evolutionary change or hesitant of new responsibilities; entrenched in the centre of the struggle for profit and with access to the arcana of the market, yet itself aloof and untinged by the motives of private gain.

We put forward later in Chapter III certain recommendations which affect the Bank of England. But these recommendations are directed to the strengthening of the Bank and to the augmenting of the forces at its disposal for the attainment of its proper objectives.

Nor do we consider that any of our recommendations are inconsistent with the general direction of change which the Bank of England has already laid down for itself, as compared with its methods and organisation in the decades before the War. We have received evidence of the Bank's willingness to adapt itself to the new conditions and problems with which it has found itself presented. It would not be a true picture to portray new and lively elements of contemporary thought and enterprise springing up elsewhere in the City but held down by the weight of the conservatism of the Bank of England.

282.—(iii) The endeavour of domestic management should be to promote the stability of output and of employment at a high level by influencing the regular flow of savings into investment at home and abroad so far as is compatible with the international situation.—The problem as to how this influence is best exercised is essentially a practical one. So far as short-term loans are concerned, the banks both are and ought to be the main source of supply; and it should lie, therefore, within the powers of the banking system to regulate their rate of flow without undue difficulty. But the main source of supply of funds for long-term investment must be, normally and properly, outside the banking system; so that the influence of the banking system on the volume of such investment must be mainly indirect.

Nevertheless, since fluctuations in the activity of long-term investment are just as likely to upset the even flow of savings into useful employment as fluctuations in the demand for short-term loans, it may be that the monetary authority will do well to concern itself more deliberately with this aspect of the market than it has done in the past.

In any case, the London machinery for the issue of long-term loans should be of such a character that the facilities for home borrowers are at least as well organised as those for foreign borrowers, so that the stream of savings is distributed appropriately

between home and foreign loans. It follows that the technique of that part of our financial system which is concerned with our function of international banking should be so adjusted as to lead it to interfere as little as possible with the maintenance of an appropriate supply of credit to meet the requirements of domestic trade and industry. We return to this matter in Chapter IV.

283. This completes our outline of the main objectives of our monetary system. If we have raised expectations that we shall be able to propose in our detailed recommendations a sure and certain means of attaining these objectives, we fear that such expectations will be disappointed.

284. There is nothing, we believe, intrinsically out of reach in any of these objectives; but this does not mean that they are easy or immediately practicable of achievement. In the first place, the most important of them depend on international agreement and collective action and cannot be reached by a single country, which belongs to an international system, acting alone. In the second place, they cannot be attained by Act of Parliament, but must result from the exercise of a skilled discretion of a somewhat novel character for the full use of which the necessary experience does not yet exist. For this reason we have reduced to the least possible the legislative changes which we propose. We have aimed, rather, at suggesting a framework within which the necessary discretion can be most successfully exercised. Indeed, we attach, in a sense, more importance to the deliberate and explicit adoption of the main objectives of the system as we have laid them down, than to our subsequent suggestions in matters of technical detail. For many of the latter do not very greatly modify or enlarge powers which already exist.

CHAPTER II.—PROPOSALS RELATING TO INTERNATIONAL MONETARY POLICY.

285. In our statement of objectives we have recommended :—

- (i) That this country should continue to adhere to the international gold standard at the existing parity;
- (ii) That we should use our influence to lower the international value of gold in terms of wholesale commodities; and
- (iii) That, after prices have been raised sufficiently, we should aim at maintaining a stability of prices at the higher level thus reached.

It is evident that the second and third objectives require international collaboration for their attainment, since any influence

which this country can exert on international prices must be, at the best, limited. We deal in the first part of this chapter mainly with proposals for attaining the third objective, which is of a permanent character, and in the second part with the second objective, which is concerned with the immediate situation to-day.

I.—PROPOSALS OF A PERMANENT CHARACTER.

1. MAIN OBJECTIVE OF CENTRAL BANKS TO MAINTAIN STABILITY.

286. The main objective of Central Banks acting in co-operation in the management of the international gold standard should be to maintain the stability of international prices both over long periods and over short periods—i.e., they should both keep the average steady over a period of years and avoid fluctuations round this average from year to year. Or alternatively—if this alternative were to receive superior support—they should prevent prices from falling to a greater extent than is justified by the increase in the efficiency of production. Stability over long periods is largely a question of the adequacy of the quantity of gold available for their reserves taken in conjunction with the proportionate volume of credit created on this basis; stability over short periods, or in other words the mitigation so far as possible of the Credit Cycle, is, we believe, largely a question of co-operative monetary management.

But while these objectives can be simply and shortly stated the difficulties in completely achieving them are great and manifold.

2. USE OF CENTRAL BANK RESERVES.

287. The first difficulty, but in our view not the greatest, is the question of the adequacy or inadequacy of the future supplies of gold to serve as a basis for the world's currency and credit systems. It is important, no doubt, not to overlook the possibility of a problem arising at some future time as the result of an excessive supply of gold and of an unwillingness on the part of Central Banks to offset an increase in their gold stocks to the degree which would be necessary to avoid a large upward movement of prices. But in order not to burden our argument with what would be in present circumstances a purely hypothetical discussion, we shall generally assume in what follows that the problem is one of preventing the inadequacy of the gold reserves of the Central Banks as a whole from unduly limiting their power to increase the volume of credit.

288. Without co-operative steps to put the Central Banks of the world in a position to counteract in case of need a possible shortage in the supply of gold, such a shortage might indeed prove a serious obstacle to future prosperity. But our belief is that such counteracting steps present little difficulty, if public opinion can be educated to regard the use of gold reserves in a reasonable

light. A fundamental step in the right direction was taken, in our view, when as a result of the War the actual use of gold coins in circulation was abandoned and the obligation was imposed on many Central Banks to convert their notes, no longer into gold coin, but into either gold bullion or foreign gold exchange at their option. Thus we may expect not only that all gold available for currency purposes will be employed henceforward in the reserves of a Central Bank as a basis for currency but that the Central Bank will be freed from the danger of an internal drain. Its primary duty indeed remains to maintain the value of its notes at par with gold, but it fulfils it, not by its obligation to change them into gold coin, but by freely shipping gold bullion or selling foreign gold balances to maintain the par value of its exchange. The sole use of a gold reserve to-day is, therefore, to enable a country to meet deficits in its international balance of payments, until the appropriate measures can be taken to bring it again to equilibrium. This being the case, it is paradoxical that, in the numerous cases where countries have since the War re-established or established for the first time the gold or gold exchange standard, the consequent legislation has almost always expressed the total reserves of gold or foreign gold exchange as a definite percentage of the Central Bank's *notes* outstanding (plus in several cases its sight liabilities). Such a basis has no meaning except in so far as the resulting size of the reserve represents by a coincidence the maximum probable export strain on the particular country in question in respect of a temporary disequilibrium in its balance of payments. It is quite clear, if we take for instance the United States and France, that this is not so in their cases and that their holdings of gold now far exceed any conceivable export strain to which they might be exposed. Moreover, the proportional gold reserve system forces an exceptionally drastic restriction of credit as soon as the reserve approaches the legal minimum and therefore impels Central Banks to keep their reserves well above the legal limit. For this reason alone, therefore, greater freedom for the Central Banks in the use of their reserves is very desirable.

289. Under this heading, we strongly agree, therefore, with the general purport of the recommendations of the Gold Delegation of the Financial Committee of the League of Nations in their Second Interim Report. We hope that the following principles will be adopted by Central Banks generally :—

(i) All gold standard countries should agree that they will not allow gold to pass into active circulation, whether in the form of coins or of gold certificates;

(ii) Central Banks should give collective consideration from time to time to the question whether it would be in the general interest that the legal requirements in force in different

countries as to gold reserves should be relaxed or tightened up, and should undertake to use their influence with their Governments to secure changes along the lines indicated, so far as is compatible with their domestic situations. At the present time it is probably desirable that the legal requirements as to the gold reserves of Central Banks should be relaxed;

(iii) Central Banks should be permitted by the laws of their respective countries to reckon balances with the Central Banks of other gold standard countries, or with the Bank for International Settlements, as the equivalent of gold for all the purposes of the law. This would be a merely optional and permissive provision and would not force the discretion of any Central Bank;

(iv) There is also a further principle of central banking of a somewhat different character which must be observed if Central Banks are to be in complete control of the situation, namely, that Central Banks must not be unduly limited in their power to expand their deposits otherwise than against a corresponding increase in their holdings of gold or the equivalent of gold. Such undue limitation may result if the class of assets which the Central Bank is entitled to hold is too narrowly prescribed by law. Similarly, it should lie within the power of a Central Bank to restrict the volume of its deposits otherwise than by decreasing its holdings of gold.

290. With these provisions it should, we think, be within the power of the Central Banks collectively for some time to come, if not indefinitely, to ensure that the available quantity of monetary gold would not operate as a limitation on the use of a wise discretion as to the volume of currency and bank credit to be created by the gold standard countries as a whole. Whether the gold factor would or would not operate in fact as a drag on the price level must, of course, depend on the way in which individual Central Banks were working the system, whether they were accumulating gold reserves greatly in excess of legal requirements, and on how far they were availing themselves of the power to hold part of their reserves as foreign balances. But this would be equally true whatever—within wide limits—might be the current supplies of gold. We hold, therefore, that the current and prospective supplies of new gold from the mines need not necessarily prevent the international gold standard from functioning successfully.

291. On the other hand, we think it very important that the above recommendations should be carried into effect. For otherwise, we fear—although, as we have explained, we do not regard the limited quantity of the supply of new gold as the main explanation of the present depression—that many Central Banks, being

anxious concerning the adequacy of their gold reserves, will be in constant danger of nipping off a revival of confidence, of causing a premature reaction in activity, and of ultimately dragging down prices or keeping them down below the level which we have indicated as desirable. Without these changes, as well as others to be mentioned below, the international gold standard will be capable of functioning to the disadvantage of the world as a whole and will lack that element of durability which is in itself an important requisite of a currency system.

3. POST-WAR CHANGES IN GOLD STANDARD.

292. But even if gold itself were eliminated as a cause of instability through being in scarce or excessive supply, and if Central Banks were to be given greater freedom than now in the use of their reserves, are we justified in supposing that comparative stability of international prices can be achieved by a wise and concerted policy on the part of the Central Banks? It has to be remembered that it is the essence of an international standard that it causes all countries adhering to it to become, so to speak, a single "magnetic field". Disturbances in one country are almost necessarily transmitted to the others, the severity of the disturbance being in proportion to the economic weight and strength of the country in which it originates. Therefore all gold standard countries, and particularly all important ones, are vitally interested in each other's stability. Particularly if any country in a dominating position pursues a course which may appear to suit its interests, but is inconsistent with the maintenance of stability in the rest of the world, much damage is done certainly to the latter and probably in the end to the former also.

293. Serious instability of price movements and interest rates is, moreover, a great obstacle to the smooth flow of capital from the creditor to the debtor countries, more being lent at times of great investment activity than the latter can properly use productively, and in the subsequent reaction the flow being completely stopped. It is not always the lending countries, however, who are at fault. It is by no means unusual for borrowing countries to borrow unwisely—in too great amounts and unproductively. Borrowing brings about an inflation of demand, rising prices, profits and all the usual appearances of prosperity. This leads the borrowing country to borrow more and the lending country to be willing to lend, until the real excessive burden on the former is revealed either by an internal reaction or by a cessation or diminution of lending, both leading to reversal of the former prosperity.

294. So great in the past ten years have been the reactions of disturbances in one country on conditions in another that, if we were to take this period as a fair criterion, it would be necessary to

conclude that the power of the Central Banks by their joint and several efforts to secure stability carried a very little way. The Federal Reserve System of the United States has endeavoured to keep that country on an even keel since the War and yet, even if we ignore the violent movements of the immediate post-war period, it has been unable to prevent one of the greatest oscillations of boom and collapse in history. Again the Bank of England has aimed for some years to bring about an equilibrium between this country's conditions and world conditions, but, while prices have fallen, costs have remained rigid and the desired equilibrium has not been attained. The Bank of France, restricted by legal enactments, was unable to prevent its vaults being filled with many millions of gold which it did not want.

295. Nevertheless the violent movements of the post-war period are no doubt exceptional and, while we cannot hope that they are yet at an end, we may reasonably look for a gradual improvement. As we have pointed out in paragraphs 245-6, the re-entry of a number of countries into the gold standard, some under the influence of deflation and others under the influence of inflation, produced anomalies which are not likely to appear in anything like so acute a form under the normal operation of the gold standard. If these anticipations are well founded, it may be asked whether the aim of Central Bank policy should not be to return to the more automatic working of the gold standard of pre-war days, when, as it is supposed, the Central Bank's discount rate was raised more or less as a matter of course when gold went out and lowered when gold came in. In fact, however, the automatic operation of the gold standard even then was more or less limited to the sphere of the Bank of England and was satisfactory in its results only because London was then by far the most powerful financial centre in the world, had "sight" claims on the rest of the world much greater than those of the world on her, and could thus by the operation of her bank rate almost immediately adjust her reserve position. Other countries had, therefore, in the main to adjust their conditions to hers. But post-war conditions are widely different. In the first place, New York has risen to be an exceedingly powerful monetary centre with as strong a pull on the gold resources of the world as London. In the second place, the liquid resources held by foreigners at both monetary centres are enormously greater than they were before the War (the aggregate amounts in London and New York alone are about £1,000,000,000), partly as a result of the French inflation and stabilisation, partly owing to widespread lack of confidence, and partly owing to the development of the gold exchange standard. Not only is the liability thus imposed on these centres great, but movements of gold may take place on a considerable scale which are due, not to any fundamental disequilibrium of prices or other deep-seated conditions, but merely to temporary causes for which a change

in bank rate may not be a suitable remedy. The gold exchange standard itself, whatever its merits in economising gold, has added considerably to the complexity of the gold standard system. In the third place, both the Federal Reserve Bank of New York and the Bank of England have developed very considerably the "open-market" system which has been found in certain respects extremely effective. It is in itself, however, the antithesis of an automatic system. Thus, we believe, all Central Banks are faced with the necessity of a greater "management" of their currency systems, involving inevitably greater responsibilities and also a more urgent need of co-operation.

4. OBSTACLES FACING CENTRAL BANKS.

296. In this task of management, the Central Banks are faced with three main classes of difficulties:—

- (i) Non-monetary causes of instability;
- (ii) Possible divergences between the interests of their own country and those of the world outside;
- (iii) Inadequate control over the monetary machine and its working.

297.—(i) We have already referred in this Report to many non-monetary causes of disturbance, such as political troubles, war debts, seasonal variations, over-production in some direction or other, changes in tariffs, the collapse of the silver exchange, large changes in fashion and in demand, embarrassments caused by budget deficits or over-borrowing by Governments, rigidity of internal economic conditions, and lack of confidence resulting from all these; such causes for instance as many of those with which the Commonwealth Bank of Australia or the Banco do Brasil has been faced. These are all conditions which must hamper and may nullify any effective control by a Central Bank.

298.—(ii) Probably the most important difficulty is the apparent, and sometimes the real, divergence between the immediate domestic interests of a particular country and those of the world as a whole. Whilst we should not deny the possibility of a real temporary divergence, we think that this would be the exception, not the rule, and that such apparent divergences of interest would generally prove to be illusory or avoidable if fully understood.

Take, for example, the position of France in 1930. It might have been supposed that France, largely free at that time from unemployment or other symptoms of industrial crisis, might have had interests divergent from most of the rest of the world, which was in the throes of an acute phase of the slump. It may indeed have been the case that an expansion of credit, such as was probably desirable elsewhere, was undesirable in France.

Nevertheless it was clearly in France's interest not to attract gold from abroad in excess of what the Bank of France really wanted. For the influx of gold was calculated to produce three sets of consequences detrimental to French interests :—

(a) It was likely to cause an unwanted expansion of credit within France ;

(b) It was likely to injure the French export trade by lowering foreign prices relatively to French prices and contracting the volume of demand ;

(c) It was likely to have a seriously disturbing effect on the stability of the existing settlements of war debts.

It follows, as M. Moret, the Governor of the Bank of France, has pointed out in his review of the year 1930, that there was no way to harmonise the interests of France and those of the rest of the world except by an increase in French foreign investment at long-term, corresponding to the increase in France's foreign favourable balance in excess of her desire for imports whether in the form of commodities or of gold. M. Moret declared that the solution could only be found by encouraging foreign loans by France at long-term, that this would be a good policy for France, and that the troubles in 1930 were due to reforms with this object in view having failed for a variety of reasons to be very effective. We think that this is the right explanation, so that there was no real divergence in this case between national and international interests.

More generally, when a situation occurs—as it well may—where the circumstances of a particular country make it desirable that there should be some temporary contraction of domestic credit at a time when there is no such necessity in the world at large, it is by no means inevitable that a disharmony of interest should arise. For in such a case the last thing desired by the country contracting credit is to attract short-term funds from abroad or to put pressure on the gold reserves of the rest of the world. An influx of gold, quite apart from any embarrassment it may cause to other Central Banks, would merely hamper and nullify the efforts of the Bank receiving the gold to control inflationary tendencies at home. Moreover, the influx of short-term foreign balances under the influence of a temporary attraction is, and should always be regarded as, the equivalent of a *negative* gold reserve and consequently as a potential source of future weakness. If this is recognised, there exists, we suggest, a way to avoid mutual embarrassment, namely, that the Central Bank which is contracting credit should offset the international effect of this by increasing its own foreign short-term assets. There would probably be a limit to the scale on which it would care to do this ; but a moderate operation on these lines might be sufficient in normal circumstances, provided that steps had been

taken in good time. This assumes that the Central Bank in question would be in the possession of a sufficient volume of assets disposable in the domestic market to be able to reduce the aggregate volume of credit to a degree adequate to its purpose and at the same time to replace a part of its existing assets by foreign balances or bills. But in any case the possibility of its being able to control its domestic situation must depend on its possession of adequate "ammunition" for the contraction of credit on the requisite scale.

In the more normal case where a Central Bank is contracting domestic credit in order to bring its local conditions into line with international conditions and so avoid a prospective loss of gold, the particular difficulty with which we have been trying to deal would not, of course, arise.

299.—(iii) But, even if there need be no real divergence of interest, a Central Bank may not possess over its own monetary system a control adequate to prevent a wide departure from stability. As we have already explained (para. 71), the control of the Bank of England over the amount of bank money in London within the limitations of an international standard is remarkably complete. But this is not equally the case elsewhere. The control of the Federal Reserve authorities over the creation of bank money in the United States, or its equivalent in the shape of direct loans to the call-market, is not as automatic, with the result that the Federal Reserve system has great inflationary and also great deflationary possibilities. Nor has either the Bank of France or the Reichsbank a control equal to that of the Bank of England.

Moreover, even if a Central Bank can control the amount of bank money and credit, it cannot easily control their uses or determine the purposes to which they shall be put. For the use to which bank credit is put the Central Bank must rely very largely on the commercial banks and other financial institutions. Furthermore, if expansion or contraction of credit leading to rising or falling prices has once gathered momentum, the capacity of a Central Bank to check it, certainly to check the contraction, becomes much more difficult, and the same volume of credit in a period of great activity has an effect on the price level quite different from that which it has during a period of depression.

300. Added to all these problems is the question as to the degree of stability which should be aimed at. We have said that the ultimate aim should be stability of the international price level, meaning by this the composite price at wholesale of the principal food-stuffs and raw materials entering into international trade as measured by the best-known wholesale index numbers. Difficult problems will no doubt arise as to whether any particular fall in prices is due to a greater ease or efficiency of production and different views may be taken as to whether such changes should be

counteracted by monetary influences. The general price level, for instance, might fall because of a heavy fall in the price of one commodity, e.g., wheat or cotton. Are Central Banks to attempt to counteract this influence by a general rise in other prices? We do not think it necessary to give a dogmatic answer to such questions. What can emphatically be said is, that instability of prices is a serious evil, that monetary influences on prices are more controllable than any other, and that the Central Banks should therefore so control such monetary influences as to favour stability rather than instability.

5. CENTRAL BANK CONTROL OVER THE VOLUME AND TERMS OF BANK CREDIT.

301. The method by which the Central Banks must attempt to achieve their aim of maintaining stability of the international price level over long and short periods is through their control of the volume and terms of bank credit. It is when we approach the questions relating to the control of credit, the causes of the Credit or Trade Cycle, and the alternations of prosperity and depression, that we reach some of the most fundamental and difficult problems in economic theory and practice, on which there still exists among experts very considerable difference of opinion. With these we do not intend to deal at length. But this should not be taken to mean that we do not regard them as of the greatest importance. When practical bankers and business men can explain clearly the causes of the Trade Cycle, why prosperity is followed by depression, and depression by prosperity, and can find practical means to avoid the economic waste caused thereby, and when they can adjust more satisfactorily the powers of the modern world to consume and absorb wealth with its powers to produce wealth, they will have more justification than they now have in ignoring and treating as of little or no consequence economic research into these very difficult but vitally important problems. The practical man is satisfied to make profits when the sun shines, and to bear his losses when the bad times come, regarding these alternations more or less as laws of nature, when very often they are due to the working of the monetary machine and are to some extent at any rate under human control. But, if they are even partly under human control, it is of the utmost importance for the betterment of humanity and the stability of society that such methods of control as may exist should be worked out and put into practice, even if, as is and will remain true, there exist no simple scientific rules by the mere application of which such control can be exercised. The management of currency and credit is essentially an art and not a science.

302. In this connection we quote Governor Strong's evidence before the Stabilisation Committee of Congress in 1926 :—“ There is no magic formula that can be introduced into the Federal Reserve

Act to control prices I have discussed these matters with many economists and students of prices and purposely have always carried the discussion through the same course. We have agreed on the record of the past in the Federal Reserve system pretty generally, as to what has been done and the effect of what has been done. We have generally agreed as to the conditions at the present moment. . . . But, when I ask them, ' Now, we have got to decide something to-day ; you are in the position of running in the Federal Reserve system ; what are you going to do to-day that will have an influence on the future ? ' the answer is always the same. ' Well, you are the practical fellows who are running this ; you have got to decide that. ' And that is the difficulty. Our examination of the past produces the most accurate knowledge of past action and re-action, but when it comes to a decision as to what we are going to do for the future, then just human judgment has got to govern. There is no mathematical formula for the administration of the Federal Reserve system or the regulation of prices."

303. The function of a Central Bank should be to regulate the volume and price of bank credit, i.e., " short " credit, so as to maintain output and employment at the maximum compatible with adherence to the international gold standard and with maintenance of the stability of the international price level. Credit is essentially unstable. Credit conditions which tend to generate a rise in prices, lead, if uncontrolled, to still higher prices, and, when the re-action commences, falling prices produce in themselves a further fall. The Credit Cycle in fact on which so much economic research has been expended seems to be the effect of monetary conditions upon human psychology. If we take the depth of a depression, we find easy money, idle balances, but no confidence, and, therefore, reduced investment and reduced output. In time, shortage of stocks, or a fall in the rate of interest, or some other cause, will bring increased demand for goods of some kind or another ; after a period of such increased demand prices will rise ; output and investment will increase, and consequently purchasing power ; the improvement will spread from one industry to another, restoring confidence ; with the increase in profits the readiness to embark on capital outlay will increase. Meanwhile the growth in employment and wages will have increased purchasing power still further and may in time bring actual rises in wages. As the process continues, capital issues become greater and greater until, finally, the new investments in buildings and fixed plant are no longer able to yield the rate of interest or profit upon which their optimistic promoters had been reckoning. At the same time, just when enterprise is beginning to yield less, the over-extension of banking credit will cause an increase in interest rates, and the pressure on the banking system for short-term advances will bring about a certain restriction of credit. Moreover, unless an equivalent rise

in prices is taking place elsewhere, the country's balance of payments may be affected, gold may be exported and pressure on the Central Bank's reserves lead to further restrictions.

304. We have attempted this very inadequate account in order to show that the problem of a Central Bank must be, not only to watch the short-money market, the gold movements and the pressure on the exchange and conditions abroad, but also the internal price level, the unemployment figures and the capital market. Control of credit conditions is always easier before a boom has commenced in earnest. When that has once happened, to prevent its development to a stage ultimately leading to a reaction, and to prevent the reaction running its full course, are both difficult. Yet a Central Bank, if it attempts to curb an upward movement, may and will be criticised for cutting short the country's nascent prosperity. Even when the recent American boom had grown to very great proportions, there was strenuous and widespread opposition in every quarter, even the most authoritative, to any attempt seriously to control it. To the difficulties of the control by a Central Bank of its own market must be added the additional difficulty of securing concerted action by several. Even if it were conceded that such concerted action would generally be effective if it were taken soon enough, it may be argued that it is not in fact practicable to detect and interpret the obscure premonitory signs of the financial weather soon enough or accurately enough, or with a high enough degree of probability, to procure concerted action amongst a number of independent authorities, each of which is likely to have its own ideas based on its local information and to maintain them with tenacity. Here again only time can show. There is no need to minimise the difficulty of the high enterprise which we should like to see the Central Banks of the world put in hand.

305. It is possible, indeed, to prescribe the objective of Central Bank policy. It is possible to suggest ways of increasing the means at the disposal of the Central Banks. But the use made of their discretionary power to vary the value of currency and credit, and the terms on which the latter is granted, must depend on experience and the daily exercise of prescience and a wide discretion. Any great measure of success, indeed, will only be reached as a result of a long process of experiment and evolution. At present, any deliberate effort at stability, however crude in its methods and partial in its success, would be a great improvement. It is sufficient for the time, therefore, to indicate the direction and objective of progress.

6. CONCLUSIONS.

306. We now venture to state our conclusions in summary form as follows :—

- (i) The aim of the Central Banks should be to maintain the stability of international prices both over long periods and

over short periods; i.e., they should both keep the average steady over a period of years and avoid fluctuations round this average from year to year.

(ii) The method of achieving this object should be so to regulate the volume and terms of bank credit as to maintain as much stability as possible in the rate of new investment and new enterprise generally, both at home and abroad. By these means alternate excesses of enthusiasm and depression might be avoided and the demand for the new output of the instruments of production and other forms of capital in the world at large kept in better equilibrium with the proportion of income which is currently available for such purposes—neither in excess nor in defect.

(iii) With this end in view the Central Banks should confer together at frequent intervals to decide whether the general tendency of their individual policies should be towards a relaxation or a tightening of the conditions of credit; and their bank rates and other instruments of credit control should then be adjusted accordingly, without prejudice to their policies relative to one another remaining at the free discretion of each separate institution. Nor should they be afraid of small and frequent changes. For otherwise action may be unduly deferred. Such small and frequent changes would also have the advantage of accustoming the public not to attach undue importance to every necessary adjustment. The Central Banks must be prepared to keep in constant touch with conditions, to make small changes in response to small indications, and to reverse the tendency with any noticeable change in the underlying facts.

(iv) This form of joint policy should be consistent with a full measure of autonomy for each national institution. In particular, each Central Bank should remain free to attract gold to itself whenever it *deliberately* desired to do so, without incurring blame or exciting complaint from the other Central Banks; to raise its own bank rate relatively to that of the others, even though this were contrary to an agreed general policy of reducing rates, if it deemed this to be necessary for the protection of its own gold position; and also to raise its own bank rate for the sake of checking inflationary tendencies at home, even if the tendencies abroad were of a contrary character.

(v) But each Central Bank should undertake to do its best to avoid the importation of unwanted and unnecessary gold merely as a result of leaving natural forces to work themselves out unchecked. It should be the duty of each Bank to avoid an unbalanced international position which was the result of accidental circumstances or the unintended repercussion abroad

of its domestic policy. In particular, if the effect abroad of a curtailment of credit, intended merely to counteract a domestic inflationary tendency, was unintentionally to attract gold, there is a presumption that this effect should be offset by the Central Bank in question being prepared to increase its own balances elsewhere.

(vi) In particular, Central Banks should consider the rate of long-term investment as well as short-term investment as falling within their purview, and should take whatever steps may lie within their power, and are suited to their local circumstances, to counteract any tendency which their own nationals may show either to keep their investible resources excessively liquid or to undertake excessive long-term commitments.

307. Doubtless experience and the natural course of evolution may suggest many modifications in, and additions to, this rough outline. But we have thought that it might serve to crystallise opinion and give aid towards a more coherent scheme of Central Bank collaboration than has existed hitherto, if we were to venture to go further than mere generalities as to the desirability of such collaboration.

II.—PROPOSALS TO MEET THE PRESENT EMERGENCY.

308. The previous section is mainly directed to more or less permanent methods for preserving economic and financial equilibrium internationally. We must now consider what special steps can be taken to escape from the existing position of acute disequilibrium.

309. Chapter IX provides an introduction to this section of our recommendations. We have there explained the difficulties which necessarily arise if the creditor nations as a whole are unwilling to lend to the debtor nations as a whole the surplus due from the latter to the former, after the former have taken all that they are disposed to take in the shape of goods. We think that the first measure towards the restoration of the international price level must necessarily be taken on the initiative of the creditor countries, and that it must consist partly in a greater willingness to buy and partly in a greater willingness to lend. The former will result from a revival of enterprise and investment within the creditor countries themselves; and the latter will permit an increase of purchasing power and a recovery of consumption, to the accompaniment of a revival of capital expansion, in the debtor countries.

310. Failing this the creditor countries will soon have sucked in all the gold available in the hands of the debtor countries and this may entail a series of defaults, preceded, in the effort to avoid such a dishonour, by a severe curtailment of credit and purchasing power attended by a low or falling price level.

311. How little margin there is left for a continuation of what has been happening during the last two years may be illustrated by the following table. The creditor countries comprise Great Britain, the United States, France, Belgium, Holland, Switzerland and Sweden. The debtor countries comprise the rest of the world except Spain and Russia which are included in neither class.

*Gold in Central Banks and Treasuries.**

	January 1st, 1929.		January 1st, 1930.		January 1st, 1931.	
	£ millions.	%	£ millions.	%	£ millions.	%
Creditor countries...	1,277	65	1,391	69.5	1,564	74.5
Debtor countries ...	680	35	610	30.5	531	25.5

* In this table the gold stocks held by Central Banks and Treasuries in 1929 and 1930 have been increased by £23 millions and £19 millions respectively in order to make the figures comparable, as during 1929 and 1930 gold was transferred from private banks in Australia to a total of about £23 millions.

312. Thus in two years the creditor countries have increased their proportion of the monetary gold in the world from two-thirds to three-quarters. The debtor countries probably require amongst them new loans from the creditor countries to an aggregate of not less than £400,000,000 per annum in normal circumstances, unless the creditor countries increase their imports relatively to their exports as compared with what they were before the commencement of the world depression. It appears, therefore, that the total gold stocks of the debtor countries would cover this sum for little more than a year. Moreover, much of the gold is held by those of the debtor countries which are least hard-pressed, and probably at least two-thirds of it is immobilised under the laws regulating their gold reserves. It is unlikely, therefore, that the debtor countries can continue much longer to square their international position by parting with gold at the rate of £70,000,000 a year, as they have been forced to do in the last two years.

313. The efforts of the debtor countries to meet their debts by contracting their imports and expanding their exports may even have the effect of worsening their position through its adverse effect on the prices of their exports. These figures emphasise the impossibility of the debtor countries as a whole meeting their obligations otherwise than out of new loans or by selling more goods at better prices. For the creditor countries to fail in taking steps to relieve this stringency would be exceedingly short-sighted having regard to their own creditor position.

314. It is, however, an important aggravation of the difficulties of solving this problem that it is not possible even for a creditor country to go far in the direction of increasing either its own buying or its own lending unless the other creditor countries are moving more or less in step. For if it does, the claims thus created against it will be used by the rest of the world not to buy more goods but to meet the demands of the other creditor countries. For this reason some measure of co-operation and consultation amongst the creditor countries is highly desirable. This means, in the main, a concerted policy between the Central Banks and issuing institutions of Great Britain, France and the United States.

315. The prospects of such a policy appear to be becoming much more favourable whilst we are preparing this Report. France, in particular, is making preparations for several important issues which are likely to be helpful to the general situation. It may be useful, however, that we should suggest briefly certain general principles of action. The most difficult task is likely to be to find borrowers of sufficient standing to give confidence to investors. We deal with this matter, therefore, rather more fully at the end of this chapter.

(i) The desirability of foreign loans being made by the leading creditor countries on a greater scale than in the past two years should be generally accepted.

(ii) It follows that the Central Banks and Treasuries of these countries should do everything that lies in their power, compatibly with the requirements of their own gold position, (a) to remove any legislative or administrative hindrances in the way of opening their financial markets to the reception of foreign loans, and (b) to permit a volume of domestic credit which will encourage the market to take full advantage of any foreign issues which they may think attractive.

(iii) It is not essential that the loans should be made to the weaker debtor countries. It is often better that such countries should be helped by improving the market for their exports than by enabling them to add to what may be already an excessive burden of indebtedness. A loan to *any* borrower who intends to employ it for increased real investment will, by raising the aggregate of buying power in the world, tend to raise both the prices of commodities and the volume which can be sold and thus to improve the trade balances of other countries. Indeed, a loan to a solvent borrower to finance new productive enterprise is a more radical remedy than a loan to a distress borrower to meet the demands of urgent creditors in respect of past transactions; for it will do much more to make the wheels of the world's commerce go round again.

(iv) It follows that it is not even essential that new loans should be foreign loans, provided that they are for the creation of new

capital assets (though the quantitative effect on the outside world of a loan of a given amount will not be so great if it is for domestic use). For construction programmes within creditor countries will tend to increase the imports of such countries relatively to their exports, and this will relieve the pressure on the debtor countries. If a creditor country is disinclined to lend its savings to a debtor country, then let it employ these savings at home. It is only to do *neither*, but to accumulate, or endeavour to accumulate, the surplus savings in gold, which serves to embarrass the debtor countries as a whole. We repeat that it is the simultaneous reluctance of creditor countries *either* to lend *or* to buy which is the cause of the crisis. If, for example, the value of the current building and construction in the United States to-day were as great as it was in 1928, the effect of this on the demand for primary commodities and on their prices would cause a large and immediate relaxation of pressure throughout the world. Similarly, the recent decline of the building and construction boom which had existed in France almost ever since the end of the War has much aggravated the effects of the reluctance of the French investor to lend abroad.

(v) It is for these reasons that Central Banks should favour a persistent and determined policy to maintain an abundance of cheap credit in their domestic money markets, sufficient both to satisfy the unusually large demands for liquid resources due to nervousness in the financial world and also to support any new productive enterprises coming forward. Very low rates of discount prevail, it is true, already, but have so far failed to bring about the transfer of money from short-term to long-term loans. The main practical obstacle which we see in the way of a resumption of long-term investment is the shortage of acceptable and willing borrowers for the purpose of new enterprise, due to the general unprofitableness of industry. The task is, therefore, a double one; partly to attract borrowers of unquestioned standing by a low rate of interest on long-term loans, partly to increase the supply of attractive loans. With the first end in view, Central Banks might use their influence to promote confidence in the duration of low short-term rates and to persuade the member banks of their system to reduce the rate of interest allowed on deposits, so as to discourage the public from withholding their resources from the investment market.

316. The greatest difficulty, however, which we foresee is the fulfilment of the second task, namely, to remedy the shortage of definitely sound borrowers for the purpose of new enterprise. The vicious circle is complete. The decline of new enterprise has reacted adversely on profits and prices, and the low level of profits and prices stands in the way of new enterprise. It is for this reason that some of us think that in the domestic field it may be necessary to invoke governmental enterprise to break the vicious circle. In the international field measures of an analogous kind

would have to take a somewhat different form. In this case also the vicious circle is complete. The unwillingness to lend, coupled with the frequently unwise use of borrowed funds, has destroyed the credit of borrowers, which reinforces the unwillingness to lend. In many cases, no single creditor is ready to take the risk which is absolutely required in the interest of creditors as a whole. It may be, therefore, that some form of guaranteed credit is required.

317. We believe that certain tentative enquiries have been made by those responsible with a view to discovering whether international action in these matters would meet with general assent. It may be that so far it would have been premature to summon an international conference. But as time passes by the readiness to seek a way out through organised international co-operation is likely to increase.

318. If, therefore, world public opinion was to become ripe, there would be advantages in a general international discussion on what might be described as "The Restoration of International Trade." In this event schemes might be considered for loans guaranteed by a joint fund to which borrowers would contribute a percentage of the sum borrowed in return for the guarantee, any ultimate deficiency on the fund being met by the guarantors.

319. A Government guarantee scheme is only one alternative, perhaps the simplest, although attended with certain dangers which we need not here elaborate. We know that other proposals with the same end in view have been under discussion by the financial authorities of the large creditor countries, such, for instance, as the creation of a private International Corporation with a large capital, partly paid, subscribed by all the big financial institutions in the centres concerned who are interested in foreign loans. Any scheme which meets the end we have in view has our sympathy.

CHAPTER III.—PROPOSALS RELATING TO DOMESTIC MONETARY POLICY.

1. THE NOTE ISSUE.

320. The function of the Bank of England which has been historically the chief concern of the legislature is the note issue. Amending Acts have been passed from time to time, but no change in principle has yet been made in the Act of 1844. The separation between the Issue Department and the Banking Department of the Bank of England and the peculiar form of the Bank's statutory return date from that Act. The Currency and Bank Notes Act of 1928 re-settled the amount of the fiduciary issue and introduced new provisions of elasticity for varying the amount of the fiduciary issue subject to certain conditions; but the principle of the fiduciary

issue was unaltered and its amount was merely adjusted to the existing position arising out of the amalgamation of the Treasury note issue with the Bank's note issue, and was not re-settled on the basis of a fundamental reconsideration of what might be appropriate in the new circumstances.

321. We think that the time has now come for a thorough review and reconsideration of the whole matter. We deal first with the principle of the fiduciary issue and secondly with the less important matter of the separation of the Departments, which is mainly a matter of form.

The Principle of the Fiduciary Issue.

322. The present system of a fixed fiduciary issue (cf. para. 53 et seq.) arose at a time when a large part of the business of the country was conducted by means of gold coins and bank notes, the system of payment by cheque being still imperfectly developed and gold coins and bank notes circulating alongside one another. There had been certain notorious occasions when the Bank of England had put an increased volume of bank notes into circulation, as a result of freely discounting bills, regardless of whether these notes were in substitution for gold or were a net addition to the monetary circulation. The reformers of 1844 thought it desirable to set a limit to the free discretion of the Bank in this respect by enacting that, beyond a fixed sum known as the fiduciary issue, the Bank of England should be prohibited from issuing additional notes except in substitution for gold coin by withdrawing an equal amount of the latter from circulation into the Bank's reserves. Long before 1914 the first stages of credit inflation had ceased to be marked by an increased issue of notes, inflation or deflation being initiated not by changes in the note circulation but by changes in the amount of the Bank's deposits. Nevertheless up to 1914, the old system retained some remaining trace of significance, inasmuch as gold and bank notes still circulated side by side in the country and were legally interchangeable. But with the exclusion of gold coins from the domestic circulation and the confirmation of this exclusion by the Gold Standard Act of 1925, the old system has lost almost entirely its original meaning.

323. In present day conditions when the active circulation of notes is mainly required for the purpose of meeting wage payments and small transactions usually settled in cash, an expansion in the active note issue is likely to be a result of active trade ensuing with an appreciable interval after an expansion in the Bank's deposits. Thus it is the latter which is now the factor of dominating importance, and the somewhat anomalous position arises that while the Bank is not regulated by law in respect of its deposits it remains so regulated in respect of the note issue which was a hundred years

ago the initiating cause of inflation but to-day is the factor which is the latest to be affected by the forces of expansion or contraction.

324. Since, however, the tendency of modern monetary management is, rightly we think, to confer upon the Central Bank increased powers of elasticity in meeting changing conditions, it should not be counted against the present system that it leaves to the Central Bank too great a power of varying the volume of deposits. The criticism to which the present system is open is rather that the principle of the fixed fiduciary issue is wrong in that it associates the amount of the gold which the Bank of England should hold immobilised and unavailable for export with the amount of the active note circulation. Formerly, when the Bank's gold was held for two purposes, partly to meet an external drain and partly to meet an internal drain, it may have been reasonable to earmark a substantial part of it for the latter purpose. But now that the second purpose has disappeared, and has in fact been abolished by law, so that the gold reserve of the Bank of England is held for no other purpose than to meet a foreign drain, the effect of enforcing the principle of the fiduciary issue is to forbid the Bank of England to use by far the greater part of its gold for the only purpose for which it is held or could be used. At present (April, 1931) the Bank holds about £145 millions in gold, at holiday seasons its note circulation rises to about £380 millions and the fiduciary issue is fixed at £260 millions. Thus £120 millions of the gold held by the Bank (the difference between the maximum circulation and the fiduciary issue) is immobilised and at certain times of the year only £25 millions is actually available. On this basis by far the greater part of the gold holding is immobilised when the note issue is at its seasonal maximum, an amount equivalent to about 30 per cent. of the note issue at those periods.

325. We cannot regard as satisfactory a system under which so high a proportion of the gold stock is locked up in such a way as not to be available for export if the Central Bank should so desire. The Act of 1928 indeed recognised the need for elasticity by empowering the Treasury, on the application of the Bank of England, to enlarge the amount of the fiduciary issue for a limited period of time. During the passage of the Bill a statement was made on behalf of the Government, with the concurrence of the Bank, illustrative of the circumstances in which the authority would be exercised. The main points of the statement are shown in the following extracts* :—

“ Clause 8 of the Bill makes a statutory provision intended to be used, not reluctantly and with hesitation in time of crisis, but whenever the Governor of the Bank feels that the present limit on the fiduciary limit is unduly restrictive, to be used, not in defiance of the law, but in

* Hansard, 14th May, 1928, Cols. 744-746.

accordance with the statutory provisions intended for the purpose. . . . We are replacing an illegality by a legal power intended to be used, not in a crisis, but before the crisis arrives. I do not pretend to be able to forecast every contingency which may cause the Governor of the Bank to make the application, and which may make the Chancellor of the Exchequer of the day agree to an increase in the fiduciary issue; but let me examine some of the possible eventualities. . . . An emergency of the type of the crises of 1847, 1857 and 1866 may never recur. Just as in 1847 and 1866 the knowledge that the letter had been issued to the Bank prevented a run upon the Bank, so the provision made in Clause 8 may itself prevent the panic from which these crises arose.

"But a new kind of emergency has become possible. Now that the foreign banks have adopted the practice of accumulating a large reserve of sterling bills, it is always possible that, owing to a change in policy upon the part of those banks, a large sum of gold might be withdrawn in a short time by the realisation of those balances. The probability is that such a measure would be avoided by co-operation amongst the central banks, as was indeed advised in the Genoa resolutions. But if the withdrawal of gold was insisted upon, it might become necessary to extend the fiduciary issue, and that would be an occasion which would justify the Governor of the Bank in asking for that expansion, and the Treasury in granting it.

"A third contingency is the possible competition for gold among the central banks. . . . Should the Bank of England find that, owing to a world demand for gold, credit would be unduly restricted, not as a check on speculation, but to the injury of legitimate requirements, then the Bank can request the Treasury to extend the fiduciary issue and so free gold in the hands of the Bank for further credit operations.

"Moreover, the principle of a fixed fiduciary issue itself necessitates some provision being made for normal growth. It was only by an accidental combination of circumstances that the Act of 1844 did not require an expansion of the fiduciary issue from time to time. . . .

"The provision in the Bill for increase in the fiduciary issue is not intended therefore to be a mere legislative substitute for the crisis letter. On the contrary, it is intended to be used not in a crisis but before it and to prevent undue stringency arising from any of the causes I have mentioned."

326. We think, nevertheless, that as a normal means of providing elasticity, in conjunction with a gold position such as that disclosed in the foregoing paragraphs, the arrangement of the Act of 1928 is open to substantial criticism. With a relatively small free balance of gold, circumstances might well arise that were yet far from emergency conditions, in which it was desirable to let gold flow freely from the country without affecting credit conditions here. It might even be desirable to increase the amount of gold available for export well in advance of this being absolutely required. Yet it seems to us that an approach by the Bank of England to the Treasury for permission to increase the fiduciary issue would be interpreted as a sign of weakness and be the occasion of nervousness at a time when the opposite effect on sentiment was to be desired. While we see no objection to the provisions of the Act of 1928 as the means of meeting a real emergency, we think that their use in relatively normal circumstances is likely to give rise

to great misunderstanding of the position and we believe that it would be preferable that the Bank should have control over a much larger proportion of the total gold stock without calling in aid these provisions. If the object of the fixed fiduciary issue is to tie up the Bank of England, well and good. This may be inadvisable but it is intelligible. But if its object is not to fetter the Bank but merely to require it to make a public declaration of what will be interpreted as weakness, at the most inadvisable moment for creating such an impression, the disadvantages of liberty and of regulation are, it seems to us, heaped on one another.

327. As regards the right principles for regulating gold reserves in the changed circumstances of to-day, we may, without entering into a long argument, summarise our views very briefly as follows :—

(i) If it is thought unnecessary to fetter the discretion of the Bank of England in regard to the volume of its deposits, which in a modern system is the significant and operative factor, there can be no good reason for fettering very narrowly its power to issue notes.

(ii) There are great advantages in a high degree of mobility for the gold reserves of Central Banks. For the task of reconciling international exchange stability with domestic credit stability will be made easier if the Central Bank is free on occasion to allow wider fluctuations in the proportion of its total assets which is made up of gold and comparable items. It is also desirable that the public should become accustomed not to attach undue importance to fluctuations which the Bank has deliberately permitted.

(iii) In present circumstances it is highly desirable that throughout the world the disadvantages of the immobility of gold, and of laws whereby a very high proportion of the world's total stock of gold is rendered sterile, should be modified, and we should not maintain any legislation which conflicts with this aim.

(iv) Nevertheless, it is not unreasonable to regard some part of a country's gold reserve as not belonging to the Central Bank's *masse de manœuvre* for normal daily use, but as an ultimate reserve, not to be brought into consideration in ordinary cases, but kept as a last resort for use only on grave national occasions and after special deliberation between the Government and the Bank. Such a reservation can be justified both by its effect on confidence and in itself.

(v) The proper amount of this ultimate reserve cannot be reached as a fixed proportion of the note circulation (which is the usual principle abroad) or as the excess of the note circulation over a fixed figure (which is the principle of the British fiduciary issue). For it depends on quite different factors from those which determine the note issue. A change, for

example, in the habits of the public in paying by note or by cheque respectively cannot affect the appropriate amount of the gold which we hold against emergencies.

(vi) Just as the amount of gold held by the Bank should be settled independently of the volume of the note issue, so any precautionary limits which it may be thought advisable to set to the Bank's power of note issue should be settled independently of the amount of gold which it is required to hold. The best form of limitation on the discretion of the Bank of England in regard to the volume of its note issue, is, we think, the system which prevailed in France for many years before the War, namely, an absolute maximum subject to modification from time to time by law or by Treasury Minute.

328. We consider, therefore, that the best means of regulating the note issue and the gold reserves of the Bank of England would be the following :—

(a) That Parliament should give the Bank of England power to put into circulation notes to an amount exceeding by a moderate figure what has been found by experience to be the normal note circulation. Thus if we take the seasonal maximum of the present note circulation (exclusive of notes in the Banking Department) at £380,000,000, the absolute maximum beyond which the Bank of England must not go might be set at £400,000,000, this figure being subject to modification by law from time to time. Provision should also be made for additional temporary elasticity by permission of the Treasury on application by the Bank of England similar to the provision in the Act of 1928.

(b) That the Bank of England should by law not be permitted to allow its gold reserve to fall below (say) £75,000,000, except temporarily by permission of the Treasury in accordance (again) with a procedure similar to that laid down in the Act of 1928. In proposing this figure as a *statutory* minimum we do not contemplate that the Bank of England would actually allow its gold to fall so low in any ordinary circumstances.

The Bank of England would thus be given greater freedom for the handling of all normal day to day problems, whilst it would be required, as at present, to confer with the Treasury and obtain its assent whenever highly exceptional circumstances might require some further temporary measures of elasticity.

329. We should add at once, to prevent misunderstanding, that we are not in favour of a reduction in the Bank of England's normal stock of gold. So far from this being the case, we recommend in para. 354 below that the Bank's normal holdings of gold or its equivalent in foreign exchange should, in view of the

large liability of London as an international banking centre, be larger than they have been in recent years. What we envisage therefore in the future is a Bank of England with both increased resources and greater freedom. It is necessary, however, to say that freedom and willingness, if occasion requires, to export gold in considerable amounts presupposes power also to draw it back from abroad in case of need. This again presupposes that this country maintains a sound position in respect both to its Government finances and its balance of payments.

The Separation of the Departments.

330. We now turn to the secondary question whether the existing separation between the Issue Department and the Banking Department of the Bank of England should be continued. This peculiar provision arose out of long-dead controversies which we need not revive; for the reasons which originally led to the separation of the departments have no interest or relevance to-day.

331. The only solid reason, apart from the advantages of continuity and the dislike of changing ancient forms, has been of a different character, namely, that the separation of the Issue Department has provided a convenient formula for dividing the profits of the Bank of England between the Treasury and the Bank itself. This division might of course have been made in a different way and is so made in other countries. But the British system is as follows. Broadly speaking the profits of the note issue belong to the Treasury and the remaining profits belong to the Bank of England; and the segregation of certain assets in the Issue Department allows of the profits of the note issue being calculated, after deduction of certain expenses, by means of the actual net profit earned by these segregated assets taking into account not only the interest earned but also capital appreciation or depreciation. This peculiar arrangement has the effect, however, of making the share of profits accruing to the Treasury depend, not (as might perhaps have been expected) on the volume of notes in circulation or on the earning assets of the Bank, but on the fixed amount of the fiduciary issue. Thus the Treasury share of the profits does not depend on the variable element in the note issue, but only on the earnings of such assets, fixed in amount (at present £260,000,000), as the Bank may choose to set against the fiduciary issue. If, however, it is desirable to calculate the Treasury's share of the profits in this way, it is not necessary to have the paraphernalia of the Issue Department for the purpose. The same formula could be used without a separation of the departments.

332. But in fact, as we have mentioned, the amount of the fiduciary issue is not absolutely fixed. It can be altered by Treasury Minute (as explained in para. 59), subject to certain limitations of time, on the application of the Bank of England. Now if the

fiduciary issue is increased, this has the effect under the present arrangement, other things being equal, of increasing the share of profits which accrues to the Treasury and of diminishing the share which accrues to the Bank of England. This appears to us to confuse in a highly disadvantageous way two matters which ought to be kept separate.

333. Witnesses from the Treasury and from the Bank of England have defended the existing system, on the ground that, if and when the fiduciary issue were to be increased, other things would not be equal. For they presume that this step would not be taken unless the Bank was losing gold and was replacing this gold by earning assets, in which case it is reasonable that the income from these additional earning assets should be assigned to the Treasury. They also told us that even if an increase in the fiduciary issue were to affect adversely the Bank's share of profits, this would have no influence on the Bank in reaching a decision whether or not to apply for such an increase.

334. This seems to us to overlook two considerations. In the first place, if the existing system were retained, it would be a mistake if the Bank were never to apply for an increase of the fiduciary issue except when it had actually lost or was about to lose gold to the full amount of the proposed increase. In the second place, even if the Bank had lost an amount of gold equal to the increase in the fiduciary issue, it does not follow that it would have wholly replaced this gold by earning assets; for the loss of gold ought sometimes to be allowed to have its direct effect of curtailing credit.

335. Thus the separation of the Departments has not, in our opinion led to a satisfactory formula for fixing the Bank's payment to the Treasury. A precautionary increase of the fiduciary issue by no more than £25,000,000 might under the present system reduce the Bank's profits for the time being at the rate of £1,000,000 per annum; and even though the Bank might be entirely indifferent to a loss of this magnitude, it is not reasonable that a necessary piece of public policy should have this arbitrary and perhaps embarrassing consequence.

336. On more general grounds we see no advantage in the separation of the departments. It is confusing and misleading to anyone who is not an expert. In particular the Bank's so-called "reserve" and its so-called "proportion" have quite different meanings from those attaching to these terms elsewhere and lend themselves to erroneous comparisons with other institutions and to an under-rating of the real strength of the Bank of England. It is inconceivable that anyone settling the matter afresh to-day would devise the present form of statutory return. Moreover, if our recommendations made above for the future regulation of the note issue and the gold reserves are adopted, the separation of the departments must necessarily come to an end.

337. We recommend, therefore, that the payment by the Bank to the Treasury should be fixed, as is in effect the case at present, by setting aside the net earnings of certain securities, but that these should not necessarily be of the value of £260,000,000. We suggest that the amount of securities so set aside should vary with the average amount over yearly periods of the excess of the Bank's notes and deposits over its stock of gold and of silver coin. This would protect the Bank from the risk of large variations in its profits arising out of fluctuations, due to considerations of public policy, in the respective proportions of its gold and its earning assets. Without such a provision the Bank might find itself seriously embarrassed on some future occasion if its stock of gold were to rise to a high level without a corresponding expansion of its notes and deposits.

338. We recommend further that the form of the Bank's statutory weekly return should be amended by the amalgamation of the statements relating to the two departments, so that the consolidated Bank return (taking for illustration the actual amounts in round figures for April 29, 1931) would appear as follows:—

	£		£
Proprietors' Capital	14,500,000	Government Securities	274,000,000
Rest	3,500,000	Discounts and Advances	7,000,000
Public Deposits ...	17,000,000	Other Securities	39,000,000
Bankers' Deposits ...	49,000,000	Silver Coin	4,000,000
Other Deposits ...	37,000,000	Gold	147,000,000
Notes in Circulation	350,000,000		
	<hr/>		<hr/>
	£471,000,000		£471,000,000
	<hr/>		<hr/>

339. The above scheme, which recognises the independence of the note issue and the gold reserve and gets away from the false suggestion that the appropriate volume of the note circulation is closely bound up with the amount of gold in the vaults of the Bank, seems to us to be the best.

340. Not only is this the best system for this country. We also attach great importance to it as a first step towards dissociating in the world at large the question of the right level of a country's gold reserve from the question of regulating the note issue. If the view could be generally accepted that gold reserves to-day are held solely to meet temporary deficiencies in the balance of international payments, and if their amounts were determined by what was reasonably necessary for this purpose, this would be the greatest safeguard we can imagine against the risks of a future shortage in the supplies of gold relative to the natural growth of the world's money-income.

341. There is a further matter, though not of fundamental significance, to which we think it desirable to call attention. It seems that a substantial proportion of the "notes in circulation" are not in fact in active circulation at all but are held, many of them

year in and year out, in the safes of the joint stock banks, which are in the habit of holding a much larger proportion of their cash reserves in the form of actual bank notes, instead of as deposits with the Bank of England, than is required by them as till-money.

342. This practice is doubtless due to historical causes. The large quantity of bank notes held by the joint stock banks is a survival from other times, when notes played a much larger proportionate part in making payments, when the banks were much smaller and less able, therefore, to average requirements over a wide area, when communications were slower, and when periodic runs on country banks were still a lively memory. Since large quantities of notes are now held continuously in the vaults of the head offices, it is evident that they are no longer needed for their former purpose. But there has been no incentive to the banks to change their habits, since neither Bank of England notes nor Bank of England deposits earn interest, so that it is a matter of indifference to the banks in which form their cash reserves are held, provided that they have enough bank notes to provide till-money and enough Bank of England deposits to provide for the clearing.

343. The total quantity of bank notes thus held by the English clearing banks has amounted recently to about £105,000,000 and has been steady round about this figure. This represents about 6 per cent. of their deposits. We understand that a smaller quantity of bank notes would be fully enough to provide the banks with till-money. If the Bank of England were to increase the facilities for obtaining notes at short notice, when required, by establishing depots in various parts of the country, some 4 per cent. of their deposits might be sufficient. This would enable the clearing banks to pay up to (say) £40,000,000 in bank notes into the Bank of England, and to increase their deposits with the Bank of England to an equal extent, without any inconvenience to themselves. We may mention that the Federal Reserve System of the United States has recognised the desirability of the member banks keeping their legal reserves in the shape of deposits with the Central Institution, and not in bank notes, by providing that only the former reckon towards a member bank's reserve requirements, till-money being for this purpose excluded.

344. If the banks were to do this, the effect would be to decrease the active note circulation by a corresponding amount and to increase the bankers' deposits with the Bank of England by the same figure. Incidentally it would mean that the present artificially inflated figures of note circulation would be reduced to an amount which corresponded to the notes actually in circulation, so that the Bank return would present a truer picture of the situation. At present the possession of these surplus notes gives the banks a certain influence over the state of the Bank of England's

return, which they may value—though it is not one which, in our opinion, they ought to have. For it enables them to affect the Bank of England's published "reserve" and "proportion" within quite wide limits, according as they choose from time to time to exchange deposits at the Bank of England for notes and *vice versa*. Changes of this kind are, at present, a most disturbing feature of the Bank's return; for it is impossible to know whether changes in the notes taken out represent a real increase in the circulation or merely a manoeuvre on the part of some joint stock bank. This fact reinforces the desirability of the change of principle which we recommend above, since after this change has been made it will make no significant difference whether the clearing banks hold notes or Bank of England deposits. But for the same reason it will make it a matter of indifference to the clearing banks themselves how they hold their reserves and thus remove any reason for reluctance which they might otherwise have felt in falling in with our suggestion to pay in notes.

345. If this proposal were adopted, it should be for consideration whether the maximum figure for the note issue should not be fixed at some lower figure than £400,000,000. Its adoption would also, it is true, greatly mitigate the practical evils of continuing the present fixed fiduciary system; indeed it might in effect give the Bank of England more latitude than our own proposals. But it would not meet the point of principle or achieve the important object of separating explicitly the question of gold reserves from the question of note issue. It would merely provide a means of rendering the existing system of regulation a dead-letter, without establishing any right principle in its place.

346. Finally, we think that it would point the right road to further progress if some provision were made, in the event of other Central Banks accepting a similar provision, for balances with the Bank for International Settlements to be allowed, at the discretion of the Bank of England, to reckon for all purposes of the law as the equivalent of gold. This provision might be of the highest value in the future course of the evolution of international banking and would provide an important precedent in the development of methods of international banking practice for the economy of gold. In the event of the Bank for International Settlements failing to develop along the lines which would make it advisable for use to be made of this discretionary power, the Bank of England would, of course, be free to make no use of it. In any case this suggestion is not directed to the immediate situation, but is, rather, a matter for consideration in connection with long-distance monetary policy.

2. THE RESOURCES OF THE BANK OF ENGLAND.

347. The outstanding characteristic of the London money and investment markets has been the comparatively small amount of the resources of the Central Institution in relation to the vast amount

of the international financial business transacted in the City. So far from this being anything new, it carries on the traditional pre-war system. This pre-war system depended on the extreme liquidity of London's claims on the rest of the world. In 1913 the sterling bill was the foundation of the system; a large part of the outstanding volume of such bills represented acceptances on behalf of foreign clients; and consequently any measures taken by the Bank of England to curtail the volume of sterling bills resulted within a few weeks in the maturing of claims by London on the rest of the world. The Bank of England chose, therefore, mainly to depend on its power to contract the volume of acceptances by its control of the money market, and was content, having this power, to economise in the amount of its other liquid resources.

348. The Bank of England still has this power in an uncommon degree and can still afford to place great dependence upon it. But relatively to the growth of other factors, its efficacy is less than it was. It is advisable, therefore, to review the position in the light of the facts and figures of to-day.

349. We pick out the following elements as deserving particular notice :—

(i) The figures given in Appendix I show that the volume of sterling acceptances on behalf of overseas clients has fluctuated widely in the course of the last four years, varying between a minimum of £123,000,000 in June, 1927, and a maximum of £203,000,000 in June, 1929.* But these figures are dwarfed by the Treasury Bills in the market, which is a new feature since the War, the amount of these Bills, outside Government Departments and the Issue Department of the Bank of England, fluctuating during the same period between £472,000,000 and £525,000,000. Moreover, since the War an acceptance market in New York has been organised on a considerable scale. Dollar acceptances on foreign account have fluctuated in the four years 1927-30 between £107,000,000 and £200,000,000.†

(ii) It has been explained to us that there is some connection between the volume of sterling acceptances for foreign clients outstanding at any time and the volume of bills and deposits held in London on foreign account. Consequently, fluctuations in the volume of sterling acceptances outstanding are partly offset by corresponding fluctuations in the volume of bills and deposits held in London on foreign account. Thus, the maximum fluctuation in the excess of such bills and deposits over sterling acceptances on foreign account is less than the maximum fluctuation in either of these elements taken separately, being no more than £50,000,000 in the course of the four years for which we have statistics.

* Taking half-yearly dates.
 † Taking end of the year dates.

(iii) Before the War London's short-term position with the rest of the world was probably well balanced. To-day her gross liabilities for foreign short-term bills and deposits are largely in excess of her claims in respect of her acceptances. (Account cannot be taken of our deposits abroad since figures are not available.) This is mainly due (as is also the case in New York) to the magnitude of the abnormal French deposits held in London and to the growing practice on the part of Central Banks and other banks abroad of holding a large portion of their liquid resources in this way. This may be expressed by saying that London is now practising international deposit banking, as distinct from international acceptance business and the deposits associated with this, on a larger scale than before the War.

(iv) There is a new feature, closely associated with (iii) above, which is at the same time a convenience and a danger. Not only is London conducting a larger business than formerly as a depository of international liquid funds, but so also—and on a still greater scale—is New York. This means that there is a substantial quantity of such funds ready to move from one money market to another, according to the attractions of the rate offered. It follows that changes in the short-term rate of interest in London relative to New York are even more potent than before the War in regulating the *net* position of our international balance sheet. Perhaps they are too potent, for part of the relief comes in a different, and less desirable, way than formerly. A rise in discount rates in the pre-war money market functioned mainly by calling in our claims on the rest of the world through the contraction in the volume of our acceptances. A rise in discount rates to-day is more liable to function in part by increasing our liabilities to the rest of the world through the attraction of short-term funds from abroad. Thus, the ease with which we can for a time meet claims on us by attracting precarious short-term deposits, while it is certainly a great convenience, may also be a danger unless we avail ourselves of it only with the greatest moderation and prudence.

(v) The volume of foreign long-term financing which is ready to offer itself in London, provided that terms can be arranged, is much greater than it used to be relatively to the annual surplus which we have available for this purpose. This applies not only to the new issue market, but also to the large volume of so-called "international" stock exchange securities which find a ready market in, and move easily between, different international centres of finance. In particular, foreign government bonds and the like which are issued in New York in the first instance are subsequently almost as likely to find a home here as in the United States. Moreover, our annual surplus for new long-term foreign investment is not only smaller absolutely than it used to be, but is also smaller relatively to our total annual savings and to the scale of the market and is subject to sharp fluctuations, amounting to as

much as £100,000,000, according to the estimates of the Board of Trade (see Appendix IV), between one year and the next.

350. All this may be summed up by saying that there is much more risk than there used to be of our financing long-term investment by means of attracting short-term foreign funds of a precarious character, and thus gradually slipping into a less liquid position than is desirable. This may result in our having to maintain short-term rates over a long period at a level inappropriate to domestic requirements in order to retain the precarious foreign funds which we have inadvisedly employed in a non-liquid way.

351. Or we may put it thus. Before the War our liquid international assets mainly consisted of the Bank of England's gold and our sterling acceptances on foreign account. These were believed to be, as a rule, at least equal to and sometimes substantially in excess of our short-term international liabilities. To-day we have greatly increased the latter as a result of the development of our functions as a depository of international short-term funds, whilst the former have not been increased correspondingly, with the result that our liabilities may be as much as double our liquid assets, reckoning these as made up of our acceptances and our surplus gold hitherto available for export. Regarded in this way our total position is much less liquid than formerly, whilst the use of our traditional balancing factor, namely bank rate, may operate as much by increasing our short-term liabilities as by calling in our short-term assets. To these latter should, of course, be added our deposits abroad held at short notice, for which we have no figures, but even so we believe the position to-day to be less liquid than before the War.

352. Our conclusion is that the Bank of England's liquid assets ought to be increased at the first opportunity to a substantially higher figure and maintained thereafter at this higher figure as the normal. At the same time we should be prepared to see without concern very wide fluctuations in the aggregate of these assets. We think that the instrument of bank rate should be used sparingly when the objective is merely to balance moderate changes in the short-term position by attracting foreign funds and not to affect the domestic situation. Bank rate is rightly used when the Bank of England deliberately desires to contract credit either at home or in the world at large. Its use is of much more doubtful utility when there is no desire on the part of the Bank to contract credit either here or abroad, the main point of maintaining a high bank rate being to attract foreign funds. The temporary contingencies which the attraction of foreign funds is intended to meet would often be better met in the opposite way, that is to say, by the Bank relinquishing its own liquid assets rather than by borrowing liquid assets from abroad. This course would not only be more prudent, but it would be much more effective in circumstances in which, apart from the exigencies of the short-term position, the wish of the Bank would be to relax credit conditions in the world at large

rather than to contract them. For rising rates in London must have a tendency to contract credit everywhere, whereas if London were both in a position to release gold and other liquid assets and willing to do so, it would have a precisely opposite tendency—which is what will be desired in the circumstances assumed.

353. For these reasons we consider that the pre-war system in this country under which only relatively small fluctuations in the gold reserve of the Bank of England were permitted, and bank rate was operated with this end in view, needs to be supplemented to-day. We think that in the modern world, having regard to the scale of international operations and the size of other money markets, the Bank of England should feel itself free to see, without anxiety, very large fluctuations in its own liquid assets between their minimum and their maximum. The magnitude of London's international operations to-day requires, that is to say, that the normal level of the Bank of England's liquid international assets should be materially higher than it now is, that these liquid assets should exist to be used at not infrequent intervals, and that money markets at home and abroad should be made accustomed to view these fluctuations as a sign of strength and as a part of the Bank's regular machinery for the control of credit. We consider that at present the disparity between London's liquid resources and those of other large international countries is too great and should be diminished.

354. The recommendations which we have made above regarding the fiduciary issue would have the effect of releasing for this purpose a larger proportion of the gold already held than is available at present. But this would not be enough by itself. It would enable the Bank's stock of gold to fluctuate between extremes of (say) £175,000,000 and £100,000,000. But for the Bank to raise its stock of gold above the former figure might be undesirable unless the present pressure on the supply of gold becomes relaxed or other Central Banks become content with a smaller normal figure for their own gold reserves. Thus it would seem advisable for the Bank to supplement its gold reserves by liquid funds held abroad either in other important financial centres or perhaps with the Bank for International Settlements if that institution evolves in a manner suitable to this purpose. We suggest, therefore, that in addition to gold reserves fluctuating between (say) £100,000,000 and £175,000,000, the Bank might maintain other foreign liquid resources fluctuating in amount up to £50,000,000. A part of these foreign resources might belong to the securities allocated against the note issue. But even so some increase in the total resources of the Bank of England might be required. We make a proposal bearing on this in paragraph 370 below.

355. We must emphasise, however, that there is one important corollary to the freer use of its liquid resources by the Bank of England based on normal holdings of an increased amount. The

Bank must not be tempted into meeting by exports of gold an adverse position of a character for which bank rate and a contraction of credit is the appropriate remedy. The exchanges may prove adverse to us either on account of a trade or investment expansion at home of an inflationary character or on account of the movement of capital items resulting from the performance of our functions as a centre of international finance. We recommend an increase in the Bank's resources and a free use of these increased resources in appropriate circumstances, because our business of international banking on a great scale may prove incompatible with the reasonable stability of domestic business and enterprise if we cannot afford to allow a movement of even ten per cent. in our liquid international liabilities without taking steps most upsetting and sometimes highly injurious to our domestic trade. But it must not be inferred from this that we are in favour of any hesitation in the use of bank rate and credit contraction when the immediate problem of management is to check boom conditions or rising prices at home and is not primarily concerned with movements of foreign capital.

3. THE DAY-TO-DAY POLICY OF THE BANK OF ENGLAND.

356. The chief means at the disposal of the Bank of England for the management of the monetary system are the following :—

- (1) The official bank rate.
- (2) " Open-market " operations (or the deliberate refraining from them) which, after taking account of the changes, if any, in the Bank's gold reserves and in the Public Deposits, have the effect of changing the aggregate amount of the Bank's Private Deposits.
- (3) " Open-market " operations which consist in changing the form of the Bank's assets without changing their quantity. This may take any of three forms :—
 - (i) The Bank may offset movements of gold by buying or selling securities;
 - (ii) The Bank may sell short-dated securities (e.g. Treasury Bills), and at the same time buy long-dated securities (e.g. Consols);
 - (iii) The Bank may force the market to discount or obtain advances on the official terms, with the object of bringing market rates into closer conformity with these, by selling securities (which might be regarded as a variant of (2) above).
- (4) There are certain technical devices for directly influencing the foreign exchanges, namely, sales or purchases of foreign balances (i.e. so-called " gold exchange " methods), dealings in forward exchange, and small variations in the Bank's buying price for gold.
- (5) The use of the Bank's personal influence over, or advice to, prominent elements in the money market.

357. Of these (1) was the traditional instrument, upon which chief emphasis was laid in all pre-war accounts of the Bank's methods. We have explained in paragraph 352 above our reasons for thinking that this instrument should be used sparingly for temporary adjustments of the international balance of payments and should be mainly reserved for occasions when the Bank deliberately wishes to contract or to expand credit either at home or in the world at large. We have also indicated in paragraph 221 the difficulties which arise in employing the instrument of bank rate when the ultimate requirement is to secure a substantial reduction in the general level of money-incomes. But between these extremes of purely temporary adjustments at the one end and exceptional long-period adjustments at the other, there are many contingencies for dealing with which the instrument of bank rate as traditionally employed by the Bank of England is excellently suited—in particular the control of the Credit Cycle and the regulation of the rate of slow, normal change in the level of money-incomes so as to maintain conformity between money-incomes at home and abroad.

358. Since the War method (2) has been greatly developed and perhaps plays the major part in the case of the smaller day-to-day movements, as contrasted with larger changes. We think that the evolution of the Bank of England's methods in the direction of a greater reliance on the habitual use of open-market operations has been wisely conceived and should be developed further. There are, however, two respects in which the Bank of England's position for the effective use of this method might be strengthened. Hitherto the Bank has had no accurate information as to the quantity of cash held by the clearing banks, whereas it is the aggregate of these banks' cash and Bank of England deposits which determines the amount of credit which they create; nor has the Bank had accurate information as to the division of the deposits of the clearing banks between current accounts and fixed deposits, whereas a change in the volume of credit produces different consequences according as it corresponds to an increase in current accounts or in fixed deposits. The volume of the bankers' deposits with the Bank of England (taken in conjunction with their holdings of bank notes which, as may be seen from Table I in Appendix I, have been remarkably steady) is the main determinant of the volume of domestic credit, and the question of the right amount of these deposits, from week to week as circumstances change, should, we think, be a main pre-occupation of the Bank of England. As appears from Sir Ernest Harvey's evidence, this is, in fact, one of the matters to which the Bank pays attention. But judging from the average amount of these deposits quarter by quarter in recent years (cf. the table in para. 167), we are not clear whether enough allowance has always been made for changing circumstances. On the other hand, the fluctuations of the bankers' deposits at the Bank of England over shorter periods

may be, from the clearing banks' point of view, more frequent and more unpredictable than they would be if the Bank were to depend for its management of the market rate of discount day by day less on restricting or expanding the banks' cash and more on direct co-operation with the banks and on the substitution of one kind of asset for another within the Bank of England's own resources. The Bank of England's difficult task of regulation may, we hope, be made a little easier by the adoption of some of our other proposals, in particular those for an increase of the detailed information at the disposal of the Bank, for a more precise understanding as to the cash reserves maintained by the clearing banks, and for a closer collaboration between these banks and the Bank of England.

359. Method (3) has doubtless been employed by the Bank from time to time, especially in cases (i) and (iii). But deliberate exchanges between the Bank's holdings of long-dated and of short-dated securities respectively, with the object of influencing the margin between the market rate of interest on the two types of securities, may not have played in the past as important a part in regulating the rate of investment as they might. We think that the policy of bringing to bear such influence as the Bank may possess for widening or narrowing the margin between long-term and short-term rates of interest in different sets of circumstances, with a view to encouraging fixed investment or liquidity as the case may be, should be frequently considered and should sometimes form the basis of action. Very often the Bank may be able to bring to bear all the influence which it needs to exercise on the long-term rate of interest by operating on the short-term rate, which has usually been considered its more direct concern. But occasions may arise when this will not be sufficient.

360. The methods which we have grouped together under (4) have played no great part hitherto in the Bank's scheme of control. We have already proposed above (para. 354) that "gold-exchange" methods might properly play a greater part to-day than formerly, and have recommended that the Bank should increase its interest in international liquid assets other than gold. We have also had before us proposals relating to the forward exchanges and to a widening of the gold points with a view to increasing the power of influencing the movement of foreign funds through changes in the margin between the spot and forward rates of foreign exchange. These are matters of detailed technique which the Bank of England will no doubt be ready to consider; but they lie somewhat beyond our own competence and we make no recommendation.

361. We come finally to method (5), that is to say to the Bank's personal influence over the other elements in the money market. These elements fall into four groups:—(a) the Money Market proper; (b) the Issuing Houses and the Accepting Houses; (c) the great Clearing Banks.

362. The contact between the Bank of England and the money market proper is adequately close and successful. The practice of frequent meetings between representatives of the Bank and the leading bill brokers by which the wishes and intentions of the Bank are confidentially communicated to the latter needs no improvement.

363. The contact between the Bank and the leading issuing houses is also intimate. We understand that important foreign issues made by these houses are seldom underwritten in London unless the Governor of the Bank of England has been first consulted and that any opinion he may offer will carry great weight. The weakness of this control arises in a different way. It is partly due to the possibility, and often the probability, that foreign bond issues may be made elsewhere and then or subsequently be to a large extent re-offered in London.

364. Coming to the third group, the great clearing banks, we think that there might with advantage be closer contact between them and the Bank of England. Our suggestions on this head follow in the next section.

4. THE RELATIONS OF THE BANK OF ENGLAND WITH THE JOINT STOCK BANKS.

365. In the United¹ States the member banks of the Federal Reserve System are required by law to maintain balances with their Reserve Bank bearing a specified relation to their deposits. Their till money is not allowed to reckon for this purpose. The proportion of reserves to deposits actually held depends on the division of the member banks' deposits between demand deposits and time deposits. But in practice it has worked out in recent years at a percentage between 7 and 9 of the deposits, in addition to till money of about 2 per cent., making in practice about 9.5 per cent. altogether.

366. In Great Britain there are no legal requirements. But for some time past, subject to one exceptional movement, the actual practice of the ten London clearing banks has not changed. They publish monthly figures of reserves in cash and at the Bank of England which up to 1927 averaged 11.7 per cent. of their deposits and now (owing to a change of practice on the part of the Midland Bank which used to keep a higher reserve than the other banks) average about 10.8 per cent. The interpretation of this figure is subject, however, to the two observations following.

367. The banks have not distinguished in their published statements between their holdings of Bank of England (or Treasury) notes and their deposits with the Bank of England. They have,

however, furnished us with separate figures for these two items, which may be summarised as follows :—

*(Annual averages of monthly figures omitting June and December.)**

—	Cash in hand (£ 000).	Per Cent. of Deposits.	Balance with Bank of England (£ 000).	Per Cent. of Deposits.
1919 ...	110,733	7·5	86,915	5·9
1920 ...	105,567	6·2	74,855	4·4
1921 ...	111,216	6·4	90,741	5·2
1922 ...	108,744	6·4	88,395	5·2
1923 ...	104,604	6·5	83,333	5·2
1924 ...	103,714	6·4	83,640	5·2
1925 ...	104,448	6·5	81,209	5·1
1926 ...	103,786	6·5	80,715	5·0
1927 ...	106,067	6·4	78,746	4·8
1928 ...	105,011	6·2	77,877	4·6
1929 ...	105,067	6·1	76,934	4·4
1930 ...	103,880	6·0	78,362	4·5

* These months are omitted because of the exceptional half-yearly window-dressing operations which are discussed later.

368. Thus of the total ratio of 10·5 per cent. here shown only 4·5 per cent. is held in the form of balances with the Bank of England. As we have already indicated in paragraph 79 the latter figure is, however, not quite what it appears to be. The monthly figures published by the clearing banks are not true daily averages but are averages of one selected day in each week of the month. It seems that, in order to present a better appearance, most of the banks concerned are at pains to manipulate their balances with the Bank of England on the selected day of the week so that they stand at a higher figure than usual. Moreover, each of the four biggest institutions pursuing these practices selects a different day of the week for the purpose, calling in loans from the money market on its own selected day, but returning them next morning in time for the next big bank to call them for its making-up day. Thus a certain part of the published reserves of the clearing banks in the shape of deposits with the Bank of England is like a stage army, the same liquid resources doing duty four times over in the course of each week. At the end of each half-year the same practice, euphemistically known as "window-dressing," is followed on a grander scale. On these occasions other banks which only publish figures at these dates also make a brave show in their balance-sheets with deposits at the Bank of England, which they temporarily acquire for the purpose. The net result is that the average Bank of England balances of the clearing

banks are less than 3.5 per cent. of their deposits (perhaps not more than 3 per cent.) and those of the banks of the country as a whole less than 3 per cent.

369. We have made some attempt to estimate the magnitude of this practice. A comparison of the balances with the Bank of England as published by the clearing banks with the bankers' balances (which include other accounts besides those of the clearing banks) as published weekly by the Bank of England suggests that the monthly "window-dressing" has the effect of increasing the apparent cash reserves of the clearing banks by at least £20,000,000 over the true average figure. In the case of the end-year window-dressing the aggregate deposits with the Bank of England offered by the banks of the country as a temporary display on December 31st—the only figures with which most of them supply their shareholders and their customers—appear to be about £75,000,000 in excess of the figure normally held.

370. We are not aware that these practices serve any useful purpose. We think that they are not creditable to our banking system; and we recommend that they should be given up at once. Our recommendations on this and allied matters are as follows:—

(1) The monthly statements now published by the clearing banks are the result of pressure put upon them 40 years ago by Mr. Goschen, then Chancellor of the Exchequer. Certain recommendations for changes were made subsequently by the Cunliffe Committee, but only one bank (Lloyds Bank) has adopted them in full. Their form is not now as useful as it could be and is capable of certain improvements. We recommend that the banks should be asked to publish their statements in future in the form set out in Chapter V which substantially corresponds with the form in which, at our request, they have kindly furnished us with their figures for recent years.

(2) In these monthly statements the returns made of the cash in hand and of the balances with the Bank of England should be true daily averages.

(3) We have shown above that the reserves now published by the clearing banks are, omitting June and December, about 10.5 per cent. of their deposits, made up of 6 per cent. in Bank of England notes and 4.5 per cent. in balances with the Bank of England. We recommend that the London clearing banks should aim at the maintenance on the daily average of each three-monthly period of an amount of cash in bank notes and balances with the Bank of England of not less than 10 per cent. of their deposits.

(4) For banks other than the London clearing banks, we have not available the statistical information necessary to make a definite recommendation as to their cash balances. Under present arrangements they often need to hold balances with their clearing agents, but we do not know the terms upon which such balances are held.

We think it possible that machinery could be devised under which these balances would be held at the Bank of England and operated upon by the clearing agents. The position of the Scottish banks is, moreover, complicated by the arrangements in connection with their note issues. We think, however, that the banks other than the clearing banks should aim at the maintenance on the daily average of each three-monthly period of an amount of cash in bank notes and balances with the Bank of England of a given percentage of their deposits and we recommend that the appropriate percentage should be arrived at in each case after consultation with the Bank of England.

These proposals would probably involve some increase in the amount of reserves held by the banks, so that it would place on them a small additional burden. It needs, therefore, to be justified in the public interest. In a modern banking system, where member banks are in a position to hold earning assets which can be quickly turned into cash at the Central Institution, indirectly as in Great Britain or directly as in most other countries, the amount of reserves which they require strictly for their own safety and convenience may be extremely small. Since their reserves earn no interest, there will, therefore, be a tendency to whittle them down gradually by one means or another to the lowest figure which will not disturb public opinion. Moreover the main reason for expecting the banks to keep reserves above the minimum needed for daily convenience is no longer primarily the safety and solvency of the banks themselves, as it was in former times, but the necessity for providing the Central Institution with adequate resources wherewith to manage the monetary system and safely furnish the member institutions with precisely those conveniences, for rapidly liquidating earning assets, upon which the latter depend when determining the amount of their cash reserves. Thus the appropriate amount of the reserves of the member banks cannot now be left to their own individual self-interest but must be governed by the proper requirements of the system as a whole.

In a country such as France, where bank notes still play a very important part, the resources held by the Central Bank against the note issue may be fully adequate to its requirements and the question of the balances held with the Central Bank by its member banks may be a matter of comparatively small importance. But in countries such as Great Britain and the United States, where the great bulk of the business of the country has come to be transacted by cheques, this is not the case. The substantial question before us is, therefore, the adequacy of the resources of the Bank of England for all possible contingencies.

We have already expressed the opinion that the resources of the Bank of England ought to be augmented with a view to increasing both the amount of its own liquid reserves and the amount of its earning assets available for various types of open-market operations.

Since 1913 there has grown up in the United States their great Federal Reserve System with aggregate deposits more than three times the banking deposits of this country. Against these deposits, reserves approximating $7\frac{1}{2}$ per cent. must, in practice, be maintained with the Federal Reserve Banks, which also have the advantage of resources held against a substantial note issue. As a result the average deposits held in 1930 by the member institutions with the Central Institution in the United States and in Great Britain respectively compare as follows :—

				£
United States	...	...	...	488,000,000
Great Britain	...	...	...	65,000,000

This disparity is far greater than that of the magnitude of the two banking systems or of their international responsibilities. We feel that it has only to be stated in order to carry the conviction that our leading banks should be expected to contribute somewhat more to the strength of the Central Institution. Some small proportion of the revenues of our banks could be spent in no better way than in thus strengthening our monetary system at its foundations. For the quantities which were appropriate to pre-war conditions are no longer in scale for a country which intends to maintain its position as one of the chief financial centres of the modern world.

(5) The adoption of these recommendations would provide some increase in the resources of the Bank of England. But it would not, we think, provide a sufficient increase in view of the considerations which we have urged above. We suggest, therefore, that the Bank of England should consider an appropriate increase in the amount of its capital.

(6) We think that there might sometimes be an advantage in allowing a slight elasticity on the initiative of the Bank of England in the reserves recommended above for the joint stock banks. That is to say, the power to relax or tighten up this figure might be a useful addition to the Bank of England's means for effecting a relaxation or contraction of credit. We make the suggestion, therefore, that as to a variation within certain narrow limits, the banks should accept the advice of the Bank of England as to the average figure at which they should keep their reserve balances—the Bank indicating to them from time to time the advisability of a change (which probably should be quite small on any one occasion). The advantage of this technique, as compared with open-market operations, would lie in the fact that the Bank of England is somewhat narrowly limited by custom in the classes of securities which it can buy or sell, whereas the effect of an alteration in the reserve proportions of the joint stock banks could be spread over the whole of the assets of those banks.

Whatever ratio of reserves be fixed as suitable, it is in any event most important that it should be rigidly adhered to by the banks. For the power of the Bank of England to control the aggregate volume of credit in the country by means of open-market operations and other measures essentially depends on the rigidity of this ratio.

(7) We have carefully considered whether our recommendations as to the cash reserves to be maintained by the banks should be given statutory effect or whether they should be left to the good-will of the banks concerned. We think that there are substantial advantages in the traditional procedure of this country by which our banks are not subjected to any special legislation. It would be preferable, therefore, that these recommendations should be carried into substantial effect by agreement between the Bank of England and the banks concerned. All the matters in question are perfectly susceptible of settlement by agreement since those who would be the parties to such an agreement are responsible and substantial concerns and few in number. We should hope, therefore, not to find any serious difficulty in the way of such a solution.

371. There remains the question whether any improvement or extension is possible in the present system of consultation and co-operation between the Bank of England and the large clearing banks. The evidence which we have received has given us the impression that these relations might with advantage be somewhat closer than they now are. It is a result of causes originating in the now distant past that there is still a degree of aloofness and remoteness in the daily relations between the Bank of England and the clearing banks which does not exist, for example, between the Bank of England and the merchant banks, the leading issuing and accepting houses, and the bill-brokers.

372. This is a matter upon which it is, of course, impossible to make precise recommendations. But we suggest for the consideration of those concerned that it might be extremely useful if there were frequent and regular meetings between representatives of the Bank of England and of the clearing banks, at which opinions would be exchanged in a free and intimate manner, the clearing banks taken into the confidence of the Bank of England to a greater degree than seems to be the case at present, and their co-operation invited with a view to making the policy of the Bank of England fully effective.

373. Perhaps we may usefully give a few examples of the sort of cases we have in mind where such co-operation might be useful. The joint stock banks play a much greater direct part than formerly in attracting foreign deposits to this country, since they accept such

deposits at rates of interest which do not always bear the same relation to the market rate of discount. It is well that there should be a harmony between their policy in this regard and the wishes of the Bank of England. Again, we consider that the rates allowed by the clearing banks on fixed deposits should not always be determined as at present but sometimes with a view to influencing the public to be more or less willing, as the varying circumstances may require, to employ their savings in less liquid forms.

374. Above all, it is desirable that the clearing banks should be made aware in the plainest possible manner whether the general tendency of the policy of the Bank of England at any time is towards a relaxation or towards a contraction of the conditions of domestic credit. At present a small expansion by the Bank of England in the basis of credit may be employed by the clearing banks in the bill market in a way which may weaken the foreign exchanges, merely because of their uncertainty whether the small expansion which they have observed represents definite intention or is merely an accidental reflection of other forces and will probably be reversed soon afterwards.

CHAPTER IV.—PROPOSALS RELATING TO THE CAPITAL MARKET FOR HOME INVESTMENT.

375. Each great financial centre has its own characteristics. But the City of London can still claim to be the most highly organised international market for money in the world. Its freedom and elasticity are without parallel. Its accepting houses and its discount market provide unequalled facilities for the financing of national and international commerce; whilst the former, in their capacity as issuing houses, play a large part in the placing of international issues of a long-term character. Lastly the great British joint stock banks have the pre-eminent merit that their financial strength and liquidity are beyond any question. It may be that we are too far removed in this country from the days of great banking failures and panics, and the ruin following from the destruction of confidence, to esteem at its proper worth the enormous value of an impregnable banking system.

376. It is noteworthy, however, that, speaking generally, the exceptional merits of the City of London lie in the facilities given by the short-term money market for the employment of home or foreign funds; in the financing of trade and commerce, also both home and foreign; and in the issue of foreign bonds, as distinguished from the financing of British industry. The combined facilities offered by the accepting houses and the discount market have for very many years been made use of by bankers, merchants and traders throughout the world; they have been equally available

to, and have in fact been largely made use of by British merchants and traders. In so far as these facilities have not been even more largely made use of by the latter, the reason must lie in the fact that they have been able to find all the credit they wanted as cheaply or even more cheaply from the joint stock banks themselves. But the relations between the British financial world and British industry, as distinct from British commerce, have never been so close as between German finance and German industry or between American finance and American industry.

377. For the peculiar characteristics of the London money market we must look naturally to its history. England has always been a great commercial and trading as well as a great industrial nation; commerce in fact preceded industry. It was in London that this commerce centred and London was the great entrepôt for trade between the Continent and the rest of the world. London's financial organisation adapted itself to the needs of this world-wide commerce and it was there that the great private merchant banking houses settled and flourished. On the other hand, when British industry began its great growth in the nineteenth century, there was no particular reason why it should look to the London market for its financial requirements. Industry in those days was, so far as each unit was concerned, on a comparatively small scale; its basis was in the main a family basis, as the names of many of the great English businesses still show; its capital was provided privately and it was built up and extended out of profits; in so far as it required banking facilities, it found them from the independent banks, often family banks, which in general had their headquarters in the provinces, and particularly in the Midlands and the North, where the new industries flourished. Moreover, there had existed for many years in this country a large class of investors with means to invest, who exercised an independent judgment as to what to invest in, and did not rely as in some countries entirely on their bankers. Industry therefore, though making full use of the ordinary banking facilities offered by the joint stock banks, maintained its independence of any financial control.

378. In Europe, particularly in Germany, there has been a different relationship between banks and industries, and bankers have been forced to associate themselves more closely with industrial development. This is not because industrialists there were more ready than in England to share the control of their businesses with bankers or financiers, or that bankers would not, conditions being otherwise, have willingly adopted the attitude of their English confrères. It arose rather out of the necessities of the situation—from the scarcity of capital and of independent investors. Industry started later in these countries than with us. In order to compete with us, it required more help than it could obtain from its own private resources or from the public, whose power of investment was small, and the banks were driven to assist industry

to obtain permanent as well as short-dated capital. Accepting these heavy responsibilities, they were obliged to keep in more intimate touch with and maintain a more continuous watch over the industries with which they had allied themselves than were the English banks. The following quotations from the evidence given to us by Dr. Goldschmidt indicate in broad outline the German system :—

“ It should never be forgotten that Germany owes the great industrial development of the sixties, the nineties and the first decade of this century in a large measure to what one may well describe as this ‘ entrepreneur ’ spirit in banking. . . . The relationship between a bank and an industrial or trading company commences with the latter’s foundation. Scarcely a single important company in Germany has been founded without the collaboration of a bank. Whether it is a case of converting a private firm into a limited company, or of exploiting a new invention by establishing a new enterprise, the assistance of a bank is always invoked. The bank examines the situation and, when necessary, obtains reports from experts in the particular line. . . . If the bank, after examination, decides to found the company, it draws up the scheme of financing, determines the amount and the type of capital to be issued, and then, in some cases, itself takes a part of the shares into its security portfolio with the idea of issuing them at a later date. In this way the founding bank becomes at the same time the issuing bank, the latter functions beginning, however, only with the introduction of the shares to the Stock Exchange through the intermediary of the bank.” (*Statement of Evidence, paras. 5-6.*)

379. In France on the other hand, while investment capital was greater than in Germany, the individual investor was, speaking generally, a very small capitalist, unwilling to exercise an independent judgment. He therefore relied almost entirely on the investments suggested to him by the big banks which made practically all the industrial issues and thus assumed a measure of responsibility for them towards the public. The connection between banks and industry thus established, while less intimate than in Germany, was much closer than in England. In addition, in Paris, certain powerful banks developed a great and influential business, not as ordinary joint stock banks of deposit like the English banks, but as “ banques d’affaires ” more closely interested in industry and development of all kinds both at home and abroad.

380. In the United States conditions were again entirely different. But it was to the development of American industry in the widest sense that the financial world of New York devoted itself rather than to international finance. The great industries and the railroads were affiliated in general to particular banking

houses, and in the building up, and in particular in the merging, of most of the great American corporations, some house or bank has played a leading part, with the consequence that the relationship between them has usually remained a close and continuous one. It may be said that all industrial issues of well-known companies are sponsored by some responsible issuing institution; the smaller issues by smaller firms, the larger by large firms or large banks. In both cases it is common for a group of issuing institutions to combine in making the issue. In every case the names of the issuing institutions appear prominently on the prospectus, so that the public are left in no doubt as to who is sponsoring the issue. Taking this responsibility, the issuing institution naturally attempts to keep in close and continuous touch with the company after the issue. So far as the large banks in New York, Chicago and other centres are concerned, the issues in which they are interested are made usually through subsidiary Securities Companies. Moreover, the American banks are closely concerned with industry from another aspect. The banks lend either directly or through brokers very large amounts of money to investors and speculators against industrial securities of all kinds. The loans of this kind made by Reporting Member Banks are sometimes at least equal to the loans made direct by them to industry. For this reason also the banks take a great interest in the stock market and in the industrial securities quoted there.

381. Thus, under a different system, American banks, private and public, perform for American industry substantially the functions that German banks perform for German industry. The connection is a looser one; the number of banks competing is far greater; the problem of finding the necessary capital no doubt is much easier; and industry often needs banking assistance far less. Yet at the same time the American banks engage their issuing credit in the eyes of the public for the soundness of the issues they support, and this very fact leads, as it must always do, to a closer and more intimate association between banks and industry than where no such responsibility is assumed.

382. But, while this cursory account indicates—what indeed is a truism—that differing historical conditions have led to different developments in each country, it is necessary to consider much more closely what, under modern conditions, is likely to be the relationship between finance and industry most beneficial to the community at large, before we can judge whether there are any improvements which can be made in the case of this country.

383. Taking first the very broadest view over the modern world, we believe that in any community which wishes to keep in the van of progress the financial and industrial worlds should be closely integrated through appropriate organisations. Bankers, or financial leaders, who are in touch with the leaders of finance

in other countries, who have a thorough knowledge of the economic and financial conditions, not only of their own, but of other countries, and who are in a position to watch and to judge of the underlying changes taking place in those conditions, should be able, if they are in confidential and continuous relationship with industrialists, not only to supplement the information at the disposal of industrialists themselves but also to give aid of very great value in all financial problems.

384. Industry is yearly becoming more internationalised, and British industry, if it is not to be stranded in a back-water, will find institutions closely in touch with international finance invaluable in many ways as intermediaries. British companies in the iron and steel, electrical, and other industries must meet in the gate their great American and German competitors who are generally financially powerful and closely supported by banking and financial groups, with whom they have continuous relationships. British industry, without similar support, will undoubtedly be at a disadvantage. But such effective support cannot be obtained merely for a particular occasion. It can only be the result of intimate co-operation over years during which the financial interests get an insight into the problems and requirements of the industry in question and the industrial interests learn the value of the support which financial interests can give. The future development of British industry, particularly in the establishment of enterprises abroad, is greatly dependent on co-operation of this character, since a knowledge of foreign conditions, farsighted planning and large supplies of capital will be, or may be, all required. And in the realm of foreign investment it is primarily towards British-owned enterprises abroad that we should wish to see our energies and capital turned rather than merely towards subscribing to foreign Government and municipal loans, which absorb our available foreign balance while doing little for our industry and commerce. So far as heavy industry is concerned, we may find ourselves cut more and more out of the world if our competitors, advancing with combined and powerful industrial and financial resources, develop abroad one "tied" enterprise after another, or in the alternative purchase from us enterprises previously "tied" to us.

385. In the last few exceedingly difficult years it would have been of high value if the leaders, for instance, of the steel or ship-building or other industries had been working in the closest co-operation with powerful financial and banking institutions in the City with a view to their reconstitution on a profitable basis. The tasks still confronting us require great financial as well as industrial experience. It has been represented to us strongly in evidence that a great deal remains to be done in more than one important industry in overcoming sectional and individual opposition to

desirable amalgamations and reconstructions designed to eliminate waste and cheapen costs. It was stated to us that very important economies and much greater efficiency are possible if there are concerted movements to that end. We believe this to be the case and we believe also that these results can often only be obtained if there is some independent authority (such as a financial institution) able to review an industry as a whole from outside, to suggest plans of re-organisation, and to assist in the provision of finance. But industrialists on their side must be willing to co-operate. There are grounds for supposing that progress has been often very slow from the fact that the industrialists interested have not been ready themselves to take any wide view or recognise the enormous changes now taking place in the world and in methods of production. The greatest possible reduction of costs is particularly essential in our basic industries and in industries which are in competition with foreign countries since only by this means can their future be secured. We are not in a position to go into detail in this matter, but we desire to express a strong opinion that sectional interests should not be allowed to stand in the way of re-organisations which are in the national interest.

386. In a second direction we see advantages in a closer co-operation of industry and finance. It is all-important to the community that its savings should be invested in the most fruitful and generally useful enterprises offering at home. Yet, in general, the individual investor can hardly be supposed to have himself knowledge of much value either as to the profitable character or the security of what is offered to him. How easily he can be misled in times of speculative fever by glittering—even tawdry—appearances is proved by the experience of 1928, as the following striking figures will show.

In that year the total amount subscribed for capital issues whether of shares or debentures of 284 companies was £117,000,000. At 31st May, 1931, the total market value of these issues as far as ascertainable was £66,000,000 showing a loss of over £50,000,000 or about 47 per cent. In fact the public's loss has been greater since many of these shares were no doubt sold by the promoters at a high premium. Still more striking perhaps, 70 of the above companies have already been wound up and the capital of 36 others has no ascertainable value. The issues of these 106 companies during that year amounted to nearly £20,000,000.

387. That you cannot prevent a fool from his folly is no reason why you should not give a prudent man guidance. We believe that our financial machinery is definitely weak in that it fails to give clear guidance to the investor when appeals are made to him on behalf of home industry. When he is investing abroad he has the assistance of long-established issuing houses, whose reputation is world-wide. When subscriptions to a foreign issue are invited by means of a public prospectus, it is almost certain

that that issue will be vouched for by one of these issuing houses whose name will be evidence that it has been thoroughly examined and the interests of the investors protected as far as possible. For the issuing house's issuing credit, which can easily be affected, is involved, and it is very highly to its own interest to make sure that the issue is sound. If, as must from time to time happen, something goes wrong with the loan or the borrower the issuing house regards it as its duty to do everything it can to put matters straight, and, indeed, to watch continuously the actions of the borrower to see that the security remains unimpaired. These duties are sometimes very onerous and involve a great deal of labour and expense, as well as judgment, skill and experience.

388. Contrast this with nearly all home industrial issues. There are, it is true, one or two first-class houses in the City which perform for certain first-class companies the same functions as the older issuing houses perform for foreign borrowers. In addition these latter are to a limited extent entering the domestic field, though, for the reasons we give later, their direct interest must probably remain limited. Again, the advice of stockbrokers, when asked for, may be a safeguard but it is scarcely sufficient to take the place of the responsibility of a first-class issuing house. With these exceptions the public is usually not guided by any institution whose name and reputation it knows. For in the main all issues are made in the same way. Each of them has in the most prominent position and in much the heaviest type on the prospectus the name of a joint stock bank—in the great majority of cases one of the "Big Five"—as receiving subscriptions to the issue. It is perfectly natural that an inexperienced investor, seeing the name of a well-known bank on the prospectus, should believe that the bank in question vouches in some way for the issue. But he is mistaken. None of the Big Five regard themselves, except in very rare cases, as fathering the issue or in any way responsible for it beyond seeing that the prospectus complies generally with the law and that the issue is on the face of it respectable. None of them would wish the public to assume that they vouched for the issue and the figures of profits and assets, etc., given in the prospectus, in the same way as the issuing houses vouch for their issues. They frequently know the company through having had banking relations with it over a series of years. On the other hand, they may know practically nothing of it. The *real* issuer may be the company itself, if it is a strong and good one, or a finance company or syndicate—few large, many small, some good, some indifferent, some bad—and sometimes it is a company or a syndicate got together for the sole purpose of making a particular issue. The investor may not realise that the all-important point is not the name of the bank receiving subscriptions but that of the company or syndicate really responsible for the issue; the

more doubtful the issue the more likely it is that this name will appear in very modest and retiring print. In the case of big, first-class companies, the names of which are a sufficient guarantee in themselves, and which probably issue their own securities, this system is adequate. But in most other cases the public is left without a guide, with the results which we have indicated above. It would in our opinion be an important reform that relations between finance and industry should be so developed that issuing institutions of first-class strength and repute should vouch to the investor more normally and more fully for the intrinsic soundness of the issues made and that the joint stock banks should not give the appearance of sponsoring issues so long as in fact their real responsibility is limited to receiving subscriptions. In this way the investor would be encouraged to support well-vouched issues and be put on his guard against others.

389. It is important, however, to recognise clearly that no financial institution which assumed the responsibility of vouching for industrial issues could do so on the basis of an isolated connection formed with the industry solely for this purpose. Responsibility of this kind can only be the outcome of a close and continuous relationship with the industry concerned, different in kind from the relationship now existing between the joint stock banks and industry.

390. While from the investor's point of view there would be undoubted advantages in a closer connection between British industry and the City of London, we think that the financial community and industry would both benefit. We believe it not unfair to say that certainly in American and German banking circles, and possibly in French also, there would be found many more men with an intimate knowledge of the problems of industry than in England. Certainly in all these countries it is easier to obtain immediately from banking sources full and accurate information on any particular industry and on any particular company in that industry. A really big American bank for instance would have a large department engaged in studying particular industries and the companies engaged in it, in keeping in close touch with developments and in being ready to provide any information required. If those at the head of our financial world have a close knowledge of industry, they will be far more able to assist in meeting the problems of the future than if finance and industry are in water-tight compartments. We have indeed no sympathy with the idea that the banks should in any way manage industry. We endorse Dr. Goldschmidt's statement that "a banker must never forget that he cannot and must not be an industrialist. He can only play his real part in assisting a company by concentrating on the tasks and possibilities which present themselves from time to time in the case of every industrial enterprise. It is and must be the rule

that the industrialists themselves should be responsible for the business and general management of a company and that the banker should be the adviser in matters of finance." (Statement of evidence; para. 14.)

391. Every industrial and commercial company has a double financial problem, namely, to provide itself with adequate permanent capital and to obtain, as occasion warrants, temporary or seasonal credits, either of a self-liquidating character or to be repaid ultimately out of the issue of more permanent capital. It may also have—and perhaps in increasing measure—a third problem, namely, to provide itself with what are known as intermediate credits. Short-dated credits are endless in the variety of their conditions, and to provide them is the principal function of the banks. As such advances form the most lucrative part of their assets the banks indeed are very willing to do so, so long as their total lies within their customary percentages and within the limits set by general credit policy. In this direction British industry certainly suffers under no handicap in comparison with its competitors. The great English banks, undoubtedly among the strongest financial institutions in the world, use and have used their resources freely, sometimes too freely, in the provision of advances to industry. In general we are satisfied that, subject to the conditions imposed by the necessity of accommodating ourselves to the outside world, our banking system is adequate and satisfactory in the provision of the normal short credits to industry and their distribution. It is appropriate to say here and in connection with short-term credit that all concerned would benefit by a more extended use of commercial bills (i.e. bills given by a purchaser to a supplier) which have largely disappeared as part of the mechanism of home business. To those who find it necessary for good reason to give extended credit, finance would be rendered more easy if their "accounts receivable" were in the form of commercial or trade bills rather than in the form of mere debts.

392. There are two other questions; whether our financial organisation is as fitted as it might be to supply industry (i) with intermediate credit and (ii) with long-dated capital.

393. Intermediate credit may be defined generally as credit advanced for periods ranging from one or two up to five years. It is necessary, we think, to divide into at least three main classes the types of transactions for which intermediate credit is required, namely: (i) hire purchase or instalment sales, (ii) advances against deferred payment, (iii) long-term contracts.

Class (i) would cover the sale of various classes of goods of which the legal ownership can be retained by the seller until payment is completed, e.g., motor cars, motor lorries, pumps, electrical machinery and appliances, agricultural implements, and so forth. These classes comprise articles represented in general by small

units which can be claimed and removed by the seller if payment is not ultimately completed.

Class (ii) would cover the sale of larger units such for instance as ships, also coke-ovens or machinery which after erection is not removable and the ownership of which, therefore, passes in fact from the seller. The security therefore no longer resides in the goods themselves and the seller must rely to a greater extent on the soundness of the buyer and on such other security as he can obtain.

Class (iii) would cover large contracts for railways, harbours, roads, drainage, water-works and so forth.

394. In the case of all these classes, we believe that adequate credit facilities for use internally in this country are available and are being developed, but that in the case of Classes (i) and (ii) not so much use is made of them as is possible and desirable. Recent experience appears to show that, on proper lines and with sound supervision, the risk of loss in the granting of such credits is small, while on the other hand their value in stimulating home consumption should be great. The use of electrical and mechanical appliances by the great bulk of the population is capable of very great extension and would, we believe, be greatly facilitated by the more widespread application of instalment buying, the advantages of which much outweigh in our view any disadvantages which are alleged against it. It is, of course, essential that British traders should be made fully aware of the facilities which exist and that they in turn should be prepared to make use of them.

395. We do not feel so sure, however, that credit facilities to cover sales or contracts abroad are so adequate, particularly in the case of Classes (i) and (ii). With the immense growth in the mechanisation of industry throughout the world, the demand for longer credits for financing the production and sale of machinery of all kinds appears to be growing. The purchaser abroad requires very often two or three years before he can complete his payments, and therefore contracts are likely to go to those sellers who can provide sufficiently long credit. Since we must look in the future particularly to exports in which skill and experience largely enter, we believe that facilities for financing exports of machinery of all kinds are of particular importance. At present, however, we do not believe that the facilities available here in the case of foreign trade are so complete as those provided in some other countries, and we think that it would in fact often be necessary for British traders to obtain either directly or indirectly such facilities from foreign institutions. This is a situation which should be remedied and British institutions, similar to those which cover the ground satisfactorily at home, should be developed for the purpose of assisting British industry and trade abroad. We see no reason why sufficiently strong institutions should not create a market for their own short-term securities by means of which any sound business negotiated might be financed.

396. As regards Class (iii), namely, long-term contracts abroad, British contractors will normally be in competition with foreign contractors. Such contracts are usually for account either of Governments or municipalities, and, as the work is often extended over some years, loans to finance them are required only gradually, and generally the authority for which the work is being carried out pays as each section of it is completed. The risks of any bank or financial institution taking up the business are first that the Government or public authority will be unable to pay; secondly, and more important perhaps, that disputes as to the carrying out of contracts will arise; and thirdly that, if the contractor were to fail, the bank might be forced to make its own arrangements to complete the work. In the past the names of the great British firms have been known in every part of the world. The first essential to-day is that the new generation of contractors should have adequate financial resources of their own. In that case we believe that the joint stock banks and other existing institutions should be able to provide at any rate some of the credit facilities required. It is true that longer credit facilities are needed in such cases than it is customary for banks to give. But up to a certain small proportion of their advances the banks would run no undue risk in financing sound contracts of this character. We suggest, however, that the financing of such contracts should be more particularly one of the functions of the class of institution to which we refer below. Foreign contractors undoubtedly obtain such facilities more easily than British contractors and it would be a misfortune if the latter were, on account of their inability to obtain the financial assistance required, to have to withdraw from a field in which Great Britain has been so prominent in the past.

397. Coming back now to the more general question of the relations between finance and industry, and in particular to the provision of long-dated capital, we believe that there is substance in the view that the British financial organisation concentrated in the City of London might with advantage be more closely co-ordinated with British industry, particularly large-scale industry, than is now the case; and that in some respects the City is more highly organised to provide capital to foreign countries than to British industry. We believe this to be due in part to the historical organisation of British industry and to the fact that industry, having grown up on strongly individualistic lines, has been anxious to steer clear of anything which might savour of banking control or even interference, this attitude coinciding with the views which prevail in this country as to the province of sound banking. Nevertheless a further development of our financial organisation is possible, which would be distinctly beneficial and need not be inconsistent with these traditions.

398. We are bound to point out, however, that unless British industry can at any rate be reasonably assured of normal profits no development such as we suggest has any chance of success. No institution acting as an intermediary between industry and investor can possibly succeed unless the securities which it induces the latter to buy prove to be sound and remunerative. Any concern devoting itself to industrial financing faces peculiar difficulties, for it must have a considerable capital and yet it is without a "bread and butter" business such as ordinary deposit banking or acceptance business provides.

399. The functions which should be performed by such a concern may be summarised as follows:—Acting as financial advisers to existing industrial companies; advising in particular as to the provision of permanent capital, its amounts and types; securing the underwriting of and issuing the company's securities to the public and, if necessary, assisting previously in arranging for the provision of temporary finance in anticipation of an issue; assisting in financing long contracts at home and abroad, or new developments of an existing company, or founding companies for entirely new enterprises; acting as intermediaries and financial advisers in the case of mergers or in the case of negotiations with corresponding international groups; and generally being free to carry out all types of financing business.

400. These are functions which are often difficult, which entail considerable risks and which may involve the temporary locking-up of large sums.

Such a concern must:—

(a) be provided with a substantial capital: where it is a case of financing large contracts for periods up to five years, it might be able to supplement its resources by the issue of its own short-term notes;

(b) be able to rely on the co-operation of existing institutions with large monetary resources in the making of temporary advances: otherwise it might either be unable to carry out its functions or its capital might have to be too big for it to earn satisfactory dividends;

(c) build up a competent and expert staff; establish gradual connections with industry; and instil confidence in its issuing ability and credit.

401. We have considered whether these are functions which the big joint stock banks might themselves carry out. They have the great advantages (i) of representing such aggregations of capital and deposit resources that their financial capacity would be undoubted; (ii) of being, through their immense number of branches and through the large sums they already lend on short credit, in touch with industry in a way not possible for anyone

else. But for various reasons we think it doubtful whether the banks can with advantage depart from their traditional banking sphere.

402. For other reasons the same conclusion seems necessary as regards the great private banking houses. These houses, with very few exceptions, undertake a large acceptance business involving them in a corresponding liability to the holders of their bills. It has always been recognised that acceptance business necessitates the maintenance of a high degree of liquidity and is not consistent with serious liabilities in respect of industrial financing.

403. While, however, we do not propose a change in the character of present banking practice, we think that the co-operation of the big banks is required both in taking an interest in the share capital of such an institution and being ready to provide such credit facilities as the institution may require pending a public issue. The best course might be if the leading private institutions and the big banks were to co-operate in creating one or more such concerns. We understand that the creation of the Bankers' Industrial Development Company was due originally to the belief that help in these directions might be given to industry by the City, which was not being given. We have been told, however, that the authorities of the Bank of England consider, as we do, that these are not proper permanent functions for a subsidiary of a Central Bank. It would seem desirable, therefore, that the Bankers' Industrial Development Company should at a convenient stage be definitely separated from the Bank of England, have an independent existence, and rely upon its profit-making capacity as a private institution. It is possible that it might form a nucleus for that closer co-operation between finance and industry which we think is required.

There is no reason why the field should be limited to any one institution. In fact it is too wide for that to be desirable. In practice, any concern entering it might find that some specialisation over one or two particular industries was desirable. We must repeat, however, that the success of institutions directing themselves to the interests of British industry must depend finally on the profit-making capacity of that industry. They may help by their co-operation towards that end, but industrial problems must in the main be solved by industry itself.

404. It has been represented to us that great difficulty is experienced by the smaller and medium-sized businesses in raising the capital which they may from time to time require, even when the security offered is perfectly sound. To provide adequate machinery for raising long-dated capital in amounts not sufficiently large for a public issue, i.e., amounts ranging from small sums up to say £200,000 or more, always presents difficulties. The expense of a public issue is too great in proportion to the capital

raised, and therefore it is difficult to interest the ordinary investor by the usual method; the Investment Trust Companies do not look with any great favour on small issues which would have no free market and would require closely watching; nor can any issuing house tie up its funds in long-dated capital issues of which it cannot dispose. In general, therefore, these smaller capital issues are made through brokers or through some private channel among investors in the locality where the business is situated. This may often be the most satisfactory method. As we do not think that they could be handled as a general rule by a large concern of the character we have outlined above, the only other alternative would be to form a company to devote itself particularly to these smaller industrial and commercial issues. In addition to its ordinary capital, such a company might issue preference share capital or debentures secured on the underlying debentures or shares of the companies which it financed. The risks would in this manner be spread, and the debentures of the financing company should, moreover, have a free market. We see no reason why with proper management, and provided British industry in general is profitable, such a concern should not succeed. We believe that it would be worth while for detailed inquiries to be made into the methods by which other countries attempt to solve this particular problem.

CHAPTER V.—PROPOSALS RELATING TO INFORMATION AND STATISTICS.

405. Exact quantitative knowledge concerning the chief elements of the monetary and financial system is, we consider, of the utmost importance, both to provide the necessary data on which to base the management of the system and also for the purpose of making gradually possible a more definitely scientific treatment of these problems than the existing state of our knowledge of the facts allows. There are, moreover, many matters of importance which are now the subject of controversy, yet need not be so if they could be put to a statistical test. We should aim, therefore, at obtaining a complete inventory of the economic life of the community under its several aspects in such a form that we could cross-check the accuracy of our information by being able to work up to the final totals from more than one direction.

406. Except in the case of unemployment statistics which are required for administrative purposes, this country (which was the pioneer in statistical surveys) has been falling seriously behind the United States. We think that a substantial annual sum could not be better spent than on the strengthening of the statistical departments of the appropriate Ministries, and that in course of time a

corpus of reliable knowledge could be built up which might save us from mistakes involving a waste of resources worth many hundreds of times the total cost of acquiring the knowledge. There can be few worse perversions of the ideal of wise economy than a narrow limitation on what we spend for the improvement of economic knowledge.

407. We are hopeful that a moderate impulse in this direction may be sufficient at the present day to produce valuable results, because we see signs in several directions of a far greater willingness than existed a few years ago to impart business and financial information. Several of the clearing banks have begun to publish figures supplementary to those traditionally required of them; and we understand that the Bank of England has taken steps of late with a view to a development of its activities in the collection of statistical information.

408. The statistical information, the collection of which we recommend, can be divided into that part which is of a definitely monetary or financial character, and that part which covers the industrial and economic field in general. But both are equally necessary for the purposes of the scientific management of the currency. For the second category of statistics is as essential as the first for the correct and prompt diagnosis and prognosis of the position and prospects from day to day.

We recommend, therefore, that the following sets of statistics be collected as completely and as promptly as the circumstances permit:—

I. MONETARY AND FINANCIAL STATISTICS.

1. THE MONTHLY RETURNS OF THE CLEARING BANKS.

409. These should be amplified on the lines, broadly speaking, of the returns for recent years with which the clearing banks have kindly supplied us as published in Appendix I. More particularly, they should show separately:—

- (i) Cash in hand (true daily average).
- (ii) Balance at the Bank of England (true daily average).
- (iii) Money at Call (a) in sterling.
(b) in foreign currencies.
- (iv) Money at Short Notice (a) to the Money Market.
(b) to the Stock Exchange.
(c) in foreign currencies.
- (v) Treasury Bills.
- (vi) Commercial Bills (a) in sterling.
(b) in foreign currencies.
- (vii) Loans and Overdrafts.
- (viii) Current Accounts (exclusive of internal funds and accounts of the bank itself).

(ix) Deposit Accounts (inclusive of internal funds and accounts of the bank itself).

(x) Investments (a) in British Government securities.
(b) in other Securities.

(xi) Acceptances outstanding (separately from engagements for forward foreign exchange, etc.).

2. CLASSIFICATION OF LOANS AND OVERDRAFTS.

410. Certain of the banks have prepared from time to time a classification of their aggregate of loans and overdrafts corresponding to the different classes of their customers. In the evidence which they have given us they have kindly amplified these particulars; but hitherto this classification has not been made regularly, or on a uniform basis, or as comprehensively as might be. We recommend that the banks should be invited to prepare at annual intervals (or at quarterly intervals if that be practicable) a classification of their total loans and overdrafts on some such broad lines as the following—

(a) Loans to concerns engaged in "productive" industry (mining, manufacture, etc.);

(b) Loans to concerns engaged in commerce, transport and distribution;

(c) Loans to concerns engaged in finance, insurance, etc.;

(d) Loans to agriculturists;

(e) Loans to concerns and persons engaged in professions, entertainments, personal services, etc.;

(f) Loans to private persons:—

(i) for house building;

(ii) for other purposes;

Each of these general headings, and particularly (a), should then be sub-divided further so far as is practicable. In fact, in some cases the banks have already proceeded to more details than the above. It would be helpful if care could be taken to sub-divide class (a) into industrial classifications which correspond as closely as possible to the classifications used in other industrial statistics (*cf.* para. 423).

3. RETURNS FROM THE OTHER JOINT STOCK BANKS.

411. It is at present a serious gap in the aggregate banking statistics of the country that no figures are available for British joint stock banks other than the clearing banks except at dates (at the end of the year or of the half-year) which are not representative of the normal position. We recommend that the Treasury or the Bank of England should be asked to prepare a list of the institutions which should be reckoned as being "banks" for the purpose of making statistical returns—a list which might be limited, if it seemed advisable, to joint stock banks with deposits in excess of

(say) £1,000,000. These institutions should be asked to supply the Bank of England with the same information as that for which we ask in the case of the clearing banks, and aggregated totals might be published monthly.

4. RETURNS FROM OTHER INSTITUTIONS.

412. There remain three important classes of institutions not covered by the above, namely the merchant bankers, British banks doing business mainly abroad though having their head office in this country, and foreign institutions with branch offices here accepting sterling deposits. It would be a great advantage if periodic statements of their sterling deposits could be obtained from all these institutions. These returns might be quarterly rather than monthly, and there would be no objection to the institutions in question being allowed to furnish the figures privately to the Bank of England, which would have the duty of publishing aggregated figures only.

5. FOREIGN BALANCES AND FOREIGN LIQUID ASSETS HELD IN STERLING.

413. We attach first-class importance to these figures being collected as comprehensively as possible and published. We have ourselves made a first attempt in this direction and have printed the results in Appendix I. Whilst these figures probably cover by far the greater part of the ground, there are doubtless omissions and defects which could be remedied with further experience; the most important omission is that of sterling bills held in their own portfolios by foreign institutions, whether located in London or abroad. We recommend that the Bank of England should be charged with the duty of collecting these statistics to the best of its ability. We think that the figures are more likely to be accurate and complete if the returns for individual institutions are treated by the Bank of England as confidential, only the aggregated results being published. We attach importance to these results being made public at monthly intervals. In the long run the advantages to confidence and prestige of the figures being known will far outweigh any supposed advantages from suppression. We believe that a knowledge of the figures which we have collected relating to recent periods would have increased confidence, if they had been known at the time. No doubt if the amount of the gold reserve had not been published hitherto some fears might be entertained as to the results of publication. So it may be in this case. But for those who would stand high in the world's estimation the greatest candour and readiness to submit to publicity are now required. Moreover, it is exceedingly desirable that the principal data on which the Bank of England bases its decisions should be generally known. For the natural action of the market is more likely in that case to march

with the intentions of the Bank and the decisions, being intelligible, will carry more weight.

We suggest, at the same time, that it might be useful for the Bank of England to collect for its own confidential use somewhat more detailed information than could easily be obtained for publication, since figures affecting the position of individual foreign institutions would be involved. In particular, the separate confidential returns made to the Bank of England might be divided up according to the country on behalf of whose nationals or institutions the bills and balances were held.

6. THE VOLUME OF ACCEPTANCES.

414. Hitherto no figures have been available for the aggregate of sterling acceptances outstanding in London on home and foreign account respectively, such as are available for dollar acceptances in New York. Even the figures for "Acceptances, etc." published by the clearing banks are liable to be deceptive, because with acceptances some of them have lumped together engagements for forward foreign exchange and other items. This is a serious gap in our picture of the financial position.

We recommend, therefore, that the Bank of England should collect comprehensive figures and publish the aggregated results at monthly intervals. In this case also the figures for individual institutions should be treated as confidential, whilst the Bank might find it useful that the confidential returns made to it should be divided up according to the domiciles of the parties on behalf of whom the bills have been accepted.

With the figures of bills and balances held, and of bills accepted on foreign account, the Bank of England will be in possession of essential data which are at present lacking. The burden of meeting liabilities to foreign institutions, should repayment be claimed, or if the net result of a great number of transactions some one way and some the other happens to be adverse, must necessarily fall on the Bank of England. Yet hitherto the Bank of England has been, as it were, in the position of a head office, charged with the maintenance of adequate reserves yet without accurate information either as to the volume of deposits and other liabilities incurred by its branches, or as to the liquid *contra* assets held by them in the shape of maturing acceptances.

7. THE VOLUME OF CHEQUE TRANSACTIONS.

415. We have at present detailed figures, admirably compiled by the officials of the Clearing House, of the volume of cheque transactions passing through the "clearing" in London and the chief provincial centres. Unfortunately these represent an incomplete

and somewhat arbitrary selection from the aggregate of cheque transactions, or "bank-debits" as this aggregate is called in the United States. For they exclude transactions between customers of a single bank which are settled internally and have no need to pass through the Clearing House (and, owing to the concentration of British banks into a small number, the amount of these is now large); and they also exclude cheques which are informally cleared between neighbouring banks in towns or localities where there is no "provincial clearing."

The total turn-over figures have in fact been given to the Board of Trade by the ten clearing banks since January, 1930, but they have not been published hitherto either by the Board or by the banks themselves. We print them in Appendix I. We recommend that similar figures should be obtained from *all* banks and published at monthly intervals. We suggest, further, that they might be subdivided into a number of groups according to the districts where they arise. The districts chosen should cover areas comparable to those used in other industrial statistics.

In general it should be borne in mind in any method of classification which is adopted that an important object of these figures is to make it possible to separate, so far as practicable, the figures arising from Stock Exchange and money market transactions from transactions arising out of the earning and spending of the community's current income.

416. We suggest that the Bank of England might usefully publish a monthly bulletin of statistics including the material which, we understand, the Bank already compiles for the information of foreign and Dominion Central Banks, and also the fresh material which would become available as the result of the preceding recommendations.

8. THE BALANCE OF TRADE.

417. We recommend that the figures now published annually by the Board of Trade, making up our international balance sheet of the items due to and by this country on income, and in part on capital, account, should be placed on a more exact basis. The figures for recent years, which we print in Appendix IV, have doubtless been the best obtainable without elaborate special inquiries for making which the necessary resources have not existed. But they have been partly based on pioneer private enquiries, made by *The Economist*, Sir Robert Kindersley and others; they have been subject in recent years to frequent (and large) revisions after publication; and it is evident that there is so much gues-

work in them as to render them liable to an unduly wide margin of inevitable error. We believe, however, that it is only a matter of taking sufficient pains to make them reasonably accurate and that it is thoroughly worth while to do this.

The collection of the figures of foreign bills and balances, which we recommend above, will go a long way towards making this possible, since the lack of such figures is the greatest gap in the compilation. But there are also other items which might be put on a more exact basis. In particular the amount of the receipts in respect of sinking funds on existing foreign loans, on which Sir Robert Kindersley has thrown much light and which he has shown to be substantial, should be regularly and precisely ascertained from the banks and issuing houses concerned. Foreign holdings in British companies, as to which *The Economist* has made some most interesting sample inquiries, should be ascertained in detail. The net proceeds to the borrower of new foreign issues currently made in London should be supplied in every case by the issuing houses. Brokers and banks (including foreign brokerage and banking houses with London offices) should be required to make returns of the volume of securities purchased and sold by them on foreign stock exchanges for British clients, and on British stock exchanges for foreign clients—vital facts, all estimates concerning which are at present pure guess-work. The estimates of the miscellaneous items forming part of our so-called "invisible exports," such as shipping earnings, acceptance commissions, insurance premiums, brokerages, tourist expenditure, emigrant remittances, etc., should all be placed on a more secure basis of ascertained fact.

Then only shall we know with sufficient accuracy the trends and changes of the financial position of this country *vis-a-vis* the rest of the world.

II. GENERAL INDUSTRIAL AND ECONOMIC STATISTICS.

9. THE CENSUS OF PRODUCTION.

418. The foundation of the general industrial statistics of this country is the periodical Census of Production. All economic enquirers owe an immense debt to the first-class pioneer work performed by the Board of Trade from the first census of 1907 onwards. But we think that the time has come for a great extension of this work and for the provision of the much larger resources necessary to secure a prompt handling of the material collected. For the value of the work done has been greatly impeded by a lack of the necessary resources, the damming up of the sources of knowledge seeming to many people the most obvious, and easiest, form of retrenchment when a demand for economy is being made.

The first Census of Production related to the year 1907, the results of the second Census relating to 1912 were never worked

up or published owing to the War, and the second effective census was not made until that relating to the year 1924. Owing to lack of staff the final and detailed results of this Census have not yet been published, although a further Census relating to the year 1930 is now in course of ascertainment.

The delay in publishing the results of the 1924 Census of Production has, indeed, been so serious that some of the results, when they are available, will be of comparatively little value except to the economic historian. The following comparison between this country and the United States may be of interest :—

	<i>Great Britain.</i>	<i>U.S.A.</i>
Census of Production relating to year.	1924	1927
First of preliminary reports ...	February, 1927	May, 1928
Conclusion of series of preliminary reports.	March, 1928	May, 1929
Final report	Only two volumes yet published (in June, 1930 and April, 1931).	April, 1930

It is also desirable that the scope of the Census of Production should be extended so as to yield similar and comparable information in regard to the distributive trades, of which no systematic statistical survey has ever been undertaken. This would probably require increased statutory powers to be given to the Board of Trade, as would be the case with a valuable minor extension of the Census of Production which should be considered, namely, the granting to the Board of Trade of powers to obtain from manufacturers details of the value of the principal materials used. This information is available, for instance, in the principal industries covered by the American and Canadian Censuses of Production, and lack of it makes many of the most important industrial statistics, relating to the dependence of one industry upon another, extremely chaotic.

We recommend that from 1932 onwards the Census of Production should be biennial or, if possible, annual, though a more completely comprehensive inquiry might be taken at quinquennial intervals as at present. The census of manufacture is now biennial in the United States and in the Dominions. Great advantages would accrue both to knowledge and to the difficult technique of carrying through these inquiries, if they could become a regular routine, instead of being spasmodic efforts at relating periods so far apart as to be, in the rapidly changing modern world, only partially comparable. It is indeed essential for sound judgment as to the trend of events that we should have accurate and up-to-date information as to the volume of the country's output and as to the change from year to year in the output per head of those

employed. We have found in the course of our inquiry that simple, fundamental facts of this kind, which ought to be securely known, are the subject of guess work and controversy about which nothing certain can be safely asserted.

10. THE VOLUME OF WAGES PAID.

419. In accordance with the recommendations of the Balfour Committee the Ministry of Labour in 1928 repeated the Census of Earnings which had been held in 1924. It is possible that this work may be repeated; and from these data, taken in conjunction with known figures of the number of insured workers in different industries, it is possible to make a good estimate of changes in the total "pay-roll" of manufacturing industry. But it would be desirable to extend the scope of these periodical inquiries into earnings. Outside manufacturing industry, the Ministry of Mines gives detailed figures of total earnings in coal mining and the Ministry of Transport gives annual figures of earnings on the railways. But for agriculture and for other forms of transport we have information relating only to time rates and not to average earnings; whilst for about a third of the whole national "pay-roll," represented by wholesale and retail distribution and domestic and personal services the only information available derives from one or two spasmodic special inquiries. In view also of the very large annual sum now paid in salaries (perhaps nearly half of the wage bill of some £1,600,000,000) it is very desirable that the Census of Earnings be extended, perhaps under the auspices of the Board of Inland Revenue, to cover the whole field of salaried workers, making it possible to obtain estimates of the total of salaries paid in various industries and services, and of changes from year to year.

11. THE VOLUME OF RETAIL SALES.

420. The Bank of England has recently undertaken the compilation of an index of retail sales based on returns from a number of the larger stores throughout the country. We think that these figures are valuable, and that their compilation should be continued and amplified as opportunity offers. Such an index with weights based on consumption at the present time rather than before the War would be of great value, particularly if it could be extended so as to give some estimate of a price index which would cover the whole field of consumption.

12. THE AGGREGATE AND THE DISTRIBUTION OF PROFITS.

421. At present we are dependent for our estimates of the profitability of business in general and of particular industries on the partial samples compiled, e.g., by *The Economist*, from the published accounts of public companies. In several respects these figures are an unreliable index of the position as a whole.

No published results in detail are available from the rich material at the disposal of the Board of Inland Revenue apart from certain special inquiries by Mr. W. H. Coates, which were published in the Appendices to the Colwyn Report on National Debt and Taxation. We strongly recommend that a fairly detailed survey of the profits of different industries and services relating to some recent year should be undertaken and published, and that thereafter the Board should use this comprehensive survey as base year and carry the figures forward annually by means of estimates so as to show year by year the movements of profits in British industry as a whole and in the main industries separately. When the figures are available over an extended period of time they should be a very useful indication of economic trend.

13. THE VALUE OF CAPITAL CONSTRUCTION.

422. Finally, we recommend that an attempt should be made to obtain early information, as accurate and comprehensive as the circumstances permit, of the value of contracts completed within the previous twelve months together with the value of contracts (as below) on hand still to be completed. These are statistics in which this country is at present particularly deficient. Yet they are of much importance to a Central Bank in determining whether and how far new capital construction needs from time to time to be encouraged or discouraged. It would probably be necessary to require that notification should be made to appropriate local authorities of all building and construction undertakings exceeding a certain minimum sum in value.

Virtually the whole field of capital construction would be covered if we could obtain full returns of the value of contracts from the following industries:—

- (1) building and contracting;
- (2) engineering (including all branches, together with constructional engineering);
- (3) electrical trades;
- (4) the heavy motor industry;
- (5) shipbuilding.

Building plans have in all cases to be referred to the appropriate local authority. But full statistical returns are only obtained from certain cities and towns, in which for certain minor administrative reasons London is not included. There is, moreover, no machinery for recording those cases where the plans are not proceeded with and the figures for some years are in consequence of little value.

There is at present no machinery for recording capital construction under the other heads indicated above and even for the total money value of all production of capital which goes under these heads we have to rely on rather difficult estimates.

Except in the case of building and constructional work, returns of orders for capital goods (machinery, etc.) exceeding a certain

minimum sum in value could probably be best collected from the engineering firms and others which manufacture the capital goods. A similar statement would be required from importers and dealers.

14. CO-ORDINATION OF STATISTICAL WORK OF DIFFERENT DEPARTMENTS.

423. At various points above reference has been made to the necessity for maintaining the proper comparability between different industrial statistics. The four Government Departments principally responsible for industrial statistics—the Registrar-General, the Board of Trade, the Inland Revenue and the Ministry of Labour—use, at present, three quite different industrial classifications. The figures of the Ministry of Labour, although this classification is now in line with that of the Census, are not fully comparable since they refer to insured workers only. Over the greater part of the industrial field it is impossible to make comparisons between the Census of Production on the one hand and the Census of Population or the Ministry of Labour figures on the other hand. Again the Earnings and Hours Inquiries of the Ministry of Labour use a classification which is similar to (although not identical with) that of the Census of Production, but which is different from the classification of their figures of employment and unemployment. In general, the most detailed and careful comparison of these various figures does not enable the investigator to make use of any industrial figures except for a few broad groups of industries. Doubtless these anomalies have grown up for reasons of administrative convenience. But for statistical and economic purposes much of their value is thus lost.

A similar difficulty prevails in regard to statistics compiled on a regional basis. It is desirable that, as far as possible, all these statistics should be on a plane of comparability.

424. It is probable that the bulk of these statistics could be obtained with the voluntary co-operation of those concerned. Nevertheless the value of statistical returns can be greatly impaired by the recalcitrancy of a few of those from whom figures are required. In any case in which the departments concerned consider that they would need a power to require information if the statistics are to be sufficiently comprehensive, we recommend that they should be given such power unless in any particular case there seems to be especial reason to the contrary. The practical value of the statistics, the regular collection and prompt publication of which we recommend, will increase considerably in course of time after a fairly long series of figures are available for purposes of comparison.

425. We attach very great importance to this part of our recommendations being carried into effect. For the completer information, which would thus be put at the disposal of those responsible for deciding policy, may prove to be an indispensable preliminary to their being able to work out practical methods of management for attaining the objectives of the monetary system. To put on a more scientific basis our acquaintance with the fundamental facts and trends of our economic life, and to replace empiricism by ordered knowledge, might prove to be the greatest step forward that it lies within our power to take towards raising the economic well-being of our country to the level which the technique of production would allow, provided only that our machinery for collective action was such as to facilitate the whole of our productive resources being brought into fruitful activity.

CONCLUDING NOTE.

426. We have now completed all the recommendations which we are able to make for remedial action by the monetary machine itself. If our recommendations relating to international action are given effect, we should hope for a great improvement in the situation in due course. If, however, progress along these lines is delayed or if the action taken is insufficient, we believe that our own monetary authorities will not be able to remedy matters without assistance from changes in other non-monetary factors by which the volume of our domestic output and employment, and in particular our balance of trade, are also much influenced.

427. Thus it is of the greatest importance that other domestic action, not of a strictly monetary character, should be taken as an essential condition to the monetary authority being in a position to employ effectively the methods of monetary policy. But when we came to consider the various alternatives which have been put before us for domestic action of this character, we found considerable difficulty in deciding just how far our terms of reference extend and where to draw the line between matters lying within them and those lying beyond. It has been a further difficulty that some of these alternatives raise matters of active political controversy and cover ground where a general agreement among the members of this Committee was scarcely to be expected.

428. In face of these difficulties some of us have felt that there is nothing which, in our capacity as members of this Committee and within our terms of reference, we can usefully add to the foregoing chapters. Other members of the Committee, however, have felt that some further exploration of the problem, even though it leads into non-monetary ground, is part and parcel of their view of the monetary situation as a whole. We have thought it best,

therefore, to give as Addenda* to this Report certain memoranda which set forth the views of those of our members who feel that our Report would be incomplete without further explanations and proposals.

We have the honour to be,

My Lords,

Your obedient Servants,

MACMILLAN, *Chairman.*

THOS. ALLEN.†

ERNEST BEVIN.†

R. H. BRAND.

T. E. GREGORY.

J. M. KEYNES.

L. B. LEE.

CECIL LUBBOCK.‡

R. McKENNA.

J. T. WALTON NEWBOLD.§

WALTER RAINE.||

J. FRATER TAYLOR.

A. A. G. TULLOCH.

G. ISMAY, *Secretary,*

23rd June, 1931.

* The Addenda are as follows :—

- I. By Sir Thomas Allen, Mr. Bevin, Mr. Keynes, Mr. McKenna, Mr. Frater Taylor and Mr. Tulloch (see page 190), subject in the case of Sir Thomas Allen and Mr. Bevin to a joint reservation (see page 209).
- II. By Mr. Brand (see page 210).
- III. By Professor Gregory (see page 217).
- IV. By Mr. Lee (see page 237).

† Subject to the Reservation on page 239.

‡ Subject to the Reservation on page 241.

§ Subject to the Reservation on page 241.

|| Subject to the Reservation on page 257.

Alphabetical List of Witnesses.

<i>Name of Witness.</i>	<i>Bodies represented.</i>
Bellerby, Mr. J. R.	—
Berkeley, Mr. Edward	National Union of Manufacturers (joint evidence).
Bolton, Mr. W. H.	Economic Freedom League (joint evidence).
Bowley, Professor A. L.	—
Catterall, Mr. W. H.	Federation of Master Cotton Spinners' Associations, Ltd. (joint evidence).
Clark, Mr. Colin G.	—
Clay, Professor Henry	—
Courthope, Colonel Sir George L., Bart., M.C., M.P.	Central Landowners' Association (joint evidence).
Dampier-Whetham, Mr. C., F.R.S.	Central Landowners' Association (joint evidence).
Davies, Mr. T. G.	Joint Parliament Committee of the Co-operative Congress (joint evidence).
Douglas, Major Clifford Hugh, M.I.Mech.E., M.I.E.E.	—
Driver, Mr. T.	Federation of Master Cotton Spin- ners' Associations, Ltd. (joint evidence).
Foà, Mr. R. H.	—
Glenday, Mr. R. G.	Federation of British Industries (joint evidence).
Goldenweiser, Mr. E. A.	—
Goldschmidt, Dr. Jakob (accom- panied by Mr. H. Powys Green- wood).	—
Goodenough, Mr. Frederick Crau- furd	Barclays Bank Limited.
Goschen, Sir W. H. N., Bart., K.B.E.	National Provincial Bank Limited.
Granet, Sir W. Guy, G.B.E. ...	—
Hall, Professor F.	Joint Parliament Committee of the Co-operative Congress (joint evidence).
Hammersley, Mr. S. S., M.P. ...	Federation of Master Cotton Spin- ners' Association, Ltd. (joint evidence).
Harvey, Sir Ernest Musgrave, K.B.E.	Bank of England.
Hawtrey, Mr. R. G.	—
Hichens, Mr. W. L.	—
Holroyd, Mr. F., J.P.	Federation of Master Cotton Spin- ners' Associations, Ltd. (joint evidence).
Hopkins, Sir Richard V. N., K.C.B.	H.M. Treasury.
Howson, Mr. R. A.	Joint Parliament Committee of the Co-operative Congress (joint evidence).
Hyde, Mr. Frederick	Midland Bank Limited.
Jenkinson, Sir Mark Webster, K.B.E., F.C.A.	—

<i>Name of Witness.</i>	<i>Bodies represented.</i>
Kindersley, Sir Robert M., G.B.E.	—
Kitchin, Mr. Joseph	—
Kitson, Mr. Arthur	Economic Freedom League (joint evidence).
Lakin-Smith, Mr. H., F.C.A. ...	Association of British Chambers of Commerce.
Lithgow, Lieutenant-Colonel Sir James, Bart., M.C.	Federation of British Industries (joint evidence).
Milne-Bailey, Mr. W.	Trades Union Congress General Council (joint evidence).
Niemeyer, Sir Otto E., G.B.E., K.C.B.	—
Norman, The Right Hon. Montagu Collet, D.S.O.	Bank of England.
Nugent, Sir Roland	Federation of British Industries (joint evidence).
Payton, Mr. E. L.	National Union of Manufacturers (joint evidence).
Pease, Mr. J. W. Beaumont ...	Lloyds Bank Limited.
Peddle, Mr. J. Taylor	Federation of Master Cotton Spinners' Associations, Ltd. (joint evidence).
Perring, Sir William, J.P. ...	National Chamber of Trade.
Pigou, Professor A. C.	—
Pogson, Mr. John	Federation of Master Cotton Spinners' Associations, Ltd. (joint evidence).
Pugh, Mr. Arthur	Trades Union Congress General Council (joint evidence).
Rae, Mr. John	Westminster Bank Limited.
Robertson, Mr. D. H.	—
Scott, Mr. George J.	Scottish Banks (joint evidence).
Simm, Mr. F.	Federation of Master Cotton Spinners' Associations, Ltd. (joint evidence).
Sprague, Dr. O. M. W.	—
Stamp, Sir Josiah C., G.B.E. ...	—
Stewart, Dr. W. W.	—
Strakosch, Sir Henry, G.B.E. ...	—
Wiggins, Mr. W. M., J.P.	Federation of Master Cotton Spinners' Associations, Ltd. (joint evidence).
Wise, Mr. E. F., C.B., M.P. ...	Independent Labour Party.
Woodburn, Mr. Arthur	National Council of Labour Colleges.
Wright, Sir Alexander K., K.B.E., D.L.	Scottish Banks (joint evidence).

Memoranda, etc., were furnished by the following, among others:—

Agricultural and Industrial Union.
 Anglo-South American Bank, Limited.
 Association of Engineering and Shipbuilding Draughtsmen.
 Birmingham Trades Council.
 Fabian Society.
 Industrial Institute.
 International Fixed Calendar League.
 League of Science.
 London Commercial Club (certain Members of).
 Manchester Association of Importers and Exporters.
 Manchester Economic Research Association.
 Monetary Reform Association.
 National Federation of Iron and Steel Manufacturers.
 National Gas Council.
 West Ham Borough Council.

Mr. J. Adamson.	Mr. P. W. Martin.
Mr. A. Linney Arnold.	Mr. Arthur G. Marshall.
Mr. Edward Batten, M.I.Mech.E.	Lieutenant-Colonel D. W. Maxwell.
Mr. C. E. Cope.	Mr. Henry Meulen.
Mr. J. F. Darling, C.B.E.	Mr. George H. Milner.
Mr. W. R. Darwin.	Mr. C. L. Nordon.
Mr. W. M. Dumbleby.	Mr. Ivan Pedersen.
Mr. W. J. Duggan.	Mr. Charles Edward Pell.
Commander P. Harrington Edwards.	Sir John Pilter.
Mons. J. Gersony.	Mr. Joseph Ricardo.
Mr. J. W. Greenwood, M.B.	Professor J. W. Scott.
Mr. M. Jones.	Sir Oswald Stoll.
Mr. Percy H. Joseph.	Mr. J. E. Tuke (and others).
Mr. Stephen J. Lett.	Mr. W. H. Wakinshaw.
Mr. A. H. Mackmurdo.	Mr. W. A. Welshman.
	Mr. F. Wigglesworth.

ADDENDUM I.

Proposals relating to Domestic Monetary Policy to meet the present emergency.

1. We have signed the Report of the Committee without reservation.* But in our opinion it is incomplete without certain further observations. Rightly or wrongly, we conceive it our duty to consider possible methods of increasing the ability of the banking system to put into effective operation the principles of action which we have recommended above. For if the situation remains unchanged in other respects, we doubt whether it lies within the power of the banking system to restore employment to a satisfactory level.

THE EXPANSION OF CREDIT FOR DOMESTIC PURPOSES.

2. The upshot of the preceding chapters may be summarised as follows. For the world as a whole the best hope of a remedy lies in a monetary policy designed to increase the volume of purchasing power, to increase the ease of borrowing if necessary by guarantees, to diminish the rate of interest long-term as well as short-term, and to stimulate in every possible way the spirit of enterprise and the volume of investment.

3. If Great Britain were, like the world, a closed system, the same monetary remedies would be equally applicable here. But unfortunately this is less true of us than of any other country. Our economic affairs are intricately bound up with an international system. Consequently the power of the Bank of England to initiate an independent policy, irrespective of what is going on abroad, is strictly limited.

4. Whether it is as limited as—to judge from its policy over recent years—the Bank of England has believed, is open to debate. Mr. Hawtrey has expressed in evidence most forcible and interesting views to the contrary. He urges that the power of the Bank to influence the rest of the world, and to refuse to be led by it, whilst not what it was before the War, is nevertheless great. He contends that the amount of foreign balances, which we run the risk of losing if we make money relatively cheap in London, is not so large as is commonly supposed. Whatever may have been true a little time back, we are not prepared to accept Mr. Hawtrey's views as fully applicable to the present very abnormal circumstances, where confidence is liable to be disturbed; and it would, we think, be asking too much to expect the Bank of England to make an experiment of uncertain outcome in the existing environ-

* Except in the case of Sir T. Allen and Mr. Bevin.

ment. It is its duty to put absolute safety first. At the same time there may be much more force in Mr. Hawtrey's general line of argument than is usually admitted. We do not believe that the position abroad need always prevent the Bank of England from furnishing additional credit, provided there is a real opening for its employment in increased domestic enterprise. It would be unsafe for the Bank to increase materially the total volume of credit without considering how it will be employed. But this should not be urged as an argument applicable to cases where there is a reasonable prospect of the new money finding its way into domestic enterprise.

5. Moreover the risks of expanding credit would be much diminished if the Bank of England would take the clearing banks more into its confidence, in the way in which it has traditionally confided in the leading accepting houses, and invite their co-operation. We desire to state this conclusion with some emphasis. While the quantity of money is controlled by the Bank of England, the way in which additional supplies are used can be largely directed by the clearing banks, and co-operation between these banks and the Bank of England is essential. The Committee as a whole have recommended in para. 372 that this should be done. If this recommendation is acted upon, so that the clearing banks on their side can make it clear when they are in a position to direct additional credit into domestic channels and when they are not, and the Bank of England on its side can tell the clearing banks when an expansion or contraction of credit is intended to have its natural repercussions on the foreign short-term loan position and when it is not, it will be much easier than it is now to ensure that domestic enterprise and investment of whatever kind shall never be starved of the accommodation which it requires. In spite of some evidence to the contrary which has been offered to us, we are not convinced that this has invariably been the case in recent years.

6. To-day, however, the main trouble is not a limitation on the amount of available bank credit, but the reluctance of acceptable borrowers to come forward. Thus the first step must probably be some kind of direct stimulus, for example, a considerable fall in the long-term rate of interest payable by typical borrowers, or some kind of State action. Either of these conditions here, without corresponding conditions elsewhere, can scarcely avoid putting some strain on the international position of the Bank of England. To meet this strain a strengthening of the country's surplus on the balance of trade is required. It is also true that the Bank would be in a better position to exercise its full moral influence internationally if its power to retain its gold was beyond question.

7. Thus we are led inevitably to consider whether any other measures are practicable which would restore or increase the Bank

of England's ability to employ its monetary power in a constructive way—though some of these measures may seem to lead us away from monetary policy proper.

AN ANALYSIS OF THE ALTERNATIVES.

8. We know no way in which the initial impetus to increased employment can be given except by (i) an increase of exports, (ii) the substitution of home-produced goods for goods now imported, or (iii) an increase of investment at home—though once the vicious circle can be broken in any of these ways the increased purchasing power of the men put back into work will further increase employment in supplying their needs.

9. This may be put quite shortly by saying that we must either increase our favourable balance of international payments, or find an outlet for more of our savings at home, or, better still, do both. Indeed the whole problem may be made to centre round the balance of trade.* We can increase our surplus by exporting more or importing less. We can export more only if world trade revives, or if we reduce our gold-costs faster than our competitors reduce theirs, or if we give the export industries some kind of special advantages. Similarly we can import less only by a relative reduction of our own costs or by some restriction on imports. Finally we can only find employment for more of our savings at home by increasing the enterprise of borrowers or by somehow subsidising the cost of borrowing.

10. In practice, therefore—putting on one side the increase of our efficiency relatively to that of our foreign competitors, the desirability of which, if we can do it, is obvious and common ground between all parties—the practical courses open to us come down to three :—

- (i) A reduction of salaries and wages ;
- (ii) Control of imports and aids to the export industries ;
- (iii) Domestic enterprise assisted by State action, or subsidies to private investment at home.

* For the amount of international surplus which we currently need for *net* foreign lending depends on how much of our saving is trying to find an outlet abroad. The greater the amount which finds an outlet at home, the smaller the international surplus which we require in order to be in equilibrium. Thus to restore our position and to make full employment possible, we require both to increase our surplus on the balance of trade and also to find increased outlets for our savings at home. When the excess of our total savings over that part of them which we can employ at home is equal to our surplus on the balance of trade, there need be no monetary obstacle to the full and profitable employment of all our resources of men and plant. This analysis enables us to narrow down the alternatives.

There is probably no serious dispute as to all these courses, considered apart from their social and long-period consequences, having *some* effect in the right direction. The difference between us and those who emphasise the importance of the first might be expressed by saying that they feel on a balance of considerations that there is not enough to be hoped for in practice from a cautious application of (ii) and (iii) and that there is great danger in losing sight of (i), which is more fundamental in their judgment and in the long run "sunder"; whereas we feel exactly the opposite, namely, that the practical results of an attempt to reduce salaries and wages are likely to be exceedingly disappointing. They feel that it might be dangerous to divert the public mind from what they believe to be the ultimate necessity of (i) by offering remedies under (ii) and (iii) which may prove specious; whereas we believe that nothing is more likely to produce stale-mate than to concentrate public attention on (i).

11. We now proceed to consider in turn the three courses open to us. The first and the second, let us repeat, would benefit the situation primarily by increasing our foreign investment and by enlarging the power of the Bank of England to pursue without embarrassment a policy of stimulating enterprise both at home and abroad; while the object of the third would be to increase home investment by methods which did not run the risk of unduly increasing at the same time the tendency to lend abroad more than our foreign trade surplus can support.

I.—A REDUCTION OF SALARIES AND WAGES.

1. THE NEED FOR SOME ELASTICITY OF MONEY-INCOMES.

12. Certain preliminary observations are here necessary for the avoidance of misunderstanding. So long as the standard of value is subject to wide fluctuations in terms of consumable commodities, it is essential that there shall be a reasonable elasticity and mobility in the level of the money-incomes which workers and others are ready to accept as equitable. If money-incomes have been established at a level appropriate to a certain purchasing power of money and if purchasing power then undergoes a large increase, the fortuitous advantage which will then accrue to those whose money-incomes are unchanged may be quite inappropriate to the new situation and without substantial justification. Great evils must needs result, and have resulted, from the excessive rigidity of various types of money-income in such circumstances. This is just as true of the rigidity of rentiers' incomes as it is of the rigidity of wage-earners' incomes. We think, therefore, that it would be quite wrong to regard the level of money-incomes, with which we happen to find ourselves at any time, as sacrosanct.

13. For example, the cost of living, as measured by the Ministry of Labour index number, has fallen 18 per cent. since 1925 and 12 per cent. since the beginning of 1929. In so far as this is due to increased productivity, or to a movement of the terms of foreign trade in favour of this country (so that our exports are exchanged per unit for a larger quantity of imports than before), it is arguable that these advantages should be enjoyed by recipients of money-incomes in the shape of increased purchasing power. But in so far as it is due to a change in the value of money for other reasons, an attempt to retain the fortuitous advantages thus accruing will involve an unjustifiable transference at the expense of the entrepreneur, which must seriously disturb the efficient working of the economic machine and be the cause of unemployment. It may be, therefore, that some downward adjustments in the quantity or value of money-incomes of every kind are called for on these grounds so long as the present low level of general prices continues. A readiness to accept the fact that the value of incomes is something which must be accommodated to changing circumstances is, indeed, an essential condition of the sound working of our economic system.

2. REDUCTIONS OF SALARIES AND WAGES AS A REMEDY FOR THE INTERNATIONAL SLUMP.

14. A primary reliance on reductions of salaries and wages as a means of restoring employment and of recovering our international equilibrium might, however, require much more drastic action than can be easily justified, or is likely to be accepted, merely on the grounds just given. It is impossible to calculate in advance what increase of employment could be expected from a given average reduction of wages. But the relation of the one to the other might disappoint the expectations of many people, inasmuch as a false analogy is often drawn from the obvious great advantages to an individual employer of a reduction of the wages which he has to pay. For each employer perceives quite clearly the advantages he would gain if the wages which he himself pays were to be reduced, but not so clearly the disadvantages he will suffer if the money-incomes of his customers are reduced. Just as it is to the advantage of each producer that every product should be cheap except his own, similarly it is to his advantage that all costs and wages should be high except those which he himself incurs—since the demand for his product comes from the incomes which are paid out as costs by other producers.

15. On the other hand, a reduction of the costs of British manufacturers as a whole which is *not* associated with an equal reduction of the incomes of their customers, plainly benefits them. So does a reduction of costs which brings them new customers. The first applies to those of them who manufacture for export,

and the second to those of them whose products, if they were cheaper, might be substituted for goods now imported. But this assumes that a reduction of costs here does not provoke a corresponding reduction by our foreign competitors. For just as a reduction of his costs only helps a domestic manufacturer if it applies to him alone and not to all his neighbours, so internationally a reduction of costs only helps British manufacturers if it applies to them alone and not to the whole world.

16. Thus there are two subtractions which it is necessary to make from the *prima facie* advantages of general wage reductions. In the first place many purely domestic industries will only obtain secondary advantages, since what they gain in reduced costs will be offset by the diminished purchasing power of their customers; so that the greater part of the primary advantages of wage reductions would be concentrated in the foreign trade industries, i.e., those which work for export or compete with imports. In the second place, even in the foreign trade industries we cannot be certain in advance that wage reductions here will not be countered by corresponding cuts on the part of our chief competitors.

17. It might be, therefore, that an attempt to remedy unemployment by general wage reductions would require very large reductions. As an illustration, an average reduction of money wages by 10 per cent. would, since it would reduce total costs by much less than 10 per cent., have much less effect on our foreign trade than a tariff of 10 per cent. on all imports and a subsidy of 10 per cent. on all exports. Yet it would be optimistic to expect even from the latter more than a partial remedy. The same conclusion follows from a comparison between the wages paid here and those paid by our chief continental competitors.

18. If the position had to be met by an average reduction of money wages only throughout all industries sufficient by itself to restore our foreign trade to an equilibrium position, it might have to be, in present conditions, as great as 20 to 30 per cent., though any such estimate must necessarily be liable to a wide margin of error. The corresponding reduction of real wages would not, of course, be nearly so great as this, inasmuch as there would be a substantial fall in the costs of home products and services. Nevertheless an attempt to secure any such reduction might be expected to produce social chaos and react most unfavourably on trade generally.

19. These considerations are far from intended to lead up to the conclusion that the remedy of reducing money-costs in terms of gold is one which can be avoided in all circumstances. But they emphasise the grave difficulties of an approach to the problem along these lines, and they raise a doubt as to whether reductions of salaries and wages are the right way of dealing with the existing

international slump. It is not easy to see how we can expect a revival in our foreign trade, on a sufficient scale to be of much value to us, by any other means than through a revival of world demand. To meet the immediate problems, arising out of the world slump, a policy intended to direct increased purchasing power into the right channels, both at home and abroad, with a view to restoring equilibrium at the *present* level of costs, would, therefore, be much wiser, in our judgment, than a policy of trying to cut our costs faster than the rest of the world can cut theirs.

3. THE ULTIMATE LEVEL OF SALARIES AND WAGES.

20. Nevertheless, it is quite possible that, when the international slump is, in the maturity of time, righting itself, we shall continue to find ourselves faced with difficulties due to our money-costs being still too high relatively to our neighbours. For in the long run we cannot support a level of money-costs in terms of gold which is out of equilibrium with similar costs elsewhere—and this is true quite independently of our adherence to the gold standard. This, perhaps, is the fundamental reason why some would think it wise to begin at once to take steps to bring down our costs, not necessarily to the level which would be required to restore our foreign trade in slump conditions, but at least to the level which may be required to put us on equal terms with our chief competitors when the slump conditions are ended. We must, therefore, endeavour to express our views on this issue as clearly as we can.

21. There are two distinct questions on which we have to form a judgment. First, what is the likelihood that the existing level of money wages will be beyond our capacity when the violence of the present Credit Cycle will have spent itself? Secondly, if in the event it does prove necessary to reduce the prevailing level of money-incomes, should the reduction be a *general* one applicable to all classes of income, and by what means should it be brought about?

22. It is obvious that it is much too soon to attempt an answer to the first question. It depends on the level at which money-costs expressed in terms of gold settle down in the countries which buy our goods or compete with us in producing them. This in turn depends on the success of the efforts recommended in the Report of the Committee for raising the international price level by increasing, through investment and otherwise, the effective volume of purchasing power throughout the world. It also depends on the time which will elapse before any success attends on these efforts and on the duration of the slump. For the longer the slump lasts, the more probable it is that country after country will feel itself compelled to resort to competition in wage-cutting.

This will be a counsel of despair, especially for debtor countries, since universal wage-cutting will help no one and will merely serve to rivet on the shoulders of the debtors a heavier burden of monetary obligation. But in the downward race anyone who can get a little ahead of his neighbours will snatch a temporary advantage, and no one can afford to lag far behind under penalty of losing all his trade. For this reason we may be compelled to follow suit. Nevertheless we should not take the lead in what is so contrary to the common interest, and we should be as reluctant as our circumstances permit to press closely behind those who are leading the way in this direction.

23. If remedial measures are delayed, the pressure towards wage reductions in the rest of the world may prove overwhelming. If so, we must grapple the problem firmly on lines to be considered below. The position may change quickly. But the available statistics have not convinced us that it is, as yet, either necessary or desirable to engage in competitive wage-cutting.

24. The matter may also be looked at from another angle. Apart from competitive considerations, does the present level of wages represent an unreasonable, and in the long run an impracticable, demand on the part of labour for too large a share of the joint product of industry? No doubt, almost everyone in a country such as Great Britain is gaining advantages in the purchasing power of his income through the exceedingly low relative prices of many articles of food, which he cannot expect to retain when the international slump is over. But this is not a peculiarity of wages—it applies equally to every class of income in a country which is temporarily in a position to import large quantities of goods at distress prices. We have, therefore, postulated some rise of international prices as a necessary condition of the maintenance of the present level of British money-incomes. The question whether the British worker is receiving too large a share of the British national dividend as compared with the other classes of the community is another matter. It is not proved, in our opinion, that wages have been recently a much larger proportion than formerly of the total value of the product—at any rate not up to 1929. The available statistics suggest that there has been a remarkable degree of stability in the proportionate division of the produce (see evidence, 47th day). Moreover there is another consideration which impresses us. If we can pay for present standards both for the employed and for the unemployed, and at the same time add to our capital wealth (as we believe to be even still the case), with nearly a quarter of our industrial resources idle, does not this suggest that we should have a comfortable margin over if we could manage to bring back into activity the whole of our resources—even after allowing substantially for the loss of our present temporary advantage from the unduly low prices of our imports?

25. Thus the problem seen in this light is one of disequilibrium rather than of excessively high standards; and the task upon which we should concentrate is that of remedying the disequilibrium so as to bring our productive resources into full play, rather than of attempting to lower standards.

4. MEANS OF ADJUSTING MONEY-INCOMES.

26. Whatever efforts we may make and however high the hopes we entertain, it remains true, unfortunately, that our efforts and hopes may be defeated. It would be absurd to maintain that we can continue to adhere to the existing level of money-incomes irrespective of the value of money. We have, therefore, to consider what measures we should recommend if an adjustment of money-incomes becomes plainly unavoidable.

27. We are here considering, not normal wage-adjustments of the kind which we have discussed at the commencement of this section, but a substantial general change, amounting to (say) 10 per cent. or more, in the level of money-costs and incomes, designed to remedy a position of national disequilibrium due to a change in the value of money.

28. We consider that a change of this character cannot, with equity, be concentrated on salaries and wages, but should apply to every category of income alike, including those protected by contract. The benefit of an increased value of money is just as fortuitous in the case of the *rentier* as in the case of the wage-earner, and the burden on enterprise and on the Budget of having to pay the same amount of money as before to meet interest charges, though the value of money is greater, is similar in character to the burden of having to pay the same money wages as before. Moreover a great social change of this kind cannot be carried through except by general consent.

29. This view is reinforced by a consideration of the monetary history of recent years. A large part of the National Debt was incurred at a price level much higher than that which now prevails. The long period of deflation which culminated in the return to gold at the pre-war parity had the effect of increasing the burden of this Debt. The fall in world prices which has occurred more recently has caused a large further aggravation of the burden. In view of the fact that the increase in the value of sterling was deliberately intended, it seems difficult to require a reduction of salaries and wages without proposing any modification of the uncovenanted blessings which accrued to the holders of the National Debt and of claims on money generally and to other classes whose incomes have remained unaffected.

30. Our conclusion is, therefore, that if a substantial change should become necessary, it must be a *general* change and apply, so far as possible, to every class of income alike.

31. If this conclusion be accepted, it follows that it cannot be left to natural economic forces to bring it about by the mere pressure of events. For this would certainly not result in an equal all-round change. In Chapter XI the Committee have explained that the pressure which can be brought to bear on the economic system by a restriction of credit, whilst suitable for the purpose of effecting the comparatively small adjustments of ordinary times, is not an appropriate means for effecting large changes. Yet, in effect, it is upon this method that we have been relying hitherto. The rate of long-term interest and the volume of credit are maintained at levels which are deterrent to investment, and the unemployment which ensues is, under a *laissez-faire* system, the natural form of pressure to secure a reduction of wages. What alternative means are open to us for an orderly contraction in terms of gold of money-incomes in general?

(a) *Devaluation.*

32. Theoretically the most obvious and comprehensive method of effecting the desired object would be to leave money-incomes alone but to change the monetary standard, e.g., by diminishing by 10 per cent. the gold parity of sterling. This would have the advantage of bringing the direct, initial benefit to those industries which need it most, namely, to the foreign-trade industries. It would involve no interference with contract, since debts are legally fixed in terms of sterling and not in terms of gold. It would affect every class of income without the necessity of any other special measures. For a country which was not an international banker and was not owed large sums from abroad fixed in terms of sterling, this would be the simplest solution.

33. We have already agreed, however, that for a country in the special circumstances of Great Britain the disadvantages would greatly outweigh the advantages, and we have concurred with our colleagues in rejecting it.

(b) *Tariffs plus Bounties.*

34. Precisely the same effects as those produced by a devaluation of sterling by a given percentage could be brought about by a tariff of the same percentage on all imports together with an equal subsidy on all exports, except that this measure *would leave sterling international obligations unchanged in terms of gold*. This proposal would avoid the injury to the national credit and to our receipts from foreign loans fixed in terms of sterling which would ensue on devaluation.

35. Under existing commercial treaties, however, there would be practical difficulties in the way of a direct subsidy to exports. Nevertheless, various plans might be propounded for combining

some form of restriction of imports with granting sundry indirect advantages to the export industries, which would represent an approximation to the above scheme. We consider that a plan of this kind would be so immeasurably preferable to devaluation, that it is foolish even to discuss the latter while the former remains untried.

36. It is worth while to remark that, if the level of domestic money-incomes is such that our international equilibrium would be restored by a reduction of money-incomes or by the devaluation of sterling, then it follows that, failing the adoption of one or other of these two expedients, the optimum distribution of the national resources between different uses will result, not from Free Trade, but from as near an approximation as is practicable to a *Tariff plus Bounties* measure on the above lines.

37. The avowed object of such a measure as this would be to reduce the value of a given money-income; though the cost of living might be expected to rise by only a fraction of the percentage rate of duty. Its advantages would be two. In the first place it would be fair; for every description of money-income would be affected equally. In the second place, it would involve no disturbance to confidence and no breach of understanding with our foreign creditors.

(c) *A National Treaty.*

38. There remains the project of a national agreement for the general and simultaneous adjustment of *all money-incomes* by a tax on incomes which, for one reason or another, are exempt from the general cut, and an adjustment of all salaries and wages and other money-incomes not protected by contract. There would, inevitably, be great practical difficulties in the way of a re-settlement of this kind, and we cannot say how far they could be overcome without giving more examination to the details of some such scheme than it has been possible for us to give. But in the last resort it is at least theoretically conceivable that by means of a National Treaty, on some such lines as this, an escape from our currency difficulties could be found.

II.—CONTROL OF IMPORTS AND AIDS TO EXPORTS.

39. Proposals under this heading raise political and social issues which extend far beyond the necessities of the present emergency. A specific may be appropriate to a particular situation, and yet be rejected in obedience to wider considerations more extended in time. We do not propose to attempt any such summing up of the final balance of advantage and disadvantage, having regard to all the relevant factors, as would be needed to justify a definite recommendation. We shall confine ourselves, therefore, to considering briefly the uses of tariffs or Import Boards, etc., and subsidies on

articles of foreign trade regarded as an expedient to meet a situation in which a country has a large unemployed surplus of labour and of plant which it is unable to bring into use in the conditions imposed on it by its economic relations, arising out of relative rates of interest and money-costs, with the rest of the world.

40. The fundamental argument for unrestricted Free Trade does not apply without qualification to an economic system which is neither in equilibrium nor in sight of equilibrium. For if a country's productive resources are normally fully employed, a tariff cannot increase output, but can only divert production from one direction into another, whilst there is a general presumption that the natural direction for the employment of resources, which they can reach on their merits and without being given special advantages at the expense of others, will yield a superior national dividend. But if this condition of full employment is neither fulfilled nor likely to be fulfilled for some time, then the position is totally different, since a tariff may bring about a net increase of production and not merely a diversion.

41. It appears to us, therefore, that, if imports were to be controlled, whether by a tariff with compensation for exports, or by Import Boards, or in some other way and home-produced goods substituted for them, there is a presumption, so long as present circumstances last, that this would mean a net increase of employment and of national productivity. Into the rate of the tariff and the classes of the articles affected we do not enter.

42. The arguments most commonly adduced on the other side—apart from long-period considerations which we are not pretending to discuss—are the following :—

(i) It is said that the restriction of certain kinds of imports would curtail foreign buying power and so diminish the market for our exports. This would be true if we were to use our improved balance of trade to import gold and the consequent loss of gold by the rest of the world had the effect of causing a contraction of total credit. But if we make use of our improved balance of trade to expand investment at home with the result of increasing our imports of food and raw materials (an expansion which would have led to a *loss* of gold by us if we had attempted it without a contemporaneous restriction of imports) or to increase our foreign lending, then it need have no adverse effect on the market for our exports.

(ii) It is said that a restriction of imports would tend to increase the cost of production of our exports. This is a question of degree depending on the kind of restriction imposed. Clearly a substantial tax on imported raw materials without a rebate for exports would have a seriously adverse effect on exports. At the other extreme, it is not evident that a tax on the importation of luxury motor cars or an Import Board for pig products would have any

appreciable consequences of this kind. It is easy to conceive both of a tariff, accompanied by appropriate rebates, and of Import Boards the effect of which on the cost of exports would be small compared with that of other factors. Nor is there any reason to suppose that the effect on exports need be commensurate with the effect on imports.

Nevertheless, even if these measures were so devised as to impose only a small handicap on our exports, this would be *pro tanto* an objection. The logical course, in our opinion, would be to find ways of giving equivalent advantages to the export industries. For much of the argument in favour of a restriction of imports applies equally to a subsidy to exports. A direct subsidy would be open to various practical objections. But it would not be difficult to find other ways of giving back to the export industries advantages at least equal in amount to the comparatively small disadvantages which would be imposed on them by those effects of restricting imports by a tariff or otherwise which would be individually too small and incalculable to be dealt with by means of a rebate.

(iii) The third objection, which is most commonly heard, relates to the effect on the cost of living of the working classes. The force of this objection depends partly on the character of the tariff or other measures in view, and partly on a comparison with the effect on the cost of living of those measures to which the tariff is offered as an alternative.

For example, a given amount of revenue raised by taxing manufactured imports would probably increase the cost of living less than if it were raised by taxes on tea, sugar, beer and tobacco. Or again, if it were to diminish the necessity to reduce wages or had the effect of increasing employment at the existing wage, its effect on working-class standards would probably be favourable. We think that a scheme could be devised which would have no adverse effects on working-class standards.

43. Since many of the arguments in favour of a restriction of imports apply equally in favour of schemes of assistance to exports, some system of restricting imports, accompanied by a policy of giving advantages to the export industries, would seem to be the most practical plan of action.

44. Finally, the immediate effect of such measures in reviving business confidence and a spirit of enterprise scarcely needs to be emphasised.

45. For these reasons and also because relief would be given both to the Budget and to the balance of trade, it would seem that restrictions on imports and aids to exports would run well in double harness with the other class of remedy which we next discuss, namely, schemes of capital development. For it is obvious that the whole of the resources required for capital development at home are necessarily found within the country and as a

result of our own efforts and sacrifices, except in so far as their effect is to diminish our net foreign surplus, whether by decreasing our exports or increasing our imports. Thus the "burden" of such schemes, for which we need to make special provision is exactly measured by the burden on the balance of trade. If, therefore, we were to expand investment at home and control imports, we should get the favourable effects of both schemes on domestic employment and avoid the disturbing effects of both on our international balance.

III.—SCHEMES OF CAPITAL DEVELOPMENT.

46. We see no reason to doubt that new capital investment at home would, in present circumstances, create additional employment—subject only to the qualifications explained below. From this additional employment being less than appears at first sight, it is likely to be considerably more. For in addition to the men directly employed and to the men occupied in making and transporting the materials required, there will be a further set of men put into work to supply the needs created by the additional purchasing and consuming power of the first set of men, and so on.

47. The objections which have been advanced against an unqualified acceptance of this conclusion are the following :—

(i) It has been argued that it is not possible to ensure that any particular scheme of investment will mean *additional* expenditure. It may merely cause a diversion of finance and of resources from different expenditure which would have occurred otherwise. If the national productive resources were fully occupied, this might be the case. Or if the banking system were to limit the volume of credit in a certain way, it might be the case. But in present circumstances, when the physical limit on further capital output is far from reached, there is no reason why the action of the banking system need stand in the way of additional investment, unless this investment was throwing too heavy a burden on the balance of trade—a contingency which we deal with below. For the theory that there is in any sense a fixed loan fund available to finance investment which is in all circumstances fully employed, or that the amount of the savings of the public always exactly correspond to the volume of new investment, is, we think, mistaken. At one time some such view as this appears to have influenced British policy. To a questionnaire from the International Labour Office in 1927 the British Government replied :— "The decision taken by the Government at the end of 1925 to restrict grants for relief schemes was based mainly on the view that, the supply of capital in this country being limited, it was undesirable to divert any appreciable proportion of this supply

from normal trade channels."* The Treasury White Paper, Cmd. 3331, p. 43, was also capable of interpretation in this sense. We gathered, however, from the evidence of Sir R. Hopkins that it would be a mistake to attribute this view to the Treasury at the present time.

(ii) It has been argued that, whilst investment spontaneously undertaken by private industry would help employment, there may, nevertheless, be some offsets to schemes deliberately engineered by the Government. For the effect of such schemes on the minds of business men might be such as to make them less inclined to launch out themselves. This might be true of "unfair" Government-aided schemes, by which some private firms received assistance from which other substantially similar firms were debarred. It might also be true that business confidence would be injured if the Government were to sponsor obviously wasteful, foolish or extravagant projects. But in general, provided the schemes are wisely selected, we see no presumption in favour of the view that "official" investment need seriously compete or interfere with "unofficial" investment. Indeed, on the contrary, if "official" investment is successful in restoring the volume of output and of profits, this may help to restore the business optimism which is a necessary condition of expansion. It may be that a dose of "official" investment will be helpful in breaking the vicious circle and restoring the conditions in which we can again increase our reliance on normal "unofficial" investment.

(iii) It has been objected that the tendency of such schemes will be in the direction of raising prices in this country and thereby hamper our export industries in their efforts to retain their hold on foreign markets. If our available plant were fully occupied, there might be much force in it. But in existing conditions, we do not doubt that output could be expanded in many directions in response to an increased demand with an insignificant increase in price. Indeed, some witnesses have gone so far as to maintain that, if output were to be increased, prices would be reduced, basing themselves upon the lower cost per unit of production when plant is fully employed.

In any case we should attach limited importance to this objection because, in so far as output cannot be increased except in response to a higher level of prices, this objection applies equally to *all* remedies for unemployment of whatever character, except those which involve a reduction of wages.

(iv) It is sometimes argued that home investment may not only embarrass our export industries for the reason just discussed, but

* "Unemployment and Public Works," International Labour Office, 1931, p. 30.

will also put a fresh burden on our balance of trade, because it will tend to increase our imports, both to furnish raw materials and to provide for increased consumption, particularly of food, by the newly employed. This is clearly, to some extent, the case. But here again it is an objection which applies to *all* remedies for unemployment. Any increase of employment is likely to bring with it increased imports of the raw materials of our industries and of the articles of working-class consumption. But this is scarcely a reason for not providing employment. The point is to be regarded, rather, as a reason for not embarking too rashly to large-scale schemes without arranging at the same time as to how the necessary increment of imports is to be paid for.

It is at this stage that considerations which are more of a monetary character come in. It is the business of the Bank of England so to regulate our net rate of foreign lending that it does not seriously exceed our available trade balance. A recovery of domestic output must, when it occurs, present the Bank with a problem of this kind. But schemes of capital development would have to be on a larger scale and mature with greater rapidity than is at all probable, before they would present the Bank with too heavy a task, unless they were to be undertaken simultaneously with a general breakdown of confidence due to other causes. We are still a creditor country on a large scale, and it would be an overwhelming condemnation of our present methods if proposals for increasing employment were to be rejected on the ground that we cannot pay for the raw materials which the men would handle and the additional food, etc., which they would consume, if they were to be brought back into employment.

(v) It is feared that State-aided schemes are likely to put some burden on the Budget and therefore to lead to the evils of increased taxation. If, however, we lump together—as we should for the purposes of this argument—the Budget and the Unemployment Fund, we feel quite confident that the relief to the Unemployment Fund and the additional yield of taxation, resulting from the increased employment provided by the schemes in question, would materially outweigh the direct cost of the schemes to the State.

(vi) A final objection—which may, we think, have weighed with the Treasury—is based on the possible effect of loans, made or sponsored or guaranteed by the Government, on the rate of interest on British Government securities, with the result of postponing the date at which large economies can be secured by a conversion of the War Debt to lower rates of interest.

This is a natural, but nevertheless dangerous, pre-occupation. Over any short period it is evident that the prices of Government securities may be affected by competing issues. But it is an exact inversion of the truth about the rate of interest to suppose that it can be reduced by *refraining* from new capital investment. Apart

from the short-period fluctuations around the equilibrium position, the rate of interest must tend to fall as the accumulated wealth and prosperity of the country in the shape of capital assets increases. The contrary view is based on some such fallacy as that "surplus" financial resources can be gradually built up, unembodied in any physical form. It is supposed that if we "save" a part of our current income and do not "use up" these savings in capital schemes, we can in some way hoard them up and use them at a later date and that these "accumulated" savings will gradually strengthen our "financial" position. These ideas are probably derived from a false analogy between the position of a particular individual or firm and that of the community as a whole. For a particular firm can clearly accumulate "liquid" resources, unembodied in any physical form so far as the firm itself is concerned and constituting realisable claims on the rest of the community. But a little reflection will show that the community as a whole cannot increase its "liquid" resources by the various members of it building up claims against one another.

We have dwelt for a moment on this highly abstract point because mistaken ideas about it may be the explanation of much latent, unexpressed hostility or reluctance to the general idea of organised capital development. It is one of the cases where uninstructed commonsense tends to believe exactly the opposite of the truth.

48. The main obstacle in the way of remedying unemployment by means of organised schemes of investment is probably to be found, not so much in any of these arguments, as in the practical difficulties of initiative and organisation. It is not easy to devise well-conceived plans on a large scale. It is not easy to fit them into the existing scheme of things, even when they have been conceived, without all sorts of difficulties, frictions and delays. And, finally, the period of preliminary planning and designing, which must elapse before they will provide their full quota of employment, may be somewhat lengthy. It is difficult to improvise good schemes. If they are to be thoroughly wise and economical, they may often need as much as two years' preliminary gestation. Yet we have seldom been ready in recent years—though subsequent experience has taught us that we ought to have been—to sit down calmly to prepare plans for the remedying of unemployment two or three years hence. This difficulty has increased with time. For by now most of the good plans which can be quickly improvised have been used up, and the best plans still left in the cupboard are those which will yield their results most slowly.

49. If, therefore, the organised planning of capital investment is to be relied on as a remedy for our economic ills, it should, we think, be approached from now on in a somewhat different spirit from that which was natural three or four years ago. We must be

prepared, that is to say, to look some way ahead, and get to work on well-conceived projects without laying too much emphasis on the rapidity with which they can be executed.

50. There is the more reason for this, in that the problem of finding an outlet at home for a substantial proportion of our current savings is likely to be with us for some time to come. We recommend, therefore, that we should now attack the task of Capital Development in this country in a much more systematic and far-sighted manner than hitherto. It should not be an objection to a scheme that its execution will be spread over many years or that the period of preparation will be somewhat prolonged. After several years of living from hand to mouth, a point has come when it need not be considered an imprudence to look ahead.

51. It falls outside our scope to proceed to details in a matter of this kind. But we may illustrate our argument briefly :—

(i) A considerable part of the larger towns and industrial centres of the country need re-building and re-planning on a comprehensive scale. At present they offer neither beauty nor convenience nor health. Much of the industrial housing of the country is of an age when buildings of that character are, of necessity, only fit to be demolished. It seems an insanity to keep a large proportion of the building trade out of employment when this is the case.

(ii) Some of our staple industries need to be refitted and re-planned on modern lines, at the cost of a substantial capital expenditure. In several cases, there is much to be said for re-planning an industry as a whole. Apart from tariffs, and the like, we see no reason why our staple industries should wait before putting their house in order. In cases of proved necessity, we should not be opposed to measures of compulsion, in conjunction with the provision of adequate and cheap finance. It may be that we should develop an improved organisation for handling all matters of this kind. It would be outside our scope to pursue this subject in detail. But we think that efficiency and fore-thought might be much increased if a body were to be set up which might be designated the Board of National Investment, in the hands of which all matters relating to the deliberate guidance of schemes of long-term national investment would be concentrated. This Board might be entrusted with the duty of raising funds not only for the local authorities which now borrow through the Local Loans Fund but also for other local authorities including municipalities, for the telephones, for the roads and for such further schemes of national development as those which we have suggested above. But this is a big subject and it would lead us too far afield to develop it as it deserves.

(iii) The recommendations of the recent Committee on the Electrification of the Railway System obviously deserve the most careful consideration in this connection.

52. The fundamental objection to these expedients, in the minds of those who dissent from them, is, however, on a different plane of thought. They consider that all these devices are merely temporary shifts to enable us to postpone facing the problem, which sooner or later we shall be compelled to face, namely, that our money-costs of production are too high compared with those elsewhere; whilst at the same time they are of a character which, to judge from experience, are often used unwisely and may remain as an incubus on our economic system long after their special purpose has passed away.

53. The ultimate differences between those who feel this and those who think that it is worth while to gain a breathing space are not so much matters of theory as of the practical judgment of probabilities and of what is most prudent. But we suggest that a heavy burden of proof lies on those who cannot join with us in our plea for efforts to increase activity rather than to reduce standards. For if we can do what we are doing with nearly a quarter of our industrial resources idle, what might we not do if they were all employed? We are impressed for many reasons with what seems to us to be the greater wisdom and prudence of concentrating public attention on constructive schemes for encouraging national trade and national development rather than on efforts to drive down the general levels of salaries and wages. Let us, in conclusion, briefly recapitulate some of them:—

(i) If, at the present juncture, when we are near the bottom of a world slump of unparalleled violence, all countries alike were to seek equilibrium by competitive wage cuts, we should merely confirm the low level of prices and rivet on our shoulders an intolerable burden of debt fixed in terms of money.

(ii) We doubt whether it is wise to attempt fundamental adjustments, which may not be required, at a time so abnormal as the present, when similar difficulties are confronting all countries alike and when it is impossible to gauge with any accuracy the degree of adjustment which may be necessary in the long run.

(iii) We see no solution of the grave problem of social justice presented by any proposal to reduce salaries and wages whilst leaving untouched those money-incomes which are protected by contract.

(iv) Even if it were desirable to secure a large all-round reduction of salaries and wages, we foresee immense practical difficulties, perhaps insuperable difficulties, in the way; whilst the social costs of an attempt which failed would be incalculable.

(v) We prefer, therefore, to pin all our hopes on a recovery of world prices, and to strain all our efforts to secure it; whilst making, immediately, a great concerted attempt to avoid the immense waste of the national productive resources now going on. If these hopes are falsified by the event, much will by then have happened in the world, which we cannot now foresee. Public opinion, both here and abroad, will be ready for many things which it would be useless to consider now. And the whole matter will have to be reviewed again.

(vi) Meanwhile, we are not convinced that we cannot in the long run, when all our productive resources are at work, continue to support permanently, and even improve, our existing working-class standards. It may well happen, if we can gain a breathing space, that the recovery of world prices, the revival of business optimism, the reorganisation of the older British industries and the steady increase of technical efficiency may eventually render unnecessary a reduction in the prevailing level of salaries and wages.

THOS. ALLEN.*

ERNEST BEVIN.*

J. M. KEYNES.

R. McKENNA.

J. FRATER TAYLOR.

A. A. G. TULLOCH.

*SUBJECT TO THE FOLLOWING RESERVATION.

We have signed Addendum I in company with Mr. Keynes, Mr. McKenna, Mr. Frater Taylor and Mr. Tulloch, but, while approving the general approach to the subject, we do not necessarily agree with every statement therein. We think it vitally important to emphasise that to acquiesce in the present or a lower wholesale price level, with the idea of adjusting everything down to it, is fatal. We are in full agreement that the only possible policy is to try to raise the wholesale price level and to maintain or improve the standard of life.

If this cannot be achieved internationally within a reasonable time, we agree that national action of an emergency or short-time character should be tried.

We should have preferred the course of devaluation because of its effect upon the whole of the dead-weight debt and other fixed

charges, but we agree that great weight must be attached to the consideration that to endorse a de facto devaluation is easier than to devalue after a return to pre-war parity.

With regard to the tariff proposal in the Addendum we take the view that, precedent to any tariff, our other recommendation for a large measure of State planning and reorganisation, particularly in the basic industries, with the provision of Transport and Power as State services, should be put into effect. Then, if the alternative remained, tariffs would be preferable to all-round reductions in wages and salaries, provided that at the same time steps were taken to safeguard the export trade and to prevent the exploitation of the consumer.

In a general way we do not believe in tariffs, and we are rather more apprehensive as to their effects than the other signatories. Nevertheless, our view is, if we have to make a choice, it should be in the direction indicated.

The other points in the Addendum, such as schemes of Capital Development, Board of National Investment, etc., have our strong support.

THOS. ALLEN.
ERNEST BEVIN.

ADDENDUM II.

1. We recommend in Part II, Chapter III, of our Report that greater freedom should be given to the Bank of England in the employment of its reserves. But this greater freedom, which also involves greater responsibility, can hardly be used satisfactorily if our exchanges are to be subjected to a constant strain with the result that, while it might always be easy to lose gold, it might be hard to get it back except by means of a restriction of credit and relatively high interest rates which would be definitely harmful. For the greatest service which the monetary machine can render British industry and commerce at the present time is to maintain plentiful credit and cheap money rates, so that, as soon as some confidence returns, production and enterprise will be encouraged by means of an increase of purchasing power without any adverse effect on our exchanges. It seems to me, therefore, of the first importance that the surplus on our balance of trade should be increased. Notwithstanding that we own greater foreign assets than any other nation and receive annually from the rest of the world, as a result of the efforts and savings of past generations, a sum of some £300 millions in respect of interest, redemption and dividends and have the greatest "invisible exports", the surplus on our balance is now small, since the great bulk of these annual sums due to us is now required to pay for our imports. Our relatively high level

of internal costs and money incomes limits the power of those of our industries which compete with foreign industries either to export or to compete with foreign goods imported into this country, while it maintains internal consumption. Thus, as is shown in Part I, Chapter V, the volume of our exports has diminished and that of our imports has largely increased. It is this condition that renders a mere increase of purchasing power without a strengthening of our balance of trade impracticable.

2. In order that the surplus on our balance of trade should be larger, it is necessary to increase our exports or diminish our imports or do both. There appears no reason, however, to suppose that the normal course of events will by itself bring this result about. Rather the contrary. For, though many other adverse circumstances have since the end of the War pressed upon our export industries, our relatively high level of costs, tending to encourage imports and discourage exports, is of long standing and has undoubtedly contributed to their difficulties. It must be remembered that, before the world slump began, the great bulk of our unemployment, which for years has never fallen below about 1,000,000, came from those of our industries which were subject to foreign competition. Unless world prices rise again quickly and substantially, the disequilibrium from which they suffered is likely to be intensified if, as is happening now, other nations, whose economic conditions are more flexible, take earlier and more definite steps than we do towards some adjustment of costs to the lower level of prices. When a crisis like the present one overtakes all countries, in none of them does the business world sit with folded hands and wait for the monetary authorities to restore the conditions previously existing. Every industrial and commercial unit in each country is moved by the incentive of self-preservation to set to at once and try to adjust itself to the altered conditions. Its essential problem is to bring costs and prices again into such a relationship that the various factors of production, those which depend on profit as well as those receiving a fixed money-income, may obtain adequate remuneration, so that the operation of each unit will again become profitable, idle plant be restarted, output increased and, gradually, new development undertaken.

As a result of the great fall of prices without an equivalent reduction of costs, production all over the world is resulting in losses instead of profits. It is sometimes argued that a reduction of costs (in particular wage costs) will do nothing to alter this situation, because the reduction of costs is a reduction of incomes and involves therefore a destruction of purchasing power. But costs do not represent the whole of the incomes derived from production and still less do wage costs. These incomes include *profits*, and it is on profits being normal that the whole activity of private enterprise depends. The first impact of a reduction of costs is felt in an increase of profits or a substitution of profits for losses. A re-

distribution of the present proceeds of industry so that more of the proceeds would accrue to the shareholder and entrepreneur would not reduce the existing volume of purchasing power, but would induce entrepreneurs, by additional orders for raw material, plant and labour, to expand the volume of employment, and thus should lead rather to an increase than to a decrease of purchasing power. So long as enterprise promises a loss rather than a profit, no one will borrow and the normal process by which money is generated through the lending operations of the banks is interrupted. But a reduction of costs would alter the outlook, borrowers would come forward and money would become available to pay the additional incomes arising from the additional production. For this process to be continued, it is necessary that the banking system should be able freely to grant the necessary credit and for this to be possible without any weakening of our exchanges the strengthening of our balance of trade is again seen to be essential.

Moreover, in the present situation, where the products of the raw-material countries are so exceptionally low in price, the manufacturing countries will be forced to reduce their costs so far as possible in order to facilitate the exchange of industrial as against raw-material products. So long as, and to the extent that, world prices do not rise, there must, therefore, everywhere be a pressure to reduce costs, either by increasing efficiency or by a direct reduction of money-incomes.

3. If this diagnosis is correct, it is likely that, failing special action on our part, our costs will become higher rather than lower relatively to other countries' costs with the consequent tendency for profits to remain low, for capital to make efforts to leave the country and for exports still further to diminish and imports still further to increase. This tendency can only be reversed by (i) a diminution of costs by means of either (a) greater efficiency or (b) a direct reduction of salaries and wages, or (ii) special measures such as a tariff for the restriction of imports accompanied presumably by some direct assistance to our exports.

4. It would no doubt be agreed on all hands, even by those who support a tariff on other grounds, that by far the best method of diminishing imports and increasing exports would be by a greater increase in our efficiency relatively to the efficiency of our competitors. It is, indeed, only by constantly increasing our output for a given amount of labour that we can increase our standard of life. If wages are to be maintained, there is need of the most active co-operation towards the greatest efficiency and elasticity by industrial and financial leaders and by Trade Unions. I believe that there is a very great deal of leeway to be made up and that opposition to reform does not come from one side alone. If the object of the Trade Unions is to maintain *real* wages by a

higher output per man, they must recognise how vital it is to remove hampering restrictions, to facilitate the greatest possible mobility of labour and to prevent unemployment insurance from being itself the inevitable cause of permanent unemployment. But prejudiced resistance to changes obviously needed in the interests of the community is to be found also in those directing and managing industrial and public utility companies. If private enterprise is to hold its own, this resistance must be overcome. I believe, therefore, that there are still very big opportunities to reduce costs by greater efficiency in the widest sense of modernising both production and selling and limiting harmful competition. With the growing mechanisation of industry throughout the world, very cheap production of many kinds of goods is possible in more backward countries even with relatively unskilled labour. It is by constantly keeping in the van in the more skilled industries that we must maintain our position.

5. Secondly, we can reduce imports and increase exports by a direct reduction in money-incomes, i.e., salaries and wages. The cost of living has fallen in this country and real incomes have, therefore, risen by 18 per cent. since 1925 and by 12 per cent. since 1929. If there is a general rise in world prices, real incomes will again fall but, even if world prices were to rise, say, to the 1929 level, the disequilibrium which already existed in that year might continue to show itself as before in large and persistent unemployment. If prices remain at or near their present level and other nations adjust their costs to that level, while we do not, then our balance of trade will probably become constantly more unfavourable, and a situation might arise which might force an adjustment of *all* money incomes. If, on the other hand—and this is perhaps the most likely outcome—a new level is established by both prices rising and costs falling, then in so far as we have not relatively increased our efficiency, we must make at least equal adjustments in costs to those made by other nations to maintain even our 1929 position. It would appear, therefore, that, so long as prices remain at or near their present level, reductions of salaries and wages (particularly in the sheltered industries), and obviously in unemployment benefit too, are necessary if we are to maintain, and still more to strengthen, the surplus of our balance of trade and thus keep monetary conditions favourable to increasing enterprise and employment at home. Reductions in salaries and wages have taken place, and are taking place, in other countries, and particularly in Germany where Reparation payments cause a strong pressure in this direction. The developments in the rest of the world in the next six months or year in the direction either of rising prices or falling costs will show us more clearly the extent of our problem in this respect. What is certain is that no country can support permanently both a fixed exchange and a fixed level of money costs

in terms of gold which is out of equilibrium with costs elsewhere. Ultimately one or the other must give way.

6. If any practicable diminution of costs under the two headings of (a) greater efficiency and (b) direct reduction of money incomes is insufficient to bring us near to equilibrium, then I do not think that we can sit down and do nothing. In order to protect our exchanges and to enable the Bank of England to maintain credit conditions favourable to home industry, it might become necessary to take steps to restrict imports either by a general tariff on all imports or by a more specialised protective tariff, or by some restriction of unnecessary imports. I say nothing about the many other important aspects of a tariff, as I confine myself here to its relationship to the monetary problem. From that point of view it does not seem possible permanently to combine Free Trade with a rigid economic system under which money-costs in terms of gold remain out of line with those elsewhere and cannot be altered. But import duties, while diminishing imports, would tend also to diminish exports, unless accompanied by rebates, subsidies, or some other aids direct or indirect, which would cheapen the cost of our goods to the foreigner at the expense of the British taxpayer. It would, moreover, be unlikely that any new exporting industries, to which in these changing times we must look forward to help us, would get under weigh, unless they also received similar assistance. Furthermore, if any rise in prices internally, resulting from a tariff, merely leads to a proportionate increase in salaries and wages, and therefore in costs, then our disequilibrium will remain unaltered and a condition of affairs will be created in which another tariff "dose" will again be necessary to produce a temporary adjustment. It was, for instance, the experience in Australia that successive increases in the tariff followed upon, or were followed by, successive advances in the cost of labour, and involved that country in a vicious circle of ever-ascending costs and prices.

Thus the strengthening of our balance of trade by means of a tariff is not likely in my opinion to be as satisfactory for our export industries as a reduction of costs under the two other heads discussed above.

A protective tariff, as distinguished from a flat-rate revenue tariff, might increase certain exports as a result of giving the industries protected a sure foundation in the home market. But, having regard to our difficulties already existing in 1929, I am doubtful whether any assistance in the form of rebates, subsidies, etc., which it will be practicable to give under a tariff system will enable exports in general to flourish without a reduction in our costs relatively to foreign costs.

7. While an increase of home enterprise is of the greatest importance, flourishing export industries are in my opinion needed both to raise our standard of life and to employ fully our population,

as well as to strengthen the surplus on our balance of payments. One-third of all the workers engaged in manufacturing are dependent directly for their livelihood on the amount of export trade which we still retain. I disbelieve wholly in any plan of insulating ourselves from the rest of the world or that there is not future scope, as world prosperity grows, for our 40,000,000 people to trade on a much greater scale than at present with the remaining 2,000,000,000 people in the world. We may aim at using nearly all our savings at home so that the pressure of capital to find an outlet abroad is diminished, but it is hardly possible to suppose that if we live to "ourselves alone" the savings available for use can ultimately be as large, and therefore our standard of living as high, as they would be if we exchanged our products freely with all the world and maintained our commerce and our shipping. It is true that, until world conditions generally improve, we cannot expect any very great increase in exports. But to diminish exports and increase imports, as we are tending to do now, to the point at which we shall ultimately require the whole of the proceeds of the interest on and redemption of our foreign assets to balance the surplus of our imports, is not to lay our foundations very safely. In the first place we should cease to be a creditor nation and have no money to lend abroad. This would not only mean a great alteration in the position of London as a financial centre. It would also be very unfortunate from the point of view of the development of the British Empire. We should be surpassed in wealth and influence by those who took our place as creditor nations. Moreover, our foreign assets constantly require replenishment, for they are always being diminished by repayment, by losses, or by the failure of our debtors and for this reason alone some surplus on our balance of payments is required.

8. I do not consider that greatly increased capital expenditure by the Government or other public authorities is a solution of our difficulties. There is everything to be said for schemes, however large, which are in themselves desirable and remunerative (such as railway electrification may prove to be) and which improve our national plant and lead directly or indirectly to large economies in costs. The fact that we are spending over £120,000,000 per annum on unemployment without anything to show for it is a strong additional reason for not rejecting off-hand projects of real promise. But the efficacy of public expenditure is severely limited by practical difficulties. Any large scheme requires many months of examination and preparation and, if commenced now, could not be actually taken in hand for at least one or two years. If a number of very large schemes were projected now, the Government might come with great demands upon the capital market at the time when conditions were improving and private enterprise itself might need large capital funds. Outside such an exceptional case as the electrification of the railways, large and remunerative schemes are probably quite

limited. If they are not remunerative, but involve annually a burden for interest and sinking fund on the Budget, they would have the great demerit of adding permanently to our expenditure at a time when direct taxation is already too high. Anything, indeed, which increases the present or prospective burdens on the Budget obviously requires the narrowest scrutiny. Whatever may be the merits of capital expenditure by the Government, they do not compare in their effect on unemployment and industry with the placing of private enterprise on a more profitable basis.

9. If prices rise not at all or only slightly and meanwhile other countries adjust themselves either by a reduction in costs or by going through a process of inflation, no lowering in costs, either by greater efficiency or by a reduction in non-contractual money incomes, can be expected to solve our problems. The burden of our high costs and our huge debt might then prove intolerable, unless mitigated by sacrifices on the part of *all* sections of the population. The problem of contractual money-incomes is, however, extremely complex, and differs fundamentally from that of salaries and wages in that the recipient of a contractual income must accept the risk of loss from movements in the value of the currency equally with the prospect of gain. The "rentier" has gained by the fall in prices; he will lose, if they rise again. An extreme illustration of his risks may be seen in the cases of Germany, France and Belgium, where a permanent depreciation of the currency has involved him in final and irrecoverable loss. Moreover, the "rentier"—and that term covers both individuals and institutions—is in fact inextricably mixed with the investing part of the community, which as a whole, has made some gain from the fall in prices through holding fixed-interest securities, but has at the same time suffered through the writing down or complete loss of part of those holdings and through the very heavy losses on their investments in shares. It is this complexity which makes the application of any general scheme to all money-incomes so difficult, and which therefore makes a rise in world prices so essential to any normal solution of our difficulties.

10. Finally, the difficulty of securing a world rise of prices and the dangers of the present world economic situation are greatly aggravated by the Reparations and Inter-Allied debt problem. In the first place, the pressure on Germany to increase her exports necessitates the utmost possible reduction in all her costs, including all salaries and wages, which have in fact already been very considerably lowered. This, in turn, increases the pressure on all her competitors and particularly on us to follow suit. Germany is so important a factor in overseas trade that this influence in the direction of holding prices down must be considerable. Moreover, the payment of these great sums, mainly to the United States and France, very considerably aggravates the

problem of the debtor countries referred to in Chapter II of Part II of the Committee's Report, renders the German situation dangerous to the whole international credit structure, and accentuates the tendency of gold to flow to the United States and France which is particularly undesirable at a time when neither of them are lending their surplus back to the world. If it were possible to wipe out the Reparations and Inter-Allied debt payments, by far the greatest single step would, in my opinion, have been taken towards the recovery of world prosperity. Indeed until some fresh settlement of this problem, rendered necessary by the great fall in prices, is made, I do not believe that we can expect any recovery.

R. H. BRAND.

ADDENDUM III.

Introduction.

1. I desire in this note to express my views upon the present situation and upon the various proposals which have been put forward as cures, or at least as palliatives, for the evils complained of; further, to present some observations upon certain of the problems which fall directly within the Terms of Reference and have already been touched upon in the Report of the Majority of the Committee.

2. It is common ground that the difficulties with which we are contending result from the accentuation of the pre-existent local depression of trade and employment through the world depression, which, beginning in the second half of 1929, has now lasted for nearly two years without showing any marked tendency to come to an end. The disequilibrium between prices and costs, which was a special characteristic of this country before the world depression, has now become a world phenomenon. But the fact that disequilibrium has become general means also that the degree of disequilibrium in this country has now grown cumulatively greater than it was before.

The Local Situation.

3. It is obviously impossible for this country, by any special action it can take by itself, to cure the world situation; although as a country which is one of the two largest creditor nations, with a capital market upon which a large part of the world habitually relies, with a Central Bank enjoying great international authority and prestige, and with a population with a high per capita volume of exports and a high per capita consumption of internationally traded goods, we are in a position powerfully to influence the course

of world events, even if the allowance is made for the special disabilities under which we are labouring. Our duty in this connection would seem to be a twofold one: to abstain from action which, if generalised, would result in making the world situation as a whole worse than it was before, and to follow policies which, whilst benefiting ourselves, will also help to alleviate the world situation. Apart from all other considerations, therefore, and considering solely the world situation, to embark upon a régime of tariffs and to refuse obstinately to face the question of costs are both undesirable. For to adopt the first will undoubtedly encourage a general tendency to further economic isolation on the part of other countries, thus impeding the recovery of world trade; whilst to refuse to face the second issue will lay us open to the charge that we are seeking the co-operation of other countries in obtaining a rise in the world-level of prices because we have neither the will nor the ability to take the steps necessary to bring us into line with what is taking place elsewhere. We must be in a position to convince other countries that we are not dependent on their goodwill to save us from difficulties which, however mistakenly, they believe to be largely of our own making, before we shall be in a position to represent to them successfully that co-operation in the field of credit is a necessary part of the process of recovery. The mischief will not stop at this point, however. By one means or another, the world, as a whole, will climb out of the present depression, as it has recovered from previous ones. If recovery takes place in the outside world without any definite steps towards international co-operation having been achieved, it is certain that they will then become impossible for a long time to come; for it is not in periods of prosperity that efforts of this kind are likely to be inaugurated. And our moral and economic position alike may be permanently injured; our moral position by our failure to convert the rest of the world to our way of thinking; our economic position by our failure to make the adjustments necessary to accommodate ourselves to changes in the world as a whole.

The World Situation.

4. As far as the world situation at the moment is concerned, two solutions are presented for consideration. It is urged on the one hand that a concerted effort should be made to raise the level of prices; it is urged on the other that the way out of the present impasse is to reduce costs.

It is argued by some of those who support the first solution that it is impossible to solve the problem of a depression in any other way: for a reduction of costs cannot result in anything else except an endless sequence of changes, in the course of which prices first fall, to be followed by falling costs, which in their turn result in prices falling again, requiring a further fall in the level of costs and

so on. Thus the only result of the process is a cumulative fall of prices, which has merely the effect of increasing the burden of indebtedness and all other fixed charges, and does nothing to revive industry and employment.

It is argued by some of those who support the second solution that concerted efforts to raise the level of prices by means of additional credit-creation are not in any case likely to be made. Secondly, that a period of falling prices and depressed trade brings with it a necessary process of elimination of unsound borrowers and undertakings whose disappearance is necessary for a revival of sound business and of confidence in borrowers—a process of weeding out which would be delayed if plentiful credit were immediately available. But the longer the process is delayed, the greater will be the liquidation necessary when, at long last, further credit creation proves unavailing to prevent the collapse of unsound institutions. Thirdly, it is argued that the process of credit-creation, if successful, involves the danger that revival may take place upon a scale and with a rapidity that may make it imperative quickly to withdraw this additional quantity of credit. But in the face of violent opposition by the business classes this necessary policy of subsequent contraction may prove impossible, and the overstimulation thus given to the upward phase of the cycle may be followed by an even worse collapse than the one to overcome which the policy was first attempted.

5. Neither set of contentions appears to dispose conclusively of the policy against which it is directed, and there seems to me to be no necessary inconsistency in the simultaneous application of both policies. To demonstrate that if costs are cut there will be a revival of trade is not tantamount to a demonstration that, therefore, the process of revival should be accomplished *solely* by this means. To demonstrate that a process of credit expansion would in the end revive business is not the same thing as proving that exclusive reliance should be placed on this method of attacking the problem. For it may well be that difficulties which would manifest themselves if only one method were employed may be absent if both are utilised.

(a) The reluctance to admit that a reduction of costs will alleviate the situation resulting from the present universal maladjustment between prices and costs, springs from a confusion between a reduction of costs and an effective destruction of purchasing power. The argument upon which this reluctance is ultimately based can be stated as follows. Money costs represent income accruing either to wage earners or others taking part in the processes of production, and in the form of income, therefore, constitute the purchasing power from which flow the receipts accruing to producers. If costs are reduced, therefore, it follows that purchasing power is diminished, and the relationship between receipts and costs remains

unaffected. At the lower level of costs, receipts will still be insufficient to cover costs, just as they were at the higher level of both costs and receipts.

(b) But the fact is that a reduction of costs is not necessarily tantamount to a proportionate reduction in aggregate receipts, because, so long as the costs remain above prices, unemployment ensues. It follows, then, in spite of the fact that what is paid out in costs reappears later in the form of receipts, that the aggregate volume of receipts is less than it would have been if costs had been lower and unemployment had been less.

Again, given the present level of prices and costs, production, it is freely admitted on all hands, results in losses to the entrepreneur. A redistribution of the present proceeds of industry, such that more of the proceeds would accrue to him, and less to the other factors of production, would not reduce the *existing* volume of purchasing power, but would induce him, by additional orders for raw material, plant and labour to expand the volume of output and of employment, though it might admittedly, so long as the aggregate volume of employment had not been appreciably affected, change the nature of demand somewhat through changes in the distribution of the proceeds of industry. But the mere fact that unemployment was falling would restore to the industries producing consumption goods part of the demand which they might have temporarily lost. It would not be true to argue that such an impulse to the expansion of production would be held up by the impossibility, at the new level of costs, of finding the volume of purchasing power, in terms of money, necessary to sustain it. For if prices and costs are in adjustment, the *de facto* volume of purchasing power available must always be sufficient. But it is not difficult to see further that once given the emergence of profits to the average entrepreneur, a series of repercussions in the field of credit-creation are likely to take place which will remove the danger (if any) that the expansion of production and employment will be checked by insufficiency of purchasing power. For entrepreneurs are more willing to borrow, and bankers more willing to lend, in a period when profits are emerging than in a period when industry as a whole is sustaining losses. It may be argued, therefore, that the adjustment of costs to prices is the necessary preliminary to the inception of monetary processes which will initiate an upward movement of prices, and thus assist such adjustment in those portions of the field of production where it has not already taken place.

(c) The view that an adjustment by means of a fall of costs, rather than by means of a rise of prices, is objectionable, not because it fails to achieve its object but because it would increase the burden of debt charges, requires separate consideration. If prices remain permanently at a lower level, the purchasing power of

debts will increase considerably; as they will equally increase if the reduction of costs takes the form of increasing efficiency. But if the adjustment of prices and costs results in increasing employment and output, the real burden represented by debt charges upon output as a whole may still be a smaller one than it would have been if the adjustment had not been made. For, if the adjustment had not been made, the debt charges would have had to be met out of a smaller dividend. Moreover, as has just been argued, it by no means follows, once prices and costs have been brought more closely into line than is now the case, that a low level of prices will be permanently imposed upon producers. Purchasing power has not been destroyed but only redistributed; and a revival of activity will, partly in virtue of the banking repercussions associated with it, partly in virtue of the direct effects produced by increased trade, help to raise the price level. There is, therefore, no reason to suppose that an adjustment of costs to prices must involve a level of prices permanently as low as that now existing: nor that, even if it did, considerations relating to the burden of indebtedness would be a final reason for refusing to make the adjustment, *if no other solution were possible*.

(d) On the other hand, it is impossible to deny that the process of adjusting costs to prices is one which necessarily involves much hardship, and individual inequality and difficulty, and raises such far-reaching issues of social stability, that, if it could be avoided, even if only in part, by cheap money and credit expansion, very weighty arguments would have to be advanced to justify inaction on the part of the banking authorities. The argument that it may later be necessary to retrace the steps taken and to deflate credit in order to avoid over-expansion at that stage, cannot be considered a sufficient reason against present action. For, in all probability, the process of recovery from a depression so severe as the present one will be slow, and ample statistical and other material is available for the guidance of the monetary authorities, nor will the technical forms, which any repressive measures (which may indeed subsequently prove necessary) would have to take, present any unusual features. In these circumstances the case against present action, *on these grounds alone*, cannot be considered conclusive, though I would agree that the dangers apprehended are by no means entirely imaginary. Nor, in my opinion, can the argument that some liquidation of weak positions is a necessary part of the process of recovery be pressed too far. For, as the depression continues, the circle of weak borrowers becomes wider and wider; for the losses sustained as a consequence of the depression gradually undermine the position even of those who were originally entirely creditworthy. To assert so much is by no means to deny the truth that in the upward phases of every cyclical movement of trade some branches of production and some sources

of supply become over-developed, and that additional credit creation cannot overcome the difficulties associated with the position of such industries and areas. All that is contended for here is that efforts to prevent the general situation from deteriorating too markedly should not be withheld because such efforts will be unable to solve the special difficulties associated with particular cases. To attempt to prevent prices from falling further is not "inflation" but an effort at stabilisation.

6. Thus the short-run problem must be attacked, in my judgment, both from the side of cost-reduction and of credit policy. The important issue from the standpoint of this country is the price level which will ultimately emerge as the result of the policies actually pursued. It would be unwise to calculate upon a price level being reached, even if recovery takes place now, which would restore the precise relationship which existed, before the events of 1929, between the level of British money incomes and prices and those of the outside world. Even this relationship was an unsatisfactory one. From the standpoint of this country, then, a still lower level of outside costs and prices would mean an intensification of our problems, and this makes the task of suggesting remedies still more difficult than it would in any case be.

The Economic Position of Great Britain.

7. It is impossible to judge between the merits of the various alternatives which lie before this country without some previous consideration of its economic position. If all the available evidence pointed unambiguously in a single direction, choice between alternatives might be easier. But, unfortunately the position is not so simple; the evidence available allows no such unmistakable inferences to be drawn.

(i) It would be an error to assume that there has not been a substantial increase in productivity during the last decade and unjustifiable to argue that the general economic position is one of unrelieved gloom. On the contrary, unnecessary apprehensions on these grounds are entertained both at home and abroad, and the widespread impression to the contrary which has been allowed to prevail has itself been a factor of some importance in aggravating the undoubted difficulties of recent years. It appears from the evidence submitted to us that the index of output per head rose between 1924 and the first quarter of 1930 by as much as 13 per cent. (manufacture and mining combined) whilst aggregate output rose during the same period by nearly 10 per cent., and in manufacturing industry alone by 13 per cent. General considerations, moreover, warrant the assumption that considerable improvements in productivity must have taken place. For, though a large part of the explanation lies in the change in our favour of the terms of trade, owing to the extraordinary fall in the prices of food and

raw materials and the reduction in the *net* volume of our foreign investment, the paradox of a rising standard of life coinciding with unemployment both for capital and labour upon a considerable scale throughout the last decade would otherwise be inexplicable.

(ii) In spite of the known difficulties in transferring labour from one occupation to another, it is well-known that transfer on a considerable scale has in fact taken place, with the result that the proportion in different industries has shifted markedly. Moreover, whilst between June, 1924, and August, 1930, the numbers of unemployed in all insured industries rose from 1,085,000 to 2,119,000, the numbers seeking employment rose from 10,430,000 to 12,094,000. The numbers actually in employment at the later date were thus 600,000 in excess of those employed at the earlier date, in spite of a doubling of the volume of unemployment.

(iii) Though the volume of our export trade in 1929 was still below what it had been in 1913, nevertheless it is not the case that particular branches of British export industry have shown no elasticity. The contrary impression which has grown up is due to the fact that in 1913 so large a proportion of our total exports of manufactured articles were concentrated in just those groups of commodities which have suffered severely since, so that, if a weighted average of all exports is taken, the total still falls considerably below that of 1913. But this conceals the important fact that, in other directions, the volume of British exports in 1929 was above that of the last pre-war year. Thus it appears from the calculations of Professor G. W. Daniels* that, taking the volume of trade in British exports (articles wholly or mainly manufactured) as 100 in 1913, the volume in 1929 was only 86.1. But out of the twenty groups comprised within this rubric, twelve showed an increase over 1913, eight showing a decline: the latter apart from the Miscellaneous Class including Cutlery, Machinery, Manufactures of Wood and Timber, Cotton and Woollen and Silk Yarns and Manufactures and Apparel: whilst other groups (including even Iron and Steel and Manufactures thereof) had either maintained their position or in some cases had substantially improved it.

(iv) Nevertheless, there are other aspects of the situation which are not so encouraging, and which require to be taken into consideration before final judgment can be passed.

(a) The fact that the terms of trade have shifted in favour of this country has meant that we have been able to buy our imports of food and raw materials on cheaper terms, i.e., to obtain the same or a larger volume of such goods at less expense to ourselves in terms of the volume of exports. This necessarily reacts on the volume of employment in the exporting industries, other things being equal. But what is true of this country vis-à-vis of countries

* Recent Changes in the Overseas Trade of the United Kingdom. Manchester Statistical Society. November 1930, Table VII, p. 17.

producing foodstuffs and raw materials, is equally true of all other industrial nations and does not therefore serve fully to explain why the rate of growth in our exports should have fallen behind those of our leading competitors. The recent investigations of Mr. Loveday have shown that some of the conventional explanations, particularly the handicap imposed by an appreciating currency, fail to account for this phenomenon, since other countries which have undergone the same monetary experiences have expanded their trade more rapidly than we have.*

Moreover, if it is argued that our older, staple export industries have suffered from the effects of changes in demand which lower prices for our exports could not have prevented, it must be borne in mind that this is only part of the truth. For competition between articles is, partly at any rate, a matter of price, and lower prices might have prevented, e.g., part of the substitution which has been going on between different fuels. Moreover, part of our export markets have been lost to new competitors producing the same article, e.g., cotton goods, and in this case, at least, it is clear that comparative prices must have played a considerable rôle.

(b) Again, even before the world-depression began, the volume of unemployment was in the neighbourhood of one million. It is known that this figure does not represent an unchanging army of individuals crystallized out of the main body of wage-earners and unable to find work, but largely represents a body of persons sometimes in employment and sometimes out of employment. Moreover, absence of adequate training or of natural aptitude, housing difficulties and the like causes of immobility between employments (including the psychological and other effects of unemployment insurance) make it impossible to argue simply from the fact of unemployment to the fact that existing levels of wage-costs are necessarily too high to enable the expanding trades to absorb the whole of the labour available at the existing level of selling prices. But, since it is probable that with lower wage-costs a lower level of prices could have been established, and therefore a lower level of demand could have been tapped, there is reason to suppose that *part* of the failure to absorb unemployed labour must be connected with the level of British costs. How much of the continuing volume of unemployment can be explained on this ground alone it would be difficult to say, but in my opinion it is a considerable part of the whole. For a rigid level of costs not only fixes the margin of profitable exploitation of *existing* industries at a point different (and higher) than it would have been if costs had been lower, but also inhibits *new* industries from establishing themselves at all.

(c) Lastly, there is the undoubted fact that throughout the greater part of the period which has elapsed since the return to the gold standard the Central Bank has found the task of main-

* A. Loveday. *Britain and World Trade* : especially pp. 152-171.

taining the international parity of the pound sterling a difficult one. The difficulties with which the Bank of England has been contending can be easily enough explained, if the fact is accepted that, at the time when the gold standard was restored, the then level of sterling prices, costs and money-incomes was inappropriate to the parity chosen, and that, in the absence of a rise in world prices sufficient to diminish the disparity between world costs and British costs, the only alternatives open were to reduce British costs sufficiently, or to pursue a monetary policy which would offset the tendency to increasing imports and diminishing exports resulting from an unadjusted cost position. There is thus no difficulty in understanding the course of monetary policy in recent years. The easiest method of adjusting the money market position which arose from inelastic exports and rising imports, combined with the desire to invest abroad, was to maintain a level of money rates which would allow of the use of foreign balances as an equilibrating item.

It is true that the problem thus presented to the Bank of England was eased by the gradual improvement in the volume of British exports before the world depression began, and has been eased since by the fall in the world prices of food and raw material imports. Moreover the figures cited in paragraph 260 of the Report warrant the assumption that there has not been, in recent years, a *progressive* increase in our reliance on the method of equilibrating the Balance of Payments by taking up foreign balances, but rather the contrary. Nevertheless, the Bank is still faced with the task of preventing too rapid an outflow of the volume of foreign balances now held here: the level of money rates is still managed with this end in view, and the assumption that our monetary position would be more comfortable if the level of our costs permitted a greater elasticity in our export trade is not invalidated by showing that, so far as our short debt position is concerned, the dangers and difficulties of the position have been somewhat exaggerated in the past, and that, over a course of years, improvement had been taking place. But in so far as optimism is warranted on this ground, and if the fuller information now available suggests that the precariousness of the position of the Balance of Payments has been exaggerated, one is entitled also to draw the inference that some of the emergency measures which have been put forward as means towards *improving* the Balance of Payments are perhaps not as urgent as they appear to some of my colleagues.

8. The attitude to be adopted towards measures for overcoming the present difficulties must to a large extent turn on the assumptions to be made regarding the future developments of the economic position of this country. If the view is taken that factors intrinsic to this country make continued participation in world developments on the old scale impossible to us, or if, alternately,

the opinion is entertained that the trend of world events is in any case such as to require a fundamental change in the direction of our productive efforts, more drastic modification of our economic institutions may be required than would otherwise be the case.

It is certainly one of the consequences of the increasing command over resources that all over the world the demand for direct services and for luxury goods is expanding more rapidly than the demand for the older staple products: a change which is indicated by the growth in all countries of the distributive trades, the amusement-industries, and so on. From the standpoint of the older exporting nations, such developments of demand involve both losses and gains. In so far as they can no longer rely upon the same proportion of the population finding employment in the traditional manner it implies immediate loss: in so far as these changes in demand imply alternative methods of employing population within their own frontiers the loss is balanced by gain: for the growth of these industries everywhere implies that, provided the transfer problem can be solved, there is no reason to suppose that a failure of foreign trade to expand in the old directions means a permanent loss of well-being. Moreover, a failure of demand to expand does not necessarily, in the case of the older industries, mean that the *absolute* scale of the industries concerned must *contract*. All that it means is that they will no longer expand at the old rate. Provided that there are not at work specially deterrent *local* influences, the shift in demand does not mean a present loss of employment, but only that, in the normal course of development, other industries and employments will gradually assume greater importance. And, as regards the newer industries producing luxury goods, the development of an export trade in these is stimulated by the very causes which explain the relative stagnation of the older staple trades, i.e., the emergence of new kinds of demands.

9. Turning now to the case of Great Britain, the following conclusions appear to be warranted:—

(a) The material prosperity of a country does not depend directly upon whether it is engaged upon manufacturing for export (thus obtaining indirectly the goods it requires for its own consumption) or whether it meets its own needs for goods by direct local production, but upon the productivity of its capital and labour. Thus a decline in foreign trade is consistent with increased prosperity, provided that increased efficiency means the replacement of foreign by home-produced goods at falling costs, and provided that demand shifts towards sources of satisfying wants which cannot be supplied from abroad (e.g. services).

(b) On the other hand, so long as world population and trade continue to expand, there is no reason to suppose that

this country cannot continue as a great exporting nation, furnishing either staple products or new products, so long as our costs are upon a competitive level.

(c) Even if there are changes in the world situation disadvantageous on balance to us (and some unfavourable phenomena are certainly present) one-third of our workers in manufacturing industry are still engaged in working for export. Any emergency measures which may be adopted for the purpose of reducing this proportion cannot possibly appreciably diminish the magnitude of the population so engaged in the *short-run*, whilst they might have serious repercussions upon that part of our foreign trade which under any circumstances we would require to maintain. And the *indirect* benefits which might be expected to follow from such measures, i.e., the stimulation of demand for products of many different kinds due to increased employment and production, would equally follow if the mass of unemployment in the export trades were reduced, e.g., by a reduction of costs.

10. The nature of the problem which we have to solve is often misunderstood. It is not merely a question of providing alternative sources of employment at *any* standard of life: any amount of employment of a sort could be found by the simple expedient of cutting off all foreign trade. The problem is to find alternative sources of employment yielding (without adventitious assistance through subsidies or other transfer-expenditure) at least as high a standard of life to the mass of the population as was yielded by the old sources of employment. Whatever may be the case in the long run, I do not myself believe that this problem can be solved without the assistance of vigorous and flourishing export industries: or of industries capable, by their efficiency, of replacing goods at present imported by new domestic production.

Suggested Remedies.

11. It is, I think, common ground that a failure of world prices to rise above the very low level which they have now attained—still more, a further fall—would, in any event, create a situation of great gravity for this country, both as regards the question of adaptation to the new level of costs elsewhere, and also as regards the continuance of the stream of income from abroad, representing interest and sinking fund payments on its past investments. Something in the nature of the National Treaty advocated by Mr. Keynes and those of my colleagues who have signed Addendum I might then become almost inevitable, and the sacrifices of money-income called for from producers of all classes might have to be compensated by additional taxation on rentier and contractual incomes (or alternatively by revalorisation agreements on the lines of those

which have sometimes been adopted after a period of currency instability, so as to bring debts more into consonance with the altered value of money). There is no need to emphasise the great difficulties which would attend measures of this kind, but their immediate adoption is not in question. Some recovery of world prices is to be expected, and in so far as prices do recover, the margin of cost disadvantage to be overcome will correspondingly diminish. If it is admitted, on the one hand, that there might have to be an adjustment of the scale of money-incomes of so abnormal a kind as to require a special procedure, and if it is admitted, on the other hand, that some adjustments of incomes are "normal" in the sense of arising inevitably out of the changing conditions and circumstances of economic life, and therefore require no special justification, one is left with an intermediate region of adjustment, greater than the normal, less than the absolutely abnormal, which does require separate discussion. But until we have seen at what level of prices world recovery will take place, this intermediate region is necessarily indeterminate in magnitude. The alternatives before us are simple. We may attempt to adjust costs: or we may attempt by special devices to interpose a cushion between ourselves and the outside world, in the hope that thereby we may avoid, in part or in whole, the adjustments which might otherwise seem inevitable. Three other alternatives are also open to us: to do nothing at all, but deliberately await events, hoping that a favourable further turn of the tide may float us away from the dangerous rocks towards which we are drifting: alternatively by some national action (if that be possible) to change the whole direction of our productive effort. Lastly, we may devalue or abandon the gold standard.

12. If we do nothing at all but wait upon events we must face the danger, though not the certainty, of a cumulative loss of export markets, of growing lack of confidence in the economic strength of Great Britain as a consequence of continued large-scale unemployment, heavy fiscal burdens, and of what would be read by the world as our evident and acknowledged inability to overcome the rigidities and inelasticities of our economic and social system. We would not, in any case, have to face any sudden catastrophe, for so long as our foreign balances are not swept away by a sudden panic, the excess of our visible imports over our visible exports can be compensated by a gradual decline in the volume of our *new* foreign investments: a decline which would become inevitable if increased taxation reduced the margin of new saving through inability on our part to expand the national income. All that would happen would be that our economic strength would gradually diminish, and with the diminishing of that strength would go the hope of a progressive improvement of the standard of life of the population as a whole. What has just been said assumes no

improvement in the world price-level, and adjustment to that price-level by all countries other than ourselves : a process which in any event involves the danger that our sterling assets in the shape of foreign loans will have suffered a substantial diminution in consequence of voluntary or involuntary default. For my own part, I do not believe it possible to sit still with folded arms waiting for something favourable to turn up.

13. There is no reason to reargue here the case against a tampering with the standard of value. Independent and premeditated action on these lines would represent such a violent breach of national faith, and give such a blow to confidence that its ultimate consequences can hardly be foreseen. That they would be of the gravest and most unfavourable kind, at any rate to a nation situated as we are, can hardly admit of doubt.

14. National action to change the direction of our productive effort would have to take the form of a large scale development of Public Works, planned in advance to absorb a large proportion of the national labour-force for perhaps a whole generation. As a contribution to our immediate difficulties such a plan suffers from the most obvious defects. So long as capital equipment and labour-power are out of employment, and current savings are hoarded because of lack of confidence, it is, of course, true that national works are not impossible because they cannot be financed except at the expense of withdrawing resources from other possible avenues of employment. But the most urgent problem which we have to face concerns the export industries, and it is not easy to see how plans of national development would much assist these industries in the short run. Development works of any kind will (i) absorb unemployed labour of *some* kind, (ii) give assistance to the constructional trades supplying material and equipment, (iii) indirectly stimulate demand for other labour through increasing the purchasing power of workers and employers engaged in the constructional trades and of the workers directly employed in the development work itself. But the indirect demand under heading (iii) will not necessarily be confined to home products, so that, to the extent that imports of foodstuffs and raw materials increase, no direct stimulus to home demand will result under this head. How much assistance will then be afforded to the capital and labour in the export industries must thus be very conjectural, depending upon (a) the rapidity with which plans can be developed, (b) the amount of work which can be set in hand within a given period of time, (c) the nature of the work undertaken, (d) the demand generated directly, and the proportionate distribution of this demand between home and foreign products, (e) the direct proportion of the demand accruing to industries formerly engaged in making for export, (f) the transferability of labour and capital to take advantage of improvements in demand for goods other than those which they formerly helped to make. As a short-run contribution to the

problem, I cannot believe that the policy of Public Works has much to offer to the *export industries*, in which, after all, the bulk of our unemployment is concentrated. As a long-run contribution to our economic problems, it raises other issues, both fiscal and economic, which fall outside the scope, however interpreted, of the present inquiry.

The Problem of the Tariff.

15. It has, however, been suggested that a remedy lies within our grasp, which *can* be applied in the short-run, and from which, at any rate in one of its forms, much can be expected. It has been suggested that the imposition of a Customs duty (of say 10 per cent.) upon all imports, accompanied by a subsidy upon all exports (also of 10 per cent.) would (a) improve our balance of trade, (b) reduce the real burden of *all* the sterling costs of British industry, including fixed charges, (c) increase revenue, less, of course, the cost of subsidies. It would be equivalent in its effects upon *home-income* to a devaluation of 10 per cent. in the standard of value, without raising any of the difficulties attendant upon a direct attempt at devaluation. Even if such a tariff policy proved impracticable, import duties could still be imposed, accompanied by aids to the export industries, similar in effect to, though not identical with, a direct subsidy. It has even been suggested that such a tariff, in the light of our present situation, is the ideal method of securing the optimum distribution of our national resources.

This last point, though of no great practical importance, would, if it were true, be of great scientific interest. I believe it to be invalid. A flat rate of import duty accompanied by a flat rate of subsidy on the f.o.b. value of exports would indeed make conditions even as between the export industries and industries using home-produced materials and domestic labour, and selling in the home-market. But it would *not* make conditions even as between the production of either of these classes of goods and the production of goods intended for home consumption out of imported raw materials: nor would it make conditions even between the first two classes of goods and the rendering of services, in so far as those who render services would have to pay more than before for raw materials and equipment without receiving a subsidy. (Are, e.g., ships built of foreign steel but owned by English firms on the British register to receive a subsidy or not?) But this point is of quite subsidiary importance as compared to the other issues raised.

16. It is only as a possible solution of the monetary difficulties associated with the present emergency that I am concerned with this, or indeed any alternative, proposal involving the imposition of duties upon imports. As a suggested method of overcoming disequilibria associated with monetary difficulties the tariff suffers,

indeed, from the fact that it is unable to remove the fundamental defect which is complained of, so that, unless it is constantly being adjusted to meet changes in the situation, its use as a monetary instrument is liable to create new difficulties of its own. Moreover, a review of history does not warrant giving the tariff a very high place as a method of relief from monetary distress. But neither *a priori* considerations nor historical example constitute, in our present circumstances, a sufficient answer to the case put forward by some of my colleagues.

I demur, in the first place, to the definition of this expedient as an emergency measure; one which can be dropped without difficulty when the circumstances which called it into existence have passed away. For such a tariff would tend to perpetuate those disparities between British and foreign costs to the existence of which it would, *ex hypothesi*, owe its existence. So long as these disparities lasted, retention of the tariff could and would be urged as a method of defence, but so long as it was hoped that the tariff would remain, there would be no need to make the efforts necessary to overcome the disparities involved. It might, perhaps, be said that some recovery of world prices is to be expected and that, in so far as foreign money-costs rose, the fact would become so patent that a widespread agitation directed to the removal of the duties would follow. But if a rise in world prices is to be seriously hoped for, within a measurable period of time, this very fact would be a decisive reason for avoiding (unless other grounds than the nature of the present emergency can be invoked) any measures which, once imposed, would involve, in the virtue of their very nature, their permanent retention. If a revival of world prices is not to be hoped for, the tariff ceases to be an emergency measure and would become an integral part of the fiscal and economic system of the country: the more certainly, the longer the period of time involved. Moreover, the tariff history of other countries shows with what tenacity a tariff is clung to, even when, to the eyes of impartial spectators, the industries calling it in aid are clearly able to do without its assistance. If the tariff does what it is asked to do during the emergency period, there will be a natural reluctance to part with so valuable an instrument: if it does not, it can be pleaded that failure to achieve success was due to the inadequacy of the tariff protection actually afforded. If the tariff is to be adopted at all, it is likely to be permanent.

But if anticipations in this respect are well-founded it appears impossible to suppose that Parliament and public opinion will be concerned mainly with the monetary (and supposedly temporary) aspect of the proposal. Discussion would turn, and turn rightly, upon the relative merits of the proposal, as compared with possible

alternatives, as a permanent instrument of fiscal policy. What is recommended for a special and temporary reason would be attacked and defended on other and more far-reaching grounds altogether.

17. I question, in the second place, whether a tariff would not result in a spurious equilibrium likely to cause a new series of disequilibria in the course of time. In general, the beneficial effects anticipated could only follow if the reduction in real costs were effective. An attempt to adjust the level of costs, especially wage rates, to the effect of a rise in the cost of living, would at once produce new disequilibria. But, apart from its intended effect in assisting British industry to replace competitive imports by British products (which would assist employment) it is claimed for the measure that it would help in reviving business confidence and the "spirit of enterprise". But in order that it should have these effects, it is not enough that it should create a temporary mood of optimism, to be dashed later on by the failure of the tariff to function as it was intended to do. If, as a result of the imposition of tariff duties, a sharp fall in the volume of competing imports takes place, and the volume of foreign investment is not adjusted to the change in the position of the Balance of Payments, gold would flow in freely, to be utilised to serve as the basis of an expansion of credit.

Thus, if the tariff is at all successful in achieving its objects, it seems reasonable to suppose that it would result in a temporary boom in home industries, and that, under these circumstances, a check would be given to foreign investment, at least for the time being. In the early stages of revival, the Central Bank might find it difficult to offset gold imports by sales of securities, for it would then be liable to be attacked for running counter to the policy of the Government of the day in restoring "confidence", and the anticipated effects upon the volume of credit are, therefore not only possible, but, under the circumstances, not improbable.

The money-income of society would thereupon expand: especially if diminishing unemployment and rising prices led to a rise of money wages. Thereupon, at the new level of money-incomes (the tariff being supposed to remain unchanged) a new stimulus to imports and check to exports is brought into being, and a new disequilibrium between domestic and foreign costs is set up: to be followed either by the collapse of the boom or the imposition of a still higher level of tariffs in order to avoid the threatened breakdown of "confidence". I agree that the question can only be answered definitely by a comparison between particular, alternative projects. A slight measure of tariff protection would necessarily have slight effects. But this would apply to the beneficial, as well as to less attractive, consequences to be expected from the imposition of import duties.

18. Thirdly, I believe that the proposal for a tariff upon all imports accompanied by a subsidy upon all exports would prove hopelessly impracticable, and that the effects of any tariff which would be likely to be imposed would differ markedly from those which, it may be held, would follow from a flat rate of import duty accompanied by a flat rate of subsidy. My belief is not based merely upon the circumstance that, if such a flat-rate tariff and subsidy were imposed, it would be met by countervailing anti-dumping duties in foreign countries and that, in order to avoid the danger of the application of such duties, equivalent advantages to the export industries would have to be devised, the subsidy being dropped in favour of such alternatives. I do not think that the technique of tariff-making is so little understood by foreign countries as to make it at all difficult for them to apply special measures against British goods, merely because we would attempt to grant our export trades concealed, instead of open, bounties.

The main object of the proposed tariff is not to collect revenue but to counterbalance the disadvantages of the British level of costs, as well as to keep out part of the existing imports of goods. But I feel that Parliament would not view with any great favour a scheme of tariff legislation which, whilst it would involve, in all probability, very considerable administrative expenses, would not have the advantages of leaving a large additional net revenue in the hands of the State. In combination with a subsidy, which would make an additional volume of exports possible, the revenue aspect of the proposal is hardly worth taking seriously into consideration. But this would diminish the practical attractiveness of the proposal very much.

19. The probability then is that the tariff as introduced would depart from the postulated simplicity of form and purpose contemplated. Though this is not the place to discuss at length the advantages and disadvantages of Protective Tariffs, it is not straying beyond the limits of the permissible to point out that the more complex and elaborate the tariff, the less can be predicted, in the absence of definite knowledge of what the concrete details are, of the effects of a tariff upon the position of the export trades. In considering the effects of the imposition of a tariff upon exports, it is not enough to take account of the direct reactions which might be expected to result, but attention must also be paid to the indirect reactions. Foreign goods excluded from the British market do not simply disappear; they reappear, in the guise of increased foreign competition, in neutral markets. The net increase in employment under all heads which will result from the imposition of tariffs is therefore likely to be smaller, and the damage to the export trades greater, than appears at first sight. The trade of the world as a whole, of course, is not a fixed magnitude, and it by no means follows that in the long run neutral markets will not be in a position

to absorb both a greater amount of British goods and of the goods of countries directly competing with ourselves. But if this argument is valid, it is also valid to argue that an increase in the imports of manufactured articles into this country is not inconsistent with an increased demand for domestic products, in the long run, provided the productivity, and therefore the consuming power of the country, continues to increase.

The Problem of Costs.

20. The only alternative which has not yet been discussed is a reduction of costs. Since cost reduction is inextricably mixed up with the question of wage levels, both absolute and relative, and with the question of the standard of life of the population, it is inevitable that this issue should be one which rouses some unintentional, and perhaps as much interested and calculated, misapprehension. I propose to set out the issue as succinctly as possible.

(a) The problem arises partly because we may not have increased our efficiency in the last ten years as rapidly as some of our competitors; partly because we had not, even before the world slump, entirely overcome the disadvantages attaching to the choice of ratio at which we returned to the gold standard; partly because world prices have fallen heavily since. It is very natural that producers, both employers and employed, should resent the imputation that the whole of the problem of adjustment is due to faults originating on their side: that it is entirely a question of deficiency of organising skill, and of productive capacity. But it does not follow that additional efforts and sacrifices may not now have to be called for.

(b) A reduction of costs is not necessarily tantamount to a reduction in wage-rates, still less of money-incomes. What is required is a reduction of cost *per unit of output*, and such a reduction may be quite consistent with rising money-incomes. Thus the workers may be right in insisting that a reduction of costs should not take place uniquely at their expense, through wage-cuts and nothing else. Our methods of organisation, salesmanship, the choice of leadership, etc., are all elements over which Labour has little direct executive control, but which are extremely relevant to the problem of cost-reduction. Still, if costs are to be cut by improved organisation and technique, it must be borne in mind that the Labour movement must contribute its fair share to the solution of the problem. Public attention is largely concentrated upon wage-issues, but there are other elements in the situation as well; insistence upon the maintenance of practices and regulations which have the direct effect of keeping costs up. If Labour desires to cut costs and refuses to allow wages to alter, it must at least be willing to alter practices which increase per unit cost. It can hardly be asserted with truth that this has always been the case.

(c) If it is urged that "finance" must contribute its share to the burden of cutting costs, the answer is that through conversions and reorganisations the fixed capital involved does have its remuneration reduced, whilst the owner of equities gets nothing, or gets less, unless and until profits begin to re-emerge.

(d) It may be argued that, if the cutting of costs leads to a fall of prices, and British goods can again be sold at a competitive level, profits will not re-emerge, i.e. purchasing power will be destroyed and not re-distributed. But an increase of sales which permits of a reduction of overhead costs on the whole of the output may still be consistent with the emergence of profits.

(e) It is argued that not only labour-incomes, but all incomes, have benefited, in terms of real purchasing power, from the fall in foreign prices relative to our prices. This is true, but if it is used as an argument against a possible reduction of wage-rates, it is invalid. For the level of money-wages may be too high to permit of full reabsorption in other directions. The gain through the alteration of the terms of trade in our favour involves a transfer of labour into alternative occupations, and, if it is to be absorbed in these occupations, labour may have to accept a lower marginal wage, because in those other occupations, there has *not* been a shift of the terms of trade in favour of the British seller.

(f) Whatever reduction of wages and salaries may ultimately prove to be necessary, it by no means involves an equivalent reduction in the standard of life. A 10 per cent. wage or salary reduction is not equivalent to a reduction of real income of as much as 10 per cent., even if other costs do not fall.

(g) If no wage and salary reductions take place and unemployment expands, a point must come when working-class purchasing power as a whole will be less, given a certain combination of employment at given wage rates plus unemployment at a certain rate of unemployment pay, than it would be if wages and unemployment were both lower.

(h) There is nothing in the fact of wage or salary reduction which implies that wages and salaries can never be raised again: or that an immediate wage reduction implies a *permanent* lowering of the standard of life of the bulk of the population. The standard of life of the world, and of particular areas, is governed in the end by productivity, and there is every reason to suppose that, highly organised as the Labour Movement is almost everywhere in the modern world, successive increases in productivity will be reflected in a rising standard of life, as has indeed been the case throughout the modern industrial era.

(i) The view that a reduction in the price of British exports due to wage reductions would be nugatory, because such reductions would simply force on equivalent reductions elsewhere, is not in accordance with the facts. Such wage reductions as are taking

place—some at least on a scale which suggests that not all the organised workers in the country are entirely beyond being appealed to in these matters—have followed and not preceded reductions elsewhere. Moreover, it is not necessarily the export industries themselves which should suffer any reduction of wage rates, but the ancillary and sheltered trades whose wage rates and standards have been maintained at the expense of the standard in industries less able to protect themselves.

21. There is no reason to suppose that this country has exhausted the possibilities of rationalisation, using that word in the largest sense: and it may very well be the case that, in order to push on as fast with rationalisation schemes as the urgency of the situation requires, intervention by the State, both in the way of arming an industry with statutory powers and by way of guarantee, may be required. But—even in the absence of a catastrophic alteration of world prices—such schemes may not prove enough: and some alteration in the scale of wage rates may be necessary. Those who do not wish to see wage rates reduced, or who think it impossible to do so, in the main urge measures which will have the same economic effect—the imposition of a general tariff. Indeed, unless the tariff does have this effect, it will not be a solution of that aspect of the British economic situation which concerns the members of this Committee.

22. It is true that a tariff, *if successful in reducing the standard of life all round*, would hit classes of the community who would not only not be affected unfavourably by a reduction of costs, but who would gain from such a reduction. That wage-earners should dislike wage reductions at a time when it can be plausibly argued that the rentier gains is no doubt perfectly natural, even though the economic depression has much reduced the value of investments in industry, and even though among the ultimate beneficiaries from the rise in real value of the National Debt are the working-class members of Trade Unions, Friendly and Building Societies, etc., owning blocks of War Loan. But the problem confronting us is one which cannot be settled on emotional grounds alone. The difficulties in the way of special taxation of the rentier are very great. But it is clear that any considerable reduction in the money value of the National Income must involve increased direct taxation to meet debt charges, unless a successful large-scale conversion operation can be undertaken in the near future. Such increased taxation (the basic rate of Income Tax having already risen in recent years by 12½ per cent.) will fall in the main upon rentier and contractual income, and constitutes an offset to any increase in non-working-class well-being due to reduction of prices and costs, which would not, if money wages fell, accrue to those dependent upon incomes from labour.

23. In the course of the last decade we have become, as a nation; highly sensitive to considerations of equity as between class and class. At the same time, partly in consequence of our desire to translate our ideas of equity into practice, our economic and social structure has become less fluid and less amenable to change. To sacrifice elasticity to equity is tolerable so long as, in the outside world, changes are not proceeding at so rapid a pace as to make adaptation on our part, even if only with a time-lag, ultimately impossible. It may be that we are now faced by a turning point in the history of the world price level, to which, in the end, the level of costs in the outside world will adapt itself. If this diagnosis of the situation proves to be correct, it would be out of the question for us to maintain a level of costs out of all proportion to costs elsewhere. It may, on the contrary, prove to be the case that the world is now in the trough of an unusually deep depression, recovery from which will bring with it a renewed rise of prices. It is too early yet to say definitely which of these things will happen : but it is clear that a world rise of prices would greatly mitigate the severity of the task which would otherwise confront us. So long as the present degree of uncertainty as to the future level of prices prevails, to defer action, in order to take thought, is perhaps legitimate. But to defer action simply because we are as a nation afraid of acting at all would be a confession of moral weakness, neither creditable to the traditions nor beneficial to the economic future of the country.

T. E. GREGORY.

ADDENDUM IV.

1. As the result of the construction which has been placed upon the terms of reference the question of how Industry could be re-organised, reconditioned and financed has not been touched upon in the Report. In consequence the evidence which has been received on behalf of Industry has been singularly deficient in constructive proposals which might suffice to place Industry once more on a sound financial and competitive basis, and this deficiency is observable particularly with reference to those branches of Industry which rely to a large extent on their export trade. It was reiterated by most witnesses representing industry that costs of production were much too high, that reductions could be brought about, and that the trade of the country could be retained if not regained (i) by an increase in the efficiency of both employers and employed, (ii) by an all-round reduction in salaries and wages, (iii) by the setting up of a general system of tariffs. But no evidence was received as to the effect which all or any of these vital proposals would have either on the cost of living or on the cost of production

or on the export trade. The process of rationalisation is now well advanced in certain industries but this process cannot be successful without a clear conception of what is being aimed at and how it is to be achieved. And if this process is to be continued and even accelerated it is of the highest importance to consider how it may be affected by the adoption of the proposals (ii) and (iii) and what under altered conditions may be the results of the process in the transitional stages of re-organisation. It is difficult to see how these three proposals or any of them could be accepted or acted upon without the most careful investigation.

2. It undoubtedly is the case that defective methods of distribution and the want of adaptability in some trades have been factors contributing to the loss of the export trade no less than high costs of production. The need for a concerted plan in dealing with each trade or certain groups of related trades was never more apparent. If it is by mass production, by careful and systematic investigation of our markets, by reaching the consumers and knowing their needs that the bulk export trade is to be won back, then all sections of each particular trade should be linked up so that production could be concentrated in the works best equipped for the purpose.

3. So long as industry delays in adapting its selling and distributive methods to the new circumstances of world trade, so long may we expect to lose ground in the world markets. In these circumstances new capital necessary for keeping plant up to date, apart altogether from expansions, will be unobtainable, and without up to date equipment there is no hope of competing on equal terms in overseas markets. And so the vicious circle will continue.

4. The only hope of the necessary investment on reasonably low terms depends in many industries on the assistance of some form of State guarantee. But the State in the interest of its own financial responsibility, and in the interests of the trade concerned, should make its assistance dependent on rapid re-organisation. The guarantee of a whole trade linked up for a common purpose is far more secure than that of particular enterprises whose power to repay may be destroyed by the unfair competition of enterprises hard pressed for ready cash in their own locality.

5. The leaders of the Trades Unions should be brought into much more active touch with employers in the process of re-organisation and so increasingly to understand and appreciate the difficulties with which employers have to contend and the urgent necessity for greater efficiency.

6. Greater efficiency, however, is required not only in the workshop but in the office and the board room, and the leaders of the Trades Unions ought to be able and ought to be encouraged to promote such efficiency by pointing out what they regard as causes of friction and loss of energy and to make suggestions for their

removal. Employers often overlook the fact that the workers in a trade are as much concerned to promote its prosperity as they themselves.

7. By such co-operation it should be possible to build up a live machine which would be able to devote itself to retaining and regaining trade instead of dissipating energy in perpetual disputes on questions of wages and conditions of work.

8. While I venture to express my regret that the scope of the inquiry was held to exclude an examination of the probable effects on finance and industry of proposals to which I have referred, I am conscious that this is not the place in which an individual member can fittingly attempt such an examination and subject to the foregoing comments I am content to sign the Report.

L. B. LEE.

RESERVATION BY SIR T. ALLEN AND MR. BEVIN.

We join in signing the foregoing Report in the belief that its recommendations tend to alter the direction of our monetary system from the basis of a contractionist policy to one of expansion, but desire to make the following reservations on certain items.

With regard to the terms " money costs ", " wage costs ", and " wage rates ", which are mentioned in various paragraphs of the Report, we may state that the Committee had no opportunity of examining any evidence on international wage costs, so that no real inference can be drawn as to money costs in the different countries, merely from the figures of actual time rates of wages.

On the other hand, we take the view that insufficient emphasis has been given in the recommendations to other money costs, particularly the effect of the dead-weight debt. Evidence was given that the effect of this is such that where in 1911 for the National Debt internal interest alone industry had to find £16 millions per annum, it now has to earn and hand over to the State £277 millions. while other fixed charges on industry have increased in like proportion.

At the same time the State, Public Authorities, and Public Utility Bodies have had to incur fresh debt on the construction of public work as a consequence of the depression and the failure of private enterprise to keep the workers fully employed. Hence it will be seen that Management and Labour are called upon to bear a burden almost too great for them, especially having regard to the falling price level.

We disagree with the recommendation in paragraph 202, page 90 :—

“ Nevertheless it would appear as if a most important consideration for those in charge of the public revenue to bear in mind, so long as the future course of prices is uncertain, is the avoidance of any form of obligation involving a large addition to the contractual obligations of the State.”

We take the view that any such recommendation would render impossible any solution or easement of the unemployment situation and would hold up such necessary internal work as Housing, Slum Clearance, Public Work and other schemes as mentioned in Addendum I.

In fact, private enterprise having proved totally unable to lift the country out of the morass in which it is, there seems no alternative but for the State to grapple with the problem and for large measures of State planning, which must involve further contractual obligations, to be adopted.

We also desire to point out that the Committee decided to examine monetary policy only on the basis of the gold standard and, therefore, no alternative to the gold standard was examined or discussed; but we take the view that, if it is found impossible to give effect to the recommendations on international policy (paragraph 251 and Chapter II, Part II), owing to unwillingness on the part of the countries concerned to co-operate, a point may be reached when this country may be compelled to go off the present form of the gold standard, and we take the view that the Treasury and the Bank of England should be considering an alternative basis in order to minimise disturbance if such a contingency should arise.

In regard to paragraph 281, we are firmly convinced that the great powers which the Bank of England already possesses, and which are contemplated should be developed more fully in the future, ought no longer to be left in the hands of a body which is in form a private profit-making institution, even though in practice it acts as if it were a public body. From the point of view of popular confidence, which is so great an element in these matters, we are convinced that the Bank of England ought to be transformed into a public corporation. While it should remain free from political influence, its Governing body should not, even in form, be representative of private stockholders, nor should its membership be drawn very largely from one financial group. We think the minimum change required is the appointment of the Governors by the Crown, the establishment of an Advisory Council representing industry, commerce, etc., and the transformation of the stock into fixed-interest bonds.

With reference to the recommendations in Part II, Chapter IV (paragraph 403), we join in the recommendation for the creation

of new machinery for financing industry, but strongly recommend that, instead of being a private institution, it should be a public corporation.

THOS. ALLEN.

ERNEST BEVIN.

RESERVATION BY MR. LUBBOCK.

I have signed the Report, with the following reservations :—

(1) With regard to Chapter III of Part II in particular and also to other portions of the Report which relate to the Bank of England, I refrain from expressing assent or dissent, because, while I have shared in all the Committee's discussions, I have felt that it would not be proper for me, as a Director of the Bank who has been closely concerned in its policy and administration, to be a party to any conclusions or recommendations affecting the Bank which it may be my duty hereafter to consider in my capacity as one of its Directors, and with regard to which it may be that my position has disabled me from taking an entirely impartial view.

(2) By the terms of our reference we were limited to the consideration of Banking, Finance and Credit, and it is only with regard to these questions that the Committee can make recommendations : but I do not fully share the hopefulness indicated by some passages in the Report that some form of positive action on the part of those in control of Banking and Credit would be effective in relieving the present economic depression. " Banking action necessarily follows, not leads, Industry " (Clay §25); and while the monetary machine must do what it can to open the way for a revival of our Industries, it is in other (non-monetary) directions and by other means that the conditions of such a revival must principally be sought.

CECIL LUBBOCK.

RESERVATION BY MR. NEWBOLD.

1. Whilst concurring generally in those chapters which are purely descriptive of the existing monetary situation and of the features of the post-war world as set out in the Majority Report, I do wish most definitely to declare that neither in the evidence presented to us nor in the deliberations within the Committee has it been proven to my satisfaction that either the difficulties peculiar to this country or those experienced by the world at large

can be attributed in the main to monetary causes. Further, I wish to dissociate myself from the opinions implicit in the arguments of my colleagues that this complex crisis has resulted from some inexplicable variation from the normal functioning of what they call the economic system. Rather do I regard the *impasse* at which has been arriving every country wherein prevails the economy of commodity production and marketing as the inevitable consequence of the operation of principles whose finally irreconcilable character has only been made visible when they have become not local and exceptional but world-wide in their application. The theories which my colleagues have brought to bear upon the mass of material coming within the purview of this Committee have borne at every stage the stamp of their origin within an age and an environment wherein it was taken for granted that the whole world responded or reacted to the ordered rhythm of the classic finance, commerce and industry of this country. Always, the gold standard game has been regarded as only properly to be played to the rules accepted in London. That others should have adjusted it to what they regarded as the requirements of their agriculture, industry and commerce has been treated as if it was a grievance. The approach to the whole problem has been insular, as if the objective to be attained was the restoration in this country of conditions for everyone as far as possible akin to those of a nationally exclusive past rather than of an internationally inclusive future. At the same time, as could only be expected of those who think within the limitations of an economic system wherein the prime motive is the making of a profit, the minds of the majority of the Committee have sought always a measure of relief for those categories of income rendered most rigid by the necessity of maintaining "the sanctity of contract" by recommendations that, if they mean anything at all, mean the drastic reduction of wages and salaries. This is a measure to which, equally in the nature of things and not because of any conscious conspiracy, is turning the employing class of every country. Failing that co-operation between them which, save under the panic impression of the superiority of the State-directed competition of the Five Year Plan, they find it so distasteful to adopt, this process of ever reducing the real wages of the working class is something which will be continued indefinitely. But now that the debtor countries are being subjected to the same insistent demands for a reduction of their standards of life, e.g., Australia, Brazil, Germany, etc., in order that the creditors may not suffer, the crisis is in a fair way to become chronic. In such an event nothing but obstinacy can blind us to the fact that the whole economic and social structure of a country such as this, organised over generations with a view to world-wide commerce, is in imminent peril of complete collapse. Organised with a view to world-wide commerce this country may

be, but for a commerce which was not competitive with others and which has in its every participant a prejudice or, at any rate, a predisposition against abandoning his own independence and cooperating otherwise than on paper with his compatriots. Such considerations are, I contend, if non-monetary in character, yet as essential to the stating of the problem as the numbers and conditions of our unemployed population. The mere fact that the "pressure of unemployment in an industry as an instrument for persuading men to accept wage reductions is made much less important than it used to be" by reason of the unemployment insurance system, as urged by Professor Pigou and that, thereby, the edge is taken off the internal operation of the bank rate, doubtless determined the majority of the committee to give so much attention to these matters. But an alternative item in the special problems of Great Britain I suggest, with all due respect to my colleagues, is the backwardness of the technique and management and salesmanship of industrialists and traders which causes them always to seek at the expense of others, be it the Bank or the wage-workers or the unemployed, the economies which they cannot see how to make in their own expenditure, whether in or out of business hours. There is in every class in this country an attitude towards individual expenditure which, however appropriate to the conditions of a world wherein its industry, its commerce and its finance were virtually unchallenged and unchallengeable in their self-sufficiency, is now a national danger. Savings urgently needed for the replenishment of the capital requirements of industry and commerce can be and are dissipated not only by the drawing of these into and through the Treasury to be paid out to the recipients of what are erroneously called social services to expend at their own discretion, but just as much by the direct uneconomic outlay of individuals. The right of the latter to do what they like with their own is equally anti-social and contrary to the interests of the nation if advanced by a workman or a rentier. Resistance must be put up relentlessly to the argument, from whatever angle offered, that a greater part of the national increment shall be made available to or retained by the consumer. Whether the capital accumulations are directed into reproductive channels by private or public authority is not the direct concern of the economist. That is for others to decide, not for the members of this Committee.

2. The tendency in the world is towards some or other form of planned economy. That is determined by three prime considerations. The first is, no doubt, a reaction from the altogether temporary ecstasy of *laissez-faire* that prevailed in the interlude between the breakdown of a society rooted in agriculture and the development of another based on industry. The second results from the recognition of an evident necessity to adjust the relations, internally as well as externally, of economic entities which

do not exist any longer *in vacuo* as did England in the age of the Industrial Revolution. The third springs spontaneously out of the requirements of the new technique of power and transport. This latter being comparatively recent is still so novel to monetary theorists and practitioners—always in the nature of things tending to be removed as far as possible from realities—as to encounter from them a frank denial. But even if it is fantasy to the banker, to the engineer it is a fact.

And in this difference of outlook begins the difficulty of bringing into conjunction the banker and the industrialist. For the latter has evolved, in the age of the engineer, a complex of commodities which, as each has been swung into its place in the scheme of production, has lost its original economic character and become a value only under a certain set of circumstances. It has become so static as to have forfeited almost every quality of the commodity. It has ceased to be negotiable. It can no longer enter into exchange. Such being the case, the banker must regard it with extreme suspicion. For he has gone in exactly the opposite direction, evolving an ever more abstract equivalent of the commodities of commerce so that, even more than the merchant, he must endeavour to maintain his medium negotiable under all conceivable conditions.

3. The bankers' bank, which is the Bank of England, has therefore a duty to do that renders it functionally antipathetic to the immediate requirements of industry. Apart from its management of the National Debt, its receipt of monies of the Government and its issue of the currency—which latter services as is shown elsewhere mingle with its banking transactions—the Bank of England has as its particular rôle the rendering of a series of services not to industry but to commerce.

Its long-term investments must have the negotiability of assets guaranteed by Parliament or public authority or public corporation of unimpeachable solvency. Its short-term investments must have equally the exchange value attached to the most impeccable commercial paper.

Historically, the Bank guards the subject against the fraudulent default of the Crown in its engagements to restore borrowed monies intact. So, also it has not ceased for centuries to safeguard him against that abuse to which is prone all sovereign power—the debasement of the currency.

This latter is the invariable expedient of the spendthrift. From it result most of the evils of this present day in so far as these are attributable to monetary causes and which must ensue from either such a condition as prevailed during and immediately after the War in all belligerent countries or as recently existed in the United States.

4. It is in my judgment inherent in certain of the proposals made in the Majority Report. Subject to the unceasing criticisms of its credit policy when no longer acting in accordance with parliamentary statute, it will be very difficult for the Bank of England continuously to resist the pernicious counsels of inflation. The abandonment of the gold standard being recognised as something which, directly demanded, would be rejected outright, the eventual attainment of this objective is sought, like certain other oblique attacks on the wages of the workers, to be obtained by these indirect means. If reductions in the wages of the workers are unavoidable, then we will have them made in honest money. At least, we wish to know where we are and not to be made the victims of that supreme confidence trick, a price index to be compiled and corrected according to the conflicting estimates of a committee of economists whose minds would invariably be in a state of unstable equilibrium. The bias which is as visible as it is unwitting in the whole method of approach of the theoretical supporters of the existing economy, makes it impossible for the workers or their representatives to trust their rates of remuneration to a method of adjustment that is so subjective. That fact, taken together with the inadequacy of economic science, makes it essential that the measure of value shall continue to be as nearly as possible automatic. This automatic character indispensable in the measure of value is attained most completely by gold. To this latter material belongs the peculiar quality of attracting and retaining over very long periods of time a socially necessary quantum of labour substantially invariable. This quality formerly possessed in considerable degree by a second metal, viz., silver, has been forfeited by it during more recent years with the result that it has become desirable to take formal cognisance of an actual change and all the world over to arrange for its de-monetization.

5. The changed conditions of metalliferous mining which have resulted in the enormous increase in the output of silver, since it is brought to the surface in the same complex ores as the zinc and lead in such immense demand as base metals of modern industry, have made this step, so disastrous for the owners of boards of that metal in China and India, eventually unavoidable. But, in view of the known fact that so great a superstition attaches itself to the subject of the monetary media—whether metal or paper—as often to assume nothing less than the grossest form of fetishism even in countries of high economic and cultural development, it is open to question whether the decision to implement the demonetisation of silver was made with the necessary caution and tact. The same disregard of the interests and beliefs of others than the monied magnates which marked the return to the gold standard in Europe has characterised its adoption in Asia. So, in both continents have the final arbiters of economic and, consequently, of political power aggravated the unrest already result-

ing from industrial and agrarian revolutions of the most unsettling character. Now, as in preceding centuries, the development of trade and, in its train, of industry is conditioned by the volume, the velocity in circulation and the unvarying value of the monetary media. Such being the case, the opening up of China and India necessitates the adoption of a sound and stable currency and the establishment of a banking system similar in character to that already existing in Europe and America. All the more urgent is it, therefore, that as little prejudice as possible shall be aroused in East as well as in West against a machinery that is absolutely essential to civilised society.

6. In view of the recognised relationship between the difficulties in the Eastern markets and the collapse of industry and employment in this country, as also to no small extent in Central Europe, I have no apology to make for labouring a point which I believe my colleagues have most unhappily avoided.

7. Returning to the main theme of the gold standard, I wish to dissociate myself entirely from the viewpoint of those who regard our difficulties as due to the inadequacy or even the maldistribution of gold. These supposed causes are themselves merely phenomena resulting from factors far more fundamental. Gold is but the objective basis whereon can be reared, so far as the subjective factor of confidence permits, an edifice of monetary media equalling the sum total of the mass of values existing within any given area within which those media circulate. The subjective factor of confidence is at least of equal importance with the objective factor of gold. They vary in inverse ratio to each other. Credit was the creation of the years during which peace between the nations of high commercial development and within the nations of high industrial productivity was virtually undisturbed. Credit was an expansion of the monetary media which radiated outwards from the centre of the most stable State and, as time went on, encountered and inter-mingled with similar if less vigorous emanations from the centres of such States as had adopted as the measure of value and the standard of price the same objective reality—gold.

8. The subjective factor of confidence has become since the outbreak of the Great War a variable and ever more uncertain quantity. The destruction wrought by the actual conflict as well as the disorganisation of commerce and industry caused by the severance of trade connexions and the diversion of capital and labour to employment of little economic value, was aggravated by the altogether reckless distortion of currency and credit all of which left an appalling legacy of deceit in the guise of internal indebtedness. Then, as the incompetence and ruthlessness of governments became utterly intolerable, there ensued revolutionary movements which, together with the disturbances of the normal economic intercourse perpetuated or provoked by the Peace Treaties, caused a

flight of capital from one after another country of Eastern and Central Europe. The efforts made to stabilise the new States as well as to repair the damage done to the financial fabrics of Austria and of Germany have all been futile. The whole crazy improvisation is in imminent danger of collapse.

9. In this intensification of the chaos which is the normal condition of capitalism, there has occurred a continuous, if by no means constant, dislocation of industry in the creditor as well as the debtor countries. Wages have been driven down, employment has been disorganised. Simultaneously, the resolve of the United States to avoid internal conflicts calculated to shake there, also, the edifice of an economy jerry-built about a skyscraper of credit, has led to the restriction of immigration. So, there has been no outlet for the surplus labour of the Old World.

10. It has been necessary, therefore, to find the money to maintain the mass of workers who could not be employed at a profit. This money can only be raised, at any rate immediately, from those who have a surplus over and above what they need to maintain themselves and perpetuate the profit-making species. In such a situation, widening since the autumn of 1929 until it has come to coincide with well-nigh the whole world, it is absurd to lay the blame for the crisis upon a mere measure of value. It is not gold which is scarce but confidence which has fled.

11. Even more absurd, if anything, is it to pretend that by the erection of still more obstacles to the free flow of commodities any nation requiring to supplement its native resources by means of imported food-stuffs and raw materials, as does ours, can do other than intensify the chaos from which, as an economy organised to produce for export, we stand more than any other on the whole planet to suffer.

12. In view of the fact that the industries of this country, apart altogether from those obviously producing primarily for export, have been operated for years, for decades and, in some cases, for generations to supply the needs of shipping, of shipbuilding, of railway communications (almost invariably promoted to feed one or other of the great ports), and of the equipment of the works and the foddering of the workers engaged in export business, nothing but an invincible ignorance of the economic history of Great Britain can palliate the suggestion that we ought, otherwise than gradually, and working to an agreed plan, to substitute a home demand for an overseas trade.

13. In the latter, also, this country has developed a financial as well as a commercial connexion and an aptitude for the exchange of commodities and the furnishing and supervision of credit facilities which, employing no inconsiderable part of the population,

constitute at the same time services of which the whole world has need now and will continue to have indefinitely far into the future.

14. In the retention, the improvement and the extension of these activities, needing less the investment of huge aggregations of capital than the ever more expert activities of the human element, I would strongly urge my countrymen to seek the maximum gain from the highly individualistic character of the national genius.

15. Since, however, an active commerce cannot continue to exist apart from a vigorous industry, it is necessary that the latter should be able to hold its own with industry in other countries whose original lee-way of technical inexperience, capital insufficiency, political insecurity or geographical inequalities is now being rapidly overcome.

Again, special aptitudes for the production of articles of enduring quality suggest that more emphasis should be laid upon the training and equipment of the national labour force than upon the reduction of its wage rates to the level of a labour force recruited rather for low-grade production.

16. It is eminently reasonable to infer that so soon as the mass demand of the world has been met for articles of indifferent finish and unimaginative uniformity—a proceeding not likely to be very long deferred should the world be enabled by its creditors to escape from the present *impasse*—there will arise an ever greater and greater demand for articles of more marked individuality than standardised industry can produce. It is such a market which we must maintain our disproportionately numerous craftsmen and tradesmen again to supply.

17. The temptation to yield to an entirely ephemeral preference on the part of our overseas customers for the articles of crude workmanship and indifferent finish is one which must be decisively rejected.

18. That being so, alike abroad and at home, it is essential that the banking institutions, subserving the needs of a highly individualistic commerce and a specialised rather than a rigidly standardised industry, shall attain in their *personnel* a ready adaptability to continuously changing conditions of trade rather than that they shall be required to immobilise vast credits in the finance of grandiose plans for reconquering markets in Latin America or securing a substantial share of so unsubstantial a demand as offers in Soviet Russia.

19. Liquidity of assets is so paramount a necessity for banks of commerce that it is impossible otherwise than emphatically to reject counsels, from whatsoever quarter they come, which would have as their consequence the ear-marking for years ahead

of such revenues as might or might not result from so many superficially attractive propositions as have been dangled before us.

20. This same consideration causes me to view with no less distrust the continuance on the boards and, may be, in the management of the joint stock banks of a *personnel* so obviously drawn from families, traditionally associated with the constituent firms by the amalgamation or absorption of which "the Big Five" and the several more provincial banks have swelled to their present impressive proportions, linked altogether too closely in blood relationship and in business connexions with great industrial enterprises urgently needing to be subjected to what Sir Josiah Stamp described as "a few healthy bankruptcies." I cannot rid myself of the feeling that much of the criticism levelled at the Bank of England by the spokesmen of the industrialists and their friends among the joint stock bankers is motivated by such "unmentionables" as the frozen credits of the boom years of inflation.

21. The volume of overdrafts which, in the event of a general movement to liquidate the cotton, woollen, coal, steel, shipbuilding and certain other industries one after the other, if not all at once, would be discovered to be as rigid as the Greenland ice-cap, the wary answers of witnesses coming before us from the joint stock banks made abundantly evident. To be brutally frank with the critics, let me say that the suppleness and ingenuity of their argumentative methods have in no sense detracted from the impression made on my mind that their real grievance against the system of credit control exercised by the Bank of England is that it compels, as an alternative to extinction, an accommodation of industrial, commercial and banking practice to the conditions of a world economy that will not wait upon the customary convenience of England.

22. Exposed, the one much more and the others much less immediately to the buffets of the external money market, after all these years of experience, it ought not to be beyond the powers of the Bank of England and the banks of commerce to adapt themselves to an epoch of economic change which, far from approaching an end, is only at its very outset.

Either those in control have not yet felt to the full the discomfort and distress which, in ever widening circles, sweep upwards through the rest of society or else these people, highest and, therefore we may assume, oldest in the hierarchy of capitalism, are in the economic sense so senile that they are incapable of evolving any new ideas of practical utility.

23. Since no new form of organisation can properly take its place on the stage of history until that out of which it springs is already outworn, there can be no question of substituting the present controllers of the credit system so long as they can satisfy the reasonable needs of the public.

But the latter cannot tolerate indefinitely the continuance of those mutually exclusive poses which have, from 1826 onwards, in greater or lesser degree characterised the relations of the new banks, arising out of the Industrial Revolution and the old Bank, that has held on its haughty way ever since it was constituted to give permanent shape to the principles of the Whig Revolution.

24. Both of them continue to live, so far as practicable, in the past. So, not needing unduly to make a virtue of its necessity, I content myself with recommending to the banks of commerce the timely example of the Bank of England which has relegated the profit-making instincts of its stock holders to the rear, has selected its directors much more with a view to give expression to the several economic interests of the country than was formerly the case and is slowly but surely accustoming itself to the idea, altogether without precedent, that it should become the servant not of property alone but of the entire public.

For neither party can the change-over be easy. Each of them shares too much in the rigidity of mind and method that characterises a commerce and an industry which have so casually evolved over generations from such rudimentary origins as have those of Great Britain.

25. Here, in a measure equalled nowhere else in the world, the three forms of economy have grown up not apart from but inextricably entangled with each other. The merchant has been manufacturer at one and the same time that he or his nearer relations have been engaged in the business of banking. The entire economic structure of this country requires overhauling and to complain as querulously as many people continue to do that it is too big a problem is no more and no less than moral cowardice.

26. Immediately, however, my concern as a member of this Committee is with banking, finance and credit, and to that I am addressing myself when I insist that never must there be a repetition of the laxity, the favouritism and the general muddle which have marked the relations of the commercial banks with the moribund industries of this country since the end of the War.

27. Sir Josiah Stamp, answering Mr. Lennox Lee concerning the "great personal jealousies" in the business world, went on to say that "behind them are various banking positions of unknown degrees of solidity and jealousy I cannot help thinking—this is only an impression of mine, and I am not able to back it up with statistics or facts—that the joint stock banks who are carrying the weak members should once and for all give up looking for better times for those particular members and also maintaining the priorities for their own benefit and keeping the beautiful position of their own balance sheet. They ought to precipitate

matters by pressing the debtors and making them deal with the situation." (Q. 4070-71.)

But "hard doctrine" as this seems to Sir Josiah Stamp, still harder must it seem to many of the hereditary banking dynasts whose votes count on the boards of the "Big Five" as well as in the ordinary and extraordinary general meetings of colliery, steel and kindred concerns in South Wales, on the Tees, around Sheffield and to the landward side of Newcastle, Glasgow and Liverpool.

28. The majority on these bank boards would do well, however, to note that whilst Sir Josiah Stamp said, replying to a question by Mr. Bevin as to whether by healthy bankruptcies he meant those of the banks, that the latter "are so strong that they can stand a good bit of it," there may well come a point at which even they may be pulled over. So soon as that point is approached it is probable that opinion will undergo a subtle modification and that, so far from it being insisted that "it is best to keep politics out," the responsible heads of the commercial banks will have discovered, as on other occasions, that there are limits to the risks that private enterprise can reasonably be expected to incur. But it is equally probable that opinion will have altered at least as much, if in an exactly opposite direction, so far as concerns the rôle of the state in relation to private enterprise suffering from the consequences of its own ineptitude.

29. This warning is perhaps the more necessary in view of the disposition shown before this Committee of bankers to expect the Chancellor of the Exchequer to be as reluctant to restrict borrowing by means of Treasury bills when they have difficulty in finding employment for their cheap money, as he should be eager to do so when the difficulty in finding employment is confined to the wage-workers.

30. At this stage it may be as well to remind the Bank of England that the wage-workers, constituting as they do the overwhelming majority of the electorate, are labouring under no unwarranted apprehension when they see in the raising or lowering of the Bank Rate a means deliberately designed and operated "to adjust" their wages. The possession of such a power by an institution, acting in complete independence of parliamentary control, is an anomaly which could not continue to exist in this country, side by side with popular sovereignty, were it to be exercised other than with an ever-growing discretion.

Unless it be that we are the least logical of people or that the exercise of this power rests with a man held in immense regard, there is no reasonable explanation to be offered for the perpetuation of a condition of affairs that flies in the face of common-sense.

31. But whilst, in principle, I agree with Mr. Bevin and Sir Thomas Allen that the Bank of England should not be an institution owned and operated privately, I am unable to see any case adequate for the change they propose in its constitution other than as an integral part of a carefully co-ordinated plan for such a fundamental re-organisation of our national economy as lies beyond the terms of reference of this Committee.

Already acting under Charter from the Crown and hedged about in their control of the currency by Parliament—from a whittling away of which control, as will be seen below, not they, but I dissent—so long as the Governor and the Court of the Bank of England continue to show themselves, in the essential spirit of our unwritten constitution, so eminently ready to adjust their methods to fit in with those of the Government of the day, I am not prepared to waste words over what seems to me to be purely a point of political theory.

32. At the same time I dissent, along with Lord Bradbury, from the proposed reform in the law relating to the note issue recommended by the Majority of the Committee. It is a relaxation of the control properly to be exercised by the Treasury (and so by Parliament) over the monetary attributes of sovereignty, from time immemorial vested in the Crown.

Robed in whatever fine phrases, supported by whatsoever specious reasoning, it remains a challenge presented naturally enough at this particular stage of social democratic advance to parliamentary ascendancy by the protagonists of private property ready, as soon as the State no longer reflects their interests, to push it to one side.

Collaborating, as it is ever more necessary that the Bank of England should, with the Central Banks of other sovereign States, it must not cease to be, in the final analysis, at all times *en rapport* with the Treasury.

Released from the legal limitations imposed upon its powers of note issue, extremely improbable as it is that under the existing control there would be any departure from the solid gold basis of the currency, the human factor alone would stand between the country and the possibility of inflation. There is no guarantee that another Governor might not reverse the policy of the present. The latter is probably strong enough a personality to stand up against the influences to which, in the event of the adoption of the Majority recommendations, he would certainly be ceaselessly subjected. But there is no guarantee that his successors will be as unbending.

In any case, I am at one with Lord Bradbury in regarding the proposed change as in the highest degree mischievous.

33. An expansion of credit is something that can only be embarked upon with safety to the extent that collaboration can be assured between the Central Banks. The bigger the reserve of

gold or the less the degree of uncertainty existing in and between the several countries the greater can be the amount of credit made available.

34. But the experience the world has had of the results of credit expansion in the United States during the last decade, when the powers of production have been developed without any effort at regulation other than by the rate of profit to be made over a very short period, should have afforded it a salutary lesson in the fallacy of the quantity theory of money. Drawn thither by a number of forces, not least powerful among which was the desire of propertied classes of Europe to evacuate the not inconsiderable part of their wealth that could, under present day conditions transferred abroad, the gold that poured into New York became the basis of a fabric of original bank credit which found embodiment in a technique of production capable of attracting to it a mass of labour-power that, despite the high level of wages, grew by leaps and bounds. Remaining in private control in the same way as had done the much less phenomenal gains of British manufacturers during the heyday of their prosperity, it found outlets of re-investment that were no more economically sound (or, for that matter, socially desirable) because they happened to be located at home rather than sought overseas. Put back into the businesses of the owners or made the basis of loans to others, the actual and anticipated profits of American capitalism in the twentieth century differed in degree rather than in kind from those of British capitalism in the nineteenth. That the collapse has been cataclysmic is to be explained by reason of those tremendous changes in technique to which, in his evidence, Dr. W. W. Stewart, former Director of Research to the Federal Reserve Board of the U.S.A., and, later, Adviser to the Bank of England, so continuously referred. The industries of to-day as distinct from those of yesterday are locked into great chains of production, process linking with process, so that finance has had, willy-nilly, to follow suit. The immobilisations of capital and of credit so demanded having been such as bankers are properly loath to make, the tendency in this, as in previous cycles of "boom" there and elsewhere, was for the pyramiding one on top of the other of ill-considered and ill-managed corporations given the flattering name of investment trusts.

35. The dire and long-drawn process of liquidation of all the multiplicity of crazy ventures—and not a few that did not even go crazy, but which have been pulled down in the common wreck—should, supposing it stops before it completes the ruin of an already war-shattered world, leave the tangible assets of the many in the effective possession of few enough financial houses to make their reduction and reorganisation according to something like a world plan of rationalisation possible.

36. Such being the obvious tendency consequent upon the continuous deflation of credit, hitherto available from banking as well as non-banking sources for the unregulated development of the world-wide production and distribution complexes made possible only by the most modern technique, it seems to me essential that whatever plans may be evolved in this country for the reconditioning of the basic industries should not run counter to this drift, or becoming more definite and deliberate, towards an international economy. Since dominant political influences in all countries without exception reflect the passions and prejudices surviving from a dead past rather than any purpose in a living present, the more separate these new economic entities can be kept from the structure of the national state, here as elsewhere, the better. Whilst it appears, unhappily, all too probable that governmental compulsion will require to be applied in this country—and that quickly—to overcome the opposition and inertia of old-fashioned business men to what is called rationalisation (much better if brought about by the banks) and that a National Planning Council may become a necessary organ of the State, it would be calamitous that the basic industries of this country should be reorganised into national units with a view to make them ready to compete rather than to be co-ordinated with their opposite numbers in other countries.

37. Such a development must involve ever more rapidly repeated calls for new capital expenditure which, whether made by public or private enterprise, will come to entail an intolerable drain on the resources of this country.

Not once only will it be necessary to accept such recommendations as, with the commendable logic of capitalism, Mr. Brand is frank enough to make in his addendum, but again and again, as often as new funds must be attracted to or, at least, dissuaded from fleeing the country.

38. However, wages cannot be cut and social services slashed in this and in the way that Dr. Goldschmidt, of the Darmstadter und National Bank of Berlin, made it plain in his evidence (Q. 7345-48) he considered economically necessary, without provoking just such industrial, social and political reactions as have followed upon their adoption in Germany. They must, in their turn, affect unfavourably the credit, first of one country and then, as this desperate remedy becomes general in its application, of all countries.

39. Quite apart from the question whether this country can hope to command the resources necessary to retain a lead which it may have been found practicable for awhile to recover, the external repercussions of such an effort must be disastrous to the peace of the world.

40. The present opportunist drift in all parties towards an economic re-organisation either national or imperial in its loyalties must militate against the attainment of those conditions of stability with flexibility, alike at home and abroad, which can alone permit of the orderly because essentially automatic operation of the gold standard and of the credit system.

41. For that reason particularly desirable is it that the provision of the long-term credits necessary to re-habilitate British industry shall be entrusted to a corporation such as the Bankers' Industrial Development Company, the responsible heads of which are engaged in the finding of funds for similar enterprises in other parts of the world. Members of firms which are continuously figuring in consortiums of financial houses, international and intercontinental in their scope, for the collection and allocation of credits to re-organise and re-condition the basic industries and public utilities of many and varied countries are surely, subject to the checks appropriate to be provided by a National Planning Council, acting in consultation with the Bank of England, best qualified to undertake the task.

42. The actual range and method of the re-organisation of industry are no concern of this Committee except in so far as it is necessary to envisage the potentialities of the credit resources available to meet the demands that may be made upon them and to estimate the reaction of such long, intermediate, or short-term immobilisations of money on the financial fabric.

43. The urgency of improving the national trade balance does, however, require that consideration should be given to such alternative proposals as may tend in that direction. Whilst deprecating most strongly the adoption of either the expedient of a tariff of a general character, whether for revenue or protectionist purposes, or of a reduction in real wages and salaries, I would place the maximum emphasis on the need, if only as a temporary expedient during this period of acute national difficulty, for a revision on the part of everybody from the highest to the lowest of what have come to be customarily regarded *criteria* as to what constitutes essential expenditure. The dissipation of capital reserves, actual or potential, in the rendering of services or the manufacture of commodities which, whilst they may attract to the persons interested therein high wages and considerable profits, detract from rather than add to the productive capacity of the national labour force, is an extravagance which this country can no longer afford. It is monstrous that policies so calculated to dislocate our commerce as a revenue tariff, to disturb our industry as wage reductions, and to shatter our whole financial structure as a serious canvassing of devaluation, should be so much as listened to in advance of a nation-wide stock-taking of what individually, even more than collectively, we can or cannot afford. In

the event that no sustained initiative in this matter is forthcoming from those who are supposed to set the tone and give the lead to their less favourably situated fellow-subjects, then the same end must be sought by other and less agreeable means. Whether this shall be by taxation bearing much more heavily on income uneconomically expended, by drastic extension of excise duties or by a stringent limitation of imports contributory to the luxury trades, it will be for others to determine. However it is done, by voluntary action or by discipline enforced from without, steps must be taken without any further procrastination to encourage savings so that these may be made available for the re-conditioning of the basic industries and the transport services as well as for the provision of housing, health and higher educational facilities necessary to raise the intellectual no less than the physical standards of efficiency of the national labour force.

44. Going outside the terms of reference of this Committee as it would be to indicate the industries to which financial assistance might well be given, there is one exception to which it is particularly pertinent to call attention. Even as it is essential to reduce the volume of dispensable imports so is it necessary to increase the amount of exports. For this country there is a category of unusual importance, the so-called "invisible exports."

45. Amongst these is one capable of very considerable expansion, provided always, of course, that it is possible to throw off the lethargy and dispel the conservatism of those who are needed to make of it a commercial success.

The Tourist Industry has great potentialities, having regard to the romantic as well as the more nearly sentimental appeal of Great Britain and of Ireland to the more prosperous as well as the more cultured of the emigrant nations. But until much has been done to modernise hotel accommodation, to improve transport in the more picturesque parts and generally to cater for people who are accustomed to superior plumbing and a more rational system of interior lighting and heating—just to mention a few of the deficiencies—a revenue running into tens of millions sterling will continue to be lost to this country.

With the rapid falling away of our shipping prosperity, as well as the reduction of our overseas investments, this is a source of income which we can no longer neglect.

The constant presence in their midst of visitors from other lands across the seas may also prove helpful to the inhabitants in what a distinguished French economist recently described as "the Happy Valley."

J. T. WALTON NEWBOLD.

RESERVATION BY SIR W. RAINE.

1. After a most careful study of the Report and its recommendations I feel that it is too indefinite in its practical issues, consequently I consider I should express what I believe are some practical proposals for the improvement of the present position, because in my opinion it is useless to tinker longer with a situation which has every appearance of becoming even worse, unless we drastically alter our methods.

2. The Report has been largely devoted to a survey of our Financial Institutions, in order to show what important part they have played in developing British trade. It is true that in the Century concluding with 1914 the British people were so "busy" that the policy of *laissez faire* was readily accepted. It suited British psychology. The period since 1914 has shown the British people that the British system, which has worked so smoothly for them, requires revision; in fact, bitter experience has revealed the fact that had we taken earlier notice of some of the disadvantages we would not have found ourselves in the position we are to-day. The War, undoubtedly, exposed much which had before remained covered: there is no doubt also that the events which have followed in the last decade have so far as Great Britain is concerned revealed to us that, however good and efficient our system was, we must in the light of recent history adjust ourselves to the altered conditions, or the alternative will be that we shall be left behind.

3. Leaving aside the world slump which has affected everybody, the root of the trouble has been the re-division of Europe as the result of the Treaty of Versailles. Several small nations, which previously formed parts of larger units, are now working out their own destinies. The smaller nations wish to enjoy the same standard of living as hitherto. They found themselves in 1919 with legacies of war machinery, which were quickly converted into weapons of industry—new factories with up-to-date equipment. It must not be overlooked that Great Britain was not invaded during the War; Belgium and large portions of France were not only invaded but devastated. In the process of reconstruction these countries have obtained the most modern equipment. We being an older country were unable to quickly grasp the significance of all this new machinery; we were still very busy and wages were high. True we had various set-backs, but it can hardly be denied that the Ruhr trouble of 1923 again put this country in a false position; judging by subsequent events Great Britain would have suffered less without the monetary but doubtful benefits of inflated prices and booming trade of 1923. Had that not occurred, we should probably have come face to face with the realisation of the altered conditions before 1924, and with this great advantage to

ourselves, that the position would not have become so desperate as to cause us to grope almost in the dark to find a way out.

It is useless to regret what has gone, but rather, calmly and deliberately, to find a solution of the problems which beset our path.

4. Two factors require to be mentioned at the outset :—

(i) These new nations, in particular, have by means of Tariffs never hesitated to protect their industries, enabling their people to have constant employment—true at lower wages and on worse conditions than in Great Britain, which has permitted them to produce cheaply and to send us their surplus products at prices with which we could not compete.

(ii) Since 1925, we have only had on one occasion less than 1,000,000 unemployed, whereas in the meantime the Continent of Europe, as well as the United States, has enjoyed a period of almost unexampled prosperity.

These two facts, the second of which is really a corollary of the first, are worth careful examination.

5. The end of the War brought with it an ethical fervour in this country, which unfortunately had no solid foundation. Honest and praiseworthy attempts have been made by our people in all walks of life to bring about an international state of affairs, the results of which were intended to raise the standards of living of the nations, but for one reason or another success has not attended these efforts, and in particular in the realm of trade and industry.

6. In 1927 an International Conference at Geneva expressed the opinion that Tariff walls were too high. It is interesting to quote from the Report of the British Representatives. They stated that, "If other countries do not move towards a policy more in accord with the views of the Geneva Conference, a reaction from its traditional open market policy seems probable. It is believed there is a growing volume of public opinion in this country, which will not continue to accept without effective protest the present high tariffs and barriers which confront the British exporter." The reply to all this is that Tariff walls are higher to-day than ever before.

The present Government has made serious attempts to obtain reductions of Foreign Tariffs, but in vain.

7. Free Trade was undoubtedly the cause of the great prosperity of this country in the latter half of last century, but we are faced to-day with a new condition, inasmuch as the countries of Europe, and some in Asia, have reached a state of industrial development which carries with it a standard of efficiency in most respects equal to and in some cases superior to our own.

8. We have had some experience of Protection in this country from which it is safe to say that, were we to embark upon a regular system of Safeguarding, we should not be sailing upon an uncharted sea. Figures taken out of their proper setting can be made to prove anything, so I dismiss the statements as to whether in any particular year we exported more or less of any safeguarded article than before the trade in question was safeguarded, but hasten to look at the essential facts :—

(i) Are there more factories in this country producing say Motor Cars and Tyres than in 1925?

Have not some of these factories been built by foreigners as the result of Safeguarding? British labour is employed which means the wages are spent in this country.

(ii) Have not the prices to the consumers been reduced?

(iii) Are we not importing fewer of these commodities?

(iv) Are not more people employed in these and other safeguarded industries?

9. The forecast of the British Representatives to Geneva has proved to be correct. The volume of public opinion has grown which is protesting against high Tariffs that are preventing the free flow of our manufactures into other countries, whilst our open market policy enables these countries to send into Great Britain surplus manufactures at prices which in some instances would barely pay the British costs of labour. Bankers, manufacturers and even some economists who were traditionally Free-traders are amongst those who, whilst still theoretically Free-traders, now take the view that owing to the serious position in which we find ourselves some drastic changes are absolutely necessary.

10. I may add that an ex-Chancellor of the Exchequer recently addressing an assembly of business men stated that unless something is done at once this country will in the next two years become further embarrassed. The argument that imports must be paid for by exports is undoubtedly true, but how are we accomplishing this? Very fortunately for us, we, in our days of prosperity, invested vast sums abroad from which we derive annually some hundreds of millions of interest; we also render great services for which we are paid, such as shipping, banking, insurances, etc., but the policy of discrimination in regard to shipping has largely reduced this source of income and produced unemployment. Still further attempts in this direction are now being considered which will further curtail our revenues from shipping. Whether the calculations by which we arrive at the figures of our annual Balance Sheet are scientifically correct or not, the basis of comparison is more or less accurate, and the fact evolves that this account, which a few years ago showed an available balance for further investment of £150 to £250 millions, was last year only £39 millions. The

world slump had no doubt something to do with this low figure, but the naked fact remains that this process already described is proceeding with relentless certainty. It will find us before many years pass with a debit instead of a credit balance.

11. The Committee has been considering proposals to meet the present emergency. Summing up the situation I am forced to the conclusion that protection of our industries is essential and that it is necessary to state the fact in unequivocal language. I would limit the protection, however, at the outset to a Revenue Duty on all imported manufactured articles, which should be imposed immediately, the only exception being that the usual preference should be accorded to our Dominions. I do not minimise the difficulties of such a course, but I am reminded that this country is still the greatest creditor nation and we are the largest market in the world. Drastic remedies are required.

12. I do believe that such a remedy would, notwithstanding its difficulties, have the immediate effect of creating an atmosphere of confidence which would be the forerunner of a rapid improvement in trade.

13. I am not unmindful of the fact that exports are vital to the well-being of this country but I am convinced that our Dominions, as well as those foreign countries which have almost unlimited quantities of various food supplies, would be only too wishful to enter into arrangements with us for our mutual benefit. Besides, some of these countries as well as our Dominions must continue to supply us with foodstuffs in order to pay for the interest on and repayment of their indebtedness to us. Thus, if we did not arrive at the ideal state of Free Trade, we would at any rate enjoy freer trade.

14. It is unquestionable that we have lost sight of the importance of our home market. Should expectations not be realised that all foreign nations, both those who supply foodstuffs as well as those who do not, did not meet our changed policy by an adjustment of their own, some at any rate would be obliged to do so. It is anticipated we would recapture a large portion of our home trade in manufactures.

15. There is a measure of agreement amongst commercial people that this intricate question should be lifted out of the realm of party politics. I may say that I am approaching this subject with as much impartiality as is possible, but with the sincere idea that Protection of industry is one of the chief steps to be taken to save our country. Immediate action is necessary in order to save the situation; the undoubted adjustments which would have to be made could be reached later as the result of negotiations.

16. Some reference must be made to what is known as "Capital Development Schemes." During the whole of the last decade

Local Authorities have spent many millions in this way, in order as was hoped to deal with what was expected to be merely a temporary phase of unemployment. However, as the years have passed and the situation has become worse instead of better, the number of such possibilities of Capital Development has steadily decreased. Even after the deduction of much Government help, which the taxpayer has had to find (and which has kept up to a certain extent the high rate of taxation), the Local Authorities have been left with debts the liquidation of which will for some years prevent that reduction of local rates which is essential to help our manufacturers and producers to reduce their overhead costs. Moreover, it must not be overlooked that many of these schemes have not been carried out on an economic basis.

17. Judging by the limited experience of Safeguarding, new factories would undoubtedly be required, so that efforts in this method of Capital Development would be beneficial because, as soon as they were completed, they would become the means of the production of wealth.

18. Apart from such schemes just mentioned, there are two others of such magnitude that they would take years to complete; in the meantime large numbers of unemployed would find work. An additional benefit would be increased employment in the trades producing the necessary materials. Further, it is common knowledge that for every man in ordinary employment another man finds employment to produce the necessities of life for the first-named and his family. The two schemes are:—

(a) The electrification of the railways.

(b) Drainage of those parts of the country which are so frequently flooded.

19. With regard to the first, the Report of the Committee on the Electrification of Railways has just been published. It is safe to say that the change over from steam to electricity would take at least ten years, not only for monetary reasons, but also from the fact that unless it were carried out gradually the men displaced might easily outnumber, for a time at any rate, the number engaged in the new work essential for the change over to electricity.

There is no doubt, judging from the experience of other countries which have electrified their railways either wholly or partially, that the ultimate result of the change would give us a new lease of life in our transport system, besides being a great step in the direction of enabling us efficiently to compete again in the world's markets, provided that Tariff walls were not further raised against us.

20. In respect to (b) Drainage, there is little doubt that well devised schemes would avoid, probably for ever, the devastating effects of flooding which at certain seasons of the year the traveller

can see for himself from the railway train as he journeys to different parts of the country. I am informed it would improve the navigation of those rivers which are navigable. The cost of this work could in the first instance be paid for by public loans, the subsequent liquidation of which ought to be met by a small charge per acre which would amount to far less than the costs incurred at present by those concerned.

21. Both these schemes would have the result of equipping us better for the battle of life. In the case of the agriculturist it ought certainly to remove from his mind the constant fear of loss and even bankruptcy, through causes for which he is not personally responsible and over which he has no control. Certain Harbour Authorities should also derive great benefit. The main-spring of enterprise is profit. That an industrial or commercial enterprise should make profits is not injurious to the community, but under free competition rather a measure of its usefulness. The employee rightly desires his fair share of the fruits of his labour. It has been distressing to employers to have to insist on reductions of wages, but could they have acted otherwise under existing conditions?

22. I believe that, with the introduction of changes such as are advocated above, real wages will advance and the state of affairs produced will approximate to the conditions of pre-war days. Of course, we shall have Cycles of Trade, as in former days, but we will not see ourselves merely enjoying the overflow of booming conditions of Continental countries.

The British are a practical people. If they find that the expectations of the suggested changes in our Fiscal System are realised they will be grateful, but if I am wrong in my suggestions it will be recognised that an honest attempt has been made to rectify a very grave situation which has become so perilous to our welfare. Moreover, are our foreign competitors wrong in their policy?

23. I do not feel myself competent to express an opinion upon the recommendations regarding the Note Issue as set out in Part II, Chapter III.

24. I dissent from the "Proposals Relating to Information and Statistics" detailed in Part II, Chapter V. I consider that the trouble and expense is unnecessary, as the statistics when available will be out of date; besides there are now published such masses of statistical information, which should enable the practical person to form correct judgments on trade and commerce, whilst the ordinary theorist has adequate data at his disposal for the examination of all the abstract problems which he may desire to investigate.

WALTER RAINE.

MEMORANDUM OF DISSENT BY LORD BRADBURY.

1. I regret to find myself in disagreement with most of the conclusions formulated in this report. Leaving out of account for the moment the effects of the recent heavy fall of world prices, I think the main causes of the economic troubles of Great Britain since the War have been (i) the burden of unproductive debt, (ii) overlavish expenditure by the State and local authorities, (iii) excessive cost of transport and distribution and of the products of sheltered and protected industries, and (iv) the attempt by all classes to maintain a standard of living higher than is justified by the facts of the economic situation.

2. The burden of unproductive debt is partly that of ~~the~~ dead-weight debt arising out of the War. But this is by no means the whole story. The debenture debts of, and bank loans to, industries which cannot, or can only just, make ends meet, and the maintenance of railway rates at the level necessary to provide a return on capital which has to a large extent ceased to be economically productive—to take only two instances—are burdens of a very similar nature.

Out of the total produce of industry the creditor and the State—on behalf of the rentier and also to meet public expenditure on services other than the debt on a vastly enhanced scale—take a much larger proportion than before the War; transport and distribution also take a larger proportion (*teste* the wider gap between wholesale and retail prices). The remainder after providing for the remuneration of labour is in many industries not enough to leave a sufficient margin to induce the entrepreneur to continue his exertions or hazard fresh capital. The weakest close down and the maintenance of the workmen thrown out of employment increases the pressure on those still at work. The next weakest then succumb and the process seems likely to continue until the volume of production is so reduced as to be unable to support over the whole country even the standard of life at present enjoyed by the unemployed.

It is no doubt true that the payment of the interest on internal debt and allowances to unemployed workmen* are merely "a transfer of incomes within the country", but (except in so far as they are met by the taxation of rentier or the unemployed workman himself) it is a transfer from the producer to the non-producer. If it goes far enough it will leave the producer with no motive to produce and in the end cease perforce because there will be nothing to transfer.

* The burdens on productive industry arising from the charges for dead-weight debt and those arising from the cost of maintenance of the unemployed are very similar in character and effect, but the latter have the peculiarly devastating property of varying inversely with the production which has to support them.

That catastrophe has not occurred earlier is mainly the result of the tremendous strides in the technological efficiency of industry which have taken place concurrently, but to take full advantage of these considerable capital expenditure is necessary and when industry is unprofitable the necessary capital is not forthcoming.

3. If this is a true diagnosis it appears to me that the malady is too deep-seated to be removed by any manipulation of currency or credit.

True if it were possible to raise the price level the burden of our ^{own} debt would be decreased and, in the (what seems to me improbable) event of the workmen being content to accept the same money wages notwithstanding the increased money cost of living, the real price level above the level of world prices without reducing the gold value of the pound or abandoning the gold standard altogether is impossible, and I agree with the majority of the Committee that recourse to either of these expedients would be most undesirable.

I am of opinion that the real remedies for our economic troubles lie in the main in a field outside the terms of reference of the present Committee.

4. In regard to the international working of the gold standard, I agree that efforts ought to be made to secure by international agreement a better distribution of existing gold stocks and greater economy in the use of the metal but the attempt made in the Report to formulate the objectives to be aimed at seems to me in conception too ambitious and for application too nebulous.

5. Under the head of International Monetary Policy of a Permanent Character (Part II, Ch. II) a word of caution is necessary particularly as regards the objective in the more distant future. I doubt whether the fixation, by co-ordinated action of the Central Banks, of the world value of gold at such a level as would secure a stable average level of wholesale world prices is feasible or even desirable. Such a proposal really means the substitution of an index figure for gold as the standard of value and (apart from the utility of gold as an ultimate reserve in the event of the new system breaking down—a contingency which it would be imprudent to ignore) the new unit of value would, if the proposal were adopted, be better represented by a counter to be issued by a trustworthy international authority. The world would then be saved the labour and expense of gold-mining and the Central Banks the worry of having perpetually to devise expedients to adjust the value of that no longer necessary commodity to the value of the new unit.

Whatever theoretical case can be made out for such an innovation—with or without the retention of gold as an accessory—I doubt whether the proposal will come within the range of practical international politics during the lifetime of the youngest of us.

Nor is stability of average prices necessarily desirable. Suppose that the present progress of scientific agriculture is not maintained and that, owing to the increase of the population of the world, food and raw materials tend to rise in price relatively to manufactured products even though manufacture does not become more efficient, is it ideally desirable to have stability of average prices, i.e. a fall in the prices of manufactured goods to compensate for the rise in the price of food and raw materials? Surely that would intensify the difficulties of adjusting costs to prices on which my colleagues have laid so much stress.

I would, therefore, in regard to the more remote future, confide myself to aiming by international co-operation at such economies in the use of gold as will correct the ill effects of the failure of gold production to keep pace with the requirements. The difficulties in the way of effective international agreement to secure such economies are so formidable that any theoretical danger of excessive economy resulting in world-inflation may safely be ignored.

6. When I come to the measures outlined for dealing with the present world crisis, I agree that a general increase of the world price level would materially alleviate the present economic depression, and incidentally obviate the painful adjustments which will otherwise be required to bring our domestic price level into relation with that of the outside world. It seems to me, however, that the treatment of this subject in the Report is at once too sweeping and too sketchy. I cannot associate myself with such statements as that in paragraph 271 that "a failure by the Central Banks of the world to attempt to redress the fall of prices would endanger the principles on which modern economic society is founded." Nor do I regard it as advisable for the Committee to treat what may in fact prove to be impracticable as an "immediate necessity." Further, if the remedy is to be administered, those who prescribe it should at least be prepared to specify the manner and extent of its application. But the Committee (paragraph 266) "do not consider that a high degree of precision in the definition of this (price level) is necessary or practicable." In paragraph 277 similarly, they admit that they cannot "give a confident answer to doubters" as to whether a restoration of the price level is in fact feasible. Again, on the cardinal question as to whether Central Banks are to attempt to counteract a fall in the price of one commodity by a general rise in other prices, the Committee (paragraph 300) "do not think it necessary to give a dogmatic answer to such questions." Moreover, the trouble is admittedly an international one which cannot be solved by this country alone, and it is well known that in certain other countries, particularly France, public opinion is not only unwilling to promote an increase in the price level but is determined to oppose it. The Central Banks in France and most of the continental countries have no

power to undertake open market operations which will be required if any such attempt were to be made. This being the case, even if theoretically there may be much to be said for the Committee's views, they seem to have little relation to the real facts of the actual world.

7 I am in agreement as to the necessity of co-ordinated effort part of the creditor countries to aid the debtor. But it be remembered that, even before the crisis, many of the countries were applying new loans not to the creation of productive assets, but to meeting international deficits on revenue account—a process which if continued leads inevitably to default. In such circumstances the drying up of the supply is sooner or later inevitable and it is difficult to see how the stream can be kept flowing until they have put their houses in order. There is no doubt of the intention and ability to do this, but the granting of loans to tide over the necessary interval should be arranged. In some cases, no doubt, guarantees will be necessary. In such cases I should prefer, whenever possible, that the guarantees should be those of groups of private institutions, both because this would secure that the propositions handled were limited to those involving only fair commercial risks, and also because mistakes when made would be wiped out by the painful but salutary process of ordinary liquidation instead of going to swell the already well-nigh intolerable burden of permanent deadweight debt.

8. The revival of enterprise in the creditor countries themselves will, as pointed out in the Report, in itself improve the situation of the debtors and this is equally true whether the revival takes the form of increased production of capital or of consumable goods.

The tendency of long-dated high-class securities to rise in value, which is invariably observable in times of commercial depression, will undoubtedly encourage certain classes of constructional enterprise, but I cannot accept as valid much of the argumentation on this topic contained in Chapter XI of Part I or the conclusion that it would be wise to create credit for which there is admittedly no demand with the hope of artificially inflating security values and so cheapening long-date credit for capital enterprise.

The Report itself admits that such surplus credit would become dangerous and would require to be retracted once a trade recovery were well under way. The retraction would inevitably depreciate the value of the securities into which its creation had lured the investor and an unpleasant impression would be created.

In an individualist society capital can only be provided by inducing individuals to forego present enjoyment in exchange for future advantage. It is no doubt a convenience to all except the individuals who have made the present sacrifice that, the capital having been provided, the future advantage should be diminished

or fail to materialize altogether. When the capital investment takes the form of securities representing money claims this will happen if the rate of interest is reduced by artificial supplies of cheap money and if the enjoyment value of the capital claim itself is diminished by raising the price level. Both these results can be brought about by expanding credit. Indeed, if the expansion is great enough, the future advantage reaped from the sacrifice may easily in terms of enjoyment be less than the sacrifice itself—the ultimate loss of real value in respect of the capital claim being greater than the interest received by the administrator.

This superficially clever measure, if taken at the moment its *modus vivendi* is fixed, destroys the saving in order to invest in such claims.

So far as the result might be to encourage investment instead of fixed money claims the change, within limits, might be salutary, but the plan is put forward for the purpose of stimulating capital development by means of loans, and this it can only achieve in so far as it may succeed in hoodwinking the real investor.

If currency "management" is to be used to facilitate manoeuvres of this type, the sooner we return to an "automatic" system the better. Honesty, even if stupid, is a better foundation for credit than the most adroit finesse.

9. Turning to the proposals contained in the Report for action in the domestic sphere, I find little which appears to me to be likely to be useful and much that will in my opinion be positively harmful.

The recommendations for fundamental alterations in the regulations governing the note issue and for the amalgamation of the Issue and Banking Departments of the Bank of England fall into the latter category.

To allow expansions of the volume of legal tender money to be made otherwise than in exchange for gold appears to me to be a dangerous innovation which is likely to jeopardize the maintenance of the gold standard.

It must be remembered that the times at which an increase in the legal tender circulation is required are times of trade activity and rising prices—conditions which invariably go together. At such times money* tends to be plentiful and inflation is apt to develop unless the expansion is kept in check.

An outflow of notes into circulation under the existing system tends to contract the basis of credit by reducing the cash reserves

* I say "money" rather than "credit" because a large part of the increase of purchasing power arises from the coming into employment of balances previously idle without any increase in the total of bank deposits.

of the banks. If the exchanges are favourable the deficiency is made good by the import of gold. If they are unfavourable, credit expansion is checked until they become so, with the result that the price level is prevented from rising to the point at which it would cause an actual gold outflow and require an even greater restriction to stem it.

The gold reserve for the currency should, in my view, never fall below an amount equal to the maximum foreseeable contraction of the circulation at any given moment, plus whatever may be necessary to meet the maximum figure required to maintain the reserve for great national emergencies in such circumstances the drying up of the gold reserve is a process which if continued leads to a difficult to see the upgrade a reserve of gold to meet exchange requirements should these arise when there is a fall in the price level or on the downgrade and *pro tanto* the evils of high unemployment and restriction of credit are avoided at moments when gold is particularly harmful.

It is cre
 † Indeed to insist on gold import as a condition of currency expansion tends to slow down the processes of raising and lowering internal prices to adjust them to variations of world prices and so contributes towards that stability of the internal price level which the Committee recognize as a desideratum.

11. But quite apart from these considerations of practical expediency, in regard to which the balance of advantage is in my view heavily in favour of the existing regime, there are fundamental differences of principle between the two systems. The system of the Bank Act of 1844, which is continued in its essentials under existing legislation*, is based on the principle of safeguarding the gold value of legal tender money by providing that expansion and contraction in volume can only take place in exchange for gold, and of leaving the volume of banking credit, whether created by the Bank of England on the basis of the legal tender money in the Banking Department, or by the joint stock banks on the basis of legal tender in their own hands or Bank of England credit, or again by other institutions on the basis of joint stock bank credit, free to expand or contract according to the ease or difficulty of obtaining legal tender money.

So far from this being a rigid system it is, with a free gold market, a perfectly elastic system, subject only to the qualification that expansion can only take place when the foreign exchanges are favourable and contraction is enforced when they are unfavourable.

* The provisions of Section 8 of the Act of 1928 do not in themselves mean more than giving statutory recognition to the practice previously followed without legal authority in emergencies and providing machinery for varying the amount of the fiduciary issue in the event of permanent changes taking place in the total currency requirements of the country.

12. The system proposed by the Committee if carried to its logical conclusion,* ignores the volume of legal tender altogether and seeks to maintain the gold value of the pound by direct action by the Bank of England on the volume and price of bank credit. It does not, however, provide any real criterion of the occasion for such action, or of how far it should be carried when embarked upon, but leaves the settlement of these questions to the uncontrolled judgment of the Bank of England upon economic and financial tendencies which are admittedly most difficult to interpret.

Under the proposed system we have a currency system administered by the Bank of England. It is true by the issue of the reserve, the cease to credit system under which joint stock banks are free to create currency. They have a commercial inducement to expand credit to the maximum amount compatible with the safeguarding of their banking reserves and are in a position to reply to criticism (which so long as human nature remains unaltered will always be readily forthcoming) that they expand too slowly or contract without necessity that at any rate they are sacrificing profit to safety.

Under the new system the Bank of England is to have free discretion (subject only to certain extreme limits which would not in practice be enforceable) to take, according to its judgment of what is in the general interest, without risk or cost to itself—indeed the plan goes out of its way to safeguard the bank from loss arising out of its discretionary action—steps which will acutely affect the lives and fortunes of the lieges. The facts on which it has to form its judgment are so difficult to interpret that legitimate differences of opinion as to the wisdom of the steps taken are likely to arise on almost every occasion.

This surely is to place a private corporation in an impossible position and must lead before long, in a democratic community, to complete government control of the Bank of England to be followed in due course, since the plan will not work without giving wide discretionary powers to the joint stock banks also, by government control of these banks. I am in agreement with the majority of the Committee that such control is undesirable.

Further the Bank of England and the joint stock banks are not the sole credit-creating organs. A comprehensive plan

* Under the proposals as they stand the maximum limit of the fiduciary issue and the minimum limit for the gold reserve would indeed operate to require an attempt to be made to revert to something like the old system in the event of an acute crisis, i.e., in the face of the very conditions which necessitate a temporary suspension of the old system even when it has been in operation. I regard it as certain that the suggested maximum and minimum could not in practice be enforced.

for the direct control of credit would have to have regard to those institutions (which are increasing in numbers and importance) which build credit structures on the basis of deposits in joint stock banks not unlike those built by the joint stock banks themselves on the basis of their cash in hand and at the Bank of England.

13. It is no doubt true that a loss of gold sometimes—in the exceptional circumstances of recent years it would perhaps be true to say—often—arises from causes other than a real tendency of the gold to depreciate, and similarly a loss of gold from causes other than a process which has continued in the fluctuations of foreign exchanges the drying up of gold reserves, political rather than economic disturbances in particular, which tend to disturb the normal working of the monetary system. It is difficult to see how such disturbances can be avoided, and it is clear that special reserves in this connection are of great value. Such reserves might properly take the form of gold or of gold certificates, and they should be held in the Bank of England or in International Settlements (if that institution proves suitable for the purpose). By this means an additional demand on the world's gold stock would be avoided.

The same expedient might usefully be resorted to in regard to further additions to the currency reserve proper if and when a figure is reached which it is undesirable to exceed for considerations of general economy of gold.

14. On the question of the desirability of "strengthening" the Bank of England I have no real data for expressing an opinion. Whether its reserves (published and unpublished) are sufficient for the efficient performance of all its duties is a matter on which the Bank alone is in a position to judge, and the Bank has not only not asked for an increase but not even remotely hinted that an increase would be welcomed.

I see no objection to the Bank of England being allowed to increase its capital if it thinks it necessary or desirable either in its own interest or the public interest to do so.

On the other hand I see no reason for asking the joint stock banks to increase either their legal tender reserves or their balances with the Bank of England above the amounts required to provide for their actual requirements and their own security. *Per contra* I would not relieve them of the necessity of maintaining the reserves necessary to protect themselves against the depletion of their stocks of legal tender by expansion of the demand for internal circulation.

The right to issue legal tender money being a prerogative of the Crown, it is right and proper that the profits of the Issue Department should accrue to the Exchequer. This is secured by the present arrangements, which I see no sufficient reason to alter.

The Bank of England is placed in exactly the same position financially as it would be if there were no note issue and all money of unlimited legal tender were gold. I hold that the Bank of England, like any other banker, should in regard to its banking activities so arrange matters as to be able to afford to keep in the Banking Department whatever reserves of legal tender money are necessary for safely carrying on its business. After all, the object of increasing the fiduciary issue, if an increase is made, is a simple one—to provide the Banking Department with more legal tender money either to use or to hold in reserve. In so far as the additional money is used, it will be income-producing, in so far as it is held in reserve, it is unnecessary or unnecessary. If a necessary addition to cease to be, the cost of keeping it is a incidental expense of the banking business: if it is unnecessary, create it at all?

It is no doubt true—as indicated in paragraphs 334 and 335 of the Report—that if the Banking Department runs short of ready money it may have to part with income-producing assets. But that is quite a common experience in the world at large and it is not usually considered to be a ground for compensation.

It is also true, as pointed out in paragraph 337, that the cost of “sterilizing” gold imports which could not be allowed to have their normal effect of expanding the basis of credit might seriously embarrass the Bank. But this has nothing to do with the profits of the note issue, and in fact, in the interests neither of world economy of gold stocks generally nor of the proper working of our own currency system ought such surplus stocks to exist except accidentally and then for very limited periods. If surplus gold is the result of an excessive influx of foreign balances, its accumulation should be checked in the manner indicated below: if it is the result of an unduly low domestic price level, it should be allowed to form the basis of credit until the disequilibrium is corrected.

Under the gold standard, gold in quantities which can be digested is a food, in excess it becomes a poison. The system ought to be worked in such a way as to leave to other nations what they require for food, not to take it and then have to lock it up so as not to be poisoned by it.

15. As regards the proposed amalgamation of the Issue and Banking Departments of the Bank of England, this would no doubt be a natural—perhaps a necessary—consequence of the adoption of the other proposals in regard to the Note Issue.

If the present note-issue system is maintained, I would also retain the independence of the two Departments. Apart from the objection that the amalgamation removes familiar land-marks and involves a more or less prolonged period of uncertainty in the minds of those who are concerned in monetary business before experience has taught them what practical conclusions to draw from the new figures, the separation is in fact the embodiment of

the principle which has dominated the British monetary system for nearly a century that, with a strict control of currency, a large degree of freedom can safely be given to credit. The Issue Department is bound by precise rules. In the Banking Department the Bank of England has free discretion.

While it is no doubt true that since the restoration of the gold standard it has not been possible for the Bank of England to be in its credit policy wholly or even mainly by the level of the gold reserve in the Banking Department, the traditional recognition that the gold reserve has to be protected has undoubtedly strengthened the position of the Bank in taking measures which though necessary would be disagreeable.

16. I am not satisfied that all the difficulties which have caused the Bank to depart from traditional practice in the direction of elaborate "management" are permanent or irremovable.

A large part of them were the consequence of currency derangement at home and abroad resulting from the war and subsequent stabilisation.

Other disturbing influences in my view have been the enormous accumulation of liquid credit arising mainly from too narrow a margin between short and long money rates and the excessive volume of Treasury bills, and possibly the attempt (due to what I believe is a misreading of the report of the Cunliffe Committee) to maintain the gold reserve in the neighbourhood of £150,000,000 instead of allowing it to find its own equilibrium point.*

* Under the existing currency system, either as it existed before the War or in the form in which it was re-established by the Act of 1928, the total volume of legal tender adjusts itself to the requirements of the country at a level of prices determined by the balance of payments operating on the exchanges. The amount of gold which can be retained is therefore equal to the total legal tender required for circulation and bank reserves less the fiduciary issue. If, as I believe to have been the case, the total of legal tender required has since the fiduciary issue was fixed at £260,000,000 been less than £410,000,000, it follows that an attempt to retain £150,000,000 of gold is trying to put a quart—or at any rate more than a pint—of water into a pint pot.

The proposal of the Cunliffe Committee was gradually to reduce the fiduciary issue until a figure was reached which experience should prove was consistent with the retention of £150,000,000 of gold under normal conditions and then to fix the fiduciary issue at the amount to which it had actually been reduced. It became desirable, however, to make the transfer of the note issue to the Bank of England before the experiment initiated on the recommendation of the Cunliffe Committee had been continued long enough and before conditions had become sufficiently normal to arrive at a reliable judgment, and the fiduciary issue was fixed on the best evidence available at £260,000,000. If, once the £260,000,000 fiduciary issue had been fixed, the gold reserve had been left to find its own equilibrium point and this had proved to be less than £150,000,000, we could either have contented ourselves with the smaller figure or, if we still attached importance to the £150,000,000, have reduced the fiduciary issue (choosing a moment when gold was flowing in) by the necessary amount.

17. It is in my opinion highly probable that the embarrassing accumulation of what are euphemistically termed liquid funds, but which I should prefer to call surplus credit, which has been a characteristic feature of recent years has been to a large measure due to the attempt to retain a larger stock of gold than is required for the working of the currency system on the lines of the actual fiduciary issue from time to time—since 1928, £260,000,000.

An outflow of gold arises from one or more of the following three causes, an unduly high internal price level, an excess of foreign lending or a withdrawal of foreign balances. It may stemmed by a return of foreign balances, a withdrawal of money lent abroad* (or sale of securities having an international market) or an alteration in the relative volume of exports and imports, or a fall in internal prices. A rise in bank rate will tend to bring the first two corrective forces into operation more quickly than the last, but if the outflow of gold has caused a reduction of the basis of credit the return of foreign balances and withdrawal of money lent abroad will not increase it again unless and until they actually cause gold to flow in. If such an inflow begins before the price level has been adjusted the maintenance of a high bank rate can do nothing but mischief. The rate should be lowered to the point necessary to check the inflow and leave the reduction in the basis of credit to have its effect on the price level.

But if an attempt is made to maintain the actual stock of gold above the figure which represents saturation point on the basis of the actual amount of the fiduciary issue, it means that equilibrium of the exchanges will be produced by the attraction of foreign balances by means of a high bank rate with a volume of credit and currency too large to bring about the necessary adjustment of price level. If it be desired to retain the surplus gold, these balances must either be retained by the continuance of a high bank rate, or brought back by another rise, if a lowering of the bank rate has caused their withdrawal and a consequent renewal of the gold drain.

Thus the high bank rate becomes chronic and so far from doing any good merely makes matters worse, since by depressing industry it diminishes production and by releasing credit from industry increases the amount of short money, whereas, if the gold had been allowed to go and the basis of credit had been restricted in the first instance, remedial forces would have been put into operation with which no subsequent movement of balances could have interfered.

Indeed we owe the creditor position which we occupy in the world more than to anything else to our willingness in the old days to part with gold freely whenever the exchanges required it and

* i.e. British liquid funds in foreign centres or foreign bills held in London (which a bank rate higher than that of foreign centres drives to the centres having a lower rate). Long-date loans cannot, of course, be withdrawn.

to defer raising the bank rate until the depletion of the reserve in the Banking Department of the Bank of England made it necessary to do so. This kept our internal prices almost continuously down to the level necessary to secure a favourable balance on the international exchange of goods and services, which was largely absorbed by foreign investment before it could lead to an excessive gold influx.

18. The fact that this creditor position exists is not without danger, since it is obvious that it makes it possible for us to dispense with the favourable balance on goods and services so long as the deficiency can be made up by an excess of interest on existing foreign investments over new foreign investment and indeed longer if we are prepared not to increase or even to diminish the corpus of our foreign investments themselves.

But a diminution of new foreign investment will probably contract the volume of our exports and so reduce our visible exports, while the weakening of our creditor position will reduce our remuneration for international services which is a very important part of our invisible exports. Any temporary relief therefore that we might secure in this way would be at the cost of a progressive future decline.

19. But, quite apart from the undue accumulation of short money which results from attempting to deal by means of bank rate alone with a situation for which the proper remedy is an efflux of gold, the volume of such money generally since the War has been of such magnitude as to render the task of the Bank of England in controlling the supply (as distinct from the price) of the basis of credit extremely difficult. The main cause of this has been the enormous amount of Treasury bills. This has resulted not only in increasing the dimensions of the bill market (and so making larger scale operations necessary to produce a given effect) but also in altering its character. When the holdings of the market were mainly commercial bills drawn on London on foreign account, a rise in bank rate diminished the supply of these bills. Now that the market holdings are largely Treasury bills and other Government "floaters," a restriction in the volume of bankers' cash, followed by a reduction of their market money, merely drives the "market" "into the Bank," i.e., forces the Bank of England to recreate the credit it has previously withdrawn—the discomfort traditionally associated with that lodging being largely mitigated by the fact that the general taxpayer bears a large part—sometimes more than the whole—of the expense in the form of a higher discount rate when the bills fall due for renewal.

20. Apart from the difficulty which it creates in the control of the volume of credit by the Bank of England, the excessive volume of Treasury bills has harmful effects of a more general character. When credit has to be restricted the renewal of the bills comes

into direct competition with the demands of industry, tending to force up the rates which industry has to pay for accommodation. Further it encourages both directly and indirectly the accumulation of liquid funds by industrial concerns. Treasury bills not only provide a convenient and profitable vehicle for the employment of such funds, but they enable the banks to hold large fixed deposits at comparatively high rates of interest without risk to themselves.

The result has been that large and wealthy concerns to a much greater extent than formerly carry on their business by means of accumulated funds instead of with borrowed money. The consequence of this is that the pressure of credit restriction, when it becomes necessary, is rendered very unequal in its incidence. These large concerns are in no way hampered by a rise in short money rates—indeed they actually profit by it—and the whole burden is thrown on the weaker concerns which trade with borrowed money. In so far as the latter may be compelled to curtail their activities, the former can expand to fill the gap without cost to their profit and loss account for interest charges, since the loss of interest on the liquid funds so employed will be offset by the higher rate on the remainder.

21. It thus follows that the first result of an attempt to restrict credit is merely to transfer business from the weaker to the stronger concerns, and before an impression can be made on the total volume of active purchasing power the pressure on the weaker concerns may become so acute as to drive them out of business altogether. We might reach a state of affairs in which the whole of the trade and industry of the country would be carried on on the basis of credit balances against which the banks would hold cash, Treasury bills and securities only. High money rates would then be powerless to check expansion unless and until a point was reached at which it would be more profitable to the industrial concerns to keep their balances on deposit than to employ them in industry, or prices had risen so high that they not only had to employ the whole of them but borrow as well.

The former situation would be an impossible one for the banks except in so far as the deposits to be immobilized did not exceed their own short-date assets—otherwise they would lose money heavily, while the latter would not arise until inflation had gone far enough to disorganise the whole financial structure.

The truth is that any considerable volume of idle deposits representing dormant purchasing power which can at any moment become active purchasing power, not merely without the help but even in the teeth of the opposition of the banking system, is a menace to the system itself. So long as the volume of such deposits is small in proportion to bank advances, the banks can, by bringing pressure to bear on debtors, counteract the increased activity of

creditors, but a point may be reached at which this is no longer possible and then the whole machine breaks down.

22. It is very desirable—it may even in the not remote future become vitally necessary—that idle deposits in the joint stock banks should be reduced to a minimum and that the total deposits of these banks should be confined, as far as possible, to the necessary circulating medium of trade and industry.

The best methods of bringing this about are :—

(1) Reduction in the volume of Treasury bills, thus diminishing the field for the profitable employment of liquid resources generally.

(2) Working the gold standard in such a way that when a rise in the bank rate becomes necessary the period of the high rate shall be of brief duration, and for the rest keeping short money rates as low as possible (see above).

(3) Avoiding any action which will tend artificially to inflate the prices of long-date securities and so diminish their relative attractiveness as an investment for reserves.

23. I am aware that Treasury bills are a source of considerable profit both to the banks and the market and play so large a part in their daily life that they can scarcely picture—at any rate are unable to contemplate with equanimity—a world without them. But the Sabbath was made for man not man for the Sabbath, and if it is desirable, as I believe it is, in the interests of the financial system as a whole, that the amount should be drastically curtailed, the banks and the market must adapt themselves.

Inland trade bills (the revival of which would be very healthy for trade and industry themselves) might with advantage fill up a part of the gap.

24. It would be well also that the volume of inactive deposits in the joint stock banks should be reduced by the sale by the banks of long-date securities to their customers. The improvement of their cash proportion would enable them when occasion arises to increase their active deposits by purchase of inland bills and by advances to trade and industry. When there was a large number of banks whose advances were largely confined to particular localities and particular trades, a reserve of high-class readily marketable securities as a second line of defence was essential and an "over-lent" position was rightly regarded as evidence of weakness. This is still the case in regard to the surviving smaller banks and might be the case in regard to the big banks if they pursued sufficiently different policies to cause large cash transfers from one to another, but so long as they "keep in step" and confine their advances to proper banking propositions (covering any which become "frozen" by creating reserves) there is now no real necessity for maintaining a large volume of investments.

25. It is a mistake to suppose that, during the period from the restoration of the gold standard until the beginning of the world slump, trade and industry in Great Britain were uniformly or even generally unprofitable. The Income Tax returns, indeed, are conclusive evidence to the contrary. Generally speaking, apart from the export industries and industries (including agriculture) directly exposed to foreign competition in the home market profits were above the normal, and this notwithstanding the burden of taxation, unemployment and high money rates. This to my mind proves that the trouble was due not to a shortage but to an excess of currency and credit which had the effect of raising prices wherever prices could be raised and raising costs generally, including those in the export industries and industries in which prices could not rise because of foreign competition. The effect of "safeguarding" in certain of the latter industries was to extend to them the advantages of the naturally "sheltered" industries and increase the pressure on the remainder. In these conditions—I am dealing with the period prior to the world slump—a diminution of internal purchasing power resulting in a fall in the domestic price level would have been far from being the unmixed evil which some of my colleagues appear to imagine. A comparatively small fall in prices would have encouraged the export trades and diminished the pressure of foreign competition in the home market on those industries which are exposed to it. Even assuming the rigidity of money wages, which is by no means absolute, some costs would have fallen and more certain markets and increased output at the lower price level might have compensated largely for the lower prices themselves. To the sheltered and protected industries on the other hand and to the distributing trades, reduced purchasing power in the hands of the public would have meant diminished sales, with the result that they would have cut prices (as they could well afford to do) in the hope of recovering their turnover. The result would have been a much healthier distribution of profits as between sheltered and unsheltered trades, and a diminution in the cost of living greater than the fall in prices in the unsheltered trades. This would have paved the way to a reduction of money wages without diminution—possibly even with increase—of real wages in these trades and in the transport services. The latter, if it could have been effected, would have reduced the cost of living still further and given further help to the export trades.

26. It is possible that these desirable changes may still come about without deliberate restriction of credit if recovery from the world slump proceeds more slowly in this country than abroad—a not improbable event, regard being had to the fact that our disequilibrium before the slump began was more pronounced than that of most foreign countries. A rise in world prices with domestic prices remaining stationary, or following only slowly,

would have the same effect as a fall in domestic prices not reflected in world prices and would avoid a large part of the friction inseparable from the latter process.

But this hope will be disappointed if the price level is prematurely raised by well-meant but ill-advised measures directed to accelerating trade recovery.

27. In the case of a country situated as we are, a recovery to be durable must begin with the export trade. This will give a firm foundation for expansion of the home trade. Attempts to revive the home trade while the export trade remains unprofitable will, if successful, merely re-establish the old disequilibrium.

28. Another cause of trouble has been the excess of long-term foreign investment over what was available from the balance of international payments. This became possible without loss of gold by reason of the inflow of foreign short money but it made necessary the stereotyping of high money rates to retain that short money. The effect of continuously high rates for short money was to increase the attractiveness of short as compared with long-date investment at home. This should have been counteracted by a fall in the price and improvement in the yield of long-date securities but the excessive amount of unemployed bank deposits, and probably to some extent the necessary preoccupation of the Treasury and the Bank of England to secure the most favourable terms for funding maturing obligations and to pave the way for a conversion of the 5 per cent. War Loan, inhibited this tendency, thus increasing the relative attractiveness of the high rates offered by foreign long-term borrowers.

Governments can, and do, do much—sometimes salutarily but more usually with mischievous consequences—to interfere with the free play of economic forces but no Government has yet succeeded, though many have tried, to prevent capital finding its way to a more attractive market. Measures designed for that purpose are as effective as the fabled enterprise of building a wall round a swallow in order to enjoy the blessings of perpetual spring.

In the old days the British investor was content with a much lower return on home than on foreign investments by reason of his conviction that the former gave him better security. This was an enormous advantage to British industry. More lately the preference has been less marked. Recent and prospective events rather tend to show that after all Great Britain may not compare unfavourably with the rest of the world for political and economic stability and the old preference may revive. But be that as it may, excessive foreign investment and consequent trouble with the exchanges can only be checked by a fall in price of home securities to whatever may be in fact the competitive level.

29. It is in my view of great importance that the present opportunity created by the prevailing distrust of foreign investment,

cheap money and absence of industrial competition which have restored the market in home gilt-edged securities to favour should be taken advantage of first to fund a convertible proportion of the Treasury bills (other than those held by the Bank of England and public departments) and other Government debt of England maturity and to effect, if possible, a conversion of the 5 per cent War Loan, and that thereafter home securities should be allowed to find their natural level.

30. It will be seen, therefore, that so far as the relation to currency and credit is concerned I would, I believe, remove the removal of obstacles which have arisen to the operation of the existing system and have no confidence that to result from a radical change in the system itself.

The steps which I have suggested for removing such obstacles would, I believe, restore to our financial system the ability to perform its proper function—that of honest broker between nations who have real values to exchange at home or abroad. To expect more of it is to fall into the ancient fallacy of mistaking money for wealth.

The existing system thus restored to efficient working would resume its old role of an efficient policeman to prevent our buying from abroad more than we can afford.

The proposed system gives no such safeguard and requires the creation of elaborate machinery for securing the maintenance of a proper balance of international payments.

As to the nature of that machinery the Report is silent, but I understand that various members will have diverse and possibly conflicting panaceas to present in addenda. Until light shines upon this chaos it seems imprudent to proceed further with the creation of the new world.

31. The Report contains proposals relating to International Monetary Policy of a Permanent Character, proposals relating to International Monetary Policy to meet the present emergency and proposals relating to Domestic Monetary Policy of a Permanent Character, but there are no proposals relating to Domestic Monetary Policy to meet the present emergency.

Here again alternative suggestions will, I believe, appear in addenda.

Expedients which have been much canvassed—not necessarily as alternatives—are intensive capital development and attempts to stimulate agriculture and the industries whose products are subject to foreign competition in the home market by import duties.

32. The latter seems to me to be merely enlarging the list of sheltered trades at the expense of the export trades while, if these are compensated by bounties, we may find ourselves subsidizing the

ish goods at the expense of the British
 imports—a net loss to the national economy
 foreigners* to buy
 consumer of for
 whole. As intensive capital development any suggestion
 stimulated by credit inflation regardless of the
 27. that his cessful are likely to create a situation which can
 dura' real ex- with by wide-spread liquidation, followed by still
 four' ex- pression. Further, it is doubtful whether the infla-
 th' only ers' cash would have any early result other than to
 if more purchase of securities by the banks from their
 tic, thus increasing their idle deposits with the danger of
 § an unmanageable credit situation when a real revival

in this connection it must be realised that only current savings
 available for capital expenditure. Past savings in the form of
 bank deposits can, it is true, be so employed by their owners,
 but, if and when they are so used, the use of them, unless credit in
 general is restricted *pro tanto*, will have the same effect on the
 price level as the creation of an equal amount of new credit.

The same considerations apply to works undertaken by the State
 or Municipalities out of the proceeds of state or municipal loans
 and to works financed under state guarantee, unless real savings
 are available, with the further objection, even when this condition
 is satisfied, that unless the works are sufficiently income-producing
 to cover the loan charges their effect is to increase the burden of
 dead-weight debt which is already crushing industry.

If there were substantial reason to hope that works of this
 character would permanently reduce unemployment and so save
 an appreciable proportion of the present expenditure on relief, it
 would be worth incurring this latter risk, but I am not satisfied
 that real savings sufficient for any considerable effort on these
 lines are in fact available. Savings are hard to make in hard
 times. Unless they are available, it is not feasible to start a last-
 ing trade revival by intensive capital expenditure at home. The
 essence of such expenditure is that it does not create an imme-
 diately saleable product. The expenditure itself, however, is in

* This would not be the case if the effect of the tariff was to raise the
 general domestic price level by a percentage equal to that of the duties and
 bounties, but in that event the duties would cease to be protective and the
 bounties to be helpful. The only advantage of such a plan would be that it
 would *pro tanto* reduce the real burden of debt upon production. Apart from
 many other objections to it, it is questionable whether it would afford relief
 on a scale sufficient to compensate for the friction and loss which its operation
 would entail.

† I have not space for a critical examination of the doctrine of the new
 school of economists that the profits resulting from capital expenditure will
 themselves provide the savings to finance it. The cynical maxim "let us eat
 and drink for to-morrow we die" has at least the common-sense to recognise
 by implication that difficulties may arise from the policy if death fails to ensue.

the main, through wages, upon articles of consumption and through materials, upon other immediately saleable produce of which are available for export. It will stimulate production at a rising level of prices of the articles of consumption and materials, it will also encourage imports and diminish the industries immediately affected and increase costs of other industries. It will, in fact, have an inflationary effect with that resulting from the issue of forced currency.

34. Part II, Chapter IV.—I concur in the recommendations contained in this chapter in regard to the Capital Market and Investment.

35. To sum up, I am of opinion that the causes which impeded the development of trade and industry and led to increasing unemployment during recent years are in the main outside the domain of banking, finance and credit and that any reforms within the scope of the terms of reference of the Committee at best, merely touch the fringe of the real problems.

36. As regards the matters falling within the terms of reference my conclusions are as follows:—

(1) It is to the best interest of this country to continue to adhere to the international gold standard at the existing parity, but efforts should be made to secure by international agreement a better working of that standard.

(2) Our existing domestic currency system should be maintained, reform being directed to removing the obstacles which have interfered with its efficient working and not to fundamental alterations in the system itself.

(3) The banking system discharges adequately and efficiently its proper function of providing short-date credit. It is not advisable that its functions should be extended, but a closer touch with industry in certain respects would be advantageous.

(4) Better machinery than at present exists should be devised for providing domestic industry, through institutions other than the ordinary banks, with long-date credit and permanent capital.

(5) The best contribution which the State can make to assist industry and promote employment is strict economy in public expenditure and lightening the burden of debt by prudent financial administration. Attempts to give positive assistance by diverting international trade from its natural channels, the State-financing of enterprises other than the ordinary public services, or the artificial cheapening by State guarantees of the supply of capital to particular undertakings are more likely to retard than to accelerate the restoration of a healthy and progressive national economy.

BRADBURY.

APPENDICES—TABLE OF CONTENTS.

	Page.
Table 1.—London Clearing Banks : Analysis of Monthly Returns ...	284
Table 2.—Scottish Banks : Analysis of Monthly Returns	290
Table 3.—London Clearing Banks : Summary of Monthly Averages ...	296
Table 4.—London Clearing Banks : Index number of Monthly Averages	296
Table 5.—Scottish Banks : Summary of Monthly Averages	297
Table 6.—Scottish Banks : Index number of Monthly Averages ...	297
Table 7.—London Clearing Banks : Value of Cheques drawn on customers' accounts	298
Table 8.—London Clearing Banks and Scottish Banks : Classification of Advances	298
Table 9.—London Clearing Banks and Bank of England : Deposits, etc. on foreign account	299
Table 10.—Scottish Banks : Deposits, etc. on foreign account	300
Table 11.—Deposits and Sterling Bills held in London on foreign account and Sterling Bills accepted on foreign account	301
APPENDIX II.—Bank of England : Monthly averages of Weekly Account ...	302
APPENDIX III.—Future Monetary Demand for Gold	304
APPENDIX IV.—	
Table 1.—Balance of Payments : United Kingdom	305
Table 2.—New Overseas Issues on the London Market	305
Table 3.—Balance of Payments : United States	306
Table 4.—Net increase in External Investment of, and Foreign Capital Issues in, the United States	306
APPENDIX V.—Indices of Wholesale Prices in various countries	307
APPENDIX VI.—Statistics prepared by the staff of the Economic Advisory Council :	
Table 1.—Exports as a Percentage of Production	308
Table 2.—Real Wage and Productivity changes since 1924	309
Table 3.—Employment, Output per head, etc. 1924–1929	310
Table 4.—Earnings and Productivity in Certain Industries, 1907–1924 ...	312
Table 5.—Physical Volume of Output per head 1907 and 1924	314

APPENDIX I.

NOTES.

Table 1 gives an analysis of the main items of the monthly returns of the London Clearing Banks, commencing with January, 1919, in a form which differs from the published monthly returns principally in the following respects:—

(a) Cash in hand and Balance at the Bank of England are shown separately. (The cash items in the table do not include Balances with, and cheques in course of collection on, other banks in the United Kingdom.)

(b) Money at call and short notice is shown under the heads of (i) Money at Call, (ii) Money at short notice to the Money Market, and (iii) Money at short notice to the Stock Exchange.

(c) Treasury Bills discounted and Commercial Bills discounted are shown separately.

(d) Deposits are divided under the heads of (i) Current Accounts and (ii) Deposit Accounts. There is no universally recognised line of division between the two, but as far as possible current accounts are taken as sums payable on demand and deposit accounts as sums payable after date or notice.

(e) The head of Acceptances Outstanding does not include engagements for forward foreign exchange and other items frequently grouped under this head.

The statistics are the aggregates of the ten London Clearing Banks, but in the case of the National Bank figures relating to offices in England only have been included. For some items in the table in the early years estimated figures have been taken.

Table 2 gives the monthly figures of six Scottish banks on the same basis as is adopted in Table 1. The six banks are:—Bank of Scotland; British Linen Bank; Clydesdale Bank Limited; National Bank of Scotland Limited; Royal Bank of Scotland and Union Bank of Scotland Limited. In the case of one bank money at notice to the Stock Exchange is not distinguished; in another case money at call is included with money at short notice; and in another case the balance at the Bank of England is included in cash in hand and no money at short notice is given.

Tables 9 and 10. The figures of the London Clearing Banks comprise foreign deposits, etc., held by the principal London offices and offices in Liverpool, Manchester and Bradford. The figures of the Scottish Banks cover foreign deposits, &c. in London and, in some cases, at a principal office in Scotland. Deposits, Sterling Bills and Acceptances are each classified under the heads of—

(a) Banks with Head Offices abroad (including the Dominions).

(b) Foreign (including Dominion) Governments.

(c) Other foreign customers, including companies with head offices abroad.

It should be noted that under this classification, deposits, etc., held for, e.g., the Commonwealth Bank of Australia are included, while deposits, etc., held for, e.g., the Chartered Bank of India, Australia and China, and the Bank of Australasia, whose head offices are in London, are excluded. The figures do not in every case relate to the dates indicated in the tables but they are in all cases within a few days of those dates.

Table 11. This table combines the aggregate figures shown in Tables 9 and 10 with the aggregate figures of 30 Accepting Houses and Banks, compiled on the same basis. A further addition is the aggregate amount advanced to the Discount Market by Banks with head offices abroad and other foreign customers.

As indicated in the Report, the Table does not cover sterling bills held in their own portfolios by foreign institutions and agencies whether located in London or abroad. Nor does it cover acceptances by the Exchange Banks (with one or two exceptions).

TABLE 1.—ANALYSIS OF THE MONTHLY RETURNS OF THE LONDON CLEARING BANKS.
(£000 throughout.)

Date.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Discounted.	Commercial Bills Discounted.	Investments.	Advances (i.e., Loans and Overdrafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Acceptances outstanding.
				To the Money Market.	To the Stock Exchange.								
1919.													
January	107,848	90,284	26,610	105,895	14,653	225,159	91,786	822,373	475,828	983,891	442,822	1,426,653	43,989
February	104,360	81,167	24,605	102,930	14,473	197,941	90,258	823,168	482,818	930,776	452,098	1,382,874	48,992
March	105,400	92,205	23,762	103,723	14,075	183,605	93,176	827,564	506,873	951,639	457,036	1,408,675	47,323
April	113,069	85,146	26,806	112,227	14,022	197,076	91,270	828,352	508,436	962,437	472,138	1,434,575	45,156
May	110,545	88,923	24,730	112,068	15,512	213,196	92,173	829,957	510,751	970,640	483,720	1,454,860	43,733
June	117,150	246,041	23,025	132,744	15,200	132,403	89,542	828,846	527,597	1,113,248	518,815	1,627,063	52,550
July	113,141	117,323	22,377	90,419	17,492	110,631	100,821	872,302	593,248	1,011,942	492,864	1,504,806	62,007
August	112,131	81,647	23,125	86,723	17,117	137,036	105,521	875,834	614,943	1,009,039	500,003	1,509,042	67,327
September	111,883	81,720	19,457	83,739	17,416	135,662	107,591	877,595	652,020	1,032,210	503,622	1,535,832	68,910
October	114,964	76,074	22,215	84,700	24,334	149,264	141,142	872,280	659,381	1,040,471	529,290	1,569,761	65,247
November	113,989	74,660	16,054	83,204	25,351	137,943	145,537	875,590	692,749	1,068,108	535,349	1,603,457	83,339
December	124,654	131,016	21,963	92,979	22,732	90,900	133,359	880,143	730,957	1,121,580	556,236	1,676,816	108,442
Monthly Average	112,428	103,851	22,919	90,868	17,698	159,235	106,848	851,417	579,636	1,015,910	494,833	1,510,743	61,459
Monthly Average (excluding June and December).	110,733	86,915	22,974	90,469	17,444	168,751	105,927	850,801	569,708	995,609	486,894	1,482,503	57,652
1920.													
January	113,636	88,632	21,960	96,779	22,809	104,512	162,147	880,799	777,630	1,134,732	573,302	1,708,034	107,276
February	104,983	74,678	22,013	92,691	26,285	87,186	158,034	874,612	815,761	1,114,267	569,592	1,683,859	110,687
March	95,832	69,754	20,063	87,359	27,032	73,949	138,198	870,898	861,719	1,119,925	574,017	1,693,942	99,023
April	98,415	82,775	23,548	49,520	23,965	63,794	148,497	868,223	861,661	1,118,585	588,711	1,707,296	87,463
May	100,949	60,449	23,064	48,713	22,599	79,145	132,435	870,082	860,622	1,075,201	597,180	1,672,381	72,048
June	105,922	123,898	23,224	49,680	21,201	83,520	121,273	871,039	844,438	1,103,496	615,362	1,718,858	64,205
July	103,547	73,313	24,793	55,272	20,774	115,375	143,878	869,744	838,249	1,080,481	634,756	1,715,187	59,864
August	107,731	68,456	24,497	55,309	21,329	134,931	133,473	868,495	834,014	1,076,592	643,714	1,720,306	55,987
September	108,777	74,876	24,743	56,811	21,037	137,983	133,440	864,142	831,172	1,073,771	646,269	1,720,040	54,242
October	110,861	82,277	26,351	64,081	20,114	166,740	152,933	880,377	822,807	1,084,458	666,622	1,755,080	60,667
November	110,935	68,254	25,951	54,616	18,893	177,435	163,539	857,010	815,843	1,072,446	671,097	1,743,543	69,206
December	107,836	132,324	25,681	60,989	17,805	158,196	143,798	857,097	815,123	1,113,638	684,180	1,797,818	69,340
Monthly Average	103,769	83,723	23,324	54,310	21,937	115,556	144,221	867,713	831,590	1,097,623	622,067	1,719,695	75,784
Monthly Average (excluding June and December).	105,567	74,855	23,698	54,105	22,484	114,495	146,657	868,442	831,952	1,095,441	616,526	1,711,907	77,686

1921.														
January	...	112,234	92,648	24,829	52,910	19,123	184,194	170,840	352,615	810,027	1,100,387	693,902	1,794,289	58,330
February	...	108,651	84,620	20,217	49,287	18,205	168,998	150,758	352,155	822,805	1,044,455	697,361	1,741,816	47,414
March	...	109,643	73,785	21,063	47,415	19,277	148,697	125,225	348,792	844,458	1,003,154	691,576	1,694,730	42,503
April	...	113,203	89,827	26,860	52,207	18,107	147,480	135,346	346,071	823,170	989,958	708,019	1,697,977	89,923
May	...	113,768	86,012	23,235	56,026	20,229	184,248	131,666	345,706	807,637	996,197	718,927	1,715,124	39,500
June	...	110,557	112,896	29,342	55,671	18,959	222,620	130,083	344,056	795,743	1,029,494	735,353	1,764,847	39,675
July	...	111,850	89,548	31,557	60,218	17,572	252,725	136,470	343,026	789,977	1,024,802	744,298	1,768,898	34,091
August	...	112,745	94,153	28,131	56,334	16,430	257,218	125,348	337,861	776,514	1,006,247	737,660	1,743,907	29,553
September	...	112,421	84,436	30,840	57,411	16,779	277,198	126,186	345,149	767,683	1,013,963	740,593	1,754,556	29,400
October	...	108,689	105,550	31,790	58,168	15,789	283,992	124,205	354,467	759,649	1,036,908	756,864	1,793,772	34,208
November	...	108,959	104,832	29,923	51,215	16,673	287,549	121,859	354,493	748,807	1,006,729	758,739	1,765,468	41,378
December	...	106,204	132,490	28,996	61,104	19,016	279,756	130,830	361,478	735,518	1,044,977	763,078	1,808,055	39,944
Monthly Average	...	110,744	96,065	27,232	54,829	18,013	224,556	134,068	348,822	790,166	1,024,756	728,864	1,753,620	39,410
Monthly Average (excluding June and December).	...	111,216	90,741	26,844	54,117	17,818	219,230	134,790	348,032	795,073	1,022,260	724,794	1,747,054	39,630
1922.														
January	...	111,713	93,541	34,591	60,065	22,532	280,745	134,039	390,479	735,762	1,088,376	763,378	1,801,754	40,301
February	...	108,514	81,920	35,827	61,073	19,823	264,164	124,945	414,475	725,135	1,022,568	755,604	1,778,232	39,590
March	...	107,587	97,217	27,223	54,543	22,761	220,090	101,259	416,220	725,786	987,579	729,362	1,716,941	36,204
April	...	112,626	93,322	30,314	61,364	23,280	195,782	104,188	433,434	720,183	989,062	732,388	1,721,450	36,664
May	...	108,604	88,169	33,884	59,555	25,412	205,620	120,613	433,082	699,169	994,787	728,799	1,723,586	36,126
June	...	99,870	112,935	34,163	64,822	24,417	202,160	113,511	437,613	701,719	1,013,402	729,650	1,743,052	33,322
July	...	108,300	86,873	27,116	61,209	24,391	206,727	116,050	439,570	699,509	1,005,342	705,553	1,710,895	32,084
August	...	110,612	81,623	24,915	58,809	25,478	186,674	104,889	440,459	698,020	978,463	687,656	1,666,119	28,807
September	...	108,267	82,301	28,189	56,682	22,883	177,395	105,349	430,205	695,805	963,769	674,749	1,658,518	29,564
October	...	106,398	88,249	27,746	56,670	23,123	202,242	112,207	406,752	705,891	991,364	674,965	1,666,329	34,402
November	...	104,823	90,732	26,465	54,264	22,733	184,262	106,567	405,577	717,720	984,127	667,441	1,651,568	42,512
December	...	102,392	117,719	26,662	58,082	23,777	170,086	116,413	397,049	717,288	1,011,318	659,724	1,671,042	47,527
Monthly Average	...	107,475	92,883	29,675	58,827	23,384	207,996	113,336	420,576	711,832	998,346	709,111	1,707,457	36,475
Monthly Average (excluding June and December).	...	108,744	88,395	29,627	58,322	23,242	212,370	113,011	421,225	712,298	995,544	711,995	1,707,539	36,685

TABLE 1—continued.

Date.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Discounted.	Commercial Bills Discounted.	Investments.	Advances (i.e., Loans and Drafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Acceptances outstanding.
				To the Money Market.	To the Stock Exchange.								
1923.													
January	106,768	82,655	28,047	61,917	21,259	197,154	131,402	391,542	717,458	1,015,461	655,423	1,670,884	48,003
February	104,525	88,981	24,326	58,755	25,942	159,478	111,126	382,184	729,311	975,477	647,207	1,622,684	46,980
March	104,329	71,576	24,059	57,472	28,400	142,827	108,413	369,430	732,999	949,866	629,935	1,579,801	46,605
April	103,446	84,518	28,093	60,304	27,085	133,670	119,266	369,403	729,180	959,369	635,322	1,594,691	45,529
May	105,511	84,217	23,746	59,342	26,345	138,875	117,487	369,109	730,064	952,437	636,956	1,589,393	42,835
June	94,389	99,601	24,436	65,416	29,500	136,236	119,315	374,383	733,832	984,825	643,421	1,626,246	38,396
July	103,835	83,860	21,378	60,277	24,093	144,555	128,825	379,927	728,990	973,016	645,163	1,618,179	39,028
August	105,039	81,977	24,891	59,553	21,130	137,575	120,310	379,603	724,811	945,138	644,250	1,589,388	36,978
September	105,323	83,613	24,794	61,008	20,747	139,668	115,937	379,741	722,574	942,905	648,978	1,591,883	38,345
October	103,617	86,401	22,761	59,349	22,629	151,415	117,378	378,846	730,138	951,990	668,964	1,610,954	43,299
November	103,647	85,537	24,453	63,294	23,072	140,256	117,805	378,279	731,954	941,787	666,552	1,608,339	50,030
December	105,420	114,269	26,265	55,164	23,584	131,094	129,754	378,882	742,937	994,935	669,378	1,664,313	60,232
Monthly Average	103,821	87,267	24,771	60,154	24,482	146,084	119,751	377,611	729,504	965,600	648,504	1,614,105	44,688
Monthly Average (excluding June and December).	104,604	83,333	24,655	60,127	24,070	148,567	118,795	377,806	727,728	960,745	646,875	1,607,620	43,763
1924.													
January	106,545	81,403	23,299	58,990	19,926	143,529	141,818	389,347	743,718	974,752	677,313	1,652,065	66,314
February	102,984	90,733	20,117	52,734	19,203	116,230	123,180	384,175	754,545	937,049	670,061	1,607,110	61,642
March	101,970	78,810	25,943	54,522	21,705	96,512	113,056	378,077	771,585	933,768	655,978	1,589,746	56,969
April	104,928	85,226	25,339	52,621	25,075	96,329	115,183	374,957	771,812	940,094	660,071	1,600,165	54,450
May	103,032	86,237	24,449	54,596	26,625	93,758	135,234	367,737	772,320	940,760	661,367	1,602,127	52,411
June	100,003	108,489	27,629	55,992	22,698	102,385	126,754	364,514	778,156	980,138	667,311	1,647,449	47,146
July	102,934	82,622	22,497	55,680	21,649	102,911	131,523	364,899	775,394	954,827	667,019	1,621,846	45,163
August	105,095	79,465	23,557	56,631	21,784	103,249	120,683	363,374	772,765	931,671	662,121	1,593,792	42,158
September	103,514	77,824	25,696	55,674	22,732	99,491	121,301	356,899	777,954	944,795	669,481	1,604,276	44,064
October	102,509	83,563	24,744	57,984	22,748	107,647	123,550	351,379	786,891	943,471	665,731	1,609,202	50,691
November	103,630	90,516	23,507	56,771	26,651	100,942	121,708	343,553	790,428	935,610	670,847	1,606,457	62,052
December	108,064	114,430	25,061	63,792	23,492	88,228	132,115	337,517	794,807	983,440	671,268	1,664,728	70,907
Monthly Average	103,767	88,276	24,570	57,166	22,791	104,766	125,509	364,702	774,198	950,031	665,716	1,615,747	54,498
Monthly Average (excluding June and December).	103,714	83,640	24,215	56,620	22,230	106,660	124,724	367,440	771,741	943,680	664,999	1,606,679	53,592

1925.													
January	106,807	79,027	23,299	60,872	31,809	103,622	143,002	331,501	798,529	955,483	668,741	1,624,224	78,932
February	105,275	82,828	24,714	66,562	31,550	91,935	130,958	324,710	806,186	933,978	678,120	1,612,098	71,456
March	103,818	75,216	25,223	62,178	31,878	72,726	120,563	319,889	827,876	922,484	662,204	1,584,688	67,106
April	102,500	84,779	23,722	69,026	29,960	65,839	127,451	314,821	829,923	906,292	681,734	1,588,026	68,890
May	104,204	82,853	23,180	66,165	28,465	69,962	119,174	310,184	823,785	885,173	687,689	1,572,862	56,951
June	102,337	106,573	24,650	81,286	31,098	81,642	110,887	303,509	835,616	936,100	687,983	1,623,083	50,333
July	103,769	77,068	27,114	67,065	28,292	106,228	126,146	295,083	833,141	916,570	691,134	1,607,704	47,336
August	105,426	77,794	26,724	65,149	29,049	106,155	121,531	292,019	819,496	903,865	683,333	1,587,196	47,508
September	105,368	82,271	25,043	65,101	27,812	108,296	129,301	291,238	814,844	910,845	684,969	1,595,314	50,911
October	105,480	82,775	24,242	60,493	30,807	107,255	135,601	294,030	815,981	920,072	681,150	1,601,222	56,315
November	101,852	87,479	22,743	57,259	30,964	97,271	139,962	294,495	814,916	918,858	678,315	1,597,173	66,573
December	97,183	115,611	26,904	62,136	35,357	80,572	126,709	293,556	834,507	961,726	676,571	1,638,297	68,686
Monthly Average	108,662	86,189	24,797	61,108	30,570	90,959	127,607	305,419	821,650	922,537	680,162	1,602,699	60,500
Monthly Average (excluding June and December).	104,448	81,209	24,800	60,987	30,039	92,929	129,369	306,797	818,968	917,362	679,739	1,597,101	60,698
1926.													
January	104,959	76,817	24,997	58,886	32,488	102,179	129,600	293,775	838,441	934,248	672,113	1,606,361	67,874
February	105,227	82,165	26,505	67,138	31,243	77,574	122,535	286,664	844,081	909,157	674,576	1,583,733	62,724
March	103,718	77,843	22,969	57,412	31,722	66,903	114,185	282,645	855,874	899,162	665,974	1,565,136	58,485
April	104,005	78,533	28,019	60,476	30,340	76,733	113,643	279,777	851,801	894,923	674,818	1,569,741	55,419
May	103,697	81,797	24,116	57,446	30,826	73,695	111,211	278,931	852,128	895,607	670,765	1,566,372	51,156
June	102,848	106,025	25,420	63,163	31,101	95,656	104,959	279,098	861,587	942,692	685,008	1,627,700	46,949
July	100,089	80,434	25,545	72,512	31,928	119,583	113,778	282,114	852,639	931,346	688,923	1,620,269	44,240
August	102,249	87,672	23,471	64,148	30,705	123,003	100,385	282,847	865,991	921,670	691,437	1,613,107	43,177
September	104,920	83,057	23,012	68,294	29,598	117,521	90,731	284,663	861,541	909,388	693,806	1,603,194	43,445
October	105,298	78,957	24,904	69,042	33,434	124,479	95,169	288,157	865,381	929,269	700,335	1,629,604	47,662
November	104,301	79,872	23,164	66,283	34,617	117,949	102,354	288,025	869,772	920,290	710,973	1,631,274	51,903
December	96,154	119,743	27,400	62,989	36,949	115,985	95,033	286,771	887,253	969,141	720,861	1,690,002	51,779
Monthly Average	103,072	86,076	24,960	63,149	32,079	100,938	107,799	284,456	858,039	921,408	687,466	1,608,874	52,068
Monthly Average (excluding June and December).	103,786	80,715	24,670	63,164	31,690	99,962	109,359	284,760	854,763	914,507	684,372	1,598,879	52,608

TABLE 1—continued.

Date.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Discounted.	Commercial Bills Discounted.	Investments.	Advances (i.e., Loans and Overdrafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Acceptances outstanding.
				To the Money Market.	To the Stock Exchange.								
1927.													
January	104,290	80,876	26,772	68,534	84,781	135,612	100,948	284,527	885,006	937,493	725,165	1,662,658	51,656
February	104,663	83,106	23,730	64,224	83,901	121,882	93,226	276,155	885,889	905,844	723,529	1,628,873	49,271
March	104,435	74,416	23,942	68,516	86,440	101,498	88,057	273,933	897,612	896,734	715,488	1,612,222	51,561
April	108,219	83,459	26,139	69,558	87,076	97,337	97,737	270,686	892,828	904,421	722,208	1,626,629	51,994
May	106,119	81,558	22,292	66,345	40,256	87,911	106,727	270,886	896,992	908,214	720,139	1,628,353	50,890
June	105,440	109,807	23,750	78,857	41,380	93,480	96,219	270,045	909,375	961,504	727,871	1,689,375	48,649
July	103,225	82,523	25,838	71,420	89,269	112,059	105,869	272,568	902,081	937,944	715,622	1,653,566	46,987
August	105,302	75,737	26,445	85,944	39,113	105,201	97,247	270,794	901,808	929,824	719,444	1,649,268	44,776
September	109,323	77,239	24,920	76,531	40,472	113,938	94,564	268,972	909,141	933,532	721,136	1,654,668	44,699
October	107,584	76,638	25,784	81,897	43,286	134,127	100,102	272,946	901,479	953,543	732,795	1,686,338	47,468
November	107,510	71,908	23,623	87,695	41,580	129,732	99,355	270,302	900,643	933,548	742,439	1,675,987	52,775
December	94,982	128,865	29,821	84,712	47,026	117,828	100,996	268,806	907,459	983,379	752,018	1,735,397	53,140
Monthly Average	105,091	85,344	25,238	75,853	89,548	112,550	98,421	272,552	899,193	932,123	726,488	1,658,611	49,464
Monthly Average (excluding June and December).	106,067	78,746	24,928	74,066	88,617	113,930	98,883	273,177	897,348	924,060	723,796	1,647,856	49,178
1928.													
January	107,182	77,424	28,460	79,965	45,064	127,438	117,976	279,099	913,533	967,014	748,890	1,715,904	54,268
February	105,189	70,628	29,783	77,136	47,456	100,226	108,339	280,982	909,633	929,551	738,129	1,667,680	57,625
March	105,719	70,606	30,352	76,612	50,879	80,549	101,310	273,054	922,710	920,241	729,094	1,649,336	60,286
April	103,340	71,977	28,705	81,376	51,955	85,961	109,613	271,260	911,217	930,999	733,817	1,666,815	60,204
May	103,224	79,957	27,231	78,754	49,221	76,072	115,384	271,072	922,164	927,921	736,316	1,664,237	60,864
June	93,961	106,381	28,267	74,219	48,232	100,322	122,530	266,147	927,580	977,336	753,297	1,730,538	62,507
July	100,847	82,667	28,366	81,945	44,111	121,410	139,319	271,427	922,515	968,978	759,963	1,728,941	65,743
August	102,742	81,682	27,522	78,224	42,484	130,903	125,168	273,978	922,997	943,901	762,893	1,708,594	67,758
September	107,286	77,630	27,376	76,498	45,858	121,872	117,775	280,766	919,214	945,522	762,710	1,708,232	66,925
October	106,258	86,002	25,781	78,039	50,154	118,211	116,562	279,040	927,206	958,064	768,465	1,726,529	68,976
November	108,328	80,202	25,140	74,287	49,410	120,466	124,677	277,155	930,466	949,223	777,950	1,727,178	75,855
December	109,411	118,267	34,071	77,190	50,583	118,670	124,948	281,030	943,414	1,026,169	789,038	1,815,227	83,346
Monthly Average	104,457	83,618	28,421	77,667	47,951	107,717	118,208	275,334	923,553	953,745	755,197	1,708,942	65,321
Monthly Average (excluding June and December).	105,011	77,877	27,872	78,084	47,659	107,311	117,072	275,683	921,164	944,141	752,003	1,696,144	68,800

1929.															
January	...	...	108,174	81,149	27,019	75,997	46,989	192,514	137,352	280,727	947,528	988,835	786,771	1,775,606	86,463
February	...	...	103,398	80,629	26,652	66,862	45,202	112,247	135,077	278,054	965,716	948,079	796,468	1,744,547	85,684
March	...	...	102,755	83,056	23,807	65,746	45,178	76,385	124,225	276,449	968,910	930,103	781,666	1,711,769	81,214
April	...	...	102,932	70,157	27,722	80,209	45,909	74,399	121,447	277,758	970,056	932,304	785,036	1,717,340	78,101
May	...	...	106,747	78,407	30,906	72,264	47,436	75,929	121,801	276,684	961,248	918,171	790,218	1,708,389	78,367
June	...	...	91,515	107,869	28,452	67,754	47,434	90,688	118,257	275,527	978,888	970,437	795,228	1,765,665	74,534
July	...	...	103,847	80,020	26,402	78,258	46,724	105,336	126,275	273,864	978,328	954,705	794,690	1,749,595	68,917
August	...	...	106,018	72,417	26,725	81,293	43,249	100,881	122,352	273,910	966,959	926,649	797,914	1,724,563	64,540
September	...	...	106,678	65,542	32,233	81,253	44,577	106,381	117,690	278,578	960,163	931,210	798,475	1,729,685	64,723
October	...	...	105,554	76,428	31,836	88,705	39,550	109,272	113,994	274,343	953,270	920,636	814,037	1,734,673	65,939
November	...	...	104,567	81,536	31,403	75,602	35,741	107,852	119,957	266,765	959,406	903,136	818,755	1,721,891	67,632
December	...	...	110,087	117,508	34,309	83,042	32,528	87,759	116,788	267,433	962,243	957,680	815,106	1,772,786	66,619
Monthly Average	...	...	104,856	82,893	28,906	75,990	43,376	98,304	122,851	275,008	963,976	940,162	797,880	1,738,042	73,561
Monthly Average (excluding June and December).	...	...	105,067	76,934	28,411	76,109	44,055	100,120	123,917	275,713	962,658	935,383	796,423	1,731,806	74,158
1930.															
January	...	...	106,973	75,506	40,572	78,007	31,718	111,972	124,952	269,592	955,561	918,472	814,292	1,732,764	64,668
February	...	...	104,491	71,866	32,693	70,160	31,579	90,194	113,425	266,063	960,004	875,693	802,598	1,678,291	64,410
March	...	...	102,407	67,524	30,468	75,836	34,452	83,134	97,392	262,043	961,090	876,706	780,591	1,657,297	64,446
April	...	...	105,449	74,884	32,431	75,620	33,445	89,104	131,487	265,221	948,701	901,143	797,415	1,698,558	66,699
May	...	...	102,366	82,045	29,957	72,351	35,943	97,140	152,177	269,452	939,731	897,459	819,690	1,717,049	64,532
June	...	...	96,791	108,140	30,015	79,560	32,369	111,841	140,754	270,539	954,123	954,363	826,899	1,781,262	59,308
July	...	...	103,536	83,147	32,025	90,974	27,189	138,456	137,754	281,062	934,432	936,320	828,181	1,764,501	55,190
August	...	...	105,113	79,710	31,583	83,203	23,262	139,346	132,941	290,657	918,659	915,825	821,343	1,787,168	52,148
September	...	...	103,414	76,335	33,215	82,576	23,541	155,563	123,931	294,243	913,071	927,942	820,921	1,748,863	50,868
October	...	...	103,850	84,789	35,045	90,184	22,230	164,476	125,029	298,697	906,498	928,760	837,817	1,766,577	50,381
November	...	...	101,199	87,812	30,872	83,208	22,463	180,642	127,172	302,143	904,857	924,903	844,126	1,769,029	61,362
December	...	...	107,017	122,663	38,324	79,171	23,522	181,839	119,359	308,431	904,652	991,821	846,603	1,838,424	61,764
Monthly Average	...	...	103,551	84,535	33,078	80,071	28,476	128,642	127,198	281,529	933,432	920,784	820,031	1,740,815	57,960
Monthly Average (excluding June and December).	...	...	103,880	78,362	32,860	80,212	28,582	125,003	126,626	279,937	934,240	910,322	816,687	1,727,010	58,469
1931.															
January	...	...	102,705	84,222	37,478	86,947	22,042	197,082	121,849	326,290	891,948	961,984	842,105	1,804,089	50,222
February	...	...	101,737	82,876	29,966	62,272	19,813	166,999	112,183	333,696	899,586	912,728	829,561	1,742,289	49,366
March	...	...	99,842	63,388	25,231	67,836	22,259	128,780	95,363	334,554	915,355	895,201	798,040	1,693,241	47,407

TABLE 2.—ANALYSIS OF THE MONTHLY RETURNS OF SIX SCOTTISH BANKS.*
(£000 throughout).

Date.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Discounted.	Commercial Bills Discounted.	Investments.	Advances (i.e., Loans and Overdrafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Acceptances outstanding.
				To the Money Market.	To the Stock Exchange.								
1919.													
January	10,298	2,872	1,556	3,112	274	29,116	2,991	34,518	21,590	30,791	54,346	85,137	2,187
February	9,808	2,766	150	1,937	270	22,661	3,175	35,273	22,999	26,858	54,067	80,925	2,089
March	10,015	2,740	425	3,125	271	20,539	3,360	35,366	23,612	25,930	54,700	80,630	2,155
April	10,680	2,569	1,618	4,980	276	23,844	2,811	35,823	23,353	27,648	57,250	84,898	2,204
May	11,095	2,015	305	2,152	255	26,095	3,256	35,235	24,201	27,944	57,468	85,352	1,999
June	11,234	2,052	375	2,407	190	21,603	3,464	36,335	25,581	30,835	59,628	90,463	2,280
July	11,396	2,048	1,328	9,074	195	12,017	3,607	40,791	28,777	31,832	58,977	90,809	2,460
August	10,862	2,217	330	4,105	187	9,124	4,073	43,297	29,435	28,197	60,016	88,213	2,443
September	10,634	1,903	340	3,349	193	13,571	3,601	43,144	30,232	27,742	62,160	89,992	2,338
October	11,012	1,520	1,804	4,884	195	17,594	3,817	42,915	29,281	28,745	62,806	91,551	2,449
November	11,167	561	345	3,075	159	19,324	4,564	42,858	30,001	29,021	64,145	93,166	2,976
December	11,258	559	215	2,938	143	19,968	4,755	42,854	31,597	28,632	66,361	94,993	3,266
Monthly Average	10,786	1,985	732	3,761	217	19,621	3,623	38,992	26,797	28,681	59,322	88,003	2,400
Monthly Average (excluding June and December).	10,694	2,121	820	3,979	227	19,383	3,526	38,872	26,438	28,471	58,587	87,058	2,325
1920.													
January	11,074	432	993	4,205	126	20,747	5,551	42,925	31,544	27,999	66,242	94,241	3,214
February	10,791	424	1,576	4,045	107	17,946	5,547	40,377	34,829	27,025	66,021	93,046	2,852
March	14,549	587	1,394	7,511	493	16,152	8,365	53,437	53,795	44,568	87,675	132,243	3,023
April	15,097	1,110	2,292	8,504	439	15,035	8,970	53,233	52,712	45,150	89,065	134,215	3,137
May	19,729	1,213	2,718	10,001	794	21,900	13,404	64,896	65,567	58,959	110,302	167,261	3,386
June	20,089	928	2,330	9,534	757	23,470	14,548	64,409	68,644	54,931	113,690	168,621	3,642
July	20,308	948	2,562	9,470	824	22,950	13,978	64,560	69,479	55,757	114,996	170,753	3,211
August	19,362	1,089	2,066	7,940	875	20,239	14,441	64,291	72,605	52,809	116,500	169,309	3,098
September	19,306	1,077	2,210	9,567	753	21,911	12,964	64,269	73,361	53,640	118,899	172,539	3,382
October	18,993	1,406	2,311	10,472	775	20,639	14,323	63,106	73,122	53,651	120,299	173,950	3,299
November	19,855	985	2,523	9,882	792	23,467	14,538	61,837	75,449	55,214	120,057	175,271	3,061
December	19,803	1,189	2,257	11,118	800	25,669	14,927	62,020	70,977	55,129	121,564	176,693	2,741
Monthly Average	17,412	954	2,144	8,621	631	20,844	11,796	58,280	61,840	48,569	103,776	152,345	3,176
Monthly Average (excluding June and December).	16,905	933	2,114	8,160	602	20,099	11,203	57,293	60,246	47,277	101,006	148,238	3,166

* Up to Feb., 1920, inclusive the figures cover three banks only. For March and April, 1920, they cover four banks. For May to Dec., 1920, inclusive they cover five banks, and from Jan., 1921, onwards they cover six banks.

10122

	1921.												
January	23,022	1,035	6,488	11,017	792	34,616	16,173	72,335	78,041	64,285	142,811	207,096	3,360
February	22,862	871	4,244	9,498	756	33,670	15,787	72,252	80,998	59,176	142,945	202,121	3,839
March	22,804	896	4,127	9,073	784	31,942	14,614	72,176	81,913	57,921	143,681	201,802	3,687
April	22,481	1,131	4,152	10,797	761	33,737	13,094	72,149	80,970	56,807	144,270	201,077	3,344
May	22,828	1,185	4,192	12,956	734	38,906	12,846	72,403	78,283	58,968	146,835	205,803	3,001
June	21,978	895	4,509	10,520	685	43,925	13,400	74,071	77,851	58,433	151,200	209,633	2,840
July	21,944	969	3,602	12,658	730	43,635	13,751	75,017	74,374	55,287	152,807	208,094	2,963
August	21,294	835	3,841	9,728	754	47,735	12,721	75,905	72,627	54,480	153,571	208,031	2,987
September	20,477	862	3,456	10,027	689	50,448	12,330	75,717	71,432	54,045	154,706	208,751	2,742
October	20,293	1,767	4,885	10,889	712	46,352	11,966	77,071	72,320	54,356	155,926	210,282	2,748
November	20,783	946	4,873	10,904	679	46,044	11,488	80,984	72,065	57,123	155,544	212,672	2,941
December	20,625	890	4,819	12,564	639	46,815	12,005	82,476	70,149	56,736	155,457	212,193	2,937
Monthly Average ...	21,783	1,025	4,432	10,866	726	41,480	13,348	75,213	75,919	57,300	149,979	207,280	3,116
Monthly Average (excluding June and December).	21,879	1,052	4,386	10,755	739	40,714	13,477	74,601	76,302	57,243	149,310	206,558	3,161
	1922.												
January	19,338	914	5,948	10,680	808	43,920	11,889	90,529	69,415	59,276	156,958	216,234	2,774
February	19,172	920	4,647	11,314	724	39,058	10,928	90,949	68,247	54,564	155,438	210,002	2,862
March	19,059	780	3,317	10,232	953	38,292	11,942	93,247	66,236	54,436	154,254	208,720	3,033
April	19,196	1,299	6,147	11,693	1,008	34,346	11,421	95,845	64,829	55,447	155,216	210,663	3,058
May	19,859	897	4,331	9,576	1,190	30,392	10,743	163,890	66,271	59,013	152,530	211,643	3,328
June	19,655	877	3,425	10,298	982	27,740	10,920	105,550	65,057	55,674	151,868	207,542	3,247
July	20,004	893	2,914	7,950	906	23,487	11,567	107,875	63,829	56,642	147,405	203,047	2,337
August	18,988	774	2,972	9,523	1,082	21,738	10,644	104,848	64,197	54,809	144,498	199,307	3,366
September	18,766	838	3,384	8,117	889	19,561	11,022	103,762	66,515	53,533	143,016	198,549	3,268
October	18,885	1,229	3,457	10,196	987	22,213	11,134	100,462	65,283	56,553	141,602	198,155	3,422
November	18,968	1,036	3,729	8,294	896	19,917	12,896	100,360	65,934	59,751	138,134	197,385	3,590
December	19,279	921	3,511	10,094	797	19,259	14,572	96,667	65,673	58,489	136,052	194,541	3,768
Monthly Average ...	19,262	948	3,982	9,831	931	28,329	11,640	99,498	65,957	56,432	148,083	204,516	3,170
Monthly Average (excluding June and December).	19,221	958	4,085	9,757	939	29,295	11,418	99,176	66,076	56,302	148,908	205,210	3,108

291

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TABLE 2—continued.

Date.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Discounted.	Com-mercial Bills Dis-counted.	Invest-ments.	Advances (i.e., Loans and Over-drafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Accept-ances out-standing.
				To the Money Market.	To the Stock Ex-change.								
1923.													
January	18,221	1,009	4,441	9,197	896	16,893	13,079	96,449	65,776	59,515	133,018	192,533	3,825
February	17,990	902	3,051	10,177	715	15,689	11,387	93,548	66,797	57,211	129,664	186,875	3,609
March	17,797	822	3,165	8,821	707	14,255	11,419	90,465	69,236	55,018	126,951	181,969	3,016
April	18,748	1,256	4,890	9,821	799	13,196	11,047	89,064	68,042	56,220	128,699	182,919	2,965
May	18,992	993	3,388	9,735	726	14,125	11,667	88,886	69,337	59,438	123,701	183,139	2,947
June	18,248	877	3,338	8,830	655	12,480	11,972	89,381	69,408	57,721	122,289	180,010	3,162
July	18,998	1,089	3,051	8,038	734	11,288	12,003	88,520	69,812	57,059	121,155	178,314	3,064
August	18,326	994	3,524	10,734	699	10,650	10,953	86,569	69,332	55,515	121,491	177,008	2,992
September	18,052	939	4,072	9,937	736	12,215	11,304	85,962	68,576	54,666	121,675	176,341	2,998
October	17,713	1,263	3,804	11,032	540	13,517	11,879	85,132	69,540	54,670	122,162	176,832	2,968
November	18,022	998	3,083	10,737	544	13,381	11,803	84,314	70,000	56,673	120,620	177,293	2,964
December	18,147	1,194	3,776	11,560	448	13,418	12,038	85,382	68,103	58,228	119,939	178,167	3,213
Monthly Average	18,354	1,032	3,632	9,843	693	13,424	11,713	88,473	68,663	56,828	124,114	180,942	3,151
Monthly Average (exclud- ing June and December).	18,266	1,021	3,647	9,773	710	13,521	11,654	88,691	68,645	56,598	124,714	181,312	3,133
1924.													
January	17,488	810	5,393	8,083	529	14,735	11,335	86,264	66,924	57,826	118,046	176,772	4,137
February	16,976	943	4,874	8,541	474	14,829	11,234	86,832	67,922	59,653	117,900	177,553	4,122
March	17,298	782	5,670	8,336	470	10,505	10,793	85,991	69,274	56,378	117,569	173,947	3,842
April	17,892	1,129	3,898	10,547	556	8,740	12,048	85,261	71,184	57,716	117,299	175,015	3,403
May	18,528	927	3,665	10,390	551	8,732	10,730	85,615	72,232	59,519	115,565	175,084	3,353
June	18,666	982	3,266	9,978	473	10,585	10,613	85,996	73,500	59,006	117,545	176,561	3,199
July	18,984	872	3,419	8,759	543	9,681	10,454	86,713	73,145	58,165	116,174	174,339	2,872
August	18,225	866	3,581	7,258	539	10,830	10,241	83,889	73,742	55,290	116,233	171,523	2,788
September	17,683	874	4,231	9,060	534	11,765	10,130	82,020	75,009	56,471	116,496	172,967	3,023
October	17,757	1,372	4,360	11,612	593	13,069	10,213	79,092	74,640	58,964	117,134	176,098	3,456
November	18,477	943	3,661	10,185	665	15,085	10,003	79,596	75,028	61,016	115,493	176,509	4,202
December	18,224	869	3,669	9,951	714	16,366	9,919	80,197	74,867	63,872	114,242	178,114	4,827
Monthly Average	18,011	947	4,124	9,391	553	12,077	10,643	83,955	72,288	58,656	116,716	175,373	3,560
Monthly Average (exclud- ing June and December).	17,925	953	4,255	9,277	545	11,797	10,718	84,127	71,910	58,100	116,881	174,981	3,470

10132	1925.																
	January	17,634	912	4,523	8,006	704	11,677	10,081	81,261	75,753	62,128	112,813	174,941	4,933			
	February	17,330	860	3,635	7,429	712	8,830	10,939	81,300	77,121	59,690	112,206	171,896	4,656			
	March	17,243	771	3,409	8,382	668	8,109	10,213	79,350	78,140	57,244	111,448	168,692	3,870			
	April	17,990	985	3,745	8,399	871	6,825	9,895	80,096	77,729	57,982	112,562	170,534	3,247			
	May	18,343	770	3,198	6,872	952	9,466	9,551	81,168	77,976	58,636	111,417	170,053	2,867			
	June	18,110	980	2,967	8,428	740	8,443	9,904	80,717	80,914	58,755	111,562	170,317	2,547			
	July	18,123	899	3,556	7,276	1,179	7,025	9,693	79,325	80,630	57,705	110,884	168,589	2,435			
	August	17,636	921	2,999	8,972	1,143	7,765	9,339	78,147	79,201	56,137	111,124	167,261	2,509			
	September	17,276	906	3,496	10,495	1,142	10,581	9,064	75,351	79,302	57,394	113,943	171,242	3,095			
	October	17,360	1,225	3,499	10,560	1,180	13,720	9,116	75,571	79,283	58,878	114,466	173,344	3,613			
	November	17,761	795	2,983	8,560	1,004	14,480	9,282	76,254	80,840	60,024	112,994	173,013	4,904			
	December	17,657	787	3,086	9,331	987	14,805	9,307	75,853	80,237	60,838	112,168	173,006	5,420			
Monthly Average	17,705	897	3,426	8,276	940	10,144	9,695	78,698	78,967	58,784	112,290	171,074	3,874				
Monthly Average (excluding June and December).	17,670	904	3,508	8,355	955	9,848	9,712	78,780	78,645	58,582	112,375	170,957	3,612				
10133	1926.																
	January	17,161	801	4,167	7,280	1,088	10,249	9,591	75,566	81,204	58,672	109,704	168,376	5,366			
	February	16,228	860	2,867	6,989	1,034	7,238	8,474	74,911	81,787	54,497	107,303	161,800	4,522			
	March	16,476	970	3,487	8,053	991	6,445	8,619	74,755	82,069	57,091	106,611	163,902	3,990			
	April	16,949	1,117	4,994	7,714	1,016	7,671	8,663	74,513	81,240	57,715	108,392	166,107	3,532			
	May	18,075	1,011	3,751	7,723	998	9,605	8,632	74,688	82,075	60,080	107,974	168,054	3,355			
	June	17,655	802	4,085	8,452	947	12,300	8,098	76,159	82,689	60,565	109,607	170,072	3,227			
	July	17,617	800	3,748	7,888	1,005	12,078	7,933	75,739	82,220	59,681	110,003	169,684	3,271			
	August	16,793	808	3,191	6,402	914	11,150	8,300	76,456	82,082	57,600	110,353	167,958	3,642			
	September	16,644	897	3,539	7,190	883	10,374	7,920	75,450	83,063	66,968	111,614	168,532	2,954			
	October	16,718	1,238	4,579	9,087	906	11,835	8,142	72,207	83,583	58,283	111,864	170,127	3,229			
	November	17,069	859	3,539	8,141	1,084	12,980	8,070	71,836	86,282	59,805	110,957	170,792	3,463			
	December	16,609	808	4,477	10,247	1,013	13,168	8,215	72,060	88,636	60,390	110,836	171,226	3,718			
Monthly Average	17,000	914	3,869	7,919	990	10,464	8,379	74,443	82,661	58,444	109,810	168,054	3,689				
Monthly Average (excluding June and December).	16,973	936	3,786	7,838	992	10,010	8,423	74,610	82,560	58,087	109,498	167,535	3,732				

TABLE 2—continued.

Date.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Discounted.	Commercial Bills Discounted.	Investments.	Advances (i.e., Loans and Overdrafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Acceptances outstanding.
				To the Money Market.	To the Stock Exchange.								
1927.													
January	16,405	804	4,912	8,427	1,116	11,499	8,229	72,558	83,199	59,233	108,597	167,830	3,852
February	15,936	874	3,265	8,934	1,161	10,794	7,591	72,785	82,390	57,394	108,001	165,395	4,135
March	15,996	814	3,715	7,062	1,243	9,953	7,432	74,422	84,461	58,435	108,551	166,986	4,069
April	16,848	726	4,201	7,211	1,270	8,049	7,450	75,849	84,461	58,466	108,493	166,959	3,902
May	17,512	858	3,453	8,455	1,378	7,885	7,351	75,072	85,470	61,019	106,582	167,801	3,641
June	17,478	937	3,187	7,449	1,481	9,269	7,723	74,997	86,502	62,119	107,438	169,557	3,638
July	17,860	871	3,800	7,292	1,503	7,595	8,167	73,804	87,381	61,136	105,489	166,625	3,415
August	16,983	910	4,248	7,832	1,630	7,020	8,019	72,273	87,099	59,743	106,541	166,284	3,790
September	16,910	899	4,154	9,630	1,673	7,385	8,009	71,298	87,247	61,891	106,549	168,440	3,291
October	17,039	1,159	5,266	10,007	1,490	10,546	7,692	71,531	86,324	63,559	108,136	171,695	3,685
November	17,335	738	3,908	8,927	1,255	10,279	8,355	72,398	89,103	65,728	107,356	178,084	3,963
December	17,071	821	5,114	9,004	1,083	11,621	8,672	71,584	87,917	66,311	107,059	172,870	4,324
Monthly Average	16,998	868	4,085	8,352	1,349	9,320	7,891	73,201	86,021	61,211	107,399	168,610	3,800
Monthly Average (excluding June and December).	16,882	865	4,072	8,378	1,362	9,095	7,830	73,183	85,753	60,660	107,429	168,090	3,774
1928.													
January	17,018	777	4,692	7,278	1,183	9,680	9,175	72,029	86,928	64,223	105,491	169,714	4,517
February	16,525	908	3,413	7,586	1,327	6,235	8,978	72,820	87,713	62,500	104,289	166,769	5,176
March	16,550	801	4,273	7,230	1,340	6,973	8,138	70,546	89,656	60,313	105,552	165,865	4,272
April	17,490	956	5,662	9,609	1,293	8,540	7,864	70,348	89,772	62,386	108,824	171,210	4,006
May	17,963	940	3,798	8,308	1,458	8,590	7,868	71,465	90,815	65,112	108,575	171,687	3,523
June	18,006	776	4,367	8,469	1,517	10,211	8,225	71,340	91,375	65,454	107,700	173,154	3,609
July	17,957	910	3,633	7,286	1,481	7,570	8,640	70,714	83,144	63,386	106,495	169,881	3,459
August	17,399	928	3,503	6,956	1,495	7,505	8,474	69,382	94,296	62,823	107,198	170,016	3,502
September	17,157	840	4,677	7,420	1,457	6,594	8,723	68,980	94,591	62,685	107,998	170,683	3,678
October	17,147	1,143	5,062	8,682	1,701	7,437	9,582	67,684	97,890	66,247	109,745	175,992	4,444
November	17,440	706	4,603	7,877	1,601	6,518	10,005	67,208	99,685	67,345	108,992	176,337	4,623
December	17,078	863	4,951	10,083	1,522	10,990	9,731	66,560	95,360	67,303	108,649	175,952	4,808
Monthly Average	17,306	880	4,386	8,063	1,448	8,070	8,783	69,905	92,602	64,148	107,290	171,438	4,152
Monthly Average (excluding June and December).	17,259	892	4,331	7,821	1,434	7,564	8,744	70,097	92,449	63,702	107,113	170,815	4,140

10122

1929.													
January	17,278	774	5,775	8,177	1,706	11,328	9,267	65,199	94,468	67,192	108,353	173,545	5,276
February	16,930	749	4,964	9,718	1,774	8,728	9,391	64,189	93,243	62,032	106,385	168,367	5,782
March	16,303	774	4,484	7,919	1,471	8,558	8,728	64,108	95,833	60,203	108,036	168,238	5,142
April	16,634	880	4,781	10,756	1,843	8,695	9,813	65,209	94,930	60,692	111,005	171,697	4,961
May	17,146	769	3,396	8,368	1,388	9,255	9,476	65,439	96,876	61,062	109,521	170,583	4,729
June	17,685	833	4,658	7,638	1,369	11,966	8,567	65,540	97,779	62,592	110,803	173,395	4,625
July	17,367	753	3,457	9,249	1,362	10,920	8,308	65,969	99,072	62,689	111,103	173,792	4,668
August	16,968	806	3,993	8,936	1,357	10,739	8,463	66,225	98,396	62,322	111,842	174,184	4,346
September	16,561	811	4,048	8,255	1,354	9,315	9,658	66,237	98,691	61,177	112,487	173,664	4,115
October	16,839	1,239	4,988	10,260	1,296	12,247	9,266	65,389	97,034	62,788	114,167	176,956	4,267
November	16,845	784	3,110	8,677	1,211	12,671	8,745	65,052	100,152	63,177	118,270	176,447	4,607
December	16,980	958	3,623	8,920	985	14,098	8,049	65,365	98,664	63,227	113,081	176,308	4,648
Monthly Average ...	16,961	840	4,281	8,905	1,382	10,752	8,976	65,410	97,095	62,429	110,667	173,096	4,788
Monthly Average (excluding June and December).	16,887	829	4,290	9,080	1,423	10,246	9,110	65,402	96,869	62,333	110,412	172,745	4,788
1930.													
January	16,313	716	5,928	7,978	1,010	11,250	7,801	65,062	98,820	64,543	111,535	176,078	4,496
February	15,810	726	4,084	6,179	988	8,965	7,489	66,180	99,576	59,592	109,788	169,390	4,307
March	16,130	775	3,748	8,964	958	5,848	7,793	65,104	99,484	57,601	109,947	167,548	4,177
April	16,906	822	4,612	9,362	976	4,975	8,366	65,442	99,596	60,082	109,061	169,143	4,051
May	17,579	768	3,940	10,329	1,038	3,280	7,944	65,988	101,928	63,630	106,623	170,463	3,943
June	17,642	697	4,561	11,347	994	6,526	8,279	66,258	99,639	64,982	108,140	173,122	3,847
July	17,720	830	4,160	10,931	846	7,227	8,064	66,653	98,547	66,131	106,365	172,496	3,825
August	17,374	1,157	5,452	10,492	755	7,605	7,710	67,822	98,431	66,852	107,762	174,614	3,689
September	16,924	767	4,431	14,085	678	8,975	7,966	70,212	96,573	68,188	110,590	178,778	4,066
October	16,758	1,268	7,406	11,987	527	12,506	8,226	73,740	94,729	70,483	112,385	182,868	4,010
November	17,169	873	6,471	10,345	626	14,142	7,846	77,825	93,785	71,067	112,440	185,507	4,176
December	16,952	924	6,980	8,504	666	14,517	7,672	79,468	91,030	72,037	110,233	182,270	3,930
Monthly Average ...	16,940	860	5,147	10,042	838	8,801	7,933	69,145	97,678	65,432	109,589	175,021	4,043
Monthly Average (excluding June and December).	16,868	870	5,022	10,065	839	8,457	7,924	68,403	98,147	64,817	109,670	174,486	4,074
1931.													
January	16,099	738	6,898	8,645	657	12,639	7,605	80,291	90,158	70,904	110,641	181,545	3,637
February	15,896	795	5,237	5,024	585	9,622	7,634	81,216	91,842	65,813	107,555	173,368	3,540
March	15,753	759	5,988	7,366	581	7,974	7,510	80,796	92,690	65,617	108,725	174,342	3,500

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TABLE 3.—LONDON CLEARING BANKS. SUMMARY OF MONTHLY AVERAGES (12 MONTHS) OWN IN TABLE 1.
(£ millions throughout.)

Year.	Cash in Hand.	Balance at Bank of England.	Money at Call.	Money at Short Notice.		Treasury Bills Dis-counted.	Com-mercial Bills Dis-counted.	Invest-ments.	Advances (i.e., Loans and Over-drafts).	Current Accounts.	Deposit Accounts.	Total Deposits.	Acceptances out-standing.
				To the Money Market.	To the Stock Ex-change.								
1919	112.4	103.9	22.9	90.9	17.7	159.2	106.8	351.4	579.6	1,015.9	494.8	1,510.7	61.5
1920	105.8	83.7	23.8	54.3	22.0	115.6	144.2	367.7	831.6	1,097.6	622.1	1,719.7	75.8
1921	110.7	96.1	27.2	54.8	18.0	224.6	134.1	348.8	790.2	1,024.8	728.9	1,753.6	39.4
1922	107.5	92.9	29.7	58.8	23.4	208.0	113.3	420.6	711.8	998.3	709.1	1,707.5	36.5
1923	103.8	87.3	24.8	60.2	24.5	146.1	119.8	377.6	729.5	965.6	648.5	1,614.1	44.7
1924	103.8	88.3	24.6	57.2	22.8	104.8	125.5	364.7	774.2	950.0	665.7	1,615.7	54.5
1925	103.7	86.2	24.8	61.1	30.6	91.0	127.6	305.4	821.6	922.5	680.2	1,602.7	60.5
1926	103.1	86.1	25.0	63.1	32.1	100.9	107.8	284.5	858.0	921.4	687.5	1,608.9	52.1
1927	105.1	85.3	25.2	75.4	39.5	112.6	98.4	272.6	899.2	932.1	726.5	1,658.6	49.5
1928	104.5	83.6	28.4	77.7	48.0	107.7	118.2	275.3	923.6	953.7	755.2	1,708.9	65.3
1929	104.4	82.9	28.9	76.0	43.4	98.3	122.9	275.0	964.0	940.2	797.9	1,738.0	73.6
1930	103.6	84.5	33.1	80.1	28.5	128.6	127.2	281.5	933.4	920.8	820.0	1,740.8	58.0

296

TABLE 4.—LONDON CLEARING BANKS. SUMMARY OF MONTHLY AVERAGES EXPRESSED AS AN INDEX NUMBER WITH 1924 AS BASE=100.

1919	108.3	117.6	93.3	159.0	77.7	152.0	85.1	96.4	74.9	106.9	74.3	93.5	112.8
1920	101.9	94.8	97.0	95.0	96.5	110.3	114.9	100.8	107.4	115.5	93.4	106.4	139.1
1921	106.7	108.8	110.8	95.9	79.0	214.3	106.8	95.6	102.1	107.9	109.5	108.5	72.3
1922	103.6	105.2	120.8	102.9	102.6	198.5	90.3	115.3	91.9	105.1	106.5	105.7	66.9
1923	100.1	98.9	100.8	105.2	107.4	139.4	95.4	103.5	94.2	101.6	97.4	99.9	82.0
1924	100	100	100	100	100	100	100	100	100	100	100	100	100
1925	99.9	97.6	100.9	106.9	134.1	86.8	101.7	83.7	106.1	97.1	102.2	99.2	111.0
1926	99.3	97.5	101.6	110.5	140.8	96.3	85.9	78.0	110.8	97.0	103.3	99.6	95.5
1927	101.3	96.7	102.7	131.8	173.5	107.4	78.4	74.7	116.1	98.1	109.1	102.7	90.8
1928	100.7	94.7	115.7	135.9	210.4	102.8	94.2	75.5	119.3	100.4	113.4	105.8	119.9
1929	100.6	93.9	117.6	132.9	190.3	93.8	97.9	75.4	124.5	99.0	119.9	107.6	135.0
1930	99.8	95.8	134.6	140.1	124.9	122.8	101.3	77.2	120.6	96.9	123.2	107.7	106.4

TABLE 5.—SCOTTISH BANKS. SUMMARY OF MONTHLY AVERAGES (12 MONTHS) SHOWN IN TABLE 2.

(£ millions throughout.)

10122

1919	...	...	10.8	2.0	.7	3.8	-.2	19.6	3.6	39.0	26.8	28.7	59.3	88.0	2.4
1920	...	...	17.4	1.0	2.1	8.5	-.6	20.8	11.8	58.3	61.8	48.6	103.8	152.3	3.2
1921	...	...	21.8	1.0	4.4	10.9	-.7	41.5	13.3	75.2	75.9	57.3	150.0	207.3	3.1
1922	...	...	19.3	-.9	4.0	9.8	-.9	28.3	11.6	99.5	66.0	56.4	148.1	204.5	3.2
1923	...	...	18.4	1.0	3.6	9.8	-.7	13.4	11.7	88.5	68.7	56.8	124.1	180.9	3.2
1924	...	...	18.0	-.9	4.1	9.4	-.6	12.1	10.6	84.0	72.3	58.7	116.7	175.4	3.6
1925	...	...	17.7	-.9	3.4	8.3	-.9	10.1	9.7	78.7	79.0	58.8	112.3	171.1	3.7
1926	...	...	17.0	-.9	3.9	7.9	1.0	10.5	8.4	74.4	82.7	58.4	109.6	168.1	3.7
1927	...	...	17.0	-.9	4.1	8.4	1.3	9.3	7.9	73.2	86.0	61.2	107.4	168.6	3.8
1928	...	...	17.3	-.9	4.4	8.1	1.4	8.1	8.8	69.9	92.6	64.1	107.3	171.4	4.2
1929	...	...	17.0	-.8	4.3	8.9	1.4	10.8	9.0	65.4	97.1	62.4	110.7	173.1	4.8
1930	...	...	16.9	-.9	5.1	10.0	-.8	8.8	7.9	69.1	97.7	65.4	109.6	175.0	4.0

TABLE 6.—SCOTTISH BANKS. SUMMARY OF MONTHLY AVERAGES EXPRESSED AS AN INDEX NUMBER WITH 1924 AS BASE=100.

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1919	59.8	209.6	17.7	40.0	39.2	162.5	34.0	46.4	37.1	48.9	50.8	50.2	67.4
1920	96.7	100.7	52.0	90.7	114.1	172.6	110.8	69.4	85.5	82.8	88.9	86.9	89.0
1921	...	...	120.9	108.2	107.5	115.9	131.3	343.5	125.4	89.6	105.0	97.7	128.5	118.2	87.5
1922	...	...	106.9	100.1	96.6	104.7	168.4	234.6	109.4	118.5	91.2	96.2	126.9	116.6	89.0
1923	...	...	101.9	109.0	88.1	104.8	123.5	111.2	110.1	105.4	95.0	96.9	106.3	103.2	88.5
1924	...	...	100	100	100	100	100	100	100	100	100	100	100	100	100
1925	...	...	98.3	94.7	83.1	88.1	170.0	84.0	91.1	93.7	109.2	100.2	96.2	97.5	103.2
1926	...	...	94.4	96.5	93.8	84.3	179.0	86.6	78.7	88.7	114.3	99.6	93.9	95.8	103.6
1927	...	...	94.4	91.7	99.1	88.9	243.9	77.2	74.1	87.2	119.0	104.4	92.0	96.1	106.7
1928	...	...	96.1	92.9	106.4	85.9	261.8	66.8	82.5	83.3	123.1	109.4	91.9	97.8	116.6
1929	...	...	94.2	88.7	103.8	94.8	249.9	89.0	84.3	77.9	134.3	106.4	94.8	98.7	134.5
1930	...	...	94.1	90.8	124.8	106.9	151.5	72.9	74.5	82.4	135.1	111.6	93.9	99.8	113.6

TABLE 7.

LONDON CLEARING BANKS.—TOTAL VALUE OF CHEQUES DRAWN ON CUSTOMERS' ACCOUNTS IN EACH MONTH FROM JANUARY, 1930, TO APRIL, 1931.

1930.						£
January	...	...	...	...	...	5,832,924,000
February	...	...	...	...	...	5,168,888,000
March	...	...	...	...	...	6,066,258,000
April	...	...	...	...	...	5,303,596,000
May	...	...	...	...	...	5,632,165,000
June	...	...	...	...	...	5,128,810,000
July	...	...	...	...	...	5,900,348,000
August	...	...	...	...	...	4,786,693,000
September	...	...	...	...	...	4,964,796,000
October	...	...	...	...	...	5,686,745,000
November	...	...	...	...	...	5,147,086,000
December	...	...	...	...	...	5,022,658,000
1931.						£
January	...	...	...	...	...	5,772,131,000
February	...	...	...	...	...	4,843,038,000
March	...	...	...	...	...	4,983,308,000
April	...	...	...	...	...	4,953,996,000

Note.—These figures relate to the ten London Clearing Banks but they do not cover (a) branches of those banks situated outside England and Wales and (b) non-clearing banks affiliated to or owned by a Clearing Bank. For the calculation the Banks have taken the totals of the debit entries to current accounts (deposit accounts being excluded) as shown in their books without allowance for items which are not strictly cheques or bills (e.g., transfers from one account to another).

TABLE 8.

LONDON CLEARING BANKS AND SCOTTISH BANKS. CLASSIFICATION OF ADVANCES ON VARIOUS DATES FROM 22ND OCTOBER, 1929, TO 19TH MARCH, 1930.

	London	Scottish
	Clearing Banks.	Banks.
	£	£
1. Textiles (cotton, wool, silk, linen, jute)	81,632,371	4,977,214
2. Heavy industries (iron, steel, engineering and shipbuilding).	62,962,675	7,658,164
3. Agriculture and fishing	68,630,471	7,623,448
4. Mining and quarrying (including coal)	30,003,440	2,382,899
5. Food, drink and tobacco	63,177,889	5,967,176
6. Leather, rubber and chemicals	21,969,950	1,507,903
7. Shipping and transport (including railways)	25,176,565	3,487,859
8. Building trades	47,824,549	1,578,970
9. Miscellaneous trades (including retail trades)	146,496,288	9,009,182
10. Local government authorities and public utility companies (excluding railways)	52,384,672	6,675,757
11. Amusements, clubs, churches, charities, &c.	26,502,720	770,399
12. Financial (including banks and discount houses, stock exchange and building societies).	142,547,506	24,989,966
13. Other advances	218,402,248	28,550,094
	<hr/>	<hr/>
	£987,711,344	£105,179,031

**LONDON CLEARING BANKS AND BANK OF ENGLAND. DEPOSITS AND STERLING BILLS HELD, AND (CLEARING BANKS ONLY)
ACCEPTANCES OUTSTANDING ON ACCOUNT OF FOREIGN CUSTOMERS.
(£000 throughout).**

	1927.		1928.		1929.		1930.		1931.		
	June 30th.	Dec. 31st.	June 30th.	Dec. 31st.	June 30th.	Dec. 31st.	June 30th.	Dec. 31st.	Jan. 31st.	Feb. 28th.	Mar. 31st.
<i>Deposits held on account of—</i>											
Banks with head offices abroad...	80,624	68,109	83,504	82,977	69,335	70,594	123,220	122,026	109,762	110,858	105,804
Foreign Governments	16,983	19,897	19,531	25,534	26,493	19,307	13,500	11,133	11,039	10,316	9,174
Other foreign customers... ..	20,998	21,979	22,149	22,990	23,274	21,530	25,000	21,118	21,475	20,129	20,333
Total Deposits	118,605	109,985	125,184	131,501	119,102	111,431	161,720	154,277	142,276	141,303	135,311
<i>Sterling Bills held on account of—</i>											
Banks with head offices abroad...	111,205	133,382	134,169	172,267	160,356	163,238	122,584	118,918	112,768	113,863	108,660
Foreign Governments	13,121	22,923	19,955	13,790	19,276	26,293	17,159	16,817	16,305	18,420	19,521
Other foreign customers... ..	4,216	5,150	4,107	8,471	9,608	9,923	7,862	8,740	7,088	7,952	8,482
Total Sterling Bills	128,542	161,455	158,231	194,528	189,240	199,454	147,605	144,475	136,161	140,235	136,663
Total Deposits and Bills...	247,147	271,440	283,415	326,029	308,342	310,885	309,325	298,752	278,437	281,538	271,974
<i>Acceptances outstanding on account of—</i>											
Banks with head offices abroad...	27,693	27,084	34,787	46,994	46,158	34,823	39,690	31,557	30,828	30,369	28,770
Foreign Governments	338	838	—	250	462	626	100	50	75	113	100
Other foreign customers... ..	3,086	3,296	3,124	3,180	3,614	3,744	2,630	3,219	3,150	3,319	2,727
Total Acceptances	31,117	31,218	37,911	50,424	50,234	39,193	42,420	34,826	34,053	33,801	31,597

Note—“ Other foreign customers ” includes Companies with head offices abroad.

TABLE 10.
SCOTTISH BANKS.* DEPOSITS AND STERLING BILLS HELD, AND ACCEPTANCES OUTSTANDING, ON ACCOUNT OF FOREIGN CUSTOMERS.
 (£000 throughout.)

	1927.		1928.		1929.		1930.		1931.		
	June 30th.	Dec. 31st.	June 30th.	Dec. 31st.	June 30th.	Dec. 31st.	June 30th.	Dec. 31st.	Jan. 31st.	Feb. 28th.	Mar. 31st.
<i>Deposits held on account of—</i>											
Banks with head offices abroad	2,256	4,462	4,060	5,025	4,526	4,234	6,815	7,648	7,975	7,696	8,192
Foreign Governments ...	18	19	20	20	21	21	63	2	1	—	—
Other foreign customers ...	2,366	2,350	2,784	2,885	2,717	2,604	2,802	2,682	2,575	2,568	2,661
Total Deposits ...	4,640	6,831	6,864	7,930	7,264	6,859	9,680	10,332	10,451	10,264	10,853
<i>Sterling Bills held on account of—</i>											
Banks with head offices abroad	440	159	231	762	753	733	195	203	191	160	142
Other foreign customers ...	14	5	7	23	6	39	22	47	9	8	9
Total Sterling Bills ...	454	164	238	785	759	772	217	250	200	168	151
Total Deposits and Bills	5,094	6,995	7,102	8,715	8,023	7,631	9,897	10,582	10,651	10,432	11,004
<i>Acceptances outstanding on account of—</i>											
Banks with head offices abroad ...	196	171	410	491	544	285	297	255	225	209	215
Other foreign customers ...	132	289	146	363	837	500	448	586	521	458	489
Total Acceptances ...	328	460	556	854	1,381	785	745	841	746	667	704

* The figures relate to six banks only.

TABLE 11.

DEPOSITS AND STERLING BILLS HELD IN LONDON ON FOREIGN ACCOUNT AND STERLING BILLS ACCEPTED ON FOREIGN ACCOUNT.
(£000 throughout.)

<i>Deposits with—</i>												
Bank of England, Clearing Banks and Scottish Banks (<i>see</i> Tables 9 and 10).	123,245	116,816	132,048	139,431	126,366	118,290	171,400	164,609	152,727	151,567	146,164	
Accepting Houses	76,055	89,321	96,373	104,331	86,426	79,183	86,490	82,112	76,527	75,821	81,019	
Total Deposits	199,300	206,137	228,421	243,762	212,792	197,473	257,890	246,721	229,254	227,388	227,183	
<i>Sterling Bills held through—</i>												
Bank of England, Clearing Banks and Scottish Banks (<i>see</i> Tables 9 and 10).	128,996	161,619	158,469	195,313	189,999	200,226	147,822	144,725	136,361	140,403	136,814	
Accepting Houses	9,432	13,115	9,147	16,863	14,466	19,379	8,647	8,040	6,744	7,043	7,380	
Total Bills	138,428	174,734	167,616	212,176	204,465	219,605	156,469	152,765	143,105	147,446	144,194	
<i>Advances to Discount Market by—</i>												
Banks with head offices abroad	33,405	35,560	43,050	43,425	32,965	30,535	41,070	33,625	35,846	38,956	33,619	
Other foreign customers	4,920	2,815	4,270	3,585	3,500	3,435	1,190	1,475	2,065	1,897	2,056	
Total Advances	38,325	38,375	47,320	47,010	36,465	33,970	42,260	35,100	37,911	40,853	35,675	
Total Deposits, Bills and Advances.	376,053	419,246	443,357	502,948	453,722	451,048	456,619	434,586	410,270	415,687	407,052	
<i>Acceptances on foreign account by—</i>												
Clearing Banks and Scottish Banks (<i>see</i> Tables 9 and 10).	31,445	31,678	38,467	51,278	51,615	39,978	43,165	35,667	34,799	34,468	32,301	
Accepting Houses	91,504	107,954	126,907	149,231	150,883	135,699	132,111	125,282	120,846	120,942	120,616	
Total Acceptances	122,949	139,632	165,374	200,509	202,498	175,677	175,276	160,949	155,645	155,410	152,917	

APPENDIX II.

BANK OF ENGLAND WEEKLY ACCOUNT, JAN., 1925, TO MAY, 1931.

[Monthly Averages of Wednesday Figures in £ millions]

	Notes in Circulation.	ISSUE DEPARTMENT.					BANKING DEPARTMENT.						Reserve of Notes and Coin.
		Notes in Banking Department.	Government Debt and other Government Securities.	Other Securities.	Silver Coin.	Gold Coin and Bullion.	Public Deposits.	Other Deposits.		Government Securities.	Other Securities.		
								Bankers.‡	Other Accounts.		Discounts and Advances.	Securities.	
1925 Jan. ...	383.7	20.7	19.7*	7.0	126.7	17.5	70.0	42.3	50.5	17.1	57.3	22.6	
Feb. ...	378.8	21.7	"	7.0	126.8	12.6	74.0	42.6	49.8	14.7	59.5	23.5	
Mar. ...	380.3	22.2	"	7.0	126.8	13.2	69.6	41.4	40.6	15.3	62.5	24.0	
Apr. ...	385.9	25.3	"	7.0	132.3	16.0	69.6	40.3	39.1	16.7	60.9	27.1	
May ...	384.6	25.3	"	7.0	153.4	15.0	65.4	39.3	35.8	12.8	61.7	27.1	
June ...	385.2	28.0	"	7.0	155.3	11.9	73.5	40.1	40.1	12.5	60.9	29.8	
July ...	387.2	36.9	"	7.0	159.3	14.4	77.5	40.9	38.7	14.6	61.2	36.2	
Aug. ...	380.4	35.1	"	7.0	162.2	16.3	68.0	41.0	34.3	9.7	60.6	33.7	
Sept. ...	378.5	29.0	"	7.0	159.4	17.5	70.4	41.7	37.9	10.7	62.4	36.9	
Oct. ...	376.0	24.3	"	7.0	152.4	9.7	64.3	41.4	31.3	11.8	59.6	30.8	
Nov. ...	381.4	18.6	"	7.0	143.1	10.8	67.5	40.3	39.1	15.8	59.2	26.1	
Dec. ...	373.7	20.4	"	7.0	142.6	16.9	70.6	42.0	45.6	21.4	58.6	20.4	
1926 Jan. ...	369.3	21.8	"	6.8	143.2	17.8	66.4	40.8	42.2	15.8	61.9	23.2	
Feb. ...	373.6	22.7	"	6.7	144.7	20.0	63.1	39.1	39.2	19.9	57.2	24.1	
Mar. ...	378.6	23.9	"	6.6	145.1	13.9	64.6	37.8	41.0	12.4	55.2	25.3	
Apr. ...	385.0	25.8	"	6.6	147.2	19.3	66.8	37.4	43.4	17.2	53.6	27.1	
May ...	379.3	27.4	"	6.6	148.4	12.9	78.1	39.3	44.7	21.5	53.3	28.7	
June ...	377.9	28.1	"	6.6	150.1	10.8	71.8	38.2	38.0	15.2	56.3	29.4	
July ...	376.3	31.2	"	6.6	152.6	15.6	68.2	38.7	36.6	13.9	57.6	32.5	
Aug. ...	371.0	33.8	"	6.5	154.2	16.5	65.7	39.1	34.2	13.6	56.3	35.3	
Sept. ...	371.2	32.3	"	6.3	152.4	18.3	66.6	38.7	35.3	14.9	56.7	34.4	
Oct. ...	368.7	32.3	"	6.3	151.3	20.5	62.9	38.7	34.8	14.5	56.6	33.8	
Nov. ...	374.8	30.4	"	6.3	150.3	10.6	76.7	38.7	34.6	19.4	58.1	31.7	
Dec. ...	365.8	31.9	"	6.3	150.2	13.2	78.2	38.6	32.7	22.3	59.6	33.2	
1927 Jan. ...	361.7	31.9	"	6.3	149.1	14.9	66.1	37.6	32.6	12.4	61.6	33.2	
Feb. ...	365.5	31.8	"	6.0	149.2	19.1	64.3	39.1	31.9	13.9	61.8	33.2	
Mar. ...	376.8	33.7	"	5.7	151.5	17.6	64.4	38.0	36.5	14.4	61.4	35.3	
Apr. ...	378.8	35.7	"	5.7	152.2	15.2	62.6	36.0	47.5	18.2	28.5	37.4	
May ...	378.2	33.4	"	5.7	150.6	14.9	68.4	36.8	50.9	20.0	32.0	35.0	
June ...	378.3	31.8	"	5.7	149.9	12.9	67.5	35.1	49.1	18.8	32.3	33.4	
July ...	377.6	32.8	"	5.7	150.4	15.7	64.9	35.3	52.7	14.7	32.4	34.4	
Aug. ...	374.2	33.0	"	5.7	149.6	20.1	63.1	35.1	56.4	11.0	35.8	34.6	
Sept. ...	374.0	33.4	"	5.7	149.8	21.5	64.2	36.2	49.8	14.2	40.7	34.9	
Oct. ...	373.5	33.5	"	5.7	149.7	18.3	61.0	36.6	41.9	13.9	42.9	35.0	
Nov. ...	379.5	31.4	"	5.7	149.5	13.3	73.4	36.3	45.1	16.9	45.4	32.5	

1928	Jan.	371.6	37.9		5.7	153.9	16.1	75.9	37.0	39.9	23.6	44.7	38.7
	Feb.	365.0	41.3	"	5.6	156.5	13.6	61.2	36.6	33.9	8.3	45.2	42.1
	Mar.	367.4	41.9	"	5.5	157.0	11.6	63.7	37.8	31.7	8.4	48.4	42.6
	Apr.	373.2	41.7	"	5.5	157.3	19.8	59.5	37.1	32.2	11.6	47.4	42.9
	May	371.7	44.6	"	5.5	160.2	16.3	61.0	36.5	29.8	8.6	46.8	46.3
	June	374.2	50.3	"	5.4	166.6	18.9	68.3	35.9	33.3	10.3	44.1	53.3
	July	376.2	55.6	"	5.4	172.2	16.0	75.9	36.0	29.8	17.0	40.2	58.3
	Aug.	375.7	55.6	"	5.4	171.8	14.8	65.0	35.8	28.8	9.6	37.0	58.3
	Sept.	372.8	58.1	"	5.4	173.0	14.3	65.6	37.6	31.2	9.6	34.2	60.8
	Oct.	370.1	50.6	"	5.4	164.9	11.9	62.8	38.4	36.4	11.1	30.8	52.6
	Nov.	366.3	49.4	"	5.3	161.4	17.4	61.9	37.6	47.4	11.5	25.4	50.4
	Dec.	379.7	36.2	244.6	10.2	155.9	10.1	68.8	36.8	62.0	15.9	19.0	36.7
1929	Jan.	363.9	49.6	244.7	10.2	153.5	16.9	67.6	37.4	55.1	19.2	15.9	49.8
	Feb.	353.6	56.6	245.4	9.6	150.2	14.3	62.4	36.8	48.1	9.9	16.6	57.0
	Mar.	356.4	55.8	246.0	9.1	152.2	14.8	62.0	37.1	47.0	12.1	17.0	56.2
	Apr.	360.4	54.8	246.6	8.6	155.2	17.8	62.6	36.4	51.5	12.0	15.9	55.8
	May	361.9	58.9	247.2	8.0	160.8	13.7	59.8	36.1	40.3	9.1	18.4	59.6
	June	361.7	60.3	246.8	8.4	161.6	16.3	63.8	35.8	38.3	11.6	22.5	61.3
	July	368.9	42.0	246.1	9.1	150.9	14.4	65.0	36.9	47.3	20.3	23.6	43.2
	Aug.	369.1	29.2	246.4	8.8	138.2	17.5	61.4	36.4	73.0	4.9	25.1	30.4
	Sept.	363.5	31.4	246.6	8.6	135.0	14.1	65.2	36.6	73.5	3.6	24.3	32.7
	Oct.	360.7	30.2	246.6	8.6	130.9	11.4	63.6	37.7	72.2	6.5	20.6	31.4
	Nov.	356.5	36.0	246.0	9.2	132.5	14.5	58.3	39.3	63.6	9.8	19.7	36.8
	Dec.	369.4	29.9	244.5	10.8	139.3	8.9	62.5	36.3	63.3	12.8	19.1	30.2
1930	Jan.	355.8	53.5	244.9	10.6	149.3	19.6	75.6	36.3	65.0	15.6	15.2	53.7
	Feb.	347.3	63.7	244.6	10.9	151.0	16.8	55.8	35.6	41.9	5.7	14.4	64.3
	Mar.	349.7	63.3	244.5	11.0	153.0	12.1	59.9	36.1	40.6	6.7	15.1	64.1
	Apr.	359.8	60.6	243.9	11.6	160.4	17.3	65.2	36.5	57.1	7.3	10.9	61.6
	May	356.4	63.7	243.9	11.6	160.2	18.8	60.9	36.4	51.1	6.7	11.4	64.7
	June	360.4	58.0	243.9	11.6	156.4	13.8	63.9	36.0	50.0	9.1	14.7	56.9
	July	365.0	49.8	243.9	11.6	154.8	10.1	70.3	36.7	52.4	11.2	20.8	50.7
	Aug.	365.8	48.0	243.9	11.6	153.7	15.1	63.0	34.6	51.5	6.9	23.5	49.0
	Sept.	359.5	56.2	243.9	11.6	155.7	9.8	66.0	34.2	43.4	5.8	21.8	57.3
	Oct.	357.2	60.6	243.9	11.6	157.0	19.2	61.0	34.8	42.2	6.2	22.6	61.8
	Nov.	354.2	64.8	244.0	11.5	158.4	18.3	57.8	34.4	35.0	4.8	23.0	65.4
	Dec.	368.9	41.7	244.1	11.5	150.5	7.4	81.4	34.2	60.0	15.6	22.9	42.4
1931	Jan.	351.7	51.4	243.9	11.7	143.0	19.3	64.4	33.4	48.9	10.9	23.4	52.0
	Feb.	347.1	53.4	243.1	12.5	140.5	13.7	60.1	33.5	38.1	8.5	24.7	54.1
	Mar.	349.3	52.6	244.9	10.8	141.9	9.1	60.8	33.5	30.4	9.8	28.1	53.4
	Apr.	353.7	51.9	243.2	12.7	145.6	13.4	56.6	35.3	32.0	11.4	26.9	52.8
	May	353.9	55.5	243.5	12.4	149.4	12.2	58.0	34.3	33.3	6.2	26.3	56.5

† Including Currency Notes in Circulation prior to amalgamation of the Note Issues on 22nd November, 1928.
 * These are the figures of the "Government Debt" and the "Other Securities" as shown in the Bank Return prior to 22nd November, 1928.
 † For the months prior to the amalgamation of the Note Issues on the 22nd November, 1928, the Bankers' Deposits are compiled on a slightly different basis from that adopted since that date. Comparability for statistical purposes is, however, scarcely affected.

APPENDIX III.

ESTIMATE OF FUTURE MONETARY DEMAND FOR GOLD IF NO ECONOMY IN ITS USE IS MADE.
 (REPRODUCED FROM THE FIRST INTERIM REPORT OF THE GOLD DELEGATION OF THE FINANCIAL COMMITTEE OF THE LEAGUE OF NATIONS)
 (CONVERTED TO £ STERLING.)

(£ millions.)

Year.	Estimated gold production.	Non-monetary demand.	Available for monetary purposes.	Increments to gold reserves required to provide				Excess or deficit of amount of new monetary gold available compared with increment required to provide			
				33 per cent. cover for average increases in notes and sight liabilities of :		40 per cent. cover for average increases in notes and sight liabilities of :		33 per cent cover if notes and sight liabilities increase at :		40 per cent cover if notes and sight liabilities increase at :	
				2 per cent. per annum.	3 per cent. per annum.	2 per cent. per annum.	3 per cent. per annum.	2 per cent. per annum.	3 per cent. per annum.	2 per cent. per annum.	3 per cent. per annum.
1930 ...	83.0	37.0	46.0	34.3	52.0	41.1	62.3	+11.7	- 6.0	+ 4.9	-16.3
1931 ...	82.6	37.4	45.2	34.9	53.4	41.9	64.3	+10.3	- 8.2	+ 3.3	-19.1
1932 ...	84.2	37.8	46.4	35.8	55.3	42.9	66.4	+10.6	- 8.9	+ 3.5	-20.0
1933 ...	83.6	38.2	45.4	36.6	56.7	43.8	68.2	+ 8.8	-11.3	+ 1.6	-22.8
1934 ...	82.8	38.6	44.2	37.0	58.6	44.6	70.1	+ 7.2	-14.4	- 0.4	-25.9
1935 ...	81.8	39.1	42.7	37.8	60.4	45.4	72.3	+ 4.9	-17.7	- 2.7	-29.6
1936 ...	81.6	39.5	42.1	38.6	62.1	46.4	74.6	+ 3.5	-19.9	- 4.3	-32.5
1937 ...	80.5	39.8	40.7	39.5	63.9	47.3	76.6	+ 1.2	-23.2	- 6.6	-35.9
1938 ...	78.9	40.3	38.6	40.3	66.0	48.3	79.1	- 1.7	-27.4	- 9.7	-40.5
1939 ...	76.0	40.7	35.3	41.1	67.8	49.3	81.4	- 5.8	-32.5	-14.0	-46.1
1940 ...	76.0	41.1	34.9	41.9	69.9	50.1	83.8	- 7.0	-35.0	-15.2	-48.9

APPENDIX IV.

TABLE 1.—THE BALANCE OF PAYMENTS OF THE UNITED KINGDOM ON INCOME ACCOUNT: 1924 TO 1930.
(£ millions.)

	1924.	1925.	1926.	1927.	1928.	1929.	1930.
Excess of Imports of Merchandise and Bullion	324	384	475	390	358	366	392
Government Receipts from Overseas (net)	25*	11*	4	1	15	24	21
Net National Shipping Income	140	124	120	140	130	130	105
Net Income from Overseas Investments	220	250	285	285	270	270	235
Net Receipts from Short Interest and Commissions	60	60	60	63	65	65	55
Net Receipts from Other Sources	15	15	15	15	15	15	15
Total... ..	410	438	484	504	495	504	431
Estimated total credit balance on above items	86	54	9	114	137	138	39

* Excess of Payments made Overseas.

TABLE 2.—NEW OVERSEAS ISSUES ON THE LONDON MARKET.†
(£ millions.)

British Empire	73	58	52	88	86	54	70
Foreign	61	30	60	51	57	40	39
Total... ..	134	88	112	139	143	94	109

† Midland Bank figures.

TABLE 3.—THE BALANCE OF PAYMENTS OF THE UNITED STATES: 1924 TO 1929.
(In \$ millions: Export Surplus (+) and Import Surplus (-)).

Class of Transactions.*	1924.	1925.	1926.	1927.	1928.	1929 (unrevised).
Excess of Exports of Commodities over Imports ...	+ 882	+ 633	+ 278	+ 583	+ 850	+ 734
<i>Miscellaneous Invisible Items.</i>						
Freights (net)	- 64	- 84	- 95	- 66	- 80	- 115
Tourist expenditure (net), including ocean-borne passenger traffic.	- 373	- 410	- 406	- 444	- 552	- 565
Interest on American private funds abroad	+ 635	+ 689	+ 740	+ 800	+ 893	+ 976
Interest on foreign funds in United States	- 192	- 229	- 268	- 281	- 359	- 414
War Debt receipts (interest and principal)	+ 183	+ 186	+ 195	+ 206	+ 207	+ 207
Other Government transactions (net)	- 53	- 61	- 49	- 29	- 57	- 92
Immigrant remittances (net)	- 229	- 235	- 218	- 206	- 225	- 223
Miscellaneous (net)	+ 13	+ 24	+ 28	+ 25	- 27	- 24
Total, commodity and miscellaneous (net)	+ 802	+ 513	+ 205	+ 588	+ 650	+ 484
Gold shipped or earmarked†	- 236	+ 72	- 72	+ 154	+ 272	- 120

* This classification is not directly comparable with that in the table for the United Kingdom.

† Including Paper Currency in 1924 and 1925.

TABLE 4.—DATA RELATING TO NET INCREASE IN EXTERNAL INVESTMENT AND FOREIGN CAPITAL ISSUES IN THE UNITED STATES.

Difference between American long-term investment abroad and foreign investment in the United States (net).	- 733	- 560	- 540	- 695	- 708	- 386
Change in net debt of American banks to foreigners ...	+ 216	- 61	+ 359	...	- 226	+ 13
Net Capital Movement (long and short term)	- 517	- 621	- 181	- 695	- 934	- 373
Foreign Capital Issues publicly offered (excluding re-funding issues).	969	1,076	1,125	1,337	1,251	671

APPENDIX V.

INDICES OF WHOLESALE PRICES IN VARIOUS COUNTRIES FOR EACH MONTH IN 1929 AND 1930.

(1913=100 in all cases).

	United States.		Canada.		France.*		Germany.		Italy.*		Netherlands.		Japan.	
	1929.	1930.	1929.	1930.	1929.	1930.	1929.	1930.	1929.	1930.	1929.	1930.	1929.	1930.
January	139·3	133·8	147·7	149·4	123·0	114·4	138·9	132·3	125·8	113·9	146	131	172·2	152·2
February	138·5	131·9	149·5	146·9	129·6	114·6	139·3	129·3	126·2	111·3	146	126	171·0	151·0
March	139·7	130·1	150·2	143·6	129·9	112·2	139·6	126·4	125·8	109·0	147	122	171·0	148·1
April	138·7	129·9	147·0	143·3	127·3	111·3	137·1	126·7	124·1	108·9	144	122	170·2	145·7
May	137·2	127·7	144·4	140·5	126·5	109·9	135·5	125·7	123·2	106·5	142	118	168·6	143·1
June	138·1	124·4	144·7	137·5	124·0	108·1	135·1	124·5	121·8	104·1	141	118	167·6	137·0
July	140·4	120·3	150·0	134·1	124·5	109·2	137·8	125·1	119·9	102·3	141	115	166·0	133·4
August	140·0	120·3	153·3	131·4	121·1	108·0	138·1	124·7	119·3	103·5	142	114	165·1	132·7
September	139·7	120·6	152·0	128·9	121·3	106·4	138·1	122·8	119·2	102·2	141	112	164·4	129·6
October	138·0	118·3	151·1	127·2	119·6	103·2	137·2	120·2	118·9	99·4	140	111	163·4	124·4
November	135·2	115·2	149·7	124·7	118·5	100·2	135·5	120·1	117·5	98·4	137	110	159·6	122·6
December	135·0	112·3	150·3	121·6	116·9	99·0	134·3	117·8	115·8	95·4	135	107	154·9	121·5

* In terms of present currency.

APPENDIX VI.

STATISTICS PREPARED BY THE STAFF OF THE ECONOMIC ADVISORY COUNCIL.

TABLE I.

EXPORTS AS A PERCENTAGE OF PRODUCTION.

The following table shows the diminishing importance of the export trade relatively to our whole national economy. Distinction is drawn between workers in manufacture and workers in all occupations (the latter includes building retail trade and so forth).

—	Workers Manufacturing for Export as a Percentage of all <i>Manufacturing Workers.</i>	Workers for Export as a Percentage of the Whole Occupied Population.
1907	44.5	...
1924	39.4	29.6
1929	38.4	27.4
1930 (2nd quarter) ...	33.8	23.5

The following table gives the figures on which Table I is based :—
(Figures in thousands.)

—	Workers Employed by Export Trades.		Total Engaged in Mining and Manu- facture.	Total Engaged in Building, Distribution Services, &c.
	(i) Manu- facture.	(ii) Trans- port and Distribution.		
1907	2,465	300	5,550	3,700 approx.
1924	2,485	325	6,315	3,200
1929	2,445	350	6,375	3,815
1930 (2nd quarter)...	2,000	285	5,905	3,915

TABLE 2.

REAL WAGE AND PRODUCTIVITY CHANGES SINCE 1924.

The following table examines in detail the factors relating to the rise in real wages since 1924. It will be seen that, on the whole, physical volume of output per head has risen faster than real wages, which have been held back by the fact that retail prices have fallen more slowly than wholesale. There has been some rise in the ratio of wage-costs to proceeds. The figures in the table refer to manufacture and mining.

Sources: *Board of Trade Index of Production.*

Employment estimated by method given in *Journal, Royal Statistical Society, 1929, Part I.*

Real wages from Professor Bowley's Index and Ministry of Labour Cost of Living Index.

Selling value of manufactured goods from average values of British exports.

Money value of net output from above index of selling prices and Sauerbeck index for raw materials, assuming 30 per cent. of selling value represented by raw materials in 1924 (*Vide Flux, A.W., "The National Income" in Journal, Royal Statistical Society, Vol. 92, Part I, 1929.*)

Year.	Persons Employed (000's).			Output Index.			Output per head.			Real Wages.	Index of Selling Value Manufactured Goods.	Index of Margin between Manufactured Goods and Raw Materials.	Money Value of Net Output per Man.	Money Wages.
	Manu- facture.	Mining.	Distri- bution, Trans- port, Building Services.	Manu- facture.	Mining.	General.	Manu- facture.	Mining.	General.					
1924... ..	5,220	1,093	3,229	100	100	100	100	100	100	100	100	100	100	100
1927... ..	5,470	840	3,693	109.3	95.0	106.8	104.3	123.8	106.8	105	86.5	86.0	91.7	100.7
1928... ..	5,463	771	3,767	109.4	89.2	105.5	104.5	126.4	106.8	105	86.3	86.8	92.6	99.7
1929... ..	5,547	829	3,815	115.1	96.8	111.8	108.2	126.3	110.7	106	84.0	86.8	96.1	99.1
1930... .. (1st quarter)	5,316	861	3,835	113.2	102.0	110.9	111.2	131.3	113.2	107	82.0	86.0	97.5	98.7
1930... .. (2nd quarter)	5,145	758	3,845	107.5	87.4	103.4	109.3	126.1	110.4	110	80.5	85.8	95.8	98.3

TABLE 3.

EMPLOYMENT, OUTPUT PER HEAD, ETC., IN MAIN INDUSTRIAL GROUPS, 1924-1929.

The following table examines in further detail the rise in productivity per head since 1924. Current value of net output is calculated for each group of industries on the assumption that net output is proportional to gross output.

Sources: Board of Trade Index of Production. Employment calculated from annual figures published by Ministry of Labour. Output per head from above two. Selling prices from average value of exports (except for coal and iron and steel where Board of Trade price indexes are used directly).

	Volume of Employment. (Thousands.)				Physical Volume of Output. 1924 = 100.				Output per Worker. 1924 = 100.			
	1924.	1927.	1928.	1929.	1924.	1927.	1928.	1929.	1924.	1927.	1928.	1929.
Coal mining	1,093	840	771	829	100·0	94·0	89·0	96·4	100·0	122·4	126·2	127·1
Iron and steel	245·0	235·8	227·5	231·5	100·0	110·0	102·3	114·0	100·0	114·3	110·2	120·6
Engineering and shipbuilding (including motors and electrical trades).	1,158	1,118	1,206	1,243	100·0	115·2	113·1	120·9	100·0	112·2	115·7	115·6
Textiles	1,088	1,155	1,138	1,130	100·0	101·6	99·9	98·5	100·0	94·7	95·5	94·8
Food, drink and tobacco	476·6	497·5	496·3	498·3	100·0	99·7	101·9	106·0	100·0	95·5	97·8	101·4
Leather and boots	179·1	180·8	165·6	165·0	100·0	107·7	102·0	98·5	100·0	106·7	110·4	106·9
Chemical and allied trades.	183·8	192·7	202·9	205·3	100·0	105·2	110·3	112·5	100·0	100·4	99·9	100·8
All industry	6,324	6,338	6,242	6,359	100·0	106·8	105·5	111·6	100·0	106·6	106·9	111·1

	Index of Selling Prices, 1924 = 100.				Output per Worker. (£ per annum at <i>Current</i> Prices.)				Annual Earnings. (Average per Worker.)	
	1924.	1927.	1928.	1929.	1924.	1927.	1928.	1929.	1924.	1928.
Coal mining	100·0	86·1	75·5	90·0	175	185	171	186	123	97
Iron and steel	100·0	84·3	78·7	77·5	228	219	197	211	153·1	151·1
Engineering and shipbuild- ing (including motors and electrical trades.)	100·0	96·0	96·1	94·1	214	231	238	232	131·3	135·5
Textiles	100·0	79·5	84·4	81·7	178	136	144	138	84·7	84·8
Food, drink and tobacco	100·0	86·8	88·9	81·9	371	306	323	308	105·3	105·5
Leather and boots ...	100·0	99·8	117·2	109·4	190	200	245	222	115·7	111·7
Chemicals and allied trades.	100·0	89·8	85·0	82·1	380	342	321	314	131·5	135·5
All industry	100·0	87·2	86·7	85·0	218	204	203	206	120	117

TABLE 4.

EARNINGS AND PRODUCTIVITY IN CERTAIN INDUSTRIES, 1907-1924.

The following table is designed primarily to show for certain important industries the rise in *money* wages since pre-war days as compared with the *money* value of net output per head. The division of the proceeds of industry between wages and profits is thus shown directly without the necessity of calculating "real" wages and "physical" productivity per head.

Sources: *Census of Production Preliminary Reports*. Earnings and Hours Enquiries, 1907, 1924, 1928. Selling prices index calculated from Census of Production Reports.

	Net output per Person Employed (£ per Annum).		Average Annual Earnings (£ per Annum).			Average Weekly Hours.		Earnings as Per Cent. of Net Output.		Selling Prices (1907=100).
	1907.	1924.	1906.	1924.	1928.	1906.	1924.	1906-7.	1924.	1924.
Coal	127	175	86	123	97	8 per shift	7 per shift	68	70	211
Iron and steel	115	218	82	155	153	54.5	44.8	71	71	158
Engineering	109	199	68	123	129	53.0	47.0	62	62	—
Shipbuilding	98	164	71	131	130	52.9	47.0	73	80	137
Motor and cycle	109	226	68	144	153	53.4	47.0	62	69	90
Cotton	79	159	48	93	93	55.5	47.9	61	58	251
Wool	71	187	40	102	99	55.6	48.0	56	55	280
Silk and artificial silk	55	255	34	99	103	54.5	48.0	62	39	—
Hosiery	61	159	39	88	94	33.9	47.6	64	65	258
Textile finishing	109	251	55	126	125	55.7	48.0	51	50	248
Clothing	62	151	35	70	72	51.7	46.2	56	46	256
Boot and shoe	71	170	47	115	110	53.6	47.8	66	68	179

Grain milling	178	341	61	139	138	58.1	46.7	34	41	158
Baking	104	254	54	119	116	55.5	48.6	52	47	167
Brewing... ..	325	685	63	136	135	54.9	47.9	19	20	213
Tobacco... ..	155	617	35	108	116	49.6	47.1	23	18	295
Brick	78	209	56	126	126	55.4	48.5	72	60	—
Pottery	68	156	48	98	97	52.5	46.9	71	63	—
Chemicals	183	369	63	134	139	54.7	48.1	34	36	178
Rubber	124	247	52	112	114	55.0	47.7	42	45	—
Printing... ..	108	294	59	151	154	51.5	47.3	55	51	—
Furniture	85	196	63	129	133	53.1	46.7	74	66	—
Laundry	55	136	33	78	—	54.0	47.0	60	58	—
Building	84	205	68	147	147	53.2	45.3	81	72	—
Gas	205	272	78	152	158	52.6	48.5	38	56	—
Water	411	509	70	146	149	55.1	47.5	17	29	—
Electricity	249	472	74	163	170	51.9	47.3	30	34	—
All industry (manufacture and mining)	100	220	52	120	117	54 approx.	47.1	52	55	193

TABLE 5.

PHYSICAL VOLUME OF OUTPUT PER HEAD, 1907 AND 1924.

The following table gives the results of a calculation designed to secure some measure of changes in the net output of industry expressed in an unchanging money standard. The materials of industry and the final produce of industry are obtained free of duplication and correctors applied to the 1924 figures in accordance with the rise in prices of raw materials and finished goods respectively. By subtraction, the "real" net output is obtained.

—	Value 1907. (£ million.)	Value 1924. (£ million.)	Prices 1924. (1907=100.)	1924 at 1907 Values.
Final product	1,139	2,478	190	1,304
Materials	464	848	175	484
Net output	675	1,630	—	820

This shows a rise of 21½ per cent. of "real" aggregate net output as against a rise of 10½ per cent. in the number of workers between 1907 and 1924. *But there are no statistical data as to the increase of capital which has assisted in bringing this about and which needs to be remunerated out of the product.*

Sources: Reports of Census of Production 1907 and 1924. Value of raw materials in 1924 from Flux *loc. cit.* Prices of finished goods calculated from average values in Census of Production.

INDEX TO REPORT AND ADDENDA.

(Numbers refer to paragraphs.)

Acceptances:

- on Foreign account:
 - Statistics of, 1927 to 1931, 93, 260, 261.
 - Volume of, fluctuation, 349.
 - Statistics, recommendation *re*, 414.

Accepting Houses:

- Foreign deposits, connection with accepting business, 92.
- Functions and procedure of, 88-92.

Agriculture, growing rationalisation of, 139.

Balance of trade:

- Annual figures published by Board of Trade, recommendation *re*, 417.
- Changes in, 1913 and 1930, 100.
- Effect of bank rate on, 215.
- Effects of fall in raw material prices on, 264, 265.
- Strengthening of:
 - Means of, Add. I, 12-45 (p. 193-203); Add. II, 2-6 (p. 211-4).
 - Need for, 426, Add. I, 6 (p. 191), 9 (p. 192); Add. II, 1 (p. 210-1), 7 (p. 215).

Bank Act of 1844, 50, 52-4, 57, 320, 322.

Bank of England:

- as Authority for management of currency, recommendation, 281.

Bank Notes, *see that title*.

Bankers' deposits:

- Average amount in 1930 and comparison with U.S.A., 370.
 - Average annual amounts, 1919-1930, 77, 79, 367, 368.
 - Control over amount of, by Bank of England, 71, 97.
 - Fluctuations in, 1928 and 1929, 167, 168.
 - Percentage of banks' deposits, recommendation *re*, 370.
 - Substitution of, for note holdings, 342-345.
- "Bankers' Deposits," and "Other accounts," accounts included, 65.
- Bankers' Industrial Development Company, separation from, proposal, 403.

Banking Department:

- Amalgamation with Issue Department, recommendation, 337-340.
- Assets of, 66
- Liabilities of, 63-65.
- Notes held in, 62, 66, 67.
- Reserve, fluctuations in, 1928 and 1929, 167, 168.

Bank of England—*cont.*

Banking Department—*cont.*

- Separation from Issue Department:
 - by Act of 1844, 53, 54, 320, 330.
 - no general Advantage from, 331-336.

as a Convenience for calculating profits of note issue, 331.

Capital, increase in, 370

Consultation and co-operation between banks and, closer contact, recommendation, 364, 371-374, Add. I, 5 (p. 191).

Control of credit by, and factors determining amount of, 87, 96, 358.

Day-to-day policy of, 356-364.

Discount market, relations with, 95.

Foundation of, 50.

Gold holdings, or equivalent in foreign exchange, increase desirable, 329.

Gold reserve:

Amount:

greater Freedom *re*, subject to statutory minimum, proposal, 323-329.

Minimum, 67.

Movements in, from 1926, 166, 167, 171.

"Government Securities," nature of, 66.

Issue Department, *see under* Banking Department *above*.

Issuing houses, contact with, 363.

Joint stock banks:

Connection with, through discount market, 72, 98.

Relations with, 371-374.

Liquid assets, amount:

wide Fluctuations in aggregate of, approved, 352, 353, 354.

Increase recommended, 352, 354.

Management of monetary system, means of, 356-364.

Money market, contact with, 362.

Open market operations, 63-71, 356, 358, 359.

"Other Securities," nature of, 66.

Payment to Treasury, proposed system, 337.

Policy of, factors affecting, since 1925, 170-172.

Powers of issue of bank notes, 52-61.

Resources of, 347-355.

Foreign liquid resources, proposal, 354.

Increase, recommendation, 354, 370.

Restrictions on, 51.

Retail sales, index of, 420.

Bank of England—cont.

Statistical information, collection and publication by:

Acceptances, recommendations *re*, 414.

Foreign balances and liquid assets held in sterling, recommendation *re*, 413.

Monthly bulletin of statistics, recommendation, 416.

Weekly return, proposed form of, 338-339.

Bank for International Settlements, balances with, reckoning of, as equivalent of gold, proposal, 346.

Bank Notes:

Bank of England depots for supply of, proposal, 343.

Fiduciary issue:

under Act of 1844, 53, 322.

Amount:

Alteration:

Effect on allocation of profits between Treasury and Bank, 332-5.

Provision for, 59, 320, 325, 326, 332.

under Currency and Bank Notes Act, 1928, 58.

Fixed amount, criticism of principle of, 323-326.

greater Freedom *re*, subject to statutory maximum, proposal, 322-329.

Cunliffe Committee recommendations, 57, 58.

Extension, under Currency and Bank Notes Act of 1914, 56.

Securities held against, 61.

Held by joint stock banks, proposal for reduction, 341-345.

Issue of:

Bank of England powers, 52-61.

by Private banks, former rights of, 52, 53.

Northern Ireland, issue by certain banks, 60.

Scottish banks, issue by, 60.

Bank Rate:

Bank rate policy:

and Gold movements, 219.

Limitations to usefulness unless supplemented, 218-21.

greater Publicity *re*, desirable, 218.

Working and effects of, 214-227.

Changes in:

in relation to Costs of production, 215.

Effects of:

on Credit, 215, 222-223.

on Enterprise at home, 215-227.

on Foreign exchanges, 215,

on Gold reserves, 215.

Bank Rate—cont.

Changes in—cont.

Effects of—cont.

on Investment abroad, 215.

on Investment securities, price and yield, 48.

on Prices, 215.

on Purchasing power, 215.

on Rates for short money and bank loans, 70.

Operation of, 68-70.

in relation to Wages, 215, 221.

Movements of, from April, 1927, 167, 171.

Use of, policy recommended *re*, 352, 355, 357.

Bankers' Industrial Development Company, separation from Bank of England, proposal, 403.

Banks, Central, *see* Central Banks.

Banks, Commercial:

Advances:

Ability to grant, connection with provision of necessary cash base by Bank of England, 87.

Demand for, 86.

Proportions of, to deposits, 1919 to 1930, 81, 83.

Assets, proportions of, to deposits, 80, 81, 82-84.

Assistance of industry:

Co-operation in institutions for, 403.
in Financing long term contracts, 316.

Short-dated credits, facilities, 391.

Balances at Bank of England, *see* under Bank of England.

Bills, proportions of, to deposits, 1919 to 1930, 81.

Cash, forms in which held, 22, 76.

Cash in hand:

Annual average amounts and percentages of, to deposits, 1919-1930, 77-79, 367, 368.

fuller information to Bank of England desirable, 358.

Percentage of deposits, and recommendation *re*, 71, 370.

Cheque transactions, statistics, recommendation *re*, 415.

other than Clearing banks:

Cash balances, recommendation *re*, 370.

Statistical returns from, recommendation *re*, 411.

Connection of Bank of England with, through discount market, 72, 98.

Consultation and co-operation between Bank of England and, closer contact, recommendation, 364, 371-374, Add. I, 5 (p. 191).

close Co-operation with industries, importance of, 383-404.

Banks, Commercial—cont.

Deposits:

Division of, into current accounts and deposit accounts:

1919 to 1930, 81.

fuller Information to Bank of England desirable, 358.

Factors affecting level of, 84-87.

Increase of, by loans and investments made by banks, 74, 75.

Ratio between cash and, and recommendation *re*, 71, 370.

Foreign deposits, use of, for financing home trade, 92.

Investments, proportions of, to deposits 1919 to 1930, 81.

Lending capacity of, factors affecting, 22.

Loans:

Classification, periodical return, recommendation, 410.

Proportion of, to deposits, 81, 83.

Money at call, etc., proportions of, to deposits, 1919 to 1930, 81.

Monthly returns:

Form of, recommendation *re*, 370, 409.

Returns of cash in hand and of balances with Bank of England, should be true daily averages, 370.

Notes held by, proposal for reduction, 341-345.

Overdrafts, *see* Loans *above*.

Relations with Bank of England, 371-374.

Relations with industry in other countries, 378-81, 390.

Reserves:

Alteration of, on initiative of Bank of England, recommendation, 370.

Centralisation of, 29.

and Supply of credit to industry, 223-228.

“Window-dressing,” practice of, and abolition recommended, 368-370.

Bills, commercial, extended use of, desirable, 391.

Bills of Exchange:

Development of system, 21.

Sterling bills held on foreign account, statistics of, 1927 to 1931, 93, 260, 361.

Budget, effect of fall in prices on, 200-203.

Capital construction, collection of statistics, recommendation, 422.

Capital development schemes, as a remedy for present position, considerations *re*, Add. I, 46-51 (p. 203-8), p. 210, Add. II, 8 (p. 215-6), Add. III, 14 (p. 229-30).

Capital Market:

Organisation more favourable to foreign investment than to British industry, 397.

Special organisation for assistance of industry, need for, and requirements, 397-404.

Census of Production, *see under* Production.

Central banking, development of, 28.

Central Banks:

Constitution, 32, 33.

Control over volume and terms of bank credit, 29, 301-305, 306.

Credit policy, international limitations, 240, 241.

Encouragement of foreign loans by creditor countries, proposed policy, 315-318.

Functions of, 29-34.

Gold policy, recommendations of League of Nations Delegation and support of, 149, 289-291.

Gold reserves, object of, 152, 288.

Influence upon price level, 48.

Liabilities, ratio between gold supplies and, 148, 288, 289.

“Management” of currency systems:

Difficulties involved in, 296-300.

Necessary in greater degree, 295.

proposed Policy with view to stability of international price level, 287-91, 292-95, 306-307.

Relations with State, 30, 33.

Reserves:

Concentration of all monetary gold in, desirable, 149, 288, 289.

Economy of gold by reduction of reserve ratios, 149, 289.

Requirements, 34.

Cheques:

Development of use of, and effects of, 55.

Transactions, statistics, recommendation *re*, 415.

Contracts abroad, long-term, credit requirements and facilities, 393, 396.

Credit:

Control:

by Bank of England, 96.

by Central Banks, 29, 301-305, 306.

Creation of, by Bank of England, factors guiding policy *re*, 87, 358.

Demand for, means of stimulating, Add. I, 6-11 (p. 191-3).

Effect of changes in bank rate on, 215, 222-223.

Expansion of, for domestic purposes, limitations on, Add. 1, 2-6 (p. 190-1).

Credit—cont.

Expansion and contraction of:

Effects:

- on Investment, 237-239.
- on Output and employment, 215, 218, 221, 223-230.
- on Price level, 24, 97, 214-241.

International limitations, 240, 241.

Intermediate:

Classes of transactions requiring, 393.

Facilities, 394-396.

Reduction of cost, effect on investment, 231-236.

Short-term, facilities, 391.

Credit Cycle, 280, 301, 303, 357.

Creditor countries:

Action for restoration of international price level, proposal, 309-318.

Gold stocks, 1929-1931, 311, 312.

Redistribution of lending power, 246, 247.

Cunliffe Committee, recommendations, 57, 58.

Currency and Bank Notes Act of 1914, 56, 57.

Currency and Bank Notes Act of 1928, 58, 59, 60, 62, 96, 320, 325-6.

Currency management:

by Central Banks:

Difficulties involved in, 296-300.

Necessary in greater degree, 278, 295.

Domestic:

Bank of England as authority for, recommendation, 281.

Means of, 282, 356, 364.

Need for, 280.

Currency notes:

Amalgamation of issue with bank note issue, 57, 58.

Issue by Treasury, 56.

Devaluation:

a Means of adjusting money-incomes, but not recommended, Add. I, 32, 33 (p. 199), p. 209-10.

Rejection of, 255-257.

Discount Market:

Bank of England and, 72, 95, 98.

Composition of, 94.

Resources of, 92, 94, 95.

Employment:

see also Unemployment.

Effect on:

of Expansion of investment at home, Add. I, 46-51 (p. 203-8).

of International investment, 176.

of Price changes, 193, 197, 268, 269.

Statistics, 1924 to 1930, 107.

Export trade:

see also Balance of Trade.

Aids to, and control of imports as remedy for present situation, Add. I, 39-45 (p. 200-3).

Bounty on, and duty on imports:

Consideration of, as remedy for present position, Add. III, 15-19 (p. 230-4).

as Means of adjusting money-incomes Add. I., 34-37 (p. 190-200).

Factors affecting volume of, 119-125.

Increase, means of, Add. I, 9-11 (p. 192-3).

Position in 1913 and 1929, Add. III, 7 (iii) (p. 223).

Foodstuffs, production, world increase of, 129-131, 134, 135, 136.

Foreign balances and liquid assets held in sterling, statistical information, recommendation re, 413.

Foreign deposits:

in London:

Growth of, 349 (iii).

Statistics of, 1927 to 1931, 93, 260, 261.

Use of, 92.

in U.S.A., 349 (iv).

Statistics of, 1927 to 1930, 262.

Foreign exchanges:

Effect of changes in Bank rate on, 215.

Forward, 360.

Maintenance of parity of, primary object of gold standard, 39.

Foreign investment, *see under* Investment.

Foreign loans, *see* Foreign *under* Investment.

France:

Banks, relations with industry, 379, 390.

Gold flow into, 163-166, 170.

recent Monetary policy, 163-165.

Position in 1930, 298.

Germany:

Banks, relations with industries, 378, 390.

Economic position, effect of international investment on, 179.

Gold:

Demand and supply, problem of, 144-7.

Distribution, problems connected with, 151-154.

Gold—cont.

- Industrial consumption and hoarding, 145.
- League of Nations Delegation, 140, 144, 146, 149, 289.
- Monetary, future requirements, estimate, 146.
- Movements:
 - Bank rate policy and, 219.
 - Effects, 135.
 - Policy and reserves of Central Banks, *see under* Central Banks.
 - Production, future, probable diminution, 144, 145.
- Reserves:
 - of Bank of England, *see under* Bank of England.
 - Effect of changes in bank rate on, 215.
 - sole Use to meet temporary deficiencies in balancing international payments, 324, 339-340.
- Shortage in future, possible remedial measures, 147-150, 288-289.
- Stocks:
 - Amount and distribution, changes in, since 1913, 141-143.
 - in Central Banks and Treasuries of creditor countries and of debtor countries, January 1st, 1929-1931, 311, 312.
- Supplies, relation to stability of price level, 148.
- old exchange standard, 295.
- old points, widening of, 360.
- old standard:
 - Abandonment of, in other countries, 15.
 - Automatic operation of, pre-war, 295.
 - Devaluation, rejection of, 255-257.
 - Explanation of, 36-38.
 - International standard, adherence to, 251-254, 285.
 - Post-War changes in, 292-295.
 - Primary objective of, 39, 40.
 - Return to, 13, 14.
 - Disequilibrium between costs and prices, accentuation of, 113.
 - Effect on costs of production, 123-4.
 - Secondary objectives of, 41-45.
- Working of: 156-173.
 - Central Banks, co-operation in regard to gold reserves, 288-91.
 - Conditions necessary for, 46-48.
 - Effect of financial policy in U.S.A. and France, 156-167, 170, 171.
 - in Future, 173-174, 259-65.
 - International co-operation, need for, 258.
 - Recently, 128, 242-250.
- old Standard Act of 1925, 322.
- ire purchase, credit facilities, 393-395.

Imports:

- Control of, and aids to exports as remedy for present situation, Add. I, 39-45 (p. 200-3).
- Duty on, *see* Tariffs.
- Restriction, as means of strengthening balance of trade, Add. II, 6 (p. 214).
- Income, distribution of, effect of price changes on, 190, 191, 196, 269, 271.
- Industry and Trade:
 - Adaptation of war-distended industries to peace conditions, problem of, 110.
 - Balance of trade, *see that title*.
 - Cycle of, 301, 303.
 - Depression:
 - Disequilibrium between demand and supply, 126-139.
 - Fall in prices as factor, 190-197.
 - Survey of problem, 99-125.
 - and Unemployment, general position, 12-17.
 - Effect of international investment on, 176.
 - Financial assistance, State guarantee, need for, but should be dependent on rapid reorganisation, Add. IV, 4 (p. 238).
 - Reorganisation:
 - Labour co-operation, need for, Add. III, 2 (p. 234).
 - Trade Union co-operation, need for, Add. IV, 5-7 (p. 238-9).
 - Retail sales, Bank of England index of, and recommendation *re*, 420.
 - Selling and distributive methods, need for adaptation to new circumstances, Add. IV, 2, 3 (p. 238).
 - Technical efficiency, comparison with that of competitors, 121.
- Information, *see* Statistics and Information.
- Instalment purchase, credit facilities, 393-395.
- Interest, rates, variation of, by banks according to Bank rate, 70.
- International co-operation:
 - see also* Central Banks, Gold and Gold Standard.
 - between Creditor countries in foreign investment, need for, and prospects, 314, 315.
 - Importance of, 220, 240-1, 253, 284, Add. III, (p. 218).
- International investment, *see under* Investment.
- International loans, *see* International *under* Investment.

International long-term lending, diminution of, 15.

International trade, growth of, 131.

Investment:

At home:

1928 experience, 386.

Expansion of, effect on employment, Add. I, 46-51 (p. 203-8).

Guidance of investors, need for, 386-9.

Foreign:

Annual surplus for new long-term investment, reduction in, 349 (v).

in British-owned enterprises, desirability, 384.

by Creditor countries, increase desirable, 315.

Effect of changes in bank rate on, 215.

Financing of, out of income in short term liabilities, 259, 350-351.

Increase of surplus available for, desirable, 258.

Issuing houses, responsibility of, 387.

Influence of banking system on, 231-239, 282.

International:

Affecting raw material producing countries, 180.

Connection with gold movements, 183-185.

Effect on employment, 176.

Effect on trade, 176.

Encouragement of, proposed policy, 309-319.

and Government guarantees, 319.

and International disequilibrium, 183-85.

Loans by U.S.A. and Great Britain, statistics, 1928 and 1929, 182.

Process of, 175-182.

Redistribution of lending power of creditor countries, 246, 247.

Price and yield of securities, effect of changes in bank rate on, 48.

Relation of falling prices to, 198, 199.

Restriction of, 15.

Issuing Houses:

Contact with Bank of England, 363.

Responsibility of, in connection with foreign investment, 387.

League of Nations, Gold Delegation, 140, 144, 146, 149, 289.

London money market, characteristics of, 375-7.

Monetary systems, general characteristics of. 18-34.

Money-incomes:

Adjustment, need for, and means of, 221, 245, 272, Add. I, 26-33 (p. 198-200).

Elasticity in, need for, Add. I, 12, 13 (p. 193-4).

National Debt, importance of raising international price level in relation to, 270.

Note issues:

see also Bank Notes and Currency Notes.

Monopoly of Central Banks, 29.

Paper money, development of use of, 21.

Prices:

Adjustment of costs of production to, need for, Add. III, 4-6 (p. 218-22), 7 (p. 224).

Changes in, effects of:

on Distribution of income, 190, 191, 196, 269, 271.

on Employment, 193, 197, 268, 269.

on Profits, 190, 191, 268, 271.

on Wages and salaries, 193, 194.

Disequilibrium between costs and, effect of return to gold standard, 113.

Effect of changes in bank rate on, 215.

Fall in:

Consequences of, 190-197.

Effect of, on public finance, 200-204.

Monetary and non-monetary factors as cause of, 205-210.

Raw material prices, effect on balance of trade, 264, 265.

Recent, connection of distribution of gold with, 151, 291.

Falling, relation of, to investment, 198, 199.

International price level:

recent Fall in, 15.

Raising of:

Feasibility, and need for co-operation between Central Banks, 277, 278.

immediate Necessity, 286-273, 275, 276, 285, Add. II, 9 (p. 216).

Restoration of:

Action by creditor countries proposed, 309-318.

Measures necessary, 308-319.

Stabilisation at present level, avoidance advocated, 267, 268.

Stability:

Central Banks, proposed policy for maintenance of, 287-91, 291, 295, 306-7.

Long period policy recommended 274-276, 285.

Prices—cont.

International price level—cont.

Stability—cont.

Means of control by Central Banks, 301-305, 306.

main Objective of Central Banks to maintain, 286-307.

Obstacles facing Central Banks, 296-300.

Price level:

Control of:

Credit policy and, 214-241.

Task of monetary system, 211-213.

Effect on, of creation of credit, 24, 97, 214-241.

Increase in power to exercise deliberate control over, desirable, 210.

Influence of Central Banks upon, 48.

Instability:

Effects, 293.

Factors making for, 24.

International, *see* International price level *above*.

Movements, control of, as secondary object of gold standard, 41-45.

Stability, factors affecting, 41-45, 148.

Wholesale:

Changes, lag in changes in retail prices, 187-189.

Fall in, 1924-1931, 186, 188.

Movements of, 1924-1931, and comparison with movement of cost of living index, wages and industrial production, 187-189.

Production:

Census of:

at more Frequent intervals, recommendation, 418.

Publication of results, delay in, 418.

Scope, extension, recommendation, 418.

Changes in rate of growth of demand, 138.

Control, schemes of, 136.

Costs of:

Adjustment of, to prices, need for, Add. III, 4-6 (p. 218-22), 7 (p. 224).

Bank rate changes in relation to, 215.

Causes of changes relative to costs abroad, 121-123.

Effect on, of return to gold standard, 113, 123-4.

Reduction:

greater Efficiency as means of, Add. II, 4 (p. 212-3).

Importance of, Add. II, 2, 3 (p. 211-2).

as Remedy for present position and considerations *re* effect on wages, Add. III, 20-23 (p. 234-7).

Production—cont.

Increase in, in aggregate and per head between 1924 and 1930, Add. III, 7 (p. 222).

Increase in relation to demand, effects of, 133-137.

Indices of, 132.

Output per head per hour, 1924 and 1929, 121.

Raw materials and foodstuffs, increase of, in Europe and U.S.A. 129-131.

Profits:

Effect of price changes on, 190, 191, 268, 271.

Survey of, and annual publication of figures, recommendation, 421.

Public finance, effect of fall in prices on, 200-204.

Raw materials:

Prices, fall in, effect on balance of trade, 264, 265.

Production, world increase of, 129-131, 135-136, 137.

Reparations and Inter-Allied debts, fresh settlement of problem, need for, Add. II, 10 (p. 216-7).

Salaries, *see* Wages.

Silver, fall in value of, 111.

Stable exchanges, maintenance of, effects, 220.

Statistics and information:

Acceptances, recommendations *re*, 414.

Bank of England, *see that title*.

Banks, *see that title*.

Capital construction, recommendation, 422.

Census of Production, *see under* Production.

Collection of, compulsory power in case of need, recommendation, 424.

Deposits, sterling, statistics of merchant bankers, foreign institutions, etc., recommendation, 412.

Foreign balances and liquid assets held in sterling, recommendation *re*, 413.

Government Statistical Departments:

Co-ordination of work, need for, 423.

Strengthening of, 406.

Importance of, 405. 425.

present Position, 406.

Profits, recommendation, 421.

Retail sales, Bank of England index of, and recommendation *re*, 420.

Wages, 419.

Tariffs:

Duty on imports and bounty on exports:

Consideration of, as remedy for present position, Add. III, 15-19 (p. 230-4).

as Means of adjusting money-incomes, Add. I, 34-37 (p. 199-200) (p. 230).

Foreign:

Exploitation of, for protective purposes, growth in, 139.

Influence on British trade, 139.

as Remedy for present situation, Add. I, 39-45 (p. 200-3), p. 210, Add. II 6 (p. 214).

Trade, *see* Industry and Trade.

Treasury Bills, volume of, in the market, 349.

Unemployment:

Causes, 109-13, 197.

Fall in prices, effects, 193, 197, 268, 269.

Fluctuations in percentage of, 1922 to 1930, 103-105.

National loss from, 14,

Problem, nature of, 106-10.

Spread of, in other countries, 15.

United States of America:

Acceptances on foreign account:

Statistics of, 1927 to 1930, 261, *foot-note*.

Volume of, fluctuation, 349.

Banks, relations with industry, 330-1, 390.

Boom conditions and monetary policy, 1928-29, 158-163, 169-170, 172, 173, 174.

Deposits and bills held on foreign account, 1927 to 1930, 261, *foot-note*.

United States of America—cont.

Federal Reserve System:

Deposits of member banks, 343, 365, 370.

Policy of, 157-162.

Foreign deposits, 349 (iv).

Statistics of, 1927 to 1930, 262.

Foreign investment, attitude towards, 156, 157, 159, 177-178, 182.

Gold stocks, 141, 142, 156-158, 162.

Wages:

Bank rate changes in relation to, 215, 221.

Effect on, of price changes, 193, 194.

Effect on, of reduction in costs of production, considerations *re*, Add. III, 20-22 (p. 234-6).

Money rates, 114-116.

Real:

Comparison with those paid by European competitors, 129, 121.

Movement of, 1924 to 1931, 114-117.

Reductions:

as Means of maintaining and strengthening balance of trade, Add. II, 5 (p. 213).

as Remedy for international slump Add. I, 10, 11 (p. 192-3), 14-19 (p. 194-5), 53 (p. 208).

Adjustment of money-incomes necessary in combination with, Add. I, 26-30, (p. 198), 53 (p. 208).

Statistics of pay roll:

Present position, 419.

Recommendation, 419.

Ultimate level of, Add. I. 20-25 (p. 196-8).

average Weekly, index numbers, 1924, 1928-1931, 187.

War debts, internal, importance of raising international price level in relation to, 270.



Committee on
National Expenditure
REPORT ②

*Presented to Parliament by Command
of His Majesty, July, 1931*

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COMMITTEE ON NATIONAL EXPENDITURE.

TABLE OF CONTENTS.

	PAGE
MINUTE OF APPOINTMENT	4
REPORT.	
APPOINTMENT	5
CHAPTER I—INTRODUCTION :—	
1. RETRENCHMENT AND EXPANSION SINCE THE WAR	5
2. ESTIMATED EXPENDITURE IN 1932 AND 1933	8
3. FUTURE LIABILITIES GENERALLY	10
4. FACTORS, POLITICAL AND ECONOMIC, IN THE PRESENT SITUATION	12
5. THE TASK BEFORE THE COMMITTEE	14
6. THE NATIONAL EXPENDITURE CONSIDERED IN MORE DETAIL	17
7. THE ARRANGEMENT OF THE REPORT	19
CHAPTER II—CIVIL SERVICE ADMINISTRATION	21
CHAPTER III—PAY AND PENSIONS	24
PAY :—	
1. CIVIL SERVICE (<i>excluding Industrial Employees</i>)	27
2. CIVIL SERVICE (<i>Industrial Employees</i>)	35
3. FIGHTING SERVICES	36
4. POLICE	42
5. TEACHERS	46
PENSIONS :—	
1. EXISTING PENSIONERS	51
2. FUTURE PENSIONS	52
3. GENERAL CONSIDERATIONS ON PENSIONS	54
CONCLUSION ON PAY AND PENSIONS	58
CHAPTER IV—DEFENCE	60
1. NAVY	77
2. ARMY... .. .	84
3. AIR FORCE	87
CHAPTER V—DEVELOPMENT	93
1. RESEARCH	99
2. ROAD FUND	103
3. DEPARTMENT OF OVERSEAS TRADE	108
4. RELIEF OF RATES ON INDUSTRY AND AGRICULTURE	110
5. MINISTRY OF AGRICULTURE AND FISHERIES	110
6. DEPARTMENT OF AGRICULTURE (SCOTLAND)	121
7. DEVELOPMENT FUND	122
8. BEET SUGAR SUBSIDY, GREAT BRITAIN	125
9. FORESTRY COMMISSION	127
10. EMPIRE MARKETING BOARD	131
11. COLONIAL DEVELOPMENT FUND	133
12. COLONIAL AND MIDDLE EASTERN SERVICES	134
13. UNEMPLOYMENT GRANTS COMMITTEE	136
14. DEVELOPMENT (PUBLIC UTILITY) ADVISORY COMMITTEE	140

	PAGE
CHAPTER VI—SOCIAL SERVICES	142
1. UNEMPLOYMENT INSURANCE	145
2. NATIONAL HEALTH INSURANCE	153
3. MATERNITY SCHEME	159
4. OLD AGE AND BLIND PERSONS' PENSIONS (NON-CONTRIBUTORY)	161
5. WIDOWS', ORPHANS' AND OLD AGE CONTRIBUTORY PENSIONS	167
6. HOUSING :—	
(a) ENGLAND AND WALES	174
(b) SCOTLAND	185
7. EDUCATION	191
CHAPTER VII—MISCELLANEOUS SERVICES :—	
1. WAR PENSIONS	201
2. BRITISH BROADCASTING CORPORATION	205
3. EXCHEQUER CONTRIBUTIONS TO LOCAL REVENUES	209
CHAPTER VIII—SUMMARY OF RECOMMENDATIONS AND CONCLUSION :—	
1. SUMMARY OF RECOMMENDATIONS	215
2. CONCLUSION... ..	220
RESERVATION BY SIR MARK WEBSTER JENKINSON	225

MINORITY REPORT.

INTRODUCTION	227
1. THE FIELD FOR ECONOMY IN NATIONAL EXPENDITURE	230
2. POST-WAR NATIONAL EXPENDITURE COMPARED WITH PRE-WAR	232
3. CIVIL SERVICE ADMINISTRATION... ..	239
4. PAY AND PENSIONS	239
5. DEFENCE	241
6. DEVELOPMENT	242
7. SOCIAL SERVICES	251
8. MISCELLANEOUS SERVICES	266
9. CONCLUSION... ..	269

APPENDICES.

I. TABLES OF EXPENDITURE	272
II. LETTER ADDRESSED TO THE CHANCELLOR OF THE EXCHEQUER ON AIR-SHIPS	280

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91

COMMITTEE ON NATIONAL EXPENDITURE.

MINUTE OF APPOINTMENT.

TREASURY MINUTE DATED 17TH MARCH, 1931.

The First Lord states to the Board that he proposes to appoint a Committee with the following terms of reference :—

“ To make recommendations to the Chancellor of the Exchequer for effecting forthwith all possible reductions in the National Expenditure on Supply Services, having regard especially to the present and prospective position of the Revenue. In so far as questions of policy are involved in the expenditure under discussion, these will remain for the exclusive consideration of the Cabinet ; but it will be open to the Committee to review the expenditure and to indicate the economies which might be effected if particular policies were either adopted, abandoned or modified.”

The First Lord proposes that the Committee should be constituted as follows :—

Sir George Ernest May Bt., K.B.E. (*Chairman*).
P. Ashley Cooper Esq.
Sir Mark Webster Jenkinson, K.B.E.
Charles Latham Esq.
The Lord Plender, G.B.E., LL.D.
Arthur Pugh Esq., C.B.E.
Sir Thomas Royden Bt., C.H.

My Lords concur. Let the necessary directions be given.

The expenses incurred in preparing this Report are estimated at £500 12s. 10d. of which £425 represents the estimated cost of printing and publication.

COMMITTEE ON NATIONAL EXPENDITURE.

To the Right Hon. Philip Snowden, M.P.,
Chancellor of the Exchequer.

SIR,

APPOINTMENT.

On the 11th February, 1931, the House of Commons passed by 468 votes against 21 a resolution—

“ That this House consider that, having regard to the present burden of Taxation in restricting industry and employment, the Government should at once appoint a small and independent committee to make recommendations to the Chancellor of the Exchequer for effecting forthwith all practicable and legitimate reductions in the national expenditure consistent with the efficiency of the services.”

Following the passing of this resolution, we were appointed on the 17th March, 1931 after consultation between all parties with the following terms of reference—

“ To make recommendations to the Chancellor of the Exchequer for effecting forthwith all possible reductions in the National Expenditure on Supply Services, having regard especially to the present and prospective position of the Revenue. In so far as questions of policy are involved in the expenditure under discussion, these will remain for the exclusive consideration of the Cabinet; but it will be open to the Committee to review the expenditure and to indicate the economies which might be effected if particular policies were either adopted, abandoned or modified.”

We now beg to submit our report on the matters referred for our consideration.

CHAPTER I.

INTRODUCTION.

1. Retrenchment and Expansion since the War.

1. Since 1928, it has been the practice in the expenditure statement in the annual budget to show separately ordinary expenditure, sinking fund, and self balancing expenditure (i.e. expenditure on the Post Office and Road Fund). Ordinary expenditure as thus understood is the expenditure which has to be met from the

national revenue including the profit on the Post Office and the Exchequer's share of the Motor Vehicle Duties. It is only to the extent that revenue exceeds this ordinary expenditure that a balance is available for the redemption of debt. In 1928 certain other adjustments were made in the national accounts designed to eliminate duplicate entries as far as possible. In the table below similar adjustments have been made in earlier years so that all the figures are on a corresponding basis. The table shows the ordinary expenditure for each year since the war, the amount available for the redemption of debt and the net borrowing or repayment of debt by the Unemployment Insurance Scheme.

Year beginning 1st April.	Ordinary Expenditure.			Cash avail- able for Debt Redemption.	Repayments (+) Borrowings (-) on the Unem- ployment Fund.	
	Debt Interest and Manage- ment.*	Other Expenditure.	Total			
	£.	£.	£.	£.	£.	
1921	303,900,000	652,200,000	956,100,000	70,700,000	-13,900,000	
1922	296,600,000	433,900,000	730,500,000	126,200,000	- 2,900,000	
1923	304,300,000	387,100,000	691,400,000	83,300,000	+ 6,400,000	
1924	308,700,000	373,500,000	682,200,000	48,700,000	+ 3,000,000	
1925	Audited Expenditure	304,300,000	397,000,000	701,300,000	36,000,000	—
1926		314,300,000	383,900,000	698,200,000	23,300,000	-17,400,000
1927		309,000,000	378,400,000	687,400,000	65,000,000	+ 400,000
1928		311,500,000	372,500,000	684,000,000	57,500,000	-11,400,000
1929 expenditure as per appropriation accounts.		312,100,000	397,200,000	709,300,000	33,200,000	- 3,000,000
1930 Exchequer Issues.	293,200,000	439,100,000	732,300,000	43,600,000	-36,400,000	
1931 Original Esti- mates.	302,900,000	448,400,000	751,300,000	52,000,000	-40,000,000 to 50,000,000	

* From 1923 onwards interest was paid in full to the U.S.A. Government. In the year beginning 1st April, 1921, about £46,500,000 and in the year beginning 1st April, 1922, about £20,000,000 of interest payments were suspended.

2. From 1921 to 1924 the course of ordinary expenditure was rapidly downwards; from 1924 to 1928 there was no striking change in the total; whilst from 1928 onwards, there has been an abrupt rise, the difference between the audited expenditure for 1928 and the original estimates for 1931 being no less than £67,000,000.

But the figure of £67,000,000 understates the true increase in the national burdens, for the pound sterling is worth more in services and goods in 1931 than in 1928. The Ministry of Labour index of cost of living has fallen from a total index of 164 on 1st April, 1928, to 147 on 1st April, 1931 (July, 1914 = 100): the Board of Trade index of wholesale prices

has fallen between May, 1928, and May, 1931, from 143.6 to 104.4 (1913 = 100). It would be unreasonable to expect that the national expenditure should fall fully in proportion to changes in the price level since it contains many items not responsive to such changes. But some items are affected by falling price levels and to that extent the real increase in Government expenditure is greater than £67,000,000.

3. If account be taken not only of the budget expenditure but also of the loan operations of the Unemployment Insurance Scheme the change in the situation between 1928 and 1931 becomes still more serious, for whereas in 1928 the Scheme borrowed £11,430,000, it is now estimated to need roughly £50,000,000 in 1931. In addition, borrowing to the extent of £9,000,000 is anticipated this year to meet the needs of the Road Fund. Borrowing for the Unemployment Fund alone in 1930 (£36,440,000) almost wiped out the net surplus in the year of £43,600,000. For the current year the total borrowing for unemployment insurance and the Road Fund together is likely to be considerably in excess of the amount available for redemption of debt.

4. The history in broad outline of the main financial decisions taken between 1921 and 1931 throws much light on the above figures. The slump which followed the short-lived post-war boom created a wave of public opinion in favour of economy. This came to a head in the enquiry of the Geddes Committee (which presented its final report on 21st February, 1922), but both before and after this enquiry large reductions were made in expenditure. In 1924, a policy of expansion and development replaced the policy of retrenchment. Additional commitments were undertaken in a number of directions including education, an ambitious housing scheme and extended old age pensions, and a programme of cruiser building which had been for some time under consideration. In 1925, the policy of expansion continued with the grant of Widows' Pensions and the Beet Sugar Subsidy. A further naval building programme was begun and an increased State contribution was provided for the Unemployment Fund. The danger of strife in the coal industry was averted for a time by a heavy subsidy. The items named are given as illustrations rather than as a comprehensive list. New commitments soon reached a large total, and with the prospect of a difficult Budget position in 1926 retrenchment once more came to the front. A White Paper presented to Parliament on 16th March, 1926, showed that estimates in 1926 were likely to exceed the original estimates for 1925 by as much as £34,747,000 of which £24,447,000 was due to decisions of the then Parliament and Government, and £8,250,000 to the development of schemes approved by previous Parliaments and Governments. The balance of the increase, viz. £2,050,000, which

was the net increase shown on a number of items, was largely automatic in character. In so far as the economies then decided upon involved legislation they were embodied in the Economy (Miscellaneous Provisions) Act, 1926, which was estimated to produce a benefit to the Exchequer of from £8,310,000 to £10,160,000 in 1926 and from £7,030,000 to £8,880,000 in 1927. At the moment it appeared that the difficulties of the Exchequer had been surmounted, but the coal stoppage and the national strike that followed had grave reactions both on expenditure and revenue and the pressure for economy continued throughout 1926 and 1927.

5. The economies of these years, however, produced little in the way of continuing reductions of expenditure. A number of the savings made were special measures which from their nature could not be repeated or were merely postponements of expenditure. The largest continuing item, viz. the reduction of the State contribution to the Unemployment Fund made in 1926, as events have proved, reduced the Exchequer charge but only by increasing the borrowings of the Fund to the same extent.

6. After this period, retrenchment was again relegated to the back-ground. The Derating Scheme imposed on the State a heavy burden, consisting partly of relief to certain classes of ratepayers and partly of larger Exchequer grants to local authorities. It should, however, be pointed out that except to the extent that the relief given to local authorities may have led them to increase their expenditure, this scheme was merely a shifting of part of the burden of government from ratepayer to taxpayer and not an addition to the total burden.

7. In 1929, further new expenditure was sanctioned, and a reply given in the House of Commons on 17th November, 1929, stated that the main financial commitments entered into since 1st June, 1929, viz., increased State contribution to the Unemployment Fund, the assumption by the Exchequer of the charge for Transitional Benefit, Widows' Pensions, Agriculture, Forestry, Civil Service bonus concession, proposed raising of school leaving age, Housing, paid holidays to Civil Service industrial staff and concessions on pay and retired pay of Army, Navy and Air Force officers, involved an estimated additional expenditure of £8,243,000 in 1929 and £18,967,000 in 1930. A reply to a Question in the House of Commons on 23rd April, 1931, gave the expenditure involved in commitments entered into by the present Government as £14,086,000 in 1931 in addition to £30,000,000 for transitional benefit under the Unemployment Insurance Scheme.

2. Estimated Expenditure in 1932 and 1933.

8. Any review of the course of expenditure since the War would be incomplete without some estimate of the future liabilities that have been undertaken. Some items are capable of close estimating :

others not, e.g. the large payments to the Unemployment Fund depends on the future course of unemployment. As regards this item, however, it can be said that, if the existing scheme is continued unaltered, any improvement in employment would at first probably make itself felt mainly in a reduction of ordinary benefit from the Fund thus lessening the amount borrowed by the Fund without reducing the Exchequer charge materially. For the purposes of the estimates which follow, we have therefore taken the cost of transitional benefit for 1932 and 1933 at the probable figure for 1931, viz., £35,000,000.

9. On the best estimates we can frame, if existing policies remain unaltered, the total ordinary expenditure in 1932 will be about £12,000,000 and in 1933 about £17,000,000 higher than the original estimates for 1931. These figures, however, include nothing for the schemes of expenditure, some of serious magnitude, now under consideration, whether by the Government or by Parliament. The present position is rather obscure, but we would recall the financial memoranda presented to Parliament in connection with the Education (School Attendance) Bill and the Agricultural Land (Utilisation) Bill. The total annual expenditure from public funds involved in the Education Bill was put at £6,250,000, of which £4,350,000 per annum was to fall on the Exchequer, and the Agricultural Land Bill was drawn without any financial limit on its most important item, viz., the provision of small holdings. In addition to these major bills, the aggregate cost of schemes now under consideration for Agricultural Marketing, Rural Housing, improved Maternity Service, and a number of minor services is considerable.

10. Excluding such proposals, the main services on which changes are to be expected in 1932 and 1933 are as follows:—

<i>Existing Services.</i> <i>Increases.</i>	<i>Increase</i>	<i>Increase</i>
	1932 over 1931.	1933 over 1931.
	£	£
Agriculture	200,000	300,000
Education	2,550,000	5,500,000
Old Age Pensions	1,500,000	3,000,000
Widows' Pensions	1,000,000	2,000,000
Housing	1,100,000	2,300,000
Navy	2,700,000	2,700,000
Transitional Benefit ...	5,000,000	5,000,000

(The original estimate for 1931 was £30,000,000 while the revised estimate will probably be £35,000,000.)

Total Increases	14,050,000	20,800,000
------------------------	------------	------------

<i>Decrease.</i>	<i>Decrease 1932 below 1931.</i>	<i>Decrease 1933 below 1931.</i>
War Pensions	1,900,000	3,300,000
Net increase on existing services compared with 1931	£12,150,000	£17,500,000

3. Future Liabilities Generally.

11. The consideration we have so far given to the finance of post-war years has been based mainly on the budget position. The budget is, however, only a statement of cash transactions in each financial year, and it gives no indication of the liabilities involved in services which do not mature for payment within the year. To complete the picture of the years under review, it is necessary to consider the trend of long-term commitments undertaken in those years. The result is most disquieting.

The items we propose to consider fall into three broad groups.

12. In the first place, there are services financed through loans or by subsidies based on loans. This method of finance commits future taxpayers to subsidies for services whose cost is now being met by borrowing, and to that extent restricts the field in which economy is possible. The present value of future subsidies is a considerable sum. The total for Housing subsidies alone has now reached £218,000,000, and for grants so far made on the recommendation of the Unemployment Grants Committee £45,000,000. There are a number of other cases the outstanding cost of which we have not evaluated (School Building grants, Small Holdings and so on). These outstanding subsidies are intractable items in the national expenditure, and even if the services were immediately closed down, the taxpayer must continue for many years to provide large sums annually to liquidate past commitments.

13. The second group consists of the charges for pensions to servants of the State and of local authorities. A pension liability is incurred during service; it only matures for payment at the end of service. When a service expands, or when salaries are increased, the full corresponding pension liability only emerges many years later.

14. It is of assistance in this connection to compare the position of a commercial undertaking which accords pension rights to its staff. It may do so by paying premiums to an Insurance Company. Or it may set up its own pension fund and pay into it annually the proper sum calculated on an actuarial basis to meet its future liabilities. In either case it is generally regarded as providing adequately for the pension liability. But the national

schemes are not on these lines; on the contrary, the State accords pension rights to its staff and merely pays the pensions as they arise. At the start these charges are light and the pension scheme may be considered to run cumulatively into debt each year to the extent that its actual payments fall short of the sums which it should have set aside on actuarial principles.

15. In the case of Civil Servants, police and teachers, the accruing pension liability of the Exchequer is estimated to exceed the sum which is actually now being paid in pensions by as much as £5,000,000, £1,000,000 and £8,000,000, a year, respectively. We have not been able to obtain a comparable figure for the Fighting Services.

16. Our third group consists of War Pensions and of the Social Services, in particular Old Age and Widows' Pensions. The liability for War Pensions is steadily declining. The present cost of Old Age Pensions to persons over 70 is much less than the ultimate cost, as for a variety of reasons the aged population of this country is likely to increase for many years to come. In the case of Contributory Pensions also (widows and persons aged 65 to 70) the number of beneficiaries will increase, with a consequent increase of the liabilities, but in addition the immediate cost to the Exchequer in this case has been kept down by the expedient of using the initial accumulation of contributions to meet the cost of pensions in the earlier years of the scheme though this unfortunate feature of the original scheme has been considerably reduced by the amending Act in 1929.

17. The bearing on future finance of the second and third groups of services we have considered is worth examination. In all the cases we have cited except War Pensions there is an accruing liability greater than the current charge. To the extent of the excess there is here an uncovered liability which on any proper system of accounting must be regarded as a direct set off to the Sinking Fund. Over the services in question the Government Actuary has estimated that for the last five years our accruing liabilities even after the decline in the liability for War Pensions has been allowed for may have exceeded the provision we have made by as much as £100,000,000, i.e., an average of £20,000,000 a year. **In other words, we are at present enjoying benefits for which we are not providing the cost. To the extent of about £20,000,000 a year we are leaving that cost to posterity.**

18. The bearing of all the charges we have considered in this discussion of future liabilities on the possibilities of economy is easily seen. Future revenue is mortgaged for many years to pay off the capital cost of services which we are now enjoying. Future revenue is also mortgaged to meet the growing cost of continuing services which are now being enjoyed for less than the true cost. **Only with an increasing revenue can we continue to provide even our existing services without additional taxation.**

19. In estimating the prospects of such increase of revenue being steadily realised, two weighty considerations must not be lost sight of. First, the charges we have considered are practically all fixed in terms of money. If there is a further decline in the price level they will become a proportionately heavier burden on the national revenue, since that revenue itself reflects the price level in important items and will contract still more with a further fall in prices. Secondly, we have to face in the future the probability of a retardation in the increase, and ultimately of a decline, in our population at the working ages. The Government Actuary has estimated that while at present for every 100 persons between the ages of 15 and 65 there are 23 persons over 65 years of age, in 30 years' time there will probably be 33 and in 50 years' time 38. Thus, the working population of the future, in addition to meeting that part of the liability for which provision has not been made by the present generation, will have to support a much larger proportion of pensioners.

4. Factors, Political and Economic, in the Present Situation.

20. Reviewing the course of national finance since the war one cannot fail to notice how unequal is the continual struggle between expansion and retrenchment. One Government, one Parliament can embark on schemes which for all practical purposes definitely commit future Governments, future Parliaments as far ahead as one can look. With some schemes not only are the main lines permanent, but so strong are the contractual or moral obligations involved that any modification in the direction of economy is a difficult matter. But no Government or Parliament can bind its successors to economies. A few Cabinet decisions, a few Votes of Parliament, and all the savings achieved with much labour over a period of years may easily be dissipated.

21. So heavily loaded are the dice in favour of expenditure that no representation we can make is more important than to emphasize the need for caution in undertaking any commitments of a continuing character. This need has long been recognised in the national machinery of financial control—in the admirable Standing Order of the House of Commons that it will not "proceed upon any motion for a grant or charge upon the public revenue . . . unless recommended from the Crown"; in the pre-eminence of the Treasury among Departments; in the method of preparation and presentation of estimates and in the checks on the levying of new taxation; but we must regretfully admit that—particularly since the war—this machinery has been lamentably neutralised by circumstances outside its control.

22. The cause is not far to seek. After the heavy sacrifices of the war large sections of the nation looked to the post-war period with

the natural expectation of a general improvement in the old conditions of life. The disappointment of many hopes in the economic sphere seemed to intensify demands for improvements from political action and all parties have felt the insistent pressure for promises of "reforms" as the price of support, such "reforms" being in fact mostly of the nature of privileges or benefits for particular classes at the cost of the general taxpayer. The results of this pressure are to be seen not only in the lavish promises contained in the election addresses of the period since the war but in the undertakings freely given by individual Parliamentary candidates to sections of the electorate. At election times those desiring increased expenditure on particular objects are usually far better organized, far more active and vocal than those who favour the vague and uninspiring course of strict economy; and as a result candidates not infrequently find themselves returned to Parliament committed, on a one-sided presentation of a case, to a course which on fuller knowledge they see to be opposed to the national interests. Especially serious is this danger at the present time when the mass of the electorate still does not appreciate the true economic position of the country and its problems.

23. Had we still been living in the pre-war period of growing prosperity and rising revenue, with national taxation absorbing but a comparatively small part of the annual income of the people, such a development in the working of our political machinery, though undesirable at any time, might not have had serious reactions. Far different has been the post-war position with its unprecedented trade stagnation, heavy unemployment, falling price level, and declining incomes under a system of taxation which appropriates year by year an unduly large proportion of the national income. It is only now that the nation is beginning to realise the true character of our post-war problem. Only now when we are experiencing a widespread trade depression are we learning to appreciate the fact that what our basic industries have been suffering from for nearly ten years is not a periodical and passing slump such as we encountered in pre-war days, but a deep-seated malaise arising from radical readjustments of world economy. We are at last awaking to the fact that the cure is not to be found in the temporary and limited stimulus afforded by relief works, but in a resolute grappling with the fundamental problems of each industry, in a frank recognition of world changes that are irreversible and in a re-alignment of our economic life to meet them.

24. The economic disequilibrium from which the world at large is suffering at the present time is so many sided, so deep-seated and so extensive that an immediate and rapid recovery is hardly to be expected. And the features peculiar to this country are such that even a general world revival of trade may still find us wrestling with our own special difficulties.

25. If this short diagnosis of our post-war economic troubles is correct our great need has been, and still is, to concentrate all our available energy and resources on re-establishing our competitive position in the world. We have been apt to forget that the first thing needful is to secure a return to general prosperity. This alone will go a very long way towards solving most of the problems that have been claiming the unremitting attention of Governments and Parliaments and embarrassing the national finances since the war. The general effect of Government action, national and local, since 1924 has been to add to the national burdens. These have now attained to such a proportion of the total national income that they must be considered definitely restrictive of industrial enterprise and employment. In this connection we would refer to the introductory words of the practically unanimous resolution of the House of Commons which led to our appointment, quoted at the beginning of this report.

5. The Task before the Committee.

26. It is in the light of these conclusions that we turn to the task before us. We have on the one hand to consider present and prospective revenue and on the other the future course of expenditure. Some information in regard to probable expenditure in 1932 has already been given on page 9. This shows an estimated increase over the budget estimates for the current year of £12,000,000. This estimate is on the basis of the continuance of the Unemployment Insurance Scheme unaltered and of existing policies in other directions. No allowance is made for any supplementary estimates as in the absence of new decisions of policy it should be possible to meet any incidental excesses which arise in the course of the year from savings. On this basis the national expenditure for 1932, apart from the Post Office and the Road Fund, would be £815,366,000.

27. We cannot, however, regard this figure as giving a true picture of the national burden for 1932. The exclusion of the Road Fund from the total on the ground that it is like the Post Office, a "Self-balancing Service," was justifiable as long as the income of the Fund was adequate to meet its liabilities. This is no longer the case. In the current year the Fund is estimated to borrow £9,000,000 from the Exchequer: next year it is expected to need £10,000,000 more. The prospect of repayment is dealt with in detail later in our report, but we will anticipate our conclusions there set out so far as to state that in our view this borrowing must be regarded as a revenue liability.

28. We are drawn to a similar conclusion in regard to the anticipated borrowing of the Unemployment Fund in 1932 under existing arrangements. Apart from the heavy charge for Transitional Benefit which falls direct on to the Exchequer the revenue of the Fund from the contributions of the State, employers and employed,

will fall far short of its liabilities for ordinary benefit. At the beginning of last April it was borrowing at the rate of £55,000,000 a year. Since that date there has been some transfer from ordinary to transitional benefit, but the Fund is still borrowing at little less than £1,000,000 a week. By the end of the current financial year, the debt will be considerably over £100,000,000. Whatever view may be held of the prospect of repayment of the existing debt, we cannot regard any loan from the Exchequer which may be necessary in 1932, estimated on the present scheme to amount to £40,000,000, as other than an irrecoverable advance. **Borrowing for such purposes is in reality adding to the national debt to relieve current revenue charges and is opposed to the principles of sound finance hitherto accepted without question in this country. We recommend that it be discontinued after this year.** The total of these items represents an additional expenditure to be met from revenue in 1932 as compared with 1931 of no less than £62,000,000.

29. What of the revenue? No one will be surprised in view of our previous remarks if we state at the outset that any appreciable increase in the main taxes on enterprise in 1932 could only aggravate present difficulties. Yet the revenue prospects are not reassuring. The Budget of 1931 has been balanced largely with the aid of "nest-eggs." £20,000,000 is being obtained from the capital of the Exchange Account and £3,000,000 from the excess of the assets of that Account over its liabilities. £10,000,000 is being provided by acceleration of payment of Income Tax under certain Schedules and the £4,000,000 drawn from the Rating Relief Suspense Account exhausts that Account. None of this £37,000,000 will be available in 1932, and the gap between expenditure and revenue is thus widened to £99,000,000.

30. So far we have dealt with facts which can be definitely allowed for. When we turn to other items of revenue more uncertainty arises. The Income Tax of 1932 will be assessed on the profits of 1931, and those profits will undoubtedly be substantially lower than the profits of 1930 on which the Income Tax of 1931 is based. What the reduction will be no one can foretell, but after reviewing available data we think it would be unsafe to assume that it will be less than £20,000,000. If, in regard to other items of revenue, we make the fairly optimistic assumption that receipts in 1932 will in the aggregate equal the Budget estimates of 1931 we are left with the position that to produce a properly balanced budget in 1932 including the usual provision for the redemption of debt a deficiency of the sum of £119,000,000, say £120,000,000,* has to be made good by fresh taxation or by economy, apart from any further liabilities that may be incurred under pending legislation.

* This report takes no account of any adjustments in the national accounts which may be necessitated by the moratorium on reparations and war debts now under consideration.

31. For present purposes one of the most important conclusions to be drawn from our diagnosis of the financial situation is that this gap of £120,000,000 is no transient feature to be bridged by temporary expedients. If it were, our task would be comparatively easy. Many classes and interests are readily prepared in a national emergency to accept a temporary surrender of what they conceive to be their just rights; the postponement of all works whether of a capital or of a maintenance character is a common method in everyday life of tiding over a passing stringency; while there may still be found in secluded thickets of the national accounts a few "nest eggs" that for one reason or another have not yet been disturbed and might possibly be available to make some small non-recurrent addition to the revenue side of the budget. Not so in our view can the present position be controlled. We fear that the country must face the disagreeable fact that its public expenditure—and in this we include local as well as national expenditure—is too high and that it must be brought down to a lower level. It may be that in thinking that a policy of strict economy will be necessary for some years to come we are unduly pessimistic and that the recuperative powers of the world and the resilience of our national character in periods of grave emergency will prove to be such that difficulties which now appear extremely grave will be rapidly overcome. This possibility does not however in the least alter our view as to the wise and prudent course to take now. Relaxations of conditions, increases of expenditure, expansions of services are easy and popular and can be swiftly effected should the wheel of fortune turn in our favour. Should however the trend of events become even more adverse, economies and sacrifices will prove to be far more valuable, far more effective if made at once than if we wait till they—and perhaps many more—are forced upon us by the pitiless march of events.

32. When we come to face our task in detail it is inevitable that we should find that the chief opportunities of reduction are to be found in the services of most rapid and recent growth. There are three reasons for this. First, the older commitments of the State have stood the test of many attacks and in the main have proved that they are unavoidable even in years of depression. Secondly the longer expenditure has been running, the more rights and vested interests have grown up around it. Thirdly it is a powerful argument in regard to any service to say that the nation did without it a few years ago, therefore it cannot be essential. This line of thought however leads us into some difficulty in regard to proposals now under consideration, whether by Departmental Ministers, the Cabinet or Parliament itself. We would have preferred that our task should have been limited to the expenditure now being incurred under decisions of the past without our being forced into expressing any opinion on questions of the day, and yet again and again in the course of our enquiry we have been faced with the

difficulty of going back upon past decisions. They have created expectations, moral rights and sometimes even contractual and legal liabilities. In many instances the mistake made in taking the original decision is now irremediable. Seeing this, we feel that we should be failing in our duty if while doing all in our power to reduce present expenditure we took no cognizance of proposals now under discussion for increasing it.

6. The National Expenditure considered in more detail.

33. We append to this report a classification of the national expenditure prepared by the Treasury by reference to the services or objects on which the money is spent. These figures differ from those in the Estimates and Appropriation Accounts first, in that all payments on a particular service have as far as possible been collected irrespective of the particular vote on which they are provided, and secondly, that in view of the altered financial position of the Road Fund, already referred to, we have included payments therefrom in the national expenditure.

34. The Table divide the expenditure into two parts, i.e.—

(1) Expenditure on services directly administered by the Government;

(2) Grants towards services administered by other bodies, mainly local authorities.

In regard to the former class the responsibility of the Government for the cost of the services is direct and complete; in regard to the latter the national accounts only cover a part of the total cost and however much the Government may share in the control, it has not itself the direct administrative responsibility.

35. The expenditure in these groups analysed under the more important heads is shown below for the current year (budget estimates) and 1924, when it reached its lowest post-war level. In the second group an adjustment has been made in the item Exchequer Contributions to Local Revenues allocating to the education and police services respectively, grants paid from this head in 1924 and now directly charged on the Votes (under the Local Government Acts, 1929):—

I. Nationally Administered Services.

---	1924 Audited Expenditure.	1931 Original Estimates.	Increase (+) or Decrease (-).
	£.	£.	£.
Debt Interest and Management ...	308,700,000	302,900,000	— 5,800,000
Defence	116,900,000	111,400,000	— 5,500,000
War Pensions	69,900,000	50,400,000	—19,500,000
Old Age and Widows' Pensions and Health and Unemployment Insurance.	45,200,000	99,800,000	+54,600,000
All other expenses of Government ...	45,100,000	37,800,000	— 7,300,000
TOTAL	585,800,000	602,300,000	+16,500,000

II. Grant Services.

	1924 Audited Expenditure.	1931 Original Estimates.	Increase (+) or Decrease (-).
<i>Great Britain.</i>			
Exchequer Contributions to Local Revenues (including grants for poor law, health and mental deficiency)*	£ 12,700,000	£ 46,400,000	£ +33,700,000
Education	47,900,000	56,800,000	+ 8,900,000
Roads	15,100,000	33,000,000	+17,900,000
Housing... ..	9,000,000	14,500,000	+ 5,500,000
Police	10,400,000	12,000,000	+ 1,600,000
Agriculture (including Forestry, Development Fund and Beet-sugar subsidy).	3,300,000	5,400,000	+ 2,100,000
Grants and Loans for Unemployment Works.	3,500,000	3,600,000	+ 100,000
Miscellaneous	900,000	900,000	—
Grant Services Great Britain... ..	102,800,000	172,600,000	+69,800,000
<i>Ireland.</i>			
Irish Services	8,800,000	9,800,000	+ 1,000,000
Total Grant Services	111,600,000	182,400,000	+70,800,000
GRAND TOTAL	697,400,000	784,700,000	+87,300,000

* Now merged in the block grants under the Local Government Acts.

36. These tables will repay careful study. The first one shows reductions amounting to £38,100,000 spread over every item except Old Age and Widows' Pensions and Unemployment and Health Insurance where there is an increase of £54,600,000. In the second table there are no reductions. The increases may be grouped under three heads—

- (1) Grants for various purposes of national development.
- (2) Grants for Social Services.
- (3) Other grants.

Of the £33,700,000 increase under Exchequer Contributions to Local Revenues £26,000,000 represents the cost of the rating relief given to industry and agriculture, and may fairly be included in the first category above. The balance may be regarded in the main as given in respect of social services carried out by local authorities. The bulk of the grants for unemployment works may also be

regarded as given for national development. If this division be made the increases in the three groups become:—

	£	£
(1) Home Development.		
Derating	26,000,000	
Roads	17,900,000	
Agriculture	2,100,000	
Grants for Unemployment Works ...	100,000	
	46,100,000	
(2) Social Services.		
Balance of increase under Local		
Government Acts	7,700,000	
Education	8,900,000	
Housing	5,500,000	
	22,100,000	
(3) Other Grants.		
Police	1,600,000	
Irish Services	1,000,000	
	2,600,000	
		Total £70,800,000

37. Thus of the total increases shown in the tables in para. 35 of £125,400,000 (viz.:—Pensions and Insurance £54,600,000 and Grant Services £70,800,000), about £76,700,000 (viz.:—Pensions and Insurance £54,600,000 and Education, Housing, etc., £22,100,000) may be regarded as in respect of Social Services and £46,100,000 in respect of Home Development. Other grants account for an increase of £2,600,000 and all other main groups show a reduction. If allowance be made for probable increase of the Exchequer grant to unemployment insurance this year by £5,000,000 owing to the extension of the transitional benefit period, the total of increases reaches £130,000,000 of which roughly £80,000,000 is accounted for by Social Services and £46,000,000 by Home Development.

7. The Arrangement of the Report.

38. Following the general lines of the above classification of expenditure we have divided the remainder of our report into the following main sections:—

- Chapter II. Civil Service Administration.
- ,, III. Pay and Pensions (Civil Servants, Fighting Services, Police and Teachers).
- ,, IV. Defence (Navy, Army and Air Force).

- Chapter V. Development Expenditure (Research, Road Fund, Department of Overseas Trade, Relief of Rates on Industry and Agriculture, Agriculture, Beet Sugar Subsidy, Forestry, Empire Marketing Board, Colonial Development, Colonial and Middle Eastern Services, Unemployment Grants and Development (Public Utility) Grants).
- „ VI. Social Services (Unemployment and Health Insurance, Widows' and Old Age Pensions, Housing and Education).
- „ VII. Miscellaneous Services (War Pensions, British Broadcasting Corporation and Exchequer Contributions to Local Revenues).
- „ VIII. Summary of Recommendations and Conclusion.

39. At the outset of our deliberations, two considerations became evident. First, that a detailed enquiry would take a long time. The field of Government expenditure, including as it does the Fighting Services, the Post Office, Revenue Departments, some 124 Civil Votes, several of considerable complexity, and a number of special funds could only be scrutinised in detail if many months, running possibly to years, of labour were devoted to the task.

Secondly, that the financial situation demands that steps to reduce expenditure substantially should be taken immediately. The Budget Speech delivered shortly after we began our enquiry showed that great hope was being placed on the outcome of our deliberations to ease the difficulties of next year's budget. It is almost inevitable that many of our proposals would involve legislation, and if they are to be fully effective in 1932 there is clearly no time to lose.

40. At an early stage in our enquiry we came to the conclusion that we ought to concentrate our attention in the main on selected aspects of the national expenditure with a view to producing as comprehensive a report as possible before the Summer Recess. There are many issues of great financial moment demanding immediate attention from a Committee on expenditure; there are other questions, which in the public mind are thought to present great opportunities for economy such as the creation of a Ministry of Defence or a large reduction in the personnel of the Civil Service, which we cannot ignore. But as regards the general field of Government activity any large reduction of expenditure is hardly to be expected in view of the efforts to reduce administration costs in recent years. All the large Departments have during and since the War been examined individually by Committees who have spent some months on each subject, but more important than any *ad hoc* enquiry has been the day to day scrutiny of the Treasury and the working of the system of internal financial control in each Department. We have

nevertheless pursued our enquiries into the general field so far as to satisfy ourselves that we were not overlooking substantial possibilities of economy alternative to those we recommend. We have given consideration through Sub-Committees to all the Supply Votes and we have discussed those in which any savings appeared possible with officers of the Treasury and, in some cases, of the Departments concerned. While we do not say that on these smaller votes there is no opportunity for economy, we are satisfied that if all possible savings were made, the maximum sum there available would be relatively insignificant compared with the total economy we regard as essential.

In order to shorten our report as much as possible we have not, as a rule, considered it necessary to deal with services in regard to which we do not submit any recommendation.

CHAPTER II.

CIVIL SERVICE ADMINISTRATION.

41. The Civil Service numbered in 1930-31 about 443,200 persons. Industrial workers (e.g. Dockyard and Arsenal Workmen, Post Office Linesmen, Office of Works Constructional and Maintenance Workmen, Stationery Office Printing Staffs) number 122,400 Manipulative staffs (Post Office Sorters, Postmen, Telegraphists and Telephonists) number 180,800.

The balance of 140,000 contains 17,200 Messengers, Porters, Charwomen etc., 8,400 Typists and Shorthand Typists, 29,700 Writing Assistants, Temporary Clerks, etc. leaving 84,700 as the number of Clerical, Executive and analogous staffs, Consular Diplomatic and Administrative Officers, Professional, Scientific and Technical Staffs, Inspectorates, etc.

42. The possibilities of economy in the field of Civil Service Administration depend on :—

- (a) the rate of pay.
- (b) the necessity for the existence of some of the Departments.
- (c) the efficiency of the organisation.

We shall deal with the first of these three points in a separate section of our report. Our recommendations on the second are necessarily made under the individual Departments. We propose here to deal with the third, and to look at the administrative costs of the Civil Service.

43. Anyone who has had experience of business organisation will know that detailed and continuous scrutiny is necessary (except perhaps where there is flagrant extravagance of management) to achieve savings in administrative costs. In any ordinary business, which is reasonably well run, an investigator can only find the points at which improvement of organisation is possible by actually living in the office for some time. Even then, the savings are probably individually small and a long time elapses before they amount to an appreciable total. Any such investigation is quite beyond our scope, and we have approached the subject not by trying to make individual investigations but by examining the machinery of control with a view to considering its efficiency for its purpose.

44. The post war theory of control of Civil Service organisation rests on active co-operation and goodwill between the Treasury on one hand and the Department on the other. They are jointly trustees for the efficient and economical administration of the service. In the Treasury there has been since 1919 an Establishments Department which has specialised in questions of organisation of Departments, personnel and remuneration, superannuation and so on. In the Departments, responsible officers have been appointed directly answerable to the Head of the Department on questions of office management. For a number of years now there has been going on a regular overhaul of staffs by Establishment Officers aided by advice and assistance from the expert Department of the Treasury. The process is not spectacular but it is continuous and effective. We do not believe it would be claimed that the administration of the Civil Service is perfect. Necessarily with changing policies, increases of work in some directions and decreases in others, the machine cannot always adapt itself immediately to change of policy. But we are satisfied that the method of control adopted is well calculated to maintain a high standard of administration, and that such economies as are from time to time possible will be secured as opportunities arise and will not be accelerated by any recommendations which we could make.

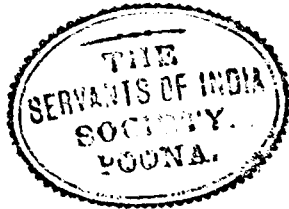
45. We are confirmed in these conclusions by an examination of particular examples. The staff of the Department of Overseas Trade was reduced from 640 to 400 in 1921 and kept round that figure until 1929. The Foreign Office Staff (including the Passport Office) was steadily brought down from 843 in 1925 to 732 in 1930. The Ministry of Transport staff of 741 on 1st April 1921 stood at about 600 from 1926-1929. The staff of the Ministry of Agriculture and Fisheries of 1,402 in 1921 was progressively reduced to 1,158 in 1928. This list is by no means exhaustive—it merely contains typical examples of progressive staff reduction.

46. Reference should be made here to one particular form of staff economy, viz., the substitution of mechanical devices for routine labour. In this respect, we believe the Civil Service to compare

favourably with the best organisations in British industry. During the last five years, as much as nearly £500,000 has been saved annually in some twelve of the largest Departments by the introduction of labour-saving machines.

47. This is not to say that the total of the Civil Service has been reduced. **On the contrary, new duties are constantly being imposed on the Civil Service and the reductions carefully and laboriously achieved year by year are frequently undone by a single Act of Parliament or Ministerial decision.** Most of the decreases referred to in paragraph 45 have in fact been subsequently swept away in subsequent increases. The Anderson Committee in 1923 reached the conclusion that the immense increase in the Civil Service pay roll had been imposed on the taxpayer for reasons which commended themselves to various Parliaments before and since 1914 and that no power except Parliament could materially reduce the load. We reach the same conclusion to-day. We believe that the Civil Service is economically organised to carry out the duties which Parliament has imposed upon it. Only Parliament can reduce the burden of those duties.

48. And the cost of carrying out those duties is increased by the special handicaps under which the Civil Service labours. We do not think it is generally appreciated how many restrictions hinder the free working of the Civil Service machine. Ex-Service men receive preferential treatment—a policy which departs from the former policy of selection solely by competence. The insatiable thirst of members of Parliament and the public for all sorts of detailed information necessitates the keeping of statistics more elaborate than are necessary outside the service. Parliament, through the Public Accounts Committee, prescribes by long tradition standards of accuracy and of procedure in matters of accounting which may be desirable in principle but are the reverse of simple in practice. Clearly a change of practice under any of these heads would involve serious issues of policy requiring far more detailed consideration than we have been able to give. We understand that considerable progress has been made in recent years in reducing clerical labour due to unnecessary checking and verification of records and accounts. Favourable consideration should in our view be given to carrying this process further.



CHAPTER III.

PAY AND PENSIONS.

49. We propose in this chapter to consider the pay and pensions of all classes of State employees and of those classes of local authorities' employees whose pay and pensions fall partly on the State through the operation of percentage grants.

The classes covered by our investigations are :—

- (a) Civil Servants (including temporary staffs and industrial employees);
- (b) Members of the Fighting Forces;
- (c) Police;
- (d) Teachers.

50. We have not considered certain special classes who receive salaries from the State such as Ministers of the Crown including the Law Officers and Members of Parliament. **We think that the Government and eventually Parliament, which was responsible for the setting up of our Committee, must decide what contribution if any should be made in the present difficult circumstances.**

51. We have also not given detailed consideration to the salaries of the Judiciary and of officers of the Houses of Parliament.

The salaries of the former, totalling £475,000 a year are charged on the Consolidated Fund. The salaries of the Judges of the Courts of Justice remain the same as before the war. In the case of County Court Judges in England and Wales, Metropolitan Police Magistrates, Sheriffs and Sheriffs Substitutes in Scotland, etc., the basic salaries are the same as before the war, but they now carry a bonus under the Civil Service cost of living scheme. The bonus varies with the salary and in the case of County Court Judges (basic salary £1,500 a year) is at present £146 8s. 0d., or less than 10 per cent. of salary. **Prima facie, the present salaries of the Judiciary do not call for comment by us.**

52. The salaries of officers of the Houses of Parliament are fixed by the House of Lords Offices Committee and the House of Commons Offices Commission respectively. **We recommend that in order to ensure that the salaries paid are commensurate with those paid in the rest of the Civil Service for duties of equal responsibility they should in future be subject to the sanction of the Treasury. If the duties of any posts are more or less nominal, the appointments should be made honorary ones.**

53. This chapter covers a wide and diverse field. Each separate branch of our enquiry has at one time or another been the subject of elaborate investigation by Committees. In the

particular case of the Civil Service, a Royal Commission has been investigating its problems for over eighteen months. It is self-evident that in the time at our disposal we have only been able to give the broadest consideration to the difficult and important questions which arise in so large a subject.

Nevertheless, notwithstanding the necessity of confining ourselves to general considerations, there are certain salient facts which demand investigation in the light of present conditions.

54. The Anderson Committee in their Report dated 25th July, 1923, stated :—

“ Two general considerations about the pay of State servants occur to us.

“ On the one hand the State should hold the scales even between its own servants and those through whose enterprises its servants are paid. On the other hand, employees of the Crown would have a real ground for complaint if their pay were related to wages in industry only in the time of low wages. If they do not get pay relative to the boom they must be spared the severity of the slump.

“ The State as a model employer offers security, a pension, a dignified service, and a moderate wage in exchange for the excitement and possibilities of private employment.”

This admirable summing-up of the difference between employees of the State and those engaged in private enterprise has been present in our minds in considering whether any, and what, reductions are now necessary.

55. We cannot, however, overlook the fact that speaking generally the present basis of pay of all classes within the scope of our review was fixed in 1919 or 1920 when, following victory in the Great War, exaggerated notions were held of the future financial prosperity of this country and when, as the result of a temporary boom in trade, profits and wages had risen to an uneconomic level only to fall as steeply, except in the sheltered industries, when the inevitable slump followed. It is true that since 1919 and 1920 certain reductions have been made in some cases, but such reductions have in the main consisted of adjustments due to the fall in the cost of living. In certain classes, little or no reduction has occurred and in the others the increased basic remuneration granted in 1919 and 1920 has not been affected. At the same time we recognise that certain classes were, in comparison with private employment, underpaid in 1914 and that some adjustment of pay was merited.

56. On the other hand, since 1919 those engaged in industry, including those engaged in business on their own account, have suffered substantial reductions in their income and many unfortunately have lost their posts after long service without adequate

compensation for loss of office. The security of tenure and pension rights of pensionable State and local authority servants represent, in our opinion, a value measured by a substantial percentage of remuneration compared with those engaged in private enterprise who do not enjoy either permanency of employment or pension rights. This factor is one to which material weight must be given when considering the subject under review.

57. The change in the cost of living in recent years has caused a considerable change in the relative position of one class of Government employees and another. When the pay of all the classes under review was considered at varying dates shortly after the war, the cost of living was very high. Pay was fixed at levels very considerably above the pre-war level. In some cases the scheme of pay included a provision for variation up or down as the cost of living fluctuated; in other cases, while provision was made for increases if the cost of living rose, no provision was made for decreases if the cost of living fell.

58. During the period since 1920, the cost of living has fallen substantially. As measured by the Ministry of Labour's index, it reached a peak figure of 176 per cent. above pre-war on 1st November, 1920, and it has fallen to 45 per cent. above pre-war on the 1st June, 1931. In some cases the absence of revision of pay as the cost of living has fallen has placed the classes concerned in an increasingly favourable position compared with the classes whose pay has been progressively and automatically adjusted, and indeed with wage earners generally.

✓ 59. We do not suggest that the adequacy of pay can be determined solely by reference to cost of living changes. If one could assume for each particular class that there was a given moment at which their pay was right and that their proper pay at any other time could be calculated arithmetically by reference to change in cost of living, our task would be an easy one, but in fact a continuous process of re-assessment of values is always at work. In the Civil Service in particular there have been numerous re-organisations, arbitration awards and the like which have altered the internal relativities and on the average have tended to offset to some extent the reductions due to the fall in the cost of living. In the Fighting Services, lower rates were introduced in 1925 for new entrants although (speaking only of officers) the old rates already included provision for cost of living variations. Clearly then, cost of living is not the only criterion.

60. The Anderson Committee stated that in their view there was only one principle in which all the factors of responsibility, cost of living, marriage, children, social position, etc., were included—the employer should pay what is necessary to recruit and to retain an efficient staff. In our view, this is broadly equivalent to the

ordinary "fair wages" basis which is the underlying principle of the pay of State and local authority servants. If, however, in one class the cost of living is taken into account and a substantial cut in pay brought about automatically as the cost of living falls, it cannot be equitable if another class suffers no deduction if at the outset the pay of both classes was fixed on a "fair wages" basis having regard to then existing conditions.

61. In the consideration we have given to each of the classes under review we have not had regard solely to cost of living. While considering the different ways in which the classes affected have been treated in respect of that factor, we have also borne in mind the fundamental basis ultimately governing their wages.

With this preamble, we turn to the discussion of individual classes, taking first the question of pay (including consideration of the value of pension rights as affecting pay), and leaving for separate consideration later the question of pensions generally.

1. CIVIL SERVICE.

(Excluding Industrial Employees.)

62. The average number of the non-industrial staffs of Government Departments in 1930-31 was 320,800. Of this number, 47,200 were staff employed part time only in the Post Office service and 800 were employed in the Diplomatic, Consular, Commercial Diplomatic and Trade Commissioner services. Of the balance of 272,800 as many as 149,100 were employed in the Post Office.

63. The remuneration of whole time non-industrial Civil Servants under £2,000 per annum varies with the cost of living. The great majority are under the Cost of Living Scheme introduced as from 1st March, 1920. A smaller number of unestablished staff are under an analogous scheme.

The cost of living scheme provides that full compensation for the increased cost of living as determined by the Ministry of Labour index figures is granted on ordinary remuneration up to 35s. a week (£91 5s. 0d. per annum). On remuneration from £91 5s. 0d. to £200 a year, approximately 46 per cent. of full compensation is granted on the remuneration above 35s. a week. On remuneration over £200 a year, approximately 35 per cent. of full compensation is granted on the excess over £200. The bonus was originally restricted to a maximum of £750 a year (£500 for certain of the highest posts in the service). Under a modification of this scheme introduced in August 1921, the bonus payable to officers on salaries of over £500 a year (basic) was substantially reduced. No bonus is now paid which would bring remuneration beyond £2,000 a year.

64. The effect of this scheme is shown in the following table :—

Basic Remuneration.	Total remuneration with Bonus paid 1st March-31st August, 1921 (Peak).	Total remuneration with Bonus now paid. (Cost of living 55).	Percentage fall (3) on (2).	Percentage increase (3) on (1).
(1)	(2)	(3)	(4)	(5)
£	£	£	Per cent.	Per cent.
100	257	152	41	52
300	590	397	33	32
500	905	635	30	27
750	1,298	905	30	21
1,000	1,690	1,161	31	16
1,500	2,250	1,646	27	10
2,200	2,700	2,200	19	0
3,000	3,500	3,000	14	0
3,500	4,000	3,500	13	0

65. The value of this table is discounted, however, by reason of the fact that basic remuneration has not remained constant, and it is clear from consideration of other matters that the cost of living scheme alone cannot be taken as an indication of the changes made in remuneration. It is impossible to disentangle the factors which have contributed to change. The age distribution of the Civil Service is not constant. An abnormal number of men found themselves near the beginning of long incremental scales in 1920 and the ordinary working out of increments has caused a steady increase. The full effects of the increases granted in 1920 were not felt at once. In addition there has been, in many cases, a revision of the basic scales themselves. These factors result in the Civil Servant now being in a better position than a mere comparison of remuneration in 1914 and 1920 would indicate. On the other hand, the average remuneration of the Civil Service has also increased through changes in its character and the changes under these heads cannot be regarded as on the same footing as the changes we have just referred to. Recruitment has been largely from ex-service men, and the entry of men on salaries appropriate to adults instead of the entry of recruits at the minima of the scales has prevented the increase arising from increments being fully offset by the savings which would have arisen had the wastage been made good by such young recruits. A further factor affecting average remuneration is the replacement of routine labour by mechanical devices. The whole position is therefore one of considerable complexity, and further exploration is necessary.

66. The Anderson Committee recognised that detailed enquiry into particular rates of pay was impossible for them. They assumed

that in the Service the internal relativities had been adjusted by the various Pay Committees which had considered the question in different Departments, by the Departments themselves and by the Treasury. They tried to gauge the general standard of remuneration by examining certain important rates.

We have proceeded on similar lines though, as our subject is much wider than that of the Anderson Committee our treatment must necessarily be on an even broader basis.

67. Any detailed treatment of Civil Service remuneration at the present time is also rendered unnecessary by the fact that a Royal Commission on the Civil Service has been sitting for a year and a half and, at the date of preparing this report, is, we understand, about to issue its findings. We presume that amongst other matters they will examine the general standards of Civil Service remuneration and through their consideration the relativities throughout the service will be brought under further review. We do not feel, however, that the existence of the Royal Commission precludes us from all reference to the Civil Service. The cost of the salaries and wages, excluding the industrial grades, was in 1930 some £66,000,000, and we cannot omit so important an element in Budget costs from our survey of National Expenditure. Moreover, we have kept before us as a constant aim the securing of fair and equitable treatment for all the classes we are reviewing, and clearly we could not ensure such fairness if we had omitted the largest class from our survey. We have confined our survey to such examination as would enable us to appreciate the possibilities on broad lines of Civil Service remuneration as a field for economy.

68. We have amplified certain statistics given by the Anderson Committee, and give the average remuneration at various dates of the different big groups in the service. We think it convenient to reserve the Manipulative and Messenger grades for separate consideration later in this part of our Report.

69. We commence with the Administrative Staff, Professional, Scientific, and Technical Staff and Inspectorates, Executive and Clerical Staff and Writing Assistants and Typists. We have added to the Anderson Committee's statistics for 1914 and 1923 broadly comparable figures for 1930. In order to give a more comprehensive picture of the trend of post-war remuneration, we have inserted figures for 1921 (when remuneration reached its peak) and for 1931, the latter figures being based on a cost of living figure of 55 above pre-war.

70. A comment should, perhaps, be made on our table. The staff group classifications and the figures appropriate to them for the years 1914 and 1923 respectively are taken from the Anderson

Report. Precise information as to the various grades included in these particular staff group classifications is not now available. The figures shown for 1930 and 1931 may accordingly not be strictly comparable group for group with the Anderson groups, but the margin of error due to the exclusion of particular grades from one group and their inclusion in some other group is not likely to be considerable.

	Adminis- trative.	Professional, Scientific and Techni- cal and Inspec- torates.	Executive and Clerical.	Writing Assistants and Typing Staffs.	Total
Numbers, 1914	1,077	20,356	33,239	3,034	57,
„ 1923	1,596	24,943	78,504	11,198	116,
„ 1930	1,708	21,764	82,900	14,046	120,
Aggregate } 1914	£ 713,000	£ 4,708,700	£ 4,416,000	£ 198,300	£ 10,036,
Salaries and } 1923	1,474,500	10,746,700	17,770,100	1,443,600	31,434,
Wages. } 1930	1,755,900	8,658,200	25,101,500	1,917,600	37,433,
Cost per head—	£	£	£	£	£
1914	662.1	231.3	132.9	65.4	173.
1921 (Bonus based on 165 over pre-war).	1,231.7	578.2	321.8	189.8	378.
1923 (Bonus based on 80 over pre-war).	923.9	430.9	226.4	128.9	270.
1930 (Bonus based on 70 over pre-war).	1,028.0	397.8	302.8	136.5	310.
1931 (Bonus based on 55 over pre-war).	985.0	372.5	281.4	124.5	289.
Percentage increase 1931 over 1914.	per cent. 48.8	per cent. 61.0	per cent. 111.7	per cent. 90.4	per cent. 66.
Percentage fall 1931 on 1921 ...	20.0	35.6	12.6	34.4	23.
Percentage fall 1931 on 1930 ...	4.2	6.4	7.1	8.8	7.

71. The conclusions to be drawn from this table are as follows :—

First, over these grades of the Civil Service there has been a substantial fall in average remuneration since the post-war peak and an appreciable fall in the last year.

Secondly, as the higher salaries rose less with the increase in cost of living and proportionately fell less with the drop, the experience of the different grades has not been widely disproportionate except as regards the Executive and Clerical staffs.

72. The disparity in this last grade calls for separate consideration. We find that a substantial part of the increase over pre-war and the absence of the same degree of fall as in other classes since the post-war peak is due to the following factors :—

There has been a large element of recruitment from ex-service men. This operates in two ways. The payment of salaries appropriate to adults for work which before the war was performed by a class containing a large proportion of boy clerks necessarily means a big proportionate increase in the average cost per head. Secondly, the ex-service men who entered the clerical class started in the lower range of a long scale of salary and there has been a steady and appreciable growth due to the annual increments which they have earned in their scales. As many as 18,550 ex-service clerks have been recruited through various clerical competitions since the war and the increasing cost of these men as they have earned increments accounts for a substantial element in the total cost.

73. In a stable Civil Service with balanced age distribution, retirements of the more highly paid men at the top and recruitment by juniors at the minimum would, other things being equal, keep the cost stationary. The present lack of balance in the Civil Service, due partly to cessation of recruitment during the war, partly to expansion after the war and partly to the special character of the post-war recruitment, must be allowed for in considering the trend of salaries, and we believe that if scientific adjustment could be made for this feature which operates with exceptional effect in the Executive and Clerical grades, it would be found that a great deal of the apparent difference of average of salaries between these grades and the other classes would be explained.

74. Having regard to these factors, we do not feel that Civil Service salaries have failed to respond satisfactorily to the fall in cost of living.

75. We have also examined the salaries in another light. We have compared the salaries of large grades, e.g., Typists, Shorthand typists, Clerks, with salaries paid in outside comparable employment. We do not find any marked divergence between the standards of remuneration which obtain and while we think that in some grades notably for the higher ranges of clerical work the remuneration is on the generous side, we do not think that on the whole the remuneration of the Civil Service is out of scale with that determined on the principle of " fair wages ".

In the case of established typists, we are of opinion that the commencing salaries are too high and that some saving would be effected by recruitment at an earlier age.

76. We turn next to the Manipulative grades, and append a table on similar lines to that given on page .

<i>Manipulative Staffs.</i>										
Numbers, 1914	...	...	...	...	...	...	...	...	...	177,747
"	1923	...	...	...	...	...	...	...	...	168,508
"	1930	...	...	...	...	...	...	...	...	184,216
£										
Aggregate Salaries and Wages, 1914	...	...	...	...	...	...	...	...	...	11,975,000
"	"	"	1923	...	...	...	...	...	...	25,011,500
"	"	"	1930	...	...	...	...	...	...	27,165,300
£										
Cost per head—										£
1914	...	...	...	...	...	...	...	...	...	67.4
1921 (bonus based on 165 over pre-war)	...	...	...	...	...	...	...	...	...	218.5
1923 (bonus based on 80 over pre-war)	...	...	...	...	...	...	...	...	...	148.4
1930 (bonus based on 70 over pre-war)	...	...	...	...	...	...	...	...	...	147.5
1931 (bonus based on 55 over pre-war)	...	...	...	...	...	...	...	...	...	134.5
Per cent.										
Percentage increase, 1931 over 1914	...	...	...	...	...	...	...	...	...	99.6
"	fall, 1931 on 1921	...	...	...	...	...	...	...	...	38.4
"	"	1931 on 1930	...	...	...	...	...	...	...	8.8

77. As regards most of the classes here covered, the rates of pay were settled by a comprehensive arbitration as recently as 1927. In the case of these staffs, we have examined the rates of the largest classes. Our examination leads us to a result similar to that of the Anderson Committee and we think that some of the maximum rates, notably those of Sorters and Telegraphists are on the high side. In the case of the latter grade we think it would be advantageous that the Post Office should consider whether female labour might not be used a great deal more than at present. Apart from suitability of work, we think that some of the present difficulties of organisation which lead to large numbers of men being simultaneously on their maximum, and thus necessitate a higher maximum than would normally be necessary, would be considerably eased by the substitution of women for men.

Apart from this criticism, our conclusions on this part of our enquiry do not differ from those we have already expressed on the Administrative and other groups of the Service.

78. Lastly, we turn to the Messenger and Cleaner Grades, and again append a table.

<i>Messengers, Charwomen, etc.</i>										
Numbers, 1914	...	...	...	...	...	...	...	...	...	13,296
"	1923	...	...	...	...	...	...	...	...	19,678
"	1930	...	...	...	...	...	...	...	...	17,396
£										
Aggregate Salaries and Wages, 1914	...	...	...	...	...	...	...	...	...	664,200
"	"	"	1923	...	...	...	...	...	...	1,995,300
"	"	"	1930	...	...	...	...	...	...	1,808,000

Cost per head—	£
1914	50.0
1921 (bonus based on 165 over pre-war)	149.3
1923 (bonus based on 80 over pre-war)	101.4
1930 (bonus based on 70 over pre-war)	103.9
1931 (bonus based on 55 over pre-war)	94.7
	Per cent.
Percentage increase, 1931 over 1914	89.4
„ fall, 1931 on 1921	36.6
„ „ 1931 on 1930	8.9

79. This group which includes not only Messengers but Porters and Charwomen being more homogeneous than any hitherto considered and more directly comparable with similar employment outside affords a closer test of the application of the fair wages principle than any of the others. We have found on examination a close similarity between the rates inside and outside the service. ✓

Summary of Civil Service Remuneration.

80. We wish to emphasise that the comparisons of rates of pay which we have made are mainly with those of employees of Banks, Insurance Companies and Finance Houses who represent the higher standard of employer—and that having regard to security of tenure and pension rights, the emoluments of the Civil Servant (with the exception of the higher grades) undoubtedly compare favourably with the reward for corresponding posts in the majority of commercial and industrial undertakings at the present day.

81. We feel, however, that the rates of remuneration in outside industry with which comparison is possible are at present in an unstable condition. The trend of outside rates must in the end determine Civil Service rates and we think that the operation of the Civil Service cost of living scheme should, in conditions such as obtain to-day, be subject to constant scrutiny to ensure that it maintains a fair relativity between Civil Service remuneration and that in those outside employments with which comparison can properly be effected. We observe that the index figure of cost of living is falling and is now 45 per cent. above pre-war compared with 55 which is the figure now operative for purposes of cost of living bonus, and that consequently further automatic cuts in remuneration are probable and it is on this assumption that our recommendations are made.

82. To sum up our consideration of the Civil Service as a whole, we do not find that the general standard of remuneration as tested by its trend since the war and by comparison of the pay of some of the large groups with outside employment is excessive, a progressive reduction having been made in accordance with the fall in cost of living. We do not therefore feel justified in recommending

any reduction on the ground that the average pay of the Civil Service is unduly high compared with what may be termed a "fair wages basis".

Leave and Hours.

83. We would refer to two other matters affecting conditions in the Civil Service which indirectly have a bearing on the subject of pay, viz., leave and hours.

Leave.

84. The leave granted throughout the Administrative, Executive and Clerical branches of the Civil Service appears to us to be on a generous scale, appreciably higher than that which is normally allowed in outside employment. In the case of the Administrative Class 48 working days are allowed after 10 years' service. In the Executive Class, 36 working days are allowed in the Junior or Training Grade, while in the Higher Grade, leave rises to 48 days after 15 years of service in a grade eligible for 36 days. In the clerical class, 24 days are allowed in the Junior Grade and 36 days in the Higher Grade. Established typists and writing assistants are eligible for 18 days (after 5 years' service, 21 days) and Established Shorthand typists to 21 days (after 5 years, 24 days). These allowances of leave are additional to the usual public holidays.

85. In considering these allowances, however, and in comparing them with the practice in outside employment, it must be remembered that the leave regulations are strictly interpreted. Casual absences for any cause other than sickness are reckoned towards the annual leave allowed, while absence on Saturday counts as a full day's leave.

86. We think that even when due allowance is made for the strict interpretation of the Civil Service regulations, the resulting allowances are unjustifiably generous. We recommend that the present scale of leave should be cut down by one third, but in such cases, Saturday holidays should be conceded equal to the number of days deducted from the present leave allowance not exceeding one Saturday a month. A Saturday during a period of continuous leave should still rank as a whole day of leave counting against the annual allowance. This change, it appears to us, would secure that a due proportion of the longer leave allowances was taken on Saturdays.

87. We recommend that the Treasury should determine the precise scope of the application of this recommendation to classes other than the Administrative, Executive and Clerical in the light of their present allowance of leave. Ultimately this change, if adopted, will lead to economy in staff.

Hours.

88. The Report of the Anderson Committee contains the following paragraph:—

“ *Hours.*—The Civil Service rule for clerical and higher grades in London is a seven-hour day, including three-quarters of an hour off for lunch; in the provinces an eight-hour day.

“ In the higher grades the seven-hour day has little importance, as overtime is not paid for and the staff as a whole give generous measure.

“ For the routine clerical classes, the normal attendance should, in our view, be eight hours, including three-quarters of an hour off for lunch.”

89. We understand that this recommendation of the Anderson Committee has not been put into force. **We are of opinion that further consideration should be given to the subject with a view to the recommendations of the Anderson Committee being adopted.**

Although the economy in staff will not be mathematically proportionate to the increase in hours, some saving must necessarily accrue.

2. CIVIL SERVICE.

(Industrial Employees.)

90. The basis for the regulation of wages in Government Industrial Establishments is the Fair Wages Resolution of the House of Commons. This resolution, though applying in terms only to Government contractors, has been extended to all direct employees of the State, and it is the practice to pay wages not less and to give conditions not worse than those operative in the nearest comparable industry. In establishments which have direct analogues in the world outside the Public Service, e.g. the Printing Factories of H.M. Stationery Office and the depots of H.M. Office of Works, it is the practice to apply the rates and conditions which operate in the areas concerned. In the mixed establishments which contain several activities which are not to be found so grouped in the outside world, e.g. the Royal Dockyards and the Ordnance Factories, the practice is to follow the trade or industry primarily concerned.

91. In 1924, awards by a special arbitration body under Sir Harold Morris and also by the Industrial Court resulted in a 6s. addition to bonus for skilled men, 5s. to unskilled men in the Ordnance Factories, and 4s. to all Dockyard employees. Since that time 2s. has been added to the bonus figure in the outside engineering industry. By consequence there are at the present time differences of 4s., 3s., and 2s., between the rates paid in the outside

engineering industry and those paid in generally comparable establishments within the Public Service. The differential cost at the present date is approximately £325,000 per annum. We have no desire to disturb the basis on which industrial wages in Government establishments are regulated but we can see no justification for the continuance of this difference of remuneration which gives more than the acceptance of the "fair wages" basis demands, the Government being regarded as a model employer. We note from the terms of the Morris award that the Arbitrator took the view that any increase granted should, if possible, be such that on reconsideration or readjustment, or by effecting further economies, the outside trade might be able to come into line with the Government standard. In the present case, that expectation has not been fulfilled, the outside bonus as we have stated having only been increased by 2s. We recommend that the position under these awards should be reconsidered with a view to the abolition of the preferential bonus. No automatic and progressive wage reductions have taken place as a consequence of the fall in the cost of living in any of the establishments affected by these awards.

92. We have noted that under a concession granted in 1929, paid leave of six days a year is now granted in the Ordnance Factories and Royal Dockyards. We are aware that paid leave is granted in outside employment in a number of trades, and that such leave had also been granted for many years in other Industrial establishments under the Government (e.g. in the Post Office, Office of Works, and Stationery Office). It is not, however, the general practice to grant holidays with pay in outside engineering and shipbuilding industry. The cost of the concession made in 1929 is £200,000 a year.

3. FIGHTING SERVICES.

93. New rates of pay of the Fighting Services were fixed in 1919, and the rates then granted represented a substantial increase over the pre-war rates. In the case of officers, pay as then fixed was made subject to variation as the cost of living fluctuated. In the case of men, no provision was included for a change of rate. We might here, however, remark at the outset that both officers and men receive allowances in addition to pay which are provided either in kind or at a cash equivalent, and inasmuch as the value of these allowances varies with commodity prices, the total remuneration includes a variable factor on this account in addition to the variation which is made, in the case of officers, in their pay.

94. The 1919 rates were reviewed in 1923 by the Anderson Committee which found that the rates of pay of the rank and file and

of the lower ranks of officers were more than were necessary. Detailed consideration was given by a Cabinet Committee to the revisions to be made in the rates and in 1925 new rates were promulgated for the ranks in question. In the case of officers, the new rates include a provision for variation as the cost of living fluctuates analogous to the provision to this effect included in the 1919 rates.

95. The new rates took effect from the 1st, 5th and 26th October, 1925, for the Air Force, Navy and Army respectively, but they were applied only to new entrants to the Services on or after those dates. There are thus now in operation in each of the Services two distinct scales of pay.

96. The problem which faces the Committee is twofold—(a) are the rates fixed in 1925 justified to-day, and (b) should action be taken as regards those officers and men who were serving before October, 1925, and who in consequence still draw the 1919 rates.

97. The rates introduced in 1925 represented reductions when fully operative of the following percentages of the pay rolls :—

	<i>Per cent.</i>						
Navy	15
Army	20
Air Force	10

Although these percentages differ appreciably, the reductions in the Navy and Army were considered to be of equivalent effect, regard being had to the different balance of rank and service in the two arms.

98. The effect of the reduction in pay for newly joined officers (combined with the further fall in the cost of living) can be seen by continuing one of the tables in the Anderson report as follows :—

On Appointment.	Age.	Pay and allowances.			1931 as percentage of 1914.	1931 as percentage of 1923.
		1914.	1923.	1st July, 1931.		
Navy—Sub-Lieutenant ...	21	£ 178	£ 335	£ 277	155.6	82.7
Army—2nd Lieutenant ...	20	164	353	304	185.4	86.1
Civil Service—Asst. Principal.	23	200	313	278	139.0	88.8

99. A statement on broader lines indicates the steady reduction in average total remuneration since 1921 as follows :—

	Average cost per head.					Per cent. Increase on 1914.			
	1914.	1921.	1923.	1930 (actual).	1930 (if 1925 rates were fully opera- tive).	1921.	1923.	1930 (actual).	1930 (if 1925 rates were fully opera- tive)
	£	£	£	£	£				
Navy—									
Officers ...	263.1	539.3	490.8	471.1	460.3	105.0	86.5	79.1	7
Men ...	69.0	196.1	171.0	160.8	148.8	184.2	147.8	133.0	11
All ranks ...	82.2	224.8	197.6	187.5	175.6	173.5	140.4	128.1	11
Army—									
Officers ...	329.8	615.0	609.0	541.0	525.1	86.4	84.6	64.0	5
Men ...	60.0	151.1	127.5	108.1	101.4	162.0	112.5	80.2	6
All ranks ...	74.9	185.3	161.2	136.0	128.8	147.3	115.1	81.5	7
Air Force—									
Officers ...	—	625.1	646.6	607.0	601.0	—	—	—	—
Men ...	—	137.0	135.8	132.6	129.6	—	—	—	—
All ranks ...	—	186.7	189.6	183.3	180.1	—	—	—	—

(These figures include pay and allowances and the cost of emoluments issued in kind, (rat clothing, fuel and light, etc) with the exception of the cost of furniture and quarters and allowances issued in lieu thereof.)

100. It appears to us on these figures that if the 1925 rates were fully operative, a substantial reduction since 1923 would by now have been effected, and while we have not pursued our enquiries into such detail as would enable us to say that in all cases we have considered each individual rate, it is clear to us that only minor adjustments would at the most be called for. In these circumstances we do not consider that there is any case at the present time for variation of the 1925 rates.

101. This conclusion is reinforced when we bear in mind the fundamental basis of wage settlement set out in the preamble to this chapter. We cannot overlook the fact that recruiting for the Army is far from satisfactory, although many factors enter into the question of recruiting besides that of pay. Unsatisfactory recruiting is not necessarily evidence of inadequate pay, but clearly the position has to be borne in mind and if recruiting is not good, a strong case would have to be made out on other grounds before reduction could be imposed.

102. We turn now to the question of the "vested rights" of those members of the Forces who were serving before October, 1925. We would say at the outset that on the basis that rates of pay should be sufficient to recruit and retain an efficient service, we can see no logical justification for treating existing personnel better than new entrants. The rate at which the new entrant is recruited is one of the measures by which the conformity of rates to outside standards is to be judged. Logic is not, however, the only factor, and in particular the rates of pay of the earlier entrants have to be considered in the light of a number of statements which have been made to the personnel concerned. These we propose now to examine.

103. No officer or man serving His Majesty has any legal claim to particular rates of pay, so that as a matter of law, the rates of pay of the Services can be changed at any time and the changes can be applied to everyone in the service. On the other hand, although this is strictly the legal position, yet a moral claim to the retention of rates of pay may be created if statements have been made or action taken which afford reasonable ground for the expectation that the rates will not be changed; and this claim is much stronger if the statements made or action taken were such as would have created a contractual obligation had it not been for the privileged position which the Crown occupies in relation to its servants.

104. The above general principle applies to all servants of the Crown. Its application to the Fighting Services presents special problems. In the case of the rank and file, enlistment is for definite periods of service and the sailor, soldier or airman is not free to withdraw his services until those periods are complete. The right of the State to alter the pay of State servants is, we presume, a particular application of the right to dismiss at will—the employee is in effect dismissed and re-engaged, and he is free to refuse re-engagement if the revised terms are not acceptable to him. Clearly then special considerations arise in the alteration of the pay of a man who is not free to withdraw his services.

105. When the revised rates were introduced in 1925, definite statements were made to the men that the new rates would not be applied to men then in the service. The decision to this effect was communicated in the case of the Admiralty by a Fleet Order in the following terms—

"Men who enter the Royal Navy or Royal Marines after 4th October, 1925, will receive the rates of substantive pay shown in the schedule to this Fleet Order, in lieu of the existing rates.

"It has been decided on the present occasion that men serving on 4th October, 1925, shall continue to be paid according

to existing scales, and the application of this decision is defined in detail in the following paragraphs. It must, however, be clearly understood that men are not entitled to claim a right to any rate of pay or other emolument under existing scales in the event of reduced scales being introduced".

Similar orders were issued in the Army and Air Force.

106. It appears to us clear from these orders that although men serving before October, 1925, were promised the retention of existing scales, it was made clear to them that they had no claim as of right to such scales if reduced scales were introduced.

107. The question of introduction of the new rates can be considered under two heads, viz., introduction on extensions of service or re-enlistment, and introduction forthwith in all cases. To the former of these two heads we can see no objection. We understand in fact that the War Office were prepared in 1925 (if the other Services followed a like course) to make the new rates applicable on extensions of service or re-enlistment, but that the Admiralty objected to this course. It appears to us that the position taken up by the Admiralty in 1925 is impossible to defend. It means that once a man has been enlisted the rates of pay in force at the time of his enlistment must apply throughout the whole period during which he may serve on successive engagements. This principle applies not only to the actual rate of the bottom rank in which he enlisted, but to the rates of all higher ranks to which he may be promoted. We believe it is admitted that a man has no right of promotion, that in fact his prospects of promotion might be considerably worsened by re-organisation of establishment or in other ways without giving him any claim to compensation. Yet, although a man's prospects might be vitally altered by changes in the service, one particular condition of service, viz., rates of pay is held to be unalterable. We can see no justification for this artificial view and we think that if other conditions can be thus altered at will during a period of engagement, the rate of pay should be alterable if necessary actually on re-engagement.

108. We think, therefore, that the least change which should now be made is that the new rates should be applied to the pre-1925 personnel as and when they enter upon a new engagement.

109. In present circumstances, we think that more than this is called for. The financial circumstances of to-day are very different from those of 1925, and if the decisions of 1925 had to be taken now, we think that they would undoubtedly be in different terms. On equitable grounds, we consider that the right expressly reserved in 1925 to alter pay ought now to be exercised and that the men on the 1919 rates should be brought at an early date on to the 1925 rates, but it is necessary to bear in mind the difference we have

already described between the position of the enlisted man and the civilian employee of the State. It has been suggested to us that if the rate of pay of an enlisted man is altered during the period of his engagement, it would be necessary to give him the opportunity of discharge if he is unwilling to accept the new rates.

110. What the effect of the grant of the opportunity for discharge would have on the personnel we are not competent to gauge. On the one hand we have the anomaly of two men doing the same work under the same conditions drawing different rates of pay—a practice which would be impossible in industry. On the other hand, we have a large body of men who may well believe that the intention in 1925 was to continue their existing rates of pay throughout their period of then enlisted service and who have re-engaged in this belief.

111. **Despite the difficulties above enumerated, we recommend that the whole position should be reviewed, as we feel that all ranks should be put on the 1925 rates of pay.**

112. **The position of officers is not broadly different from that of the men. Similarly, in their case, we think the 1925 rates should be applied to all officers.**

113. In the case of officers, a further alteration appears to us to be called for. The standard rates, both 1919 and 1925, include provision for variation with the cost of living. The original rates were applicable for five years and thereafter review has been triennial, except that a concession was made for one year from 1st July, 1930, in view of a similar concession made in the Civil Service. The relative infrequency of review means that the rates do not keep close touch with the cost of living. While the cost of living was high, especially in 1920 and 1921, the pay of officers lagged behind the actual figure of increase. While the cost of living has been falling, the rates have been higher than current figures warranted. The rate payable from 1st July, 1931, to 30th June, 1933, will be based on a figure of 65 per cent. above pre-war. If the current cost of living figure of 45 per cent. above pre-war remains unaltered, it will not reflect itself in remuneration in the Fighting Services until 1st July, 1933.

114. **We think it not inequitable that as from a date as soon as possible after 1st July, 1931, the rate of deduction should be based on average cost of living over a period of six months before that date, and that it should thereafter be subject to more frequent review.**

The effect of this would be a reduction of 11 per cent. off standard rates instead of the 8 per cent. now ordered.

115. The financial effect of the pay of the Fighting Services being placed on a uniform basis and the introduction of 1925 rates forthwith is as follows:—

<i>Saving in a full year.</i>					
£					
Navy : Officers	...	...	...	...	87,000
Men	...	...	...	...	1,030,000
Army : Officers	...	...	...	...	140,000
Men	...	...	...	...	850,000
Air Force : Officers	...	...	...	...	19,000
Men	...	...	...	...	73,000
Total ...					£2,199,000

The saving from the introduction of revised cost of living deduction is:—

£					
Navy : Officers	...	...	...	...	180,000
Army : Officers	...	...	...	...	175,000
Air Force : Officers	...	...	...	...	45,000
Total ...					£400,000

4. POLICE.

116. The approximate cost of police pay in 1931 in England and Wales is £14,000,000, and in Scotland is £1,600,000. The Exchequer pays one-half of these sums, viz., £7,800,000.

117. Before the war, the rates of pay of the police varied very considerably in the different forces. The rate in London was 30s. to 42s., in Dorset 22s. 5d. to 30s. 3d. a week (plus in each case rent aid).

118. In 1919, on the recommendations of the Desborough Committee, uniform scales for Great Britain were established of 70s. rising to 95s. a week for Constables and 100s. rising to 112s. 6d. a week for Sergeants. In addition, in each case, free quarters or an allowance in lieu, free uniform and boots or a boot allowance were provided.

These scales contained no element variable with the cost of living. The last cost of living figure available when the Desborough Committee reported was 105 per cent. above pre-war. A clue to the cost of living figure which the Committee had in mind is given by paragraph 36 of their First Report, which reads " Taking all things into consideration we think that it would be fair to suppose that

the policeman's receipts would have to be about double what they were in 1914 to compensate for the increase of prices."

119. In 1920, when the cost of living rose rapidly, the police pressed for a bonus and following investigation by another Committee a bonus was granted in respect of the increase of cost of living above a figure of 130 above pre-war in the Metropolitan area and certain other large towns, 140 above pre-war in intermediate areas, and 150 above pre-war in rural areas.

This bonus ceased when the cost of living fell again below the above figures.

120. The Geddes Committee recommended that the obligation to pay the Metropolitan scale in county and borough police forces should be cancelled, and that certain allowances should be reviewed. These recommendations were not adopted, but instead, an all-round deduction of $2\frac{1}{2}$ per cent. was made from pay (in addition to the $2\frac{1}{2}$ per cent. rateable deduction towards pension which had been made for many years), and rent allowances were reduced or a charge made if accommodation was provided.

121. As early as 1923, the question of alteration of police rates was raised, and in that year the Desborough Committee was reconstituted to advise what readjustments should be made in the standard conditions of service of the Police Forces having regard, *inter alia*, to the economic conditions since the first Desborough Reports were made, and in particular to report upon the scale of pay to be given to new entrants to the police forces.

The Committee reported in March 1924 that "inasmuch as it must be unsettling to any service to have repeated revisions of their rates of pay, we are of opinion that it is not an opportune moment for disturbing an arrangement come to so recently."

122. The rates of pay of new entrants were next considered by a Sub-Committee of the Police Council who failed to reach agreement.

123. In 1925, following consideration by a Committee under Lord Lee, the deductions from rent allowances and the supplementary deduction of $2\frac{1}{2}$ per cent. from pay were discontinued, but the normal rateable deduction towards pension was increased from $2\frac{1}{2}$ per cent. to 5 per cent.

124. Police pay was next considered in 1927 by a Committee under Lord Chalmers. The terms of reference of this Committee were restricted, so far as pay was concerned, to the pay of new entrants. They recommended that a scale of pay should be prescribed commencing at 55s. a week for Constables and rising by 2s. biennially to 75s. a week with two further increments of 2s. 6d.

each after 21 and 25 years service respectively. For Sergeants, they recommended a scale of 85s. rising by 2s. 6d. annually to 97s. 6d. a week.

These recommendations were not accepted by the Government of the day, and the pay of police remains at the level fixed in 1919, subject, however, to the additional rateable deduction towards pension of $2\frac{1}{2}$ per cent. made in 1925 in place of the temporary deduction of $2\frac{1}{2}$ per cent. from pay which was imposed in 1922.

125. The cost of living when the Chalmers Committee considered police pay in 1927 averaged about 65 per cent. above pre-war. In the light of conditions then prevailing and after detailed comparison of rates of wages paid in industry that Committee thought a reduction of 15s. a week from the minimum pay of a Constable, rising owing to the slower increments to 25s. a week after 10 years' service, and falling again to 15s. a week at the maximum, and a reduction of 15s. a week from the pay of a Sergeant were justified. These reductions were $21\frac{1}{2}$ per cent. at the minimum, $27\frac{1}{2}$ per cent. after 10 years' service, and nearly 16 per cent. at the maximum in the case of Constables, and 15 per cent. at the minimum and 13 per cent. at the maximum in the case of Sergeants. Inasmuch as the police receive allowances in addition to pay, the reductions proposed would be somewhat less than the above figures when expressed as percentages not of pay alone but of total remuneration.

126. Since those recommendations were made, the cost of living has fallen from 65 to 45 per cent. above pre-war. Wages in outside industry have also fallen.

127. If the Desborough Committee's view that the scales they proposed had to be twice pre-war, in the circumstances which existed in 1919, to compensate for the increased cost of living is taken as a basis for consideration, then inasmuch as the present cost of living is half as much again as pre-war, a reduction of 25 per cent. would be justified.

128. As the police receive allowances in addition to pay, the relative prices of food are perhaps a more appropriate guide than the total cost of living figure, and on this basis alone a still greater reduction would be justified as the cost of food on the 1st May 1931 was only 29 per cent. above pre-war, compared with a figure of 104 per cent. in June 1919.

129. We have found some difficulty in determining the reduction to be recommended. On the one hand, it is clear that a substantial reduction is due as a measure of equity to taxpayers, ratepayers and wage earners. On the other hand, we appreciate fully that the task of the police becomes increasingly difficult in many ways in modern conditions and that the police fill an increasingly important role in our social organisation. Comparisons with pre-war are not

particularly relevant. Comparison with 1919 can only be made subject to important reservations.

130. In considering what our recommendations should be we have had to bear in mind that the present scales are uniform all over the country. We have noted, however, that the payment of rent allowances introduces an appreciable element of differentiation in the total remuneration. We have considered carefully the substantial reasons which have been urged in support of the present arrangement, and having regard to the strongly expressed views of the Home Office and Scottish Office, we do not recommend disturbing the existing uniformity of scales.

131. After balancing all these factors, we recommend that a reduction of $12\frac{1}{2}$ per cent. should be made from the pensionable salaries of all Constables and Sergeants. We think that in fairness to the men and to mitigate the effects of a sudden substantial drop in pay, the reduction should be made in two equal instalments, one as soon as possible and the other a year later.

We have not considered the rates of pay of ranks higher than Sergeant, which vary under the different authorities. We recommend that the Home Office and Scottish Office should consider the pay of the higher ranks in the light of our recommendations as regards Constables and Sergeants with a view to comparable reductions being made.

132. We note that in their Report the Desborough Committee considered that the Secretary of State and the Secretary of State for Scotland should have power jointly to fix the standard scale of pensionable pay for Sergeants and Constables and that the standard should be reviewed from time to time. We have regarded the reduction we have proposed as necessary to adjust the present scales to present conditions. We recommend that the scales as now reduced should be reviewed from time to time in the manner contemplated by the Desborough Committee in the light of any change of conditions there may be in the future.

133. If our recommendation is adopted, the remuneration per week of the police will be as follows (in addition to the value of pension rights):—

	Existing pay less $12\frac{1}{2}$ %.	Boot Allowance.	Rent Allowance.
Constable Minimum ...	61/3	1/-	} Variable; the highest rates being 18/- and 15/6 for married sergeants and constables respectively in London.
Maximum ...	83/1 $\frac{1}{2}$	1/-	
Sergeant Minimum ...	87/6	1/-	
Maximum ...	98/5	1/-	

The revised pay would as before be subject to a deduction of 5 per cent. towards cost of pension.

In addition, uniform is provided, and, in some cases, plain clothes allowance of 5s. a week for Sergeants and Constables, and detective allowances of 10s. a week for Sergeants and 7s. 6d. for Constables are also paid.

5. TEACHERS.

134. The estimated cost of teachers' pay in 1931 in England and Wales is £42,900,000 for elementary teachers (towards which the State pays in general 60 per cent. or £25,740,000), and £11,250,000 for secondary and technical teachers (towards which the State pays 50 per cent. or £5,625,000). The total State contribution in England and Wales is thus £31,365,000. In Scotland, the State pays into the Education (Scotland) Fund 11/80ths of this contribution, or £4,313,000. The total State grant payable in Great Britain as regards teachers' remuneration is thus £35,678,000.

135. As in the case of police, the salaries of teachers before the war varied widely in the different areas. After the war, their salaries were considered by the Burnham Committee with a view to securing "an orderly and progressive solution of the salary problem in Public Elementary Schools by agreement, on a national basis, and its correlation with a solution of the salary problem in Secondary Schools."

136. The Burnham Committee issued a series of reports, first establishing a Provisional Minimum scale, then recommending Standard Scales for elementary teachers and dealing with the distribution of these scales over the various Education Authorities, and later recommending scales for Secondary and Technical Schools.

137. The Provisional Minimum scale, recommended when the cost of living was about 125 per cent. above pre-war, on a rough average approximately doubled the pre-war pay of assistant teachers and more than doubled that of head teachers. When the later recommendations were made, the cost of living had risen appreciably further, being about 164 per cent. above pre-war, and the standard scales meant extra remuneration to elementary teachers of 159 per cent. above the pre-war average (i.e., they were roughly 2½ times pre-war). Provision was made that if the cost of living rose above 170 per cent. above pre-war, a bonus should be granted but no provision was made for a reduction if the cost of living fell.

138. The scales thus fixed were to hold good for the four years, 1st April, 1921, to 31st March, 1925. Their full effect was not however, felt at once as the increase necessary to bring each teacher to his right position in the new scales was given in three equal annual instalments, i.e., the full scheme would not have been in operation until the year beginning 1st April, 1923.

139. In the autumn of 1921, the Geddes Committee considered education expenditure. By this time, the cost of living had fallen appreciably and the Committee commented on the fact that while reductions on the ground of the falling cost of living had been applied to most classes of the community and the process was continuing, the striking fact about teachers' salaries was that their increases had suffered no check with the large fall in the cost of living and were still automatically increasing.

The Geddes Committee clearly contemplated substantial cuts in elementary, secondary and technical teachers' salaries.

140. No action was, however, taken at the time on the Committee's implied recommendation that the teachers must in the national interest face the prospect of substantial modifications in their rates of pay. The view was apparently held that alteration at that moment would involve a breach of faith.

141. In 1922, however, with a further fall in the cost of living, it became obvious that the full Burnham rates were no longer justified, and the teachers decided on 29th December, 1922, to accept a reduction of salaries of 5 per cent. from 1st April, 1923. This reduction was continued by consent for the year 1924-25.

142. At this point, reference must be made to teachers' pensions. Before the war, the scale of pensions was inadequate, and towards these inadequate pensions the teachers contributed £3 12s. 0d. a year (men) and £2 8s. 0d. a year (women). In 1918, the contributions were abolished and the scheme of pensions was improved, being approximated to the Civil Service scheme. The pensions were paid entirely by the State. The Geddes Committee criticised a scheme under which the local authority had control of the pay, age of retirement and promotion of the staff, but no financial interest in the pensions cost. They recommended that a 5 per cent. levy should be paid by teachers towards their pensions, and this recommendation received legislative sanction from the 1st June, 1922. In considering the pension deduction then imposed in its relevance to salary comparisons, it should be borne in mind that the scheme of 1918, even with the contributions imposed in 1922, is more favourable to the teachers than their pre-war contributory scheme.

143. The Burnham scales were due for review in 1925. In 1923, negotiations were commenced and the local authorities demanded reductions of 15 per cent., then 12 per cent., then 10 per cent. as an all-round reduction before considering details. These negotiations, however, broke down, and the determination of the review to be made was referred to Lord Burnham as arbitrator. The awards then made effected a reduction on a salary bill of some £50,000,000 of a net sum of less than £500,000 or under 1 per cent.

144. The effect of the various revisions can be seen from the following table :—

	Certificated		All Certi- ficated.	All Uncer- tificated.	All Supp- lementary.	Total Men.	Total Women.	All Teachers.
	Men.	Women.						
AVERAGE SALARY AT :—	£	£	£	£	£	£	£	£
31st March, 1914	147	103	118	58	40	139	82	97
31st March, 1922 (Burnham scales in first year).	337	261	284	146	96	326	215	241
31st March, 1923 (Burnham scales in second year).	346	270	294	151	97	336	224	251
31st March, 1924 (Burnham scales in full operation but by this time subject to 5 per cent. reduction).	337	266	289	147	96	328	221	248
31st March, 1930	334	254	279	143	98	324	217	245

The full effect of the Burnham scales, had they come into operation without deduction can be ascertained by adding 1/19th to the averages on 31st March, 1924, viz :—

Average salaries on 31st March, 1924, increased by 1/19th.	355	280	304	155	101	345	233	261
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Note :—The salaries of certificated teachers in 1914 were subject to pension contributions of £3 12s. 0d. per annum (men) and £2 8s. 0d. per annum (women).

There were no pension contributions in 1920 or 1921. As from 1st June, 1922, the salaries of pensionable teachers (this includes all the classes in this table except the supplementary teachers) were subject to a pension contribution of 5 per cent. The figures in these tables show the salaries before deduction of any pension contributions.

145. The difference between the figures in the last table and the figures for 31st March, 1930, thus shows the effect of the 5 per cent. reduction in 1923-25 and the further alterations made on review from 1st April, 1925, viz. a total reduction on the average salary of all teachers compared with the full Burnham scales of 6.1 per cent.

146. The scales fixed in 1925 were subject to review after 31st March, 1931, on one year's notice. Notice has now been given to terminate them as from 31st March, 1932, and we understand that consideration is now being given to revised scales.

147. Before examining the scales in more detail, we turn to the method of review. Teachers are engaged and paid by the local authorities and the settlement of their salary scales is regarded as a matter for negotiation between representatives of the teachers and local authorities. The interest of the State arises through the payment of percentage grants. In theory the State is not committed to payment of grant on the full scales and it need only recognise for grant purposes such scales as it thinks reasonable. Various reasons have been urged in defence of this position. But whatever its theoretical justification may be, it appears to us from a practical point of view to be indefensible. The State is clearly in a very difficult position if it attempts to pay grant on scales lower than those to which representatives of the local authorities and the teachers have agreed, or which have been determined by an Arbitrator. In practice, the position must work out that local authorities and teachers determine the salaries and the State has to pay 60 per cent., or in some cases more (in the case of elementary teachers), of the bill.

148. The least reform which appears to us to be essential is that the State should be a party to the negotiations and should place before the negotiators the important national financial considerations which arise on the settlement of a matter involving so heavy a charge on the taxpayer. But in present circumstances, more than this appears to us to be necessary. In the present financial situation, it appears to us essential that the Government must itself announce to the negotiating body that grants will only be paid on the assumption that there is an overall cut in the total cost of a prescribed percentage.

149. In this connection we might point to the position of the police. Like teachers, they are engaged, paid, promoted and retired by local authorities. Unlike teachers, their pensions are paid by local authorities, aided by a percentage grant from the State. Yet in their cases the State fixes the salaries. We do not see any fundamental reason why if the fixing of salaries by the State is appropriate in the case of the police it should be inappropriate in the case of the teachers.

150. It is clear from the circumstances under which the Burnham Committee originally considered its recommendations, and in particular from their proposal that a bonus should be paid if the cost of living rose above a figure of 170 per cent. above pre-war that their scales were framed in the light of a cost of living very near the post-war peak. The fall in cost of living from 170 per cent. above pre-war down to the present level of 45 per cent. above pre-war is a fall of just over 46 per cent. If the salaries of teachers had been adjusted in accordance with the Civil Service cost of living scheme, a peak figure of £355 a year (the full Burnham average of certificated men teachers) would on the present Civil Service figure of 55 per cent. above pre-war now have fallen to £221 a year, a fall of 38 per cent., and as much as 34 per cent. below the present average salary of certificated men teachers (£334). For certificated women teachers, the peak figure of £280 a year would similarly have fallen to £168 a year, a fall of 40 per cent., and 34 per cent. below the present average (£254).

151. As was pointed out by the Geddes Committee, the majority of the profession have acquired their qualifications largely at the expense of the public at an average cost to the State of £70 a year for either two or four years.

152. The remuneration of secondary teachers has followed lines closely comparable with those of elementary teachers. A table on similar lines to that given for elementary teachers earlier in our report is appended:—

	Graduates.			Non-Graduates.		
	Men.	Women.	Men and Women.	Men.	Women.	Men and Women.
	£	£	£	£	£	£
AVERAGE SALARY AT—						
31st January, 1914 ...	225	151	194	165	123	139
31st March, 1922 ... (First year of Burnham scales).	451	343	400	357	272	301
31st March, 1923 ... (Second year of Burnham scales).	461	359	413	376	289	319
31st March, 1924 ... (Burnham scales in full operation but by this time subject to 5 per cent. reduction).	442	348	399	365	282	310
31st March, 1930 ...	436	348	397	330	256	278
31st March, 1924, increased by 1/19th.	465	366	420	384	297	326

153. It is clear from this table that the pay of graduates has followed very closely that of elementary teachers. The pay of non-graduates appears from the average figures to have been reduced more than that of the other classes, but we understand that this is due to changes in classification having been made between 1924 and 1930, and not to the scales having been modified to a degree different from the others.

154. In the case of technical teachers, there is a wider variety of qualification included in the group than in the case of elementary teachers and secondary teachers. The bulk of the technical teachers are paid on the secondary teacher scales, but a number of special posts exists.

155. The indications we have given of the effect of change in the cost of living on teachers' salaries all point to a reduction in the neighbourhood of 30 per cent. Having regard to the practical difficulty of enforcing so large a reduction even though it may be justified, and to the gradual adjustment to a higher standard of living which must necessarily have followed the increasing purchasing power of their salaries, we cannot recommend so high a reduction. We feel, however, after balancing the relative claims of the teacher and the taxpayer and ratepayer that 20 per cent. is the minimum reduction which should be made. We would point out that on the average as regards elementary teachers, this cut will still leave them with more than double their pre-war remuneration.

We recommend that provision should be made within the existing arrangements for the salaries as reduced to be reviewed from time to time in the light of any change of conditions there may be in the future.

PENSIONS.

156. The total pensions payable in 1931 to the classes covered by this part of our report are estimated to amount to:—

	£
Civil Servants (including Revenue Departments, Post Office, and civil pensions in the Admiralty, War Office and Air Ministry)	8,000,000
Fighting Services	16,500,000
Police	5,600,000
Teachers	6,500,000
	<hr/>
Total	£36,600,000
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We would emphasise that this sum of £36,600,000 includes only payments to retired servants of the State and local authorities, and not such pensions as Old Age and Widows' Pensions or War Pensions.

There are, however, included lump sum awards on retirement, gratuities on death, marriage gratuities, injury grants and a number of similar miscellaneous items.

In addition to the above sums there are pensions and allowances payable to former members of the Royal Irish Constabulary amounting to £1,812,563 gross.

157. The Exchequer does not bear the whole of this cost.

(a) In respect of Civil Servants and the Royal Irish Constabulary recoveries are effected amounting to £1,795,306 of which the largest items are :—

	£
Irish Free State	1,309,722
Northern Ireland	372,525
Savings Banks Funds	101,680

(b) In the case of police, a rateable deduction of 5 per cent. is made from pay towards the cost of pension and the Exchequer pays 50 per cent. of the net cost.

(c) In the case of teachers, contributions by the teachers and their employers of 5 per cent. of salary in each case are received.

The amount so recovered after allowing for the State grant payable in respect of the employers' contribution is :

	£
England and Wales	3,803,200
Scotland	535,602

Allowing for these contributions and recoveries, the net cost to the taxpayer of all the pensions here considered is about £29,700,000, and this charge is steadily increasing.

158. The question of pensions falls under two broad heads :—

(a) Pensions of those who have already retired ;

(b) Pensions which will ultimately accrue to those now serving or to new entrants to the services.

1. EXISTING PENSIONERS.

159. It is only in the case of existing pensions that there is any possibility of immediate economy. We recognise that the field contains widely differing types of cases ranging from some pre-war pensions which have not been increased, through many intermediate types, to post-war pensions based on salaries at their peak which have not been reduced. If adjustments are to be made to bring pensions which reflect a cost of living higher than to-day into line with those which would be awarded under present conditions (including the effect of reductions in pay which we have recommended), a wide variety of cuts would be necessary to secure

even approximate fairness over the field and the whole question would require examination in considerable detail.

160. We have considered the arguments for and against alteration of pensions. On the one hand, if existing pensions are not touched, there will be appreciable anomalies between men who retire immediately before the reductions in salary which we recommend take effect, and those who retire directly after such reductions have been effected with pensions based on the lower salary rate. Further, the increased purchasing power of the pound sterling in recent years has increased the real value of pensions as it has improved the true worth of salaries and if this were the only consideration the case for reduction of those post-war pensions which have not varied with cost of living would be indisputable. On the other hand, pensions are in a different category from salaries. It may be argued that in the case of men who have actually retired, the amount of pensions payable must be regarded as definitely determined irrespective of the actual money worth. The legal position varies between the different groups. No legal rights attach to some pensions while others could only be altered by legislation. It is represented to us that apart from any difference in the legal position a pension now in course of payment represents the fulfilment by the State (or the local authority) of the terms on which the employee gave his services and that any alteration of existing pensions would be a breach of what is morally a contractual relationship.

161. After careful consideration of the matter in all its implications, we reach the conclusion that existing pensions can only be altered if a general measure of all-round sacrifice is imposed. We defer dealing with this possibility until the conclusion of our report. We recognise that this course will lead to the anomalies we have mentioned, but we think those anomalies must be faced.

162. We do not think that this general conclusion precludes an adjustment of the pensions of officers of the Fighting Services on the same lines as our proposals in pay, to bring the variable part of pensions into earlier touch with cost of living changes.

163. If any alteration of pensions is necessary we think that before any overall deduction is made, the following adjustments of existing pensions to secure relative equality between the different classes should first be effected. In the case of the *Civil Service*, pensions awarded between the 1st March, 1920 (when the present cost of living bonus scheme began) and March, 1922, should be made subject to variation in the same way as pensions awarded after March, 1922, which contain a variable supplement. In the case of the *Fighting Services*, the new 1930 rates for men should be applied to existing pensioners. In the case of the *Police*, pensions based on Desborough pay should be reduced by the percentage by which we recommend that pay should now be reduced.

In the case of *Teachers* a similar scheme should be applied, but with a measure of grading to allow for the fact that pensions are based on average salary over five years.

2. FUTURE PENSIONS.

164. We now refer to the question of the pensions which will ultimately accrue to those now serving and to new entrants. Any economies recommended in this direction will only become effective as the employees retire and there will be no immediate relief to the taxpayer. At the same time we consider that there are various important points which require consideration.

165. In the case of all classes, except the Fighting Services, pensions are based on pay, and where we have recommended alterations of pay, alteration of pensions will automatically follow, either at once, where pensions are based on actual pay, or after a short period of years, where pensions are based on average pay. In the cases of the Civil Service and officers of the Fighting Services, a portion of the pension varies as the cost of living changes.

Civil Service—Marriage Gratuities.

166. We can find no sufficient justification for the award of gratuities to established women employees on marriage. These gratuities, amounting at the maximum to one year's pay in each case, are not awarded under statute. Their total cost is about £167,000 a year. We are not aware that gratuities are generally granted in outside employment, and we think that the practice should be discontinued. Without these special gratuities, the pension rights of women employees will still be analogous to those of men.

Police.

167. Owing possibly to the nature of the duties and the limited number of posts suitable for older men, police are allowed to retire on pension after 25 years of service. This service is often completed at 45 years of age or soon after. A member of the police force can thus retire voluntarily at an age when he will normally expect to undertake further employment, indeed the police officer will, by reason of his previous experience and of the high respect in which the police are held, be in a favourable position for obtaining it. Police who entered the service before 1919 in England and Wales are in the majority of forces qualified for their full pension of two thirds of pay after 26 years of service. Scottish police, owing to a difference of their pre-1919 pension terms, are not qualified for full pension until 30 years of service is reached. Therefore, as regards men in England and Wales who are now retiring voluntarily on pension, the full pension may be reached while a man is still at a relatively early age.

168. It should be appreciated that the present system involves a quite disproportionate non-effective charge, and the pension bill is rapidly rising. Expressed as an annual addition to salary payable throughout the service of each officer, the pension rights are worth rather more than £50 a year (from which the rateable deduction of 5 per cent. of pay has to be subtracted) in the case of police in England and Wales who entered the service before 1919. It is estimated by the Government Actuary that for every 100 men on the active list, there will, when stability is reached, be over 60 men on pension, with a pension charge after deducting contributions by the men of 46 per cent. of the salary bill. We think this a serious situation calling for immediate action with a view to the reduction of the accruing pension liability. **We recommend that the right of voluntary retirement after 25 years of service should be withdrawn from the existing personnel and that retirement should not be permitted before the age of 50 is reached. In view, however, of expectations which have doubtless been formed, we think it would be necessary to allow a period of notice (which we suggest might be five years), before this change becomes operative.**

169. **We recommend that the whole subject of police pensions should be reviewed at a very early date, with a view to determining conditions of service for new entrants which will effect a further saving in the present high non-effective cost.**

Fighting Services.

170. We have already referred to the fact that pensions in the Fighting Services are not based on pay. Consequently the reduction in pay which we recommend will not be automatically reflected in pension. In the case of officers only 20 per cent. of the pension varies with the cost of living. In the case of men's pensions, there is no provision for variation with the cost of living, and the increased pension rates fixed in 1919 are being drawn in full by all men discharged on pension since the war, and by former pensioners who rejoined for service in the war. As from the 1st April, 1930, a lower scale of pension has been introduced, representing an average reduction of about 18 per cent. in the 1919 scale, but this scale only affects men entered from that date. On the present basis, awards on the 1919 scale will continue to be made for 20 years or more, and it will be a very long time before any appreciable saving results from the new scale.

171. According to the traditional practice of the services a new pension scale is not applied to the detriment of a man during his service. In the terms of the Army Pay Warrant "A soldier entitled to pension, for the payment of which money may be voted by Parliament, may have the benefit of any Warrant or regulation in force at the date of his enlistment." This provision seems to us to

go beyond what is necessary and in the circumstances of to-day to be indefensible. In our view the appropriate time to declare a man's entitlement to pension is when he enters upon his final term of service qualifying him for pension in due course. He is then free to serve or withdraw and the State is free to accept or reject his further services. We think that a condition of acceptance for further service should be the application of the pension scales current at the time.

172. We recommend therefore that the 1930 scales of pension should be applied, on re-engagement or extension, to all men now serving. For men already serving their final term of engagement different considerations arise which require to be considered in the light of the action which may be taken on our suggestions on pay, but we think a satisfactory scheme could be framed on the basis that a man whether enlisted before or after 1925 should, as from the date of introduction of 1925 rates universally, begin to earn pension in respect of his future service on the new 1930 rates. Having regard to the different conditions on which pensions in the Fighting Services are based, this appears to us to be the greatest extent to which action can be taken in the case of the Services in harmony with what will happen automatically in the other cases we have under review.

173. In the case of officers, in view of the system of cost of living adjustment it was apparently considered unnecessary to lay down new scales of retired pay in 1930 when the men's pensions were revised. We have already recommended an acceleration of the cost of living adjustment on pay and existing pensions and a similar adjustment should be made on future pensions.

174. Apart from this change, we think that the pension scheme for officers in the three Services calls for reconsideration.

All three Services are faced with the same problem. The essential requirement of a combatant service is a high proportion of fairly young officers. Consequently, many more officers have to be recruited to the services than can hope to find life careers therein. The three services tackle this fundamental problem in different ways, and with widely different results as regards non-effective cost. In the Air Force, there is a large element of short service recruitment. Speaking broadly, only such number of officers are engaged on permanent commissions as can hope to find careers in the service, allowing a margin for selection in the filling of higher posts. In the Navy and Army, on the other hand, officers are normally engaged on pensionable tenure and reliance is placed on limitation of promotion, followed by the compulsory retirement at early ages of those who are passed over, in order to weed out those whom it is not desired to retain to fill the higher posts. In the case of the Navy, in the Executive Branch the prospect open to nearly two-thirds of the officers is

retirement as Lieut.-Commander, at or before 45; of the remaining one-third a large proportion retire before 50, as Commanders or as Rear-Admirals retired immediately on promotion.

175. The award of life pensions at early ages is expensive. Where early retirement ensues, the basis of pension naturally tends to be not only a reward for past service but compensation for premature retirement. Thus the pension cost, in terms of the annual equivalent during service, becomes out of all proportion to the effective cost in pay, etc.

176. In the case of the Navy, we find that in 1930 in the Executive Branch there were 78 retirements on retired pay, of which 36 were retirements of Commanders at an average age of 46. The average retired pay of the 36 Commanders at standard rates was £581 a year.

177. The very high cost of these premature retirements should be realised. In the case of these Commanders, the capital sum equivalent at retirement to the standard retired pay is £8,950 per officer, and the annual addition to salary during service which would have been necessary to produce this capital sum on retirement is £195 a year. This calculation is based on standard pay and the actual rates differ from standard pay by the amount of the cost of living deductions. But if an average cost of living reduction of 12½ per cent. over the whole period during which pension will be drawn is assumed, the capital value of the pension is nearly £8,000, equivalent to an annual addition to pay during service of about £170 a year.

178. The financial effect of early retirement in ranks higher than Commander is still more striking. Taking again the actual retirements in 1930, the average age at retirement of Captains and those Rear-Admirals who had spent one day only in that rank is 49. The capital value of the pension and the annual equivalent addition to pay throughout service (again making a deduction of 12½ per cent. to allow for cost of living deductions) were £11,100 and £197 a year respectively for each officer.

179. We feel that these facts merit serious consideration, although it is beyond the practical scope of our Enquiry to make concrete suggestions for reform. Any pensions scheme must necessarily coincide with the requirements of a service, but if the cost is unreasonable the requirements should be reconsidered. We cannot think that Naval requirements inevitably must involve such a rapid passage through the lists as now obtains, and we suggest that it should be possible to provide the necessary number of officers for the Navy on the basis of a longer average career, with a resulting saving not only in non-effective costs but also in the provision for training.

180. When we turn from the Executive Branch to certain other branches (Instructors, Chaplains, Doctors and Accountants) we find even higher values of pensions. Before the war, these branches of the service were retired under conditions differing from those of the Executive Branch. Compulsory retirement was at 55 or 60. The regulations are now the same as for the Executive Branch and provide not only for compulsory retirement at much earlier ages, but also ready facilities for voluntary retirement on retired pay from the age of 40. Where entry to the service is at higher ages the value of the pension correspondingly bears a higher ratio to the pay. In the most extreme case brought to our notice, the three Chaplains who retired in the years 1928-30, at an average age of 49 and with an average of 18 years' service, received pensions which represent on the average an annual addition to pay of over £260 a year for each year of service, or a capital sum equivalent to £6,900 for each chaplain.

181. In the case of the Army, the position is not unlike that of the Navy though the average ages of retirement are somewhat higher and the value of pension somewhat less. The same observations which we have made in the case of the Navy apply to the Army.

182. We think that the whole scheme of pensions in the Fighting Services calls for immediate examination in the light of its extremely expensive character. In the particular case of the Non-Executive branches, we recommend as an immediate measure that all age limits for retirement under 60 should be increased by five years pending such enquiry and that voluntary retirement on retired pay should not be permitted to an officer with less than 20 years' service.

3. GENERAL CONSIDERATIONS ON PENSIONS.

183. We have already referred in the first chapter of our Report to the manner in which liabilities for pension charges are increasing, and we feel that the immediate and prospective position of the National Exchequer is such that the steady increase, superimposed on the present large total, must be viewed with apprehension.

If our recommendations are adopted, there will, in the course of time, be some slackening in the rate of growth, but the full effect of new pension conditions cannot be felt for many years.

184. We feel that it is a matter for serious consideration whether the accepted methods of Government finance are really adequate to deal with services where there is a large deferred liability. The question is mainly one of degree. Where an employee's current service carries with it a deferred benefit representing a reasonably small percentage of salary we see no strong objection to the present

method of accounting. But where the value of the deferred benefit rises to a high percentage of the current salary charge, there is great danger of liabilities being incurred without the taxpayer realising the large extent of his commitments until it is too late substantially to reduce them. In the case of the police, teachers and the Fighting Services there should be constituted a pension fund to which the appropriate percentage of salaries should be paid in order that the expensive character of the pension schemes may be fully appreciated and the full cost of the heavy liabilities involved may be met at the time the liabilities are incurred.

CONCLUSION ON PAY AND PENSIONS.

185. In conclusion, we would stress two points. First, it has been our object to secure fairness as between the different classes we have considered. It may appear that our recommendations differ between one class and another to an extent which might suggest that we have dealt harshly with some classes. We are satisfied that this is not so, and that widely as our recommendations differ, they do no more than reflect the more favourable treatment that some classes have received since the immediate post-war period. We regard the reductions we have proposed, not as sacrifices necessitated by national financial stringency but as readjustments necessary to re-establish fair relativities over the field of Government and local authority servants and with wage earners generally.

Secondly, while we feel that our recommendations are re-adjustments, the classes concerned will probably not unnaturally regard them as sacrifices called for on their part. The spirit in which those sacrifices are made will depend on the extent to which the Government show by their actions over the whole field of expenditure that strict economy is recognised as a national necessity. No one will recognise the need for economy at his expense if he sees unrestricted expenditure continuing in other directions.

CHAPTER IV.

DEFENCE.

186. The total of the Estimates for the Fighting Services in 1931 is :—

	£
Navy	51,605,000
Army	39,930,000
Air Force	18,100,000
	<hr/>
Total	£109,635,000
	<hr/>

187. There is a deeply rooted belief in many quarters that the Fighting Services offer a large scope for economies, and we think it right to consider this expenditure from a general point of view before turning to the Services individually. We suspect that criticism of expenditure in other directions has been less readily forthcoming in the past owing to the belief that if only the Government of the day would tackle the expenditure in the Navy, Army and Air Force, large countervailing economies could be obtained. If in future State expenditure is to be adequately considered as a whole, in the light of the ability of the taxpayer to bear the burden, we think it essential that there should be a right understanding of what economies are possible in the Fighting Services and in what directions and under what conditions those economies must be sought.

188. The cost of the Fighting Services depends on three main considerations : (1) size ; (2) design ; and (3) administration. By " size " we mean the number of fighting units—ships ; battalions or brigades, etc. ; and air squadrons. By " design " we mean the tonnage, speed and armament of the several classes of ships ; the size, organisation and equipment of the several military units in the Army ; the speed, equipment and design of the several squadrons of the Royal Air Force. " Administration " requires no special definition. Of these three components it is size and design which have the greatest bearing on cost ; the effect of administration on finance is relatively less important. It is obvious at once that " size " and, to a lesser extent, " design " (which together may be described as " strength ") are determined mainly by consideration of the commitments which have been undertaken by H.M. Government, either in the interests of national security or as

matters of international obligation, and of the political situation, present and prospective, as it affects those commitments.

189. It follows therefore that the most important elements in the cost of Defence are dependent on questions of international policy. We would disclaim at the outset any desire to interfere in these matters, especially as the Government at present has the whole subject under consideration with a view to the Disarmament Conference to be held early in 1932. We have, however, had certain confidential information placed at our disposal by the Service Departments, and we are satisfied, from the evidence submitted, that the present strength of H.M. Forces is no more than adequate for requirements under present world conditions.

190. It is obvious that, so long as unlimited competition exists between different nations, any interference as a measure of economy with the development of the Services in this country would put us at a disadvantage in relation to other countries.

It appears to us therefore that, on the broad issues of size and design no reduction is possible pending a further review of the question of commitments in all its aspects such as will be undertaken at the forthcoming Disarmament Conference.

191. We would respectfully suggest that His Majesty's Government in considering the recommendations to be made on their behalf at the Disarmament Conference should have clearly before them the effect of their proposals on the national finances. We further recommend that each of the Services should be examined immediately after the Conference to determine in the light of the conditions then prevailing the organisation best fitted to carry out the national requirements with the least expense.

192. If it is accepted that any fundamental reorganisation of the Services is out of the question pending the further Disarmament Conference, it remains for us to examine what are the possibilities of economy under the head of Administration within the existing organisations.

193. It should be appreciated how much of the cost of the Services is determined once the strength is fixed. To illustrate this, we propose to analyse the gross expenditure of the three Services for 1931 on the basis of the Estimates presented to Parliament. This gross expenditure is £122,515,720, which is reduced by receipts from inter-departmental payments, Dominion, India and Colonial Contributions, etc., amounting to £12,880,720, to £109,635,000, the net figure we gave at the beginning of this Chapter.

194. We also give figures similarly analysed for 1925 and 1928 for purposes of comparison.

Analysis of Defence Expenditure.

	1925 Expenditure.	1928 Expenditure.	1931 Estimates.
Personnel—	£	£	£
Pay, Clothing, Provisions	46,591,000	43,131,000	40,301,000
Reserves of Personnel	6,174,000	6,228,000	6,571,000
Medical Services	2,107,000	2,164,000	2,076,000
Educational Services	2,014,000	1,923,000	1,866,000
Transport (Freight and Travelling) ...	4,119,000	3,610,000	3,291,000
Accommodation (including lodging allowance, fuel and light).	2,030,000	2,080,000	1,974,000
Total for Personnel and Allied Services £	63,035,000	59,136,000	56,079,000
Works, Buildings and Lands	£ 10,810,000	7,570,000	7,556,000
General and Technical Stores	£ 5,055,000	4,132,000	4,129,000
Mobile Fighting Material			
(i) New Construction of H.M. Ships	7,491,000	9,947,000	5,571,000
(ii) Repairs and Maintenance of H.M. Ships	8,378,000	7,355,000	6,741,000
(iii) Tanks, Tractors, etc.	556,000	703,000	578,000
(iv) Aeroplanes	6,362,000	5,617,000	6,809,000
Total for Mobile Fighting Material £	22,787,000	23,622,000	19,699,000
Guns, Projectiles and Ammunition	£ 4,832,000	4,248,000	3,984,000
Fuel for Ships, Mechanical Transport, and Aircraft	4,774,000	3,727,000	3,516,000
Scientific Services (including Research, Inspection, etc.)	2,841,000	2,902,000	3,016,000
Headquarters	2,918,000	2,704,000	2,651,000
Miscellaneous Services	2,339,000	1,561,000	1,418,000
Airships	401,000	383,000	59,000
Civil Aviation	279,000	377,000	651,000
Non-Effective Services (Pensions) ...	17,568,000	18,015,000	18,632,000
Gross Total	£ 137,639,000	128,377,000	121,390,000
Receipts	17,841,000	14,349,000	11,755,000
Net Total	£ 119,798,000	114,028,000	109,635,000

NOTE.—The Admiralty contribution to the Air Ministry in respect of the Fleet Air Arm has been excluded from both expenditure and receipts in the above table as it is merely an interdepartmental payment. The total cost of the Fleet Air Arm of about £3,000,000 a year is distributed over the appropriate items in the table.

195. This table indicates in broad outline how continuous has been the reduction in our defence expenditure in the last six

years. Practically all the items show a steady fall, while the total of the gross expenditure has fallen by as much as £16,249,000. It also indicates how much of the present expenditure is directly dependent on the size of the forces; thus personnel and allied services connected with personnel now account for £56,079,000 and the pension charge is £18,632,000—a total of £74,711,000 on these two groups alone, viz. :—61 per cent. Mobile Fighting Material accounts for £19,699,000, Works and Buildings for £7,556,000, General and Technical Stores for £4,129,000, Guns, Projectiles and Ammunition for £3,984,000 and Fuel for £3,516,000. These items, all of which are necessary to the manning and maintenance of the fighting forces at their present strength, absorb £38,894,000 or 32 per cent. Of the remaining items Headquarters, Scientific Services, and Miscellaneous represent £7,085,000, part of which is directly connected with " Strength " and the balance of £710,000 is expenditure on Airships and Civil Aviation borne on the Defence Votes. The table we have given does not pretend to be accurate in all details. It is impossible to make an objective analysis of Defence Expenditure so as to correspond exactly with the three subject heads, Size, Design and Administration; each of these elements enters in a greater or less degree into each of the items in the table. But the broad conclusion to be drawn is that fundamental economies are not practicable while the strength of the Forces remains on its present basis. Economies can be made in certain directions, and we make specific recommendations later, but such savings as are possible consist rather of a paring down of necessary services to the minimum consistent with efficiency, than of a fundamental excision of whole items or services. Large scale economies must await further reduction in the strength of the Services, which in turn must depend on general agreement on the policy of international disarmament.

196. In considering such small scale economies as are possible, it must be borne in mind that substantial reductions have been made in recent years in the total of our Defence expenditure as the table on page 62 shows. We shall submit comparative statistics over a series of years when we consider the Departments separately. In addition to the drastic recommendations of the Geddes and Colwyn Committees, constant pressure from the Treasury for reduction in the total expenditure has brought about an acute internal competition for money between the different branches within each service. Year by year, an internal pruning has been going on the effect of which has been to produce an increasing economy in all branches. We would take the opportunity at this stage of remarking that we have been impressed by the close attention given in recent years by each of the Services to the purely financial side of their operations, and to the ready co-operation with the Treasury which now exists in efforts to restrict expenditure to the minimum. We welcome the improvement which appears to us

to have taken place in recent years in the relations between the Services and the Treasury. To-day it can no longer be said that the Services consider that it is for the Government to determine policy and that the sole function of the Treasury is to pay the bill for carrying out that policy.

197. The reductions of recent years can be considered in another light in their bearing on our problems. In the opinion of the Chiefs of Staff—which after the frank and exhaustive evidence given to us we accept—the actual size of our Fighting Forces is now at the minimum consistent with the carrying out of their allotted task and the present standard of size is only practicable because of the high standard of efficiency both of personnel and of material maintained. We have borne this consideration in mind and realised, in making our recommendations, that if efficiency is appreciably impaired, there would be a considerable danger that some increase in the size of the Forces would be necessary to enable them to fulfil their responsibilities.

Before turning to the examination of the Departments individually there are certain matters which are best treated in regard to the services as a whole.

(i) *Ministry of Defence.*

198. We have given very careful consideration to this question, because there is undoubtedly a widespread impression in the public mind that large savings might be made in the cost of National Defence by some form of amalgamation of the three Services under a single Minister. It is suggested that such a Minister would not only be able to amalgamate common administrative services, but would also ensure that the whole problem of National Defence was studied from a single standpoint, that economy was secured by the substitution of alternative methods of defence wherever possible, and that where one of the three Forces was being developed in a particular direction, the harmonising of its growth with the strength of the other two was duly considered.

199. We have received valuable evidence on the subject from the Chiefs of Staff and from the Secretary of the Committee of Imperial Defence. We are of course primarily interested in the question from the point of view of its effect on the actual cost of the Fighting Services, but we cannot forget that, in the search for true economy, it is essential to take the wider view and consider the effect of any far-reaching change of system on the efficiency of the service.

200. Our conclusion after careful review of all the evidence is that no substantial reduction of cost would follow from the creation of a Ministry of National Defence, and that on the contrary there would be a serious risk that the efficiency of the Services might be impaired by the alteration of system involved. We have therefore rejected any idea of economy by this method; and we

hope that our conclusion will be accepted as finally disposing of the suggestion that millions of money could be saved by the formation of a Ministry of Defence.

201. In reaching this conclusion, we do not mean to imply that there is no further room for economies by means of greater co-ordination between the three Services; but we see no reason why such economies should not be achieved under the present system, in so far as it is possible to do so without loss of efficiency. Such economies will fall under two heads, Policy and Administration. (1) As regards the former, we are satisfied that the existing system of co-ordination through the Committee of Imperial Defence, meeting under the Chairmanship of the Prime Minister—the only Minister whose authority is sufficient to ensure an agreed decision on the occasions when the Services differ on questions of high policy—provides, in effect, all the advantages of a single Minister of Defence, without the disadvantages of entrusting supreme control to a single individual, responsible for and yet divorced from each of the three Services. We have been furnished with convincing evidence to show that the Committee of Imperial Defence does in fact seek to combine economy with efficiency in its recommendations; and we are confident that, in the present financial stringency, increasing attention will be given to this aspect of all problems of National Defence. (2) As regards Administration the scope for economy is, as we have already indicated, relatively small. There are, however, certain services common to the three Departments, such as Medical, Dental, Education, Chaplains, etc. The position of these Services was considered in 1924 by the Mond-Weir Committee, who reported emphatically against amalgamation, and recommended that machinery should be set up, in the form of Joint Inter-departmental Committees, to secure as large a measure of co-ordination as might be found practicable. As a result of the formation of these Committees considerable improvement has taken place, and certain economies have been effected; but we are not convinced that the process has been carried as far as it might be. It is possible in respect to these particular matters, that, if a single Ministerial authority had been responsible for the administration of all three Services, further action might have been taken, but we have already rejected that solution, on broader grounds of policy. The Committee of Imperial Defence are not concerned with the details of administrative control. The prospects for economy in this direction must therefore depend on a more determined effort at co-ordination by the Departments themselves; and this in turn must be generated by the constantly increasing application of financial pressure, which will oblige the Departments in their own interest to seek economies under the head of administrative charges rather than by sacrificing services more immediately directed to warlike efficiency.

(ii) *Burden of Empire Defence.*

202. The Colwyn Committee in 1925 made a brief reference to "the possibility of a new general scheme of distribution of the burdens of Imperial Defence between the taxpayers of this country and those of India, the Dominions and the Colonies."

203. Much has been done since that date, through the medium of successive Imperial Conferences and otherwise, to co-ordinate responsibility for Empire defence, e.g., in the development of the naval forces of the Dominions, and in the financial contributions made by New Zealand, the Federated Malay States, Hong Kong and the Straits Settlements towards the cost of the Singapore Base; while in the London Naval Treaty there emerges the idea of aggregating the naval forces of the members of the British Commonwealth of Nations for the purpose of limitation by an international agreement. But, while in these and other ways a certain re-distribution of the burden has already taken place, to the undoubted relief of the finances of this country, it nevertheless appears to us that even now the share of the British taxpayer in the responsibility for the Defence of the Empire as a whole is disproportionately large. The question is one of undoubted difficulty, raising issues of great constitutional as well as financial importance; and we make no attempt now to discuss the subject in detail, especially as this is clearly not a favourable moment for taking any practical steps. It is indeed common knowledge that certain of the Dominions, so far from being in a position to increase their share of responsibility for the common defence of the Empire, have been compelled by the present financial stringency to reduce their normal expenditure on defence. We content ourselves therefore with the recommendation that the whole question be examined afresh when their financial situation is more favourable.

(iii) *Research and Technical Development.*

204. The expenditure on research and technical development of the Services in 1931 is estimated as follows:—

—	Gross	Receipts.*	Net.
	£	£	£
Navy	804,445	5,645	798,800
Army	615,000	318,000	297,000
Air Force	1,600,000	143,000	1,457,000
Total £	3,019,445	466,645	2,552,800

* These consist mainly of interdepartmental payments.

205. This expenditure covers a wide variety of objects. Broadly speaking, it covers very little purely scientific research and is mainly concerned with the application of science to the needs of the separate services. It covers progress in all its forms—development of new arms, improvements of existing ones, improvements in protective devices, means of communication, means of locomotion and so on. It must be accepted that the Fighting Services cannot stand still, and that development is essential to them. As we have already said, the maintenance of their present high standard of efficiency is more than ever necessary if their restricted size is not to be increased, and they must remain in the front rank of development. We appreciate, also, that some forms of research lead to economy. Protective devices and improved fighting capacity save personnel and material. Research on stores, ammunition, etc., prolongs the effective life of an article and avoids expenditure on replacement. Instances have been cited to us of very substantial cash economies which have been secured by successful research.

206. On the other hand, research expenditure is not without its dangers and there are three aspects which we think should be stressed. First, inventions do not long remain the undivided property of the nation that makes them. A new device may give one nation a lead over other powers in offensive or defensive capacity but the lead is only temporary and parity is not long delayed. It appears to us that research expenditure is subject to the risk that it may provoke competition in quality which may be just as expensive as competition in quantity, and the taxpayers of the world are not going to benefit by reduction in the size of fighting forces if an expensive competition develops in their quality.

207. Secondly, successful research may lead to obsolescence of existing assets, and the replacement of such assets by others embodying the results of research means continuous expenditure. In the industrial field, an automatic check on excessive expenditure of this kind is provided by the financial results obtainable but no corresponding criterion is available in the field of defence. We believe that the Services are fully alive to the danger of embarking on production before they are certain that the results of their researches are relatively perfect and that, consequently, wasteful expenditure is generally avoided.

208. And thirdly, new inventions tend to make the unit of force more and more expensive.

209. For these three reasons, we believe that research expenditure acquires an importance not fully reflected by its own total

amount. We hope that when international disarmament proposals are under consideration, this important element will be fully considered.

210. Our present net expenditure of £2,500,000 is a large sum, and we think it susceptible of reduction. We are not in a position to assess the relative merits of the competing items and to suggest that any particular services on the present list should be excluded. Selection must be left to the experts, who, indeed, at present have to exercise a strict scrutiny over the various items and assign priorities to them in view of the limited funds available. We can only suggest an economy by the rough and ready process of rationing, and we accordingly recommend that an all-over cut of 12½ per cent. of the net expenditure should be made, it being left to a Committee of the Fighting Services to determine how this reduction can best be distributed between the three Services. We believe that in a time of financial stringency such as the present this is a right and proper course to adopt, even if it necessitates a slowing down of research work which the Services regard as of high value. We recognise that after the Disarmament Conference, our research expenditure will have to be further reviewed in the light of circumstances, and it may be that restriction such as we propose cannot be continued indefinitely in the absence of international agreement. We recommend also that in future the total Estimate of expenditure on Research, Experiment and Design in the three Services be submitted separately by the Departments for Treasury approval before the Estimates are presented to Parliament.

(iv) Disadvantage of annual estimating.

211. The estimates for the Fighting Services are fixed annually in the light of the demands made by those Services and the ability of the Chancellor of the Exchequer to meet them. We recognise that this procedure is dictated by practical considerations—it is, indeed, inherent in our national financial system. But we feel that, in respect of some items of defence expenditure, there are two directions in which it does not conduce to the most economical and efficient use of the funds available. In the first place, under our Parliamentary system any unspent balance on each Service Vote, save in so far as it may be used with Treasury sanction to make good deficiencies under other Votes, must be surrendered to the Exchequer. At one time there was undoubtedly a tendency on the part of the Departments towards the end of the financial year to accelerate or encourage expenditure in order to avoid surrender of moneys which they had—quite legitimately—counted

on being able to spend; and though we feel sure that under present conditions this is no longer the general practice, it seems natural to suppose that the temptation to spend money more freely than usual in such circumstances still exists, and is liable to affect, to some extent, the actual amount of expenditure in the last quarter of the financial year. Secondly, there is the question of placing contracts ahead and so committing Parliament to liabilities beyond the current financial year. There is no doubt that, in conformity with the maxim that the King's Government must be carried on, the Service Departments have the right to enter into long-term contracts for the provision of material, necessarily required for the fulfilment of their constitutional functions, which cannot be completed within the term of a single financial year; but whether that right would extend to the placing of an order for the delivery of say, a number of standard aircraft, each of which could be manufactured within 12 months, for a period of three years ahead, is perhaps doubtful. Of course questions of design and of the future course of markets also enter into the problem; and it may well be that the number of cases in which Departments would feel justified in committing themselves so far ahead, even if they had the power to do so, would be relatively few. Our contention, however, is that, as a matter of sound business practice, they should be given the power to enter into such contracts, subject of course to suitable control over its use.

212. With these points in mind, we think that in respect of certain services, for example, Works and Buildings, Research and Technical Development, Purchase of Naval Armaments and Warlike Stores and Aeroplanes a guaranteed income for these purposes over a series of years* would enable a wiser use to be made of the provision available; and we would go so far as to say that, if the principle is approved, the Departments should be content to accept a lower annual average provision over the period in question than their present expenditure under these heads. Reasonably long term planning ahead must, we think, be more economical than an annual programme in which each item has each year to run the gauntlet of internal competition for funds with all other services in the same arm. We have not considered in detail how such a scheme could be worked in harmony with the existing principle of annual Votes of Parliament, and with the necessities of Parliamentary and Treasury control; but we do not doubt that a satisfactory scheme could be formulated without great difficulty. **We accordingly recommend that as regards Works and Buildings,**

* Subject of course to any change of policy resulting from the Disarmament Conference, and to the exclusion of expenditure on New Formations, to which we cannot expect that either the Government or Parliament would be willing to commit themselves in advance.

Research and Technical Development, and Purchase of Naval Armaments, Warlike Stores and Aeroplanes and Engines (and possibly other items if experience showed that such a scheme would be of benefit), either a fixed annual income for a number of years or alternatively a fixed total provision over a number of years, but in either case at an average annual rate less than the actual current rate of expenditure, should be promised to the Services. We think that in the first place, as the idea is an experiment, the number of years should be three. It would have to be recognised on all sides that such a promise could not for obvious reasons, be absolute—it would have to be subject to review on major changes of circumstances—but we do not think that this necessary reservation need impair the efficient working of the scheme.

(v) *Education.*

213. The net votes for 1931 for Educational Services are :—

	<i>£</i>
Navy (Vote 5)	232,000
Army (Vote 4)	850,000
Air Force (Vote 6)	484,000
	<hr/>
	£1,566,000
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These votes include only the pay of the military and civilian staffs. Further expenditure is incurred on other votes for accommodation, rations, stores, etc., which may be put in round figures at about £1,000,000.

The educational establishments cover a wide variety of functions, embracing the training of cadets, higher and specialised training of officers, training of instructors, and vocational training for the men. We think that some of the larger establishments invite comment.

Cadet Establishments.

214. The Geddes Committee referred to the cost of education at Dartmouth, Woolwich and Sandhurst, and Cranwell. The increases in the fees paid by parents recommended by the Geddes Committee have been made in the case of Dartmouth, Woolwich and Sandhurst but not in the case of Cranwell, while there has been a substantial reduction since 1922 in the gross cost per cadet at Dartmouth and Cranwell. At Woolwich and Sandhurst, however,

the cost has increased considerably since 1922. The present figures, based as regards 1931 on the Estimates, are as follows:—

	Figures given in Geddes Report 1922.			Figures in Estimates 1931.		
	Numbers of Cadets.	Average gross cost per Cadet per year.	Maximum fees payable per year.	Numbers of Cadets.	Average gross cost per Cadet per year.	Maximum fees payable per year.
Royal Naval College, Dartmouth (including nautical training).	445	£ 462	£ 75	455	£ 354*	£ 150
Royal Military Academy, Woolwich (exclusive of riding establishment).	280	366	75	180	572	200
Royal Military College, Sandhurst.	700	373	75	510	412	200
Royal Air Force College, Cranwell (excluding flying training but including flying pay of cadets).	—	850	75	119	529*	75

* Exclusive of rental value of buildings. In the case of Cranwell, new buildings are in course of construction which are estimated to cost £300,000.

NOTE.—We have no information on the basis on which the figures in the Geddes Report were compiled and we cannot therefore be certain that they are on the same basis as the Estimates for 1931.

In the case of Woolwich and Sandhurst, some of the increase of cost since 1922 is no doubt accounted for by the fall in numbers. We think that, in this case, a determined effort must now be made to secure a reduction in the overhead costs more nearly commensurate with the fall in the number of cadets.

In the case of Dartmouth, where Cadets enter at about 13½ we think a substantial part of the cost of providing general education would be saved if the age of entry were higher. We understand that the conditions of recruitment are at present under investigation by a Committee and we hope that consideration will be given to this point with a view to some material reduction in the cost to the State.

At Cranwell, the Cadets receive pay at the rate of 7s. a day (49s. a week), from which 4s. is deducted for the cost of messing. We think the balance of pay, viz.:—3s. a day (21s. a week) is a needlessly generous allowance to boys of from 17 to 18 years of age while in receipt of education and training from the State.

Staff Colleges.

215. The higher professional training of officers is undertaken at the Royal Naval College, Greenwich, the Staff College at Camberley and the Royal Air Force Staff College at Andover.

The cost per officer under instruction at these establishments seems excessive particularly as these figures do not include the pay and allowances of the officers under instruction. The figures are :—

			<i>Number of Students.</i>	<i>Annual cost per head.</i>
				£
Royal Naval College	...	...	198	415
Staff College	...	...	120	650
Royal Air Force College	...	...	30	533*

At each of these colleges, the proportion of administrative and instructional staff and of general staff to the number of officers under instruction appears to us to be high and we think reduction should be possible.

Royal Air Force Apprentices.

216. The Geddes Committee recommended that the scheme of training of boys at Halton should be abandoned and they recommended the adoption of an alternative policy of recruiting tradesmen personnel from engineering shops throughout the country. This recommendation was not adopted.

At present, 2,620 apprentices are under instruction, mainly as aero-engine fitters and riggers for metal aircraft. The course lasts three years and the average annual intake is thus nearly 900. Entry is at the age of 16, and at 18 the boys are engaged to serve for twelve years, i.e., until reaching the age of 30. At that age, they may re-engage for a further twelve years of service.

The cost of training, including pay and maintenance, is £179 per head per annum, i.e., a total cost over three years of £537 per apprentice. Amortising this cost over twelve years of service, the average cost per year of service works out at £59. We think the high cost of this establishment should be reduced.

217. The scheme has not yet been sufficiently long in operation for any experience to be gained which would indicate how many of the men will re-engage for the second period of twelve years of service. The present wastage from all causes is 1.5 per cent. per annum.

218. In view of the expensive character of this scheme and of the risk that men who have been trained at high cost may withdraw their services from the State after their first twelve years of service,

* Exclusive of rental value of buildings.

we have re-examined the recommendations of the Geddes Committee. It appears to us after careful examination that the conclusions of the Air Ministry on this matter are sound. Industry could not at present train all the apprentices who are required and therefore some measure of State training is essential. Moreover, even if industry could train as many as are required, difference of method would be a heavy disadvantage to a service which places great reliance on uniformity of standard and inter-changeability of personnel. Some training by the State is inevitable to develop the corporate spirit essential to a Fighting Force and to turn out men capable of bearing the wide responsibilities assigned by the Air Council to N.C.O.'s and Warrant Officers.

218A. We think, therefore, that the scheme must be continued but we think it should be reviewed from time to time with a view to considering the possibilities of obtaining some recruitment from the trade, particularly if experience shows that there is a high percentage of wastage when the first twelve years of service are completed.

General.

219. Taking the Education Votes generally, we think that reduction is possible and recommend that in each service an overall cut of not less than 10 per cent. should be made on the net provision in these Votes, amounting to say £150,000.

(vi) *Inspection.*

220. We have been impressed by the large provision made in the Estimates for the Services for the cost of inspection.

The total provision is shown in the following table :—

	£
Navy	400,000
Army	498,000
Air Force	179,000
	<hr/>
Total ...	£1,077,000
	<hr/>

221. The percentage of inspection applied varies according to the type of article concerned. Where any defect would result in

loss of life or wreckage of expensive material, no inspection which would lessen such risk can be considered excessive. Similarly, where with a complex mechanism interchangeability of parts is essential to efficient and economical use, reasonable precaution must be taken to ensure that such interchangeability is obtained. On the other hand, in the case of clothing, accoutrements and the like, and even items such as gun carriages, gun mountings, and tanks, inspection is necessary mainly to ensure that the State is obtaining stores in good condition in return for its expenditure.

222. We have no desire to see any reduction in the 100 per cent. inspection applied to stores which are vital to the safety of the personnel or any neglect to ensure high efficiency of essential mechanisms in time of war, but we feel that as regards the stores which do not fall into these categories, the present inspection involves a cost which is a disproportionately high insurance premium against delivery of faulty stores. We recommend that the percentages at present inspected should be reviewed, more reliance being placed on the right to return faulty consignments to the contractor, and we think it should be possible to secure a reduction of not less than 10 per cent. in the present total cost.

(vii) *Works and Buildings Services.*

223. The gross Votes for Works, Buildings and Land for the Home Fighting Services in 1931 may be analysed as follows :—

	<i>New Works.</i>	<i>Ordinary Repairs and Maintenance.</i>	<i>Miscellaneous.</i>	<i>Gross Total.</i>
	£	£	£	£
Navy Vote 10	1,428,850	419,000	926,000*	2,773,850
Army Vote 10	922,900†	1,185,100†	828,000	2,936,000
Air Vote 4	1,228,500	495,000	422,500	2,146,000
	£3,580,250	2,099,100	2,176,500	7,855,850

* Including £656,450 Annuity, etc., in repayment of Advances under Naval Works' Acts, 1895 to 1905.

† After crediting value of stores consumed, etc., on an approximate basis.

The gross total is reduced by receipts from sales of land, buildings and old stores, contributions from Dominion and Colonial Governments, etc., and "shadow-cuts" for possible under-spending to a net total of £6,754,500.

Comparative net totals for previous years are:—

	1914-15,	1922-23 (Geddes),
	£	£
Navy	3,595,000	4,756,000
Army	2,791,000	8,185,000
Air	—	2,166,000
	<hr/>	<hr/>
	£6,386,000	£15,107,000
	<hr/>	<hr/>

224. The reduction in the estimated expenditure for 1931 compared with 1922 is particularly striking, and the net total, allowing for higher prices and the post-war introduction of air services, also compares favourably with the 1914 expenditure.

The relatively high cost of Air Works services is of course explained by the fact that the Air Force is an expanding service which has compressed into a few years the provision of a complete system of aerodromes and ancillary accommodation both at home and abroad.

225. In view of the reductions effected we are satisfied that the position has now been reached when it is no longer possible to effect large reductions by postponing new works, since as a rule postponement merely results in the liability being carried on to future Estimates, and an uneconomical expenditure on extra maintenance meanwhile.

226. We think however, that real economies may be sought in two directions.

(1) We have already recommended the stabilisation of the Works Votes over a period of say three years, at a somewhat lower figure than at present. If the new figure were put at no more than 2½ per cent. less than the present net total of £6,000,000 (excluding the Naval Works Acts Annuities), a saving of say £150,000 a year would result.

(2) With regard to the cost of new buildings, it appears to us that it may not be necessary in some cases to secure such a high standard of original construction as is now obtained. Owing to the uncertainty with regard to the future requirements of the Services, and the rapid changes in technical development, many of the buildings provided may well have an effective life beyond the period for which they are needed. It is true that we have been told that many Service Buildings urgently require to be replaced, and that the maintenance of many others is being neglected. But

it may be that the adoption of a lower standard all round would enable more of what is desirable, both by way of replacement and of current upkeep, to be carried out within the limit of existing funds.

The question appears to us to be worthy of further examination, and we recommend that it be specially investigated by H.M. Government with a view to considering whether further economies can properly be made by a change of policy in this respect.

(viii) *Contract Procedure.*

227. Under this head we make two recommendations of minor importance.

(1) In all Government contracts it is the rule that the form of tender shall set out in full all the conditions applicable to tender and contract, making a document of perhaps four pages. Some of these conditions are applicable to all Government contracts, others are special to individual Departments or to individual items of supply. We think that a small but useful saving of time and stationery would be achieved if in future a copy of the conditions which are common to all Government contracts were printed in a separate form and sent to every firm as soon as it is placed on the list of Government Contractors. Thereafter when tenders are called for, the form of tender would merely set out the additional conditions applicable to the tender and state as regards the general conditions that the tender and contract were subject to the general conditions of Government contracts. We recommend that this question should be further explored, and also that consideration should be given to the alternative possibility of contractors, on being placed on the list of Government Contractors being given either forms showing conditions of Government contracts affecting a particular trade or class of supply, or forms showing general conditions of contracts for the particular Department.

(2) It is the accepted practice that all Government contracts, for however small an amount, must be placed after calling for competitive tenders. Industrial experience shows that it is not worth while as a rule to go to the trouble and expense of open competition when the amount of the order is trifling; and we think that, notwithstanding the Parliamentary arguments in favour of the present system, the Government would be well advised to adopt the same rule. We recommend therefore that, for amounts not exceeding £10, the general rule should be that tenders are not called for but that a direct order is to be given to a firm known to be able to supply. Responsible officers should take steps of course to check the price by reference to tenders for large quantities of similar goods, and should invite supply from different firms from time to time as may be expedient.

NAVY.

228. *Analysis of Expenditure.*

	Expenditure 1925 (Actual).	Expenditure 1928 (Actual).	Expenditure 1931 (Estimated).
	£	£	£
Personnel—			
Pay, Clothing and Provisions	19,594,000	19,077,000	17,524,000
Reserves of Personnel	466,000	404,000	390,000
Medical Services	784,000	791,000	743,000
Educational Services	401,000	315,000	300,000
Transport (Freight and Travelling) ...	703,000	604,000	594,000
Accommodation (Lodging Allowances)	93,000	83,000	83,000
Total for Personnel and Allied Services £	22,041,000	21,274,000	19,634,000
Works, Buildings and Lands	2,697,000	2,318,000	2,574,000
General and Technical Stores	3,376,000	2,605,000	2,491,000
Mobile Fighting Material—			
(i) New Construction of H.M. Ships	7,491,000	9,947,000	5,571,000
(ii) Repairs and Maintenance of Ships	8,378,000	7,355,000	6,741,000
Total for Mobile Fighting Material ...£	15,869,000	17,302,000	12,312,000
Guns, Projectiles and Ammunition £	3,064,000	2,864,000	2,508,000
Scientific Services	1,198,000	1,087,000	1,120,000
Fuel for H.M. Ships	4,153,000	3,117,000	2,695,000
Headquarters	1,315,000	1,196,000	1,155,000
Miscellaneous Effective Services ...	317,000	287,000	222,000
Non-Effective Services (Pensions) ...	8,250,000	8,506,000	8,843,000
Fleet Air Arm (Admiralty Contribution)	1,320,000	1,008,000	1,126,000
Gross Total ...£	63,600,000	61,564,000	54,680,000
Receipts ...£	3,595,000	4,425,000	3,075,000
Net Total ...£	60,005,000	57,139,000	51,605,000

It will be seen from these figures that as between 1925 and 1931 there has been a reduction in the net amount of Navy Estimates of nearly £8,500,000, or, if New Construction (which depends on the building programme in force) is excluded, of £6,500,000.

229. This, however, does not represent the full measure of the fall, as in earlier years the Navy drew on stocks without replacement—a cash saving which clearly could not be obtained in-

definitely, and the following figures, supplementary to those already given, are necessary to complete the picture :—

Estimated value of stocks used without replacement.

	1922.	1925.	1928.	1931. (Estimate.)
	£	£	£	£
Vote 2 (Victualling and Clothing).	800,000	250,000	89,500	134,000
Vote 8—II. (Dockyard Material).	1,209,400	799,800	575,000	324,550
Vote 9 (Naval Armaments).	(No Estimate.)	(No Estimate.)	937,500	596,300

230. These figures show what a considerable reduction has actually taken place in Navy Estimates in the last six years, and are evidence of the results of the continuing efforts which have been made year by year by the Admiralty to restrict expenditure. They confirm the view which we expressed at the beginning of this chapter that major economies can now only be found in further disarmament.

231. We have obtained from the Admiralty a forecast of their future requirements. The only major item of change is for New Construction. The provision made in 1931 is much lower than it can possibly be in 1932 and subsequent years. The reduction in 1931 is the result of the New Construction Programmes of 1928 and 1929 announced to Parliament by the previous Government having been reduced by the present Government with the object of creating the desired atmosphere for the London Naval Conference. The curtailment of these two programmes naturally produced two years of abnormally low expenditure on New Construction in 1930 and 1931. The subsequent adoption of larger programmes based on the agreements reached at the Conference will necessarily result in the expenditure on New Construction rising from £5,570,515 in 1931 to approximately £8,230,500 in 1932. Assuming that programmes similarly based are approved in 1932 and 1933, the New Construction figures for the two following years will be approximately :—

	£
1933	8,393,180
1934	8,532,750

In the forecasts of future expenditure which we made in the opening chapter of our report, we accordingly assumed—on the basis that existing policy remained unaltered—an increase of Navy Expenditure of £2,700,000 in 1932 and 1933 compared with 1931. It is important to note that this estimate makes no provision for new Capital Ships, the construction of which has been postponed by agreement under the London Naval Treaty until after the resumption of the Naval Conference in 1935.

232. It is common knowledge that varied opinions are held in the Navy itself as to the wisdom of the policy embodied in certain designs of ships of war. How far, if at all, considerations of cost were allowed to enter into the decision of the Admiralty to adopt, say, the 8 inch 10,000 ton cruiser or the 16 inch 35,000 ton battleship we have not enquired. But the difference to the taxpayer owing to the selection of these in preference to smaller types has undoubtedly been very substantial, running into millions of pounds; and it may well be asked whether the increase in fighting value has been equal to the extra cost. Present conditions it is true, are different. No new ships exceeding 7,000 tons are being laid down at the moment, and the Admiralty have assured us that when the New Programme for the year is under consideration, the question of comparative cost is constantly in the minds of the Board. We appreciate that the size of a ship is determined by the qualities she is to possess, which in turn depend on the services she is expected to perform and on the qualities of the foreign ships she is liable to meet. Yet it is evident that, even under the restricted programme allowed by the London Naval Treaty, there is room for legitimate differences of opinion as to the size of the ships of various classes to be built, e.g., whether a new cruiser shall be of the "Leander" (7,000 tons) or the smaller class of say 5,500 tons, costing roughly £1,500,000 and £1,125,000 respectively. Moreover when the question of the capital ship comes up for further consideration at the 1935 Conference, it is clear that decisions will have to be taken which will gravely affect the total cost of naval defence.

233. We understand that the Treasury are already given an opportunity to express their views on the financial effect of the year's Programme, and we attach great importance to this practice of interdepartmental consultation, and to the Treasury being furnished by the Admiralty with full information respecting their plans at an early stage in the discussion of each year's New Construction Programme, in order that the Cabinet, when they finally come to consider the proposals of the Admiralty, may also have before them the views of the Treasury, based on the fullest knowledge that a layman can be expected to have of the questions at issue.

In furtherance of this object, we recommend that, before the next Naval Conference, the Government should appoint a representative Committee to enquire into the whole subject of naval design and to consider whether any modifications might be adopted, either with or without international agreement, which would lessen the cost of naval defence without endangering national security.

234. We propose now to pass to detailed comments on such of the items of expenditure as appear to us to be susceptible of reduction, though we would again emphasise that substantial savings have already been made and that further economies may be difficult of attainment without some sacrifice of efficiency.

Vote 1—Royal Marines.

235. The number of Officers and Men of the Royal Marines in 1931 is 9,647, and the provision in Navy Vote 1 Subhead B, for their wages and allowances is £1,054,400. In 1922-23, following on the Geddes Report, the number was 13,742, and the cost of wages and allowances £1,346,286.

In view of the not uncommon criticism that the Royal Marines are unnecessary and should be abolished, we have gone carefully into the question of their utility under present conditions. The Admiralty have satisfied us that the Corps form an integral and essential part of the Naval Forces, performing certain necessary specialist duties on shore, and forming afloat a definite part of the complement of the larger ships which would have to be completed with seamen if the Marines were withdrawn. **We are satisfied from the evidence afforded to us that the Corps could not be abolished without a definite and serious loss of naval efficiency.**

Dockyard Police.

236. Following a reference by the Geddes Committee, in 1921, to the excessive number of Metropolitan Police (1665 in all) employed in the Dockyards and other Naval Establishments, such as Victualling Yards and Armament Supply Depots, the Admiralty established a body of less expensive Royal Marine Police, recruited from Royal Marine Pensioners. As an experimental step 260 members of this force were substituted for an equivalent number of Metropolitan Police at the Armament Supply Depots, with a consequential saving on pay and allowances of £24,000 a year and further savings on pensions. The process of substitution has since been extended to the Victualling Yards, the smaller Dockyards (Rosyth, Portland and Sheerness) and other establishments, with the result that the Metropolitan Police now employed are (with a minor exception) confined to the three main Dockyards at Portsmouth, Devonport and Chatham. (At these three yards there were in 1922, 448 Metropolitan Police, who have since been reduced to 321, costing £99,882 a year in pay and allowances.) Following the experience gained elsewhere, particularly at Sheerness, the Admiralty have recently agreed in principle to the substitution of Royal Marine Police for Metropolitan Police at Chatham Dockyard and the necessary administrative changes are now under consideration. A saving of about £50,000 would result from the substitution of Royal Marine Police at all three Dockyards, and having regard to the experience now gained of the new force, we see no reason why the use of Metropolitan Police in Naval Establishments should continue for any longer than is necessary to effect the substitution. **We recommend that this matter should be taken up with a view to the realisation of this useful economy at the earliest possible date.**

Vote 2. Clothing Allowances.

237. The Geddes Committee recommended "that in all three Fighting Services the clothing allowance should be reduced by one-third, so that the uniformed forces should, like civilians, economise in their clothes, but it should be definitely understood that the standard of repair of uniform is correspondingly lowered."

The case for such an economy seems even stronger to-day than in 1922; and though a saving of one-third seems excessive, a reduction by 10 per cent. should be possible. The total cost of clothing and allowances in lieu in 1931 is £880,000. **On the basis of a reduction of 10 per cent. a saving of £88,000 should be possible in 1932.** We understand that Naval Clothing may be purchased either from retailers or under contracts made by the Navy and that the majority of the men adopt the former course although the supplies under Naval contracts are cheaper. It appears to us clear that a saving can be made by the men and that the reduction we propose is not in essence a reduction in pay.

Vote 8. Dockyards.

238. Any detailed enquiry into the Dockyards would involve more time than we are able to give. We are, however, aware that the Dockyards have been the subject of full investigations during recent years and we have heard evidence on the actions which have been taken as a result of those enquiries. Accordingly we confine our recommendations on this subject to certain broad questions of principle.

239. Following the Report of a Committee under the Chairmanship of Sir John Biles in 1926, the introduction of a new and modern system of cost accounting in the Dockyards was begun and we are informed that it is now in operation at Portsmouth and Devonport and is in process of introduction at other Yards. It is reported to us that this system is as complete as any yet adopted in commercial shipyards but we have not been able to carry out any investigation.

On the assumption that the cost of Dockyard operations can now be accurately ascertained on a basis comparable with outside contractors we consider that Naval construction work should only be undertaken in the Dockyards where the cost is definitely not more than it would be if carried out by outside firms. For a variety of reasons we agree that it will still be desirable to carry out ship repairs in the Dockyards apart from the question of competitive prices. **If this policy is adopted, the number of men employed in the Yards should be restricted to the number actually required and the recent practice of maintaining the full complements subject only to wastage should be discontinued.** It seems to us evident that economy will result from this course, though we cannot place a definite money value on it.

(b) Provision made for maintenance, running repairs, etc. :—

							£
1929	...	...	...	...	...	...	73,402
1930	...	...	...	...	...	...	72,445
1931	...	...	...	...	...	...	71,365

We are informed that the Admiralty keep the needs of each Yard and Depot under constant review, and we make no recommendation on this subject.

Votes 8 and 9.—Naval Armaments and Naval Stores, Etc.

242. The Admiralty have furnished us with very full information respecting the size and nature of existing stocks, both of naval armaments of all kinds, naval stores, fuel supplies, victualling and clothing stores; the basis upon which reserve requirements are calculated in each case; and the extent to which existing stocks conform to such requirements. We do not think it desirable that we should go into a detailed analysis of the facts; it will suffice to say that, broadly speaking, we have no fault to find with the present Admiralty practice. We note however that considerable modifications of the rigidly high standards which formerly prevailed have been adopted by the Board in recent years under the pressure of financial stringency, apparently without ill effect. **We are not prepared to suggest any particular directions in which the process could be carried still further. At the same time, we consider that the Board of Admiralty should continue to give the matter their close attention.**

ARMY.**243. Analysis of Expenditure.**

	1925 Expenditure.	1928 Expenditure.	1931 Estimate.
Personnel—	£	£	£
Pay, Clothing and Provisions... ..	21,424,000	18,938,000	17,344,000
Medical Services	989,000	1,069,000	1,012,000
Education	1,105,000	1,091,000	1,071,000
Transport	2,950,000	2,612,000	2,308,000
Reserve Forces—Territorial Army, Army and Supplementary Reserves, Officers Training Corps, Military Hospital Reserve, Colonial Militia, etc.	5,410,000	5,290,000	5,582,000
Accommodation (i.e. quartering, lodging, fuel and light).	1,549,000	1,626,000	1,421,000
Total for Personnel and Allied Services £	33,427,000	30,626,000	28,738,000
Works, Buildings and Land£	4,801,000	3,189,000	2,936,000
Technical and General Stores£	831,000	876,000	829,000
Mobile Fighting Material: Tanks, Tractors and Motor Vehicles (other than those operated by the R.A.S.C.).	556,000	703,000	578,000
Armament £	1,430,000	1,003,000	952,000
Scientific Services (including Research, Design and Inspection).	1,084,000	1,102,000	1,074,000
Fuel for Mechanical Transport	75,000	77,000	94,000
War Office	897,000	855,000	837,000
Miscellaneous Effective Services	1,914,000	1,169,000	1,086,000
Non-Effective Charges (Pensions)	9,179,000	9,298,000	9,515,000
Gross Total £	54,194,000	48,898,000	46,639,000
Receipts	9,851,000	8,101,000	6,709,000
Net Total£	44,343,000	40,797,000	39,930,000

The main items of Army Expenditure on which comment is necessary have been dealt with in the general part of this Chapter. Our remaining recommendations on the Army are therefore confined to certain minor points.

Vote 5. Subhead J. War Department Vessels.

244. The following provision is made in 1931 :—

	£
(1) Shipping Establishment, Woolwich Arsenal ...	5,250
(2) Wages of Crews of Vessels, Pilotage, Towage, etc.	58,750
(3) Construction, Purchase and Repair of Boats and Vessels	26,000
	£90,000

The War Department vessels number 208, and their crews 366. They are used for artillery targets, and for the conveyance of personnel, stores and heavy guns, coastwise and even for Ireland.

It is for consideration whether economy could not be effected by the Admiralty and War Office keeping each other supplied with programmes of the movements of Naval Armament and War Department vessels in order that advantage might be taken of opportunities of saving separate journeys in some cases.

Vote 6. Subhead J. Subsidies for Mechanical Transport.

245. Subsidies at the rate of £40 a year are paid to owners of certain types of lorries. The vehicles are to be available for purchase by the War Department in case of emergency. The maximum amount payable in any one year is £40,000, but it is not anticipated that the full number will be enrolled in 1931, and provision has been made in Estimates for £20,100.

This scheme is clearly not producing the results which were expected and we recommend that it be discontinued. In addition to the saving of the subsidy, there should also be saving from reduction of the staff employed for inspection.

Vote 6. Subhead P. Light Horse Breeding Scheme.

246. This scheme provides for the payment of premiums to breeders to encourage the production of a type of horse required for

the Army. The provision made in Estimates for 1931 is £30,000. In view of the diminishing importance of the horse to the Army, we recommend that this subsidy should be discontinued.

Vote 7. Clothing.

247. As in the case of the Navy, we recommend that a reduction of 10 per cent. should be made in clothing allowances. The saving would be £55,000.

Ordnance Factories.

248. The functions of the Ordnance Factories are (1) to manufacture warlike stores in peace and war, (2) to provide a nucleus for expansion in emergency, (3) to maintain a check over trade prices, (4) to provide for experimental manufacture often of a secret nature. These functions demand first that a nucleus establishment be kept at the Ordnance Factories irrespective of actual peace-time needs for warlike stores, and secondly (and of no less importance) that the efficiency of the Ordnance Factories for their proper purposes be kept as high as possible and the cost of their operations as low as possible, subject to the maintenance of proper conditions of service and to any unavoidable loss caused by the first condition.

249. We understand that the "nucleus establishments" at Enfield and Woolwich were revised in 1923 and fixed at 1,050 and 4,332* respectively; that the Enfield establishment was further reviewed in 1929/30, and reduced to 920, to be reached mainly by normal wastage; and that the Army Council now have under consideration the question of reviewing the establishment at Woolwich, where the numbers at present actually employed are still considerably above the present authorised nucleus.

250. We recommend that the review of the Woolwich establishment should be put in hand at once, and that, when the numbers have been fixed, the question whether it is necessary to place orders in excess of the amount required to keep the nucleus establishment fully employed, and, if so, in what proportion such orders should be distributed between the Trade and the Factories, should be considered in the light of their respective cost.

As regards wages in the Factories, we refer to chapter III. of our Report, in which we recommend that the preferential rates now paid in Government Industrial establishments should be discontinued.

* Excluding the Engineering Department, Central Office, with, say, 2,400 employees.

AIR FORCE.251. *Analysis of Expenditure.*

	1925 Expenditure.	1928 Expenditure.	1931 (Estimates).
	£	£	£
Personnel—			
Pay, Clothing and Provisions... ..	5,573,000	5,116,000	5,433,000
Medical Services	334,000	304,000	321,000
Technical Training and Education ...	508,000	517,000	495,000
Transport	466,000	394,000	389,000
Reserves	298,000	534,000	599,000
Accommodation (including lodging allowance, fuel and light).	388,000	371,000	470,000
Total for Personnel and Allied Services £	7,567,000	7,236,000	7,707,000
Works, Buildings and Lands	3,312,000	2,063,000	2,046,000
Technical and General Stores£	848,000	651,000	809,000
Mobile Fighting Material£	6,362,000	5,617,000	6,809,000
Guns, Projectiles and Ammunition ...£	338,000	381,000	524,000
Scientific Services (including Research Design, Inspection, Meteorology and Rewards to Inventors).	559,000	713,000	822,000
Fuel for Aircraft, etc.	546,000	533,000	727,000
Headquarters	706,000	653,000	659,000
Miscellaneous Effective Services—			
Airships	401,000	383,000	59,000
Civil Aviation	279,000	377,000	651,000
Miscellaneous	108,000	105,000	110,000
Non-Effective Services (Pensions) ...	139,000	211,000	274,000
Gross Expenditure ...£	21,165,000	18,923,000	21,197,000
Receipts	5,715,000	2,831,000	3,097,000
Net Expenditure ...£	15,450,000	16,092,000	18,100,000

252. The largest single Subhead in the Air Estimates is Vote 3, Subhead A, £6,529,000 for Purchase of Aeroplanes, Seaplanes, Aero Engines, etc. This includes some £300,000 on account of New Formations in 1931; the remainder is expended on Re-armament and Maintenance of existing formations (say £5,250,000), and Research and Technical Development (£914,000).

Apart from restrictions on the size of the Royal Air Force we have considered the possibility of reducing this very large block of expenditure in the following directions, viz.: (1) Limitation of expenditure on Research and Technical Development; (2) Stabilisation of Estimates; (3) Rationalisation of Aircraft Manufacturing Industry;

(4) Reduction of number of different types of aircraft and aero engines in use by the Ministry; and (5) Liability for the cost of production of Prototype machines. The first two points have been dealt with already in paras. 204 to 212 of our Report and will, we hope, lead to certain economies; we now discuss the last three in order.

Rationalisation of Aircraft Manufacturing Industry.

253. The number of firms in receipt of current orders for aircraft from the Air Ministry is 16. They differ widely in size and command of financial resources, and in the types on which they chiefly concentrate.

254. *Prima facie* we should have thought that the benefits which are commonly found to accompany a wise scheme of amalgamation in other industries, e.g., a reduction of overhead charges, a more economical use of design staff, and a lowering of production costs, would have resulted equally from a well conceived application of the principles of rationalisation to the aircraft manufacturing industry; and we had hoped that the Air Ministry would share our view. The Ministry, however, have opposed the suggestion on a number of grounds, which we do not propose to discuss in detail, but to which we have naturally given due weight. Nevertheless we remain of the opinion that the present number of competing firms, relying in effect for their continued separate existence on the deliberate policy of the Air Ministry in the distribution of orders is excessive, and that some diminution of their number is desirable and can be achieved without involving the disadvantages which the Air Ministry are rightly determined to avoid, in particular a diminution in the present competitive and fruitful activity in design. We wish to make it clear that the form of amalgamation which we have in mind is not the concentration in a single unit of all the makers of one particular type of aircraft, but the combination, in suitable cases, of makers of different types, which can be treated as complementary to each other, i.e., a vertical, not a horizontal sectionalisation. Although each group need not necessarily produce all the classes and types required, it should make two or three of the classes and as many types in these classes as possible if economies are to be effected. We believe that this process, if introduced gradually, and with suitable precautions, should prove of real advantage both to the State and to the industry, and we earnestly hope that H.M. Government will consider by what means they can influence its introduction.

Reduction of number of different types of Aircraft, etc.

255. At present there are in daily use in the Royal Air Force not less than 44 different types of aircraft and 35 different types of

engine, each one consisting of from 2,000 to 3,000 definite numbered parts. Quite apart from the cost of store-keeping, inspection and technical control generally (on which emphasis was laid by the Air Ministry themselves as a material factor in the cost of their overhead charges), it seems obvious that a reduction in the number of different types, both aircraft and engine, should lead to a substantial reduction in cost, by enabling the industry to spread their overheads over a larger output of the same type. The Air Ministry do not of course differ from this view in principle, and are perfectly ready, we understand, to apply it in practice as soon as design has become sufficiently stabilised. They contend however that the time for doing so on a large scale has not yet arrived, the Royal Air Force being still in the evolutionary stage; but they hope to carry out a gradual process of reduction as time goes on.

256. We attach importance to this as a source of economy, and consider that the Ministry should carry it into effect as and when practicable.

Liability for cost of Prototype Machines.

257. At present aircraft in the experimental stage are bought by the Air Ministry either (a) for research in aero-dynamical problems, etc., or (b) for development into types which can be produced in quantity for the Royal Air Force.

We have no quarrel with expenditure under (a); but we have felt considerable doubt whether purchases under (b) of what may be called "prototype" machines are a proper liability of the State; and we have accordingly examined carefully the possibility of leaving it to the industry to develop such machines at their own expense and risk. The case against such a change, put briefly, is that:—

(i) It is essential that the R.A.F. should make up in quality for what it lacks in quantity; and the maintenance of the present high standard of technical efficiency obliges the Air Ministry to retain in its own hands the control of technical development instead of allowing design to progress along the lines dictated by the interest or preference of individual manufacturers.

(ii) The Air Ministry must also co-ordinate aircraft design with concurrent engine development, and must have regard to the whole efficiency of the aircraft as a fighting machine, including military load, range, consumption and armament, as well as the more spectacular qualities such as speed.

(iii) It is possible that the designer would seek to recover the cost of experimental work from production contracts, and that the consequent saving might not be as great as would at first appear to be the case.

These arguments appear to us to have some force; and in the present state of the industry we think that it would be a mistake to depart from the present system, which should, however, be regarded as a provisional arrangement, dictated by the conditions of development of the industry, and requiring reconsideration as soon as circumstances permit.

Vote 2. Uniform.

258. As in the case of the Navy and Army, we think that a reduction of 10 per cent. might properly be made in Clothing Allowances. The saving would be £11,000 a year.

Vote 3. Airships.

259. We print as an Appendix to this Report a copy of a letter we addressed to the Chancellor of the Exchequer on the 6th May, 1931, on the subject of Airships.

Vote 4. Pembroke Dockyard.

260. The Air Ministry have explained to us a proposal to transfer a flying boat squadron from Felixstowe to Pembroke Dock. The construction of the necessary accommodation will cost £107,000. The present cost of maintaining Pembroke Dockyard on a "care and maintenance" basis is approximately £5,500 a year, but receipts for the rental of part of the Dockyard not required for Air Force purposes and for the supply of electric current reduce the net cost to about £2,500. The cost of maintenance when the squadron is in occupation will be increased by about £2,000 a year, i.e., the cost of maintenance (over and above the maintenance of the squadron itself at any home station) will be £4,500 a year.

Having regard to the fact that we are informed that pressure on existing accommodation for Flying Boats in Home Waters renders the provision of a new station essential, that alternative accommodation at Felixstowe would be more expensive and that Pembroke possesses advantages as a station by reason of its situation near the Bristol and St. George's Channels, we have no recommendation to make on this proposal.

Vote 8.—Civil Aviation.

261. The Vote for Civil Aviation (Air Vote 8), which does not include provision either for the purchase of experimental civil aircraft or for Airships (both of which are included in Vote 3) is £470,000 net for 1931, including £365,000 net on account of Subsidies to Air Transport Services. We understand that the policy of His Majesty's Government is to stabilise the net Vote at approximately £500,000 per annum.

262. At present the Air Ministry have entered into contracts with Imperial Airways for the payment of subsidies for 10 years in respect of (a) European services, viz., London-Brussels-Cologne, London-Paris-Basle-Zurich, and such other services in Europe as may be agreed upon by the Air Council and the Company, and (b) a London-Egypt-Karachi service; and for 5 years from the date of the first through services, which it is hoped will be before the end of 1931, in respect of a London-Egypt-South Africa service. From the commencement of the contracts the aggregate liability of the United Kingdom in respect of the two former services is £2,490,000, and in respect of the South African service is £270,000 net. We observe that the placing of the contracts for the European and Indian services, though on each occasion the facts were notified to Parliament in a White Paper, and appear to have met with little or no criticism, would seem to have been contrary to the accepted principle that, except in so far as may be necessary for the fulfilment of their statutory functions, Departments have no constitutional authority to pledge Parliament to provide money in a future financial year. Since 1930 the position has been rectified by the passing of the Air Transport (Subsidy) Agreements Act of that year. We observe also that, while the subsidy in respect of the South African service is shared on what appears to us to be an equitable basis between the United Kingdom Government, the Government of the Union of South Africa and the Governments of the intervening Colonies and Territories, the subsidy in respect of the Indian service is borne wholly by the United Kingdom Government; moreover, the usefulness of the service has been adversely affected by the absence of a continuation service from Karachi to other parts of India.

263. It is possible to argue with great force both for and against the policy of a subsidised air transport service, and we recognise that so long as other countries subsidise their own national services (at far greater total cost than we do), it is impossible for this country to adopt a completely different policy without risk to national prestige. In any case no useful purpose can be served by our discussing the propriety of the expenditure to which His Majesty's Government is already committed under contract.

264. As regards the future, however, we think that the time has come for a further independent enquiry into national policy, covering such questions as (i) whether it is expedient to enter into any fresh agreements with Imperial Airways, especially during the present financial depression, and if so, on what terms: (ii) whether any such agreement should be confined to fast mail transport only, and if so whether the existing agreements for passenger-cum-mail service might with advantage be revised, subject, of course, to agreement with Imperial Airways: and (iii) whether the responsibility for air-mail service contracts ought not to be vested in the Post Office rather than the Air Ministry.

265. We observe that the Programme of Research and Technical Development includes provision for an expenditure in 1931 of £48,000 on Experimental Civil Aircraft, of which £5,000 is in respect of a New Programme commencing with the year 1931, involving a total commitment of £40,000. We recognise that, in the present state of the industry, progress in design without the assistance of the Air Ministry, may be slow; and we hesitate to recommend the abolition of this expenditure altogether. But we think that the results are too remote from our immediate necessities for us to be able to afford provision on this scale under present conditions. We therefore recommend that the New Programme for 1931 be abandoned, resulting in a saving of £5,000 this year, and that the expenditure in future be restricted, subject to existing commitments, to a sum not exceeding an average of, say, £20,000 a year.

Vote 10.—Air Ministry.

266. The gross cost of the Air Ministry Headquarters for 1931 is £656,000 which is 3.11 per cent. of the total expenditure on Air Services. The Admiralty and War Office Headquarters cost £1,154,673 and £837,000 respectively and the percentages are 2.11 per cent. and 1.79 per cent. These comparisons cannot however be taken at face value. The administration of the R.A.F. is more centralised particularly as regards technical, scientific, and inspection services, whilst the Air Ministry also controls Civil Aviation and Meteorological Services which are extraneous to the military service. Further the Estimates of the two senior services include large sums for retired pay and pensions, in respect of which administrative costs are small. We are assured that if allowance is made for these factors it can be shown that the percentage costs of the Headquarters Administration of the R.A.F. is not appreciably higher than obtains in the other Services. There has indeed been a steady improvement in this respect in recent years.

267. In the case of Admiralty and War Office establishments a comprehensive enquiry was made in 1923 by a Cabinet Committee under the Chairmanship of Lord Weir, but the then uncertain state of Air policy precluded its extension to the R.A.F. establishments. We recommend that an investigation similar to that conducted by the Weir Committee should now be undertaken for the Royal Air Force as in our view, as there has been a decade of expansion and active development of policy there is a *prima facie* case for a similar general review of Air establishments. This review should cover the whole field of organisation, i.e., Commands as well as Headquarters.

CHAPTER V.

DEVELOPMENT.

268. The comparative statistics of expenditure given on page 19 show that State expenditure intended to promote economic development in this country has increased by £46,000,000 per annum in the past seven years. Such charges, and the similar expenditure on Empire development, appear in many places in the national accounts and cover a wide field. The precise limits of the field are a matter of opinion. We propose in the present chapter to deal with expenditure which should, in our opinion, be looked at primarily from the standpoint of economic benefit. On this basis, we select the following items from the national accounts.

CIVIL ESTIMATES, 1931.

<i>Class I.</i> —Vote	4.	Treasury	£
		Economic Advisory Council ...	6,500
		Advisory Committee under the Trade Facilities Acts ...	2,802
	Vote 23.	Scottish Office	
		Western Highlands and Island Transport Service Subsidy	31,000
<i>Class II.</i> —Vote	6.	Empire Marketing Board ...	659,000
	Vote 7.	Oversea Settlement	264,750
	Vote 9.	Colonial and Middle Eastern Services	1,610,716
	Vote 10.	Colonial Development Fund, etc.	758,342
<i>Class IV.</i> —Vote	9.	Scientific Investigations, etc.	
		Grants to Royal Societies ...	12,050
		Grant to North Sea Fisheries Investigation	1,150
		Grant to Medical Research Council	148,000
<i>Class V.</i> —Votes	1A and 13.	Grants to Unemploy- ment Schemes in Necessitous Areas	175,000
	Vote 8.	Ministry of Labour Transference and training ...	894,100
	Vote 9.	Grants in respect of Unemploy- ment Schemes (Unemployment Grants Committee)	3,000,000

	£
<i>Class VI.</i> —Vote 1. Board of Trade	
Standards Department ...	11,016
Vote 3. Mercantile Marine Services ...	350,209
Vote 4. Department of Overseas Trade	424,507
Vote 5. Export Credits (token vote) ...	100
Vote 6. Mines Department	320,521
Vote 7. Crown Lands Office	32,214
Vote 8. Ministry of Agriculture and Fisheries	2,310,152
Vote 9. Beet Sugar Subsidy	2,150,000
Vote 11. Forestry Commission	665,000
Vote 12. Ministry of Transport	163,522
Vote 13. Development Fund (Development Commission)	500,000
Vote 14. Development Grants (Development (Public Utility) Committee)	400,000
Vote 15. Department of Scientific and Industrial Research	456,004
Vote 16. State Management Districts (token vote)	100
Vote 17. Scottish Department of Agriculture	572,313
Vote 18. Scottish Fishery Board	81,507
<i>Class X.</i> —Votes 1 and 2.	
Relief to Industry and Agriculture from Derating ...	25,895,780
<i>Road Fund.</i> —Grants to local authorities	33,395,000
	£75,291,355

269. This total does not include the cost of allied services in connection with the above Votes, charged under the Government system of accounts on the Works, Stationery Office, Post Office and Superannuation Votes. Neither does it include expenditure that is being recovered by fees or other charges. This applies to the two token Votes above and to the expenditure of the Post Office on the development of its State enterprises. The large electrical developments now taking place under the aegis of the Central Electricity Board and the Electricity Commission are also on a self-supporting basis.

270. If one is to obtain a complete picture of the extent to which the State has undertaken liabilities of a development character since the War it would be necessary not only to include this recoverable expenditure but also to take account of the heavy capital

liabilities which have been accepted in connection with unemployment schemes of various kinds. Some of these are only contingent liabilities such as the guarantee in respect of principal and interest of loans under the Trade Facilities Acts now standing at £62,000,000 or the liability under the Export Credits Scheme now standing at £4,000,000. In other cases the grants (shown in the above table) represent contributions in respect of interest or sinking fund or both, which will continue (at a declining rate) for the next thirty years. Since its inception the Unemployment Grants Committee has assisted schemes estimated to cost in all £187,000,000 and on the 30th June, 1931, the capital value of its outstanding liabilities amounted to £39,650,000 which does not include the capitalised liabilities in respect of road schemes transferred to the Road Fund in 1926 (see paragraph 291).

271. The other committee operating under the Development (Loan Guarantees and Grants) Act, 1929, has, with Treasury approval, promised grants of present value about £8,250,000 towards schemes estimated to cost £35,125,000.

272. In reviewing in some detail the great variety of objects on which this expenditure is being incurred we find considerable difficulty in elucidating the principles that are being followed, and where they have been made plain to us we are by no means entirely in agreement with them. With the fundamental immediate object of improving employment in this country no one will disagree, nor will anyone dispute that one of the most important lines of advance towards this goal is the economic development of this country; but when we find golf courses, tennis courts and swimming baths being subsidised as economic development, when we find roads being constructed at great cost in the remoter parts of Scotland, or to meet holiday traffic on the South Coast whereas the road needs of industry and trade lie rather in our congested urban streets; when we find grants paid to local authorities for 10 years in succession for accelerating work which it was their duty to carry out if it should be done at all; when we find Government departments giving free of cost to private traders services which more progressive traders are providing for themselves; when we find schemes of land settlement or development proceeding at a cost out of all commercial relation to any results likely to be attained; when in short we see these and many other activities being pressed forward to the embarrassment of the national finances with danger of increased taxation and serious repercussions on the general economic position of the country, then indeed we think it is time for a careful review of the whole policy of development.

273. An examination of the field of development expenditure reveals a broad distinction of services into those more or less permanent in character which have been held to be justifiable as normal activities of the State and special measures of a temporary

character relating to the present trade depression. The first category may be sub-divided into :—

- (a) services in aid of home industries generally ;
- (b) services in aid of particular home industries ;
- (c) State enterprises ;
- (d) Empire development ;

the second category we deal with as a whole.

These divisions are not entirely watertight ; some services fall into more than one category and some services which have originated with the trade depression may eventually establish a footing as normal services. Nevertheless the classification is a useful guide to any review of the field. The references in the table are to the respective class and vote in the Civil Estimates.

I.—NORMAL DEVELOPMENT SERVICES.

(a) Services in Aid of Home Industries Generally.

(i) *Research and standardisation.*—Such activities appear in many places in the national accounts, the more important being shown under the heads :—

Department of Scientific and Industrial Research (VI 15).

Board of Trade (Standards Department) (VI 1).

Medical Research Council (IV 9).

Agricultural and Fishery Research by the English and Scottish Departments of Agriculture and Fisheries (VI 8 & 17).

Development Commission (Grants) (VI 13).

Forestry Commission (Grants) (VI 11).

Empire Marketing Board (Grants) (II 6).

Ministry of Transport (Research on road materials, &c.).

Post Office.

Navy, Army and Air Force Votes.

(ii) *Power and Transport.*

Ministry of Transport, including—

Road Fund.

Electricity Commission.

Central Electricity Board.

Supervision of Railways, Canals and Docks, &c. (VI 12).

Board of Trade (Gas and Shipping) (VI 1).

(iii) *Trade Intelligence.*

Department of Overseas Trade (VI 4).

(iv) *Provision of Labour.*

Ministry of Labour (Employment Exchanges—Training and Transference) (V 8).

(v) *Relief of Rates on Industry and Agriculture.* (X 1 & 2).

(b) Services in Aid of Particular Home Industries.**(i) Agriculture and Fisheries.**

Ministry of Agriculture and Fisheries (VI 8).
 Scottish Department of Agriculture (VI 17).
 Scottish Fishery Board (VI 18).
 Development Commission (VI 13).
 Empire Marketing Board (II 6).

(ii) Beet Sugar Industry.

State subsidy (VI 9).

(iii) Forestry.

Forestry Commission (VI 11).

(iv) Coal Mining.

Mines Department (including Reorganisation Commission)
 (VI 6).

(c) State Enterprises.

Postal, Telephone and Telegraph Services.
 State Management Districts (Liquor control) (VI 16).

(d) Empire Development.

Empire Marketing Board (II 6).
 Oversea Settlement (II 7).
 Colonial Development (II 10).
 Colonial and Middle Eastern Services (II 9).

II.—TRADE DEPRESSION SERVICES.

Trade Facilities Scheme (now closed except as regards past guarantees).

Export Credits Scheme (VI 5).

Training and transference by the Ministry of Labour (V 8).

Unemployment Grants Committee (V 9).

Development (Public Utilities) Committee (VI 14).

Grants for unemployment works in Necessitous Areas
 (limited to £500,000 in all) (V 1A).

Unemployment road and bridge schemes.

Unemployment drainage and water supply schemes
 (VI 8 & 17).

✓

GENERAL CONSIDERATIONS.

274. The general criterion which we have in mind in selecting services for consideration in this chapter is that of economic benefit. We do not suggest that it is already a dominant consideration in regard to the whole of this great miscellany of activities, but we are definitely of the opinion that this is demanded by our present economic conditions. This benefit may appear in the form of direct profit on an enterprise; more commonly is it to be found in the general assistance which the State action affords to those engaged in industry. These indirect gains make it desirable for the State to take a much broader view than the private investor in deciding whether a given expenditure will, or will not, be a profitable investment of the national resources, but the task is thereby rendered much more difficult. The difficulty of making the decision does not however detract in any way from the importance of keeping this criterion of economic benefit steadily in view.

275. There has in our view been an unfortunate tendency since the war to confuse economic development, or, to put it plainly, profitable development, with what we may term "amenity development", especially in the field of Trade Depression Services. We do not dispute the need for the Government to do its best during a trade depression to break the vicious circle of declining confidence, falling off of investing, growing unemployment and increasing burdens on production. At such a time it behoves the Government to show its faith in trade recovery and to try to re-establish confidence, but this will not be achieved by expenditure on amenities likely to increase still further the burdens on production.

✓ 276. We are aware that expenditure during a trade depression on public works of any kind is often advocated as a means of preserving the morale and physical fitness of the workers and also on the ground that the unemployed have to be maintained in any event and that the nation ought to make some use of their labour. We are not greatly impressed by the first as an argument in favour of amenity development. It is to be expected that the more nearly a scheme approaches ordinary commercial activity of the kind to which the man is accustomed, both in the nature of the work and in the manner in which it is being executed, the more the employment approximates in its effect to normal employment. On the other hand we share the view commonly expressed that to the extent that the employment is unusual to the man, that the work is obviously of little immediate value, that it is not being carried out under normal commercial conditions, any effect on the man's morale may be discounted. Even as regards maintaining a man's physical fitness for his normal occupation there are serious limitations to the value to be attached to public works, where the only

labour open to the unemployed man is mostly of a heavy manual character.

277. The problem of securing some useful work from the man who is being maintained in idleness is an ancient one and many attempts have been made to find a solution. A line of argument that has been found very attractive in many quarters proceeds from the fact that the margin between profitable and unprofitable employment is often smaller than the cost to the community of maintaining a man in idleness. Would it not, so the argument proceeds, be better to subsidise the employer to maintain the man in employment and the country's trade in its normal channels, rather than pay more to keep the man in idleness. Expressed in this simple form the question would appear to admit of only one answer, but closer investigation shows the danger of grave abuse. It would be impossible in practice to draw a sharp line in industrial operations between work which would have been done in any event and work which would not have been profitable without a subsidy. Even a stipulation that the subsidy should only be given in respect of unemployed men taken on for the work could be easily evaded by a manufacturer discharging his men and taking them on afresh. Under such conditions the arrangement might easily degenerate into a subsidy to wages, recalling the classic abuse of the poor law of a century ago, associated with Speenhamland.

278. The only cases in which it has hitherto been found practicable to work a system of subsidies to operations of a commercial character are the grants for capital works carried out by public utility companies such as railway, dock and harbour companies, where a reasonable degree of assurance is forthcoming that the works would not have been undertaken at the present time without a subsidy. As long as the operations are of a commercial character and the measure of State assistance does not exceed the saving to the country in respect of the maintenance of the unemployed, an arrangement of this character is not undesirable, but if the test of profit be absent and the State grant be increased above the saving to the community the system may easily become wasteful. We revert to this matter below in dealing briefly with such of the above mentioned services as call for special comment.

I. RESEARCH.

279. The war gave a great stimulus to scientific research in this as in other countries. It was a vast object lesson to the mass of the people in the applications of science and led to a marked change in the national outlook towards scientific research. This process has been quickened by the many readjustments which post war conditions have made necessary in our national life; in our industries, our methods of locomotion and transport and even in our recreations. Necessity is the mother of invention and our

necessities since the war have been many and great. In these circumstances it is not surprising to find a rapid development in research expenditure both by the Government and also by private enterprise during this period.

280. We do not doubt that the need for such expenditure will increase rather than diminish. This country is finding its long established pre-eminence in certain basic industries seriously challenged by the sedulous fostering of such industries by other nations in an endeavour to be more self-contained. In regard to other industries the world is turning to rival products and leaving productive capacity in these industries both here and abroad much in excess of probable requirements. It is no use hoping or trying to reverse these tendencies; we must face the fact that much of the decline in some of our most important industries will be permanent and we must turn our attention therefore more and more to the development of other existing or new industries which demand a higher degree of skill and scientific equipment. The State can render great assistance to this process of readjustment by promoting research and standardisation due precautions being taken against transferring to the State the burden of ordinary industrial research which has become one of the essential costs of production.

The chief dangers to be avoided are (a) duplication of effort and (b) the expenditure of money on research, which however interesting does not afford the prospect of benefit to the country commensurate with the cost.

(a) *The co-ordination of research.*

281. With a view to preventing duplication of effort it is most desirable that the research work being carried on, not only in each industry but in the country generally, should be properly co-ordinated and that the co-ordinating bodies should include a strong representation of persons in close touch with national needs. Both objects are secured in considerable measure by the present organization of the Department of Scientific and Industrial Research and the Medical Research Council under the Privy Council and we were glad to learn in the course of our enquiry that steps had been taken to establish a somewhat similar Advisory Council for Agricultural Research. The Government will now have at its service three advisory bodies composed of distinguished independent experts fully competent to give advice on all questions falling within their respective spheres which together comprise the whole range of economic research. The common responsibility of these advisory bodies to the Lord President of the Council will facilitate the handling of questions falling within the sphere of more than one of them.

282. We recommend that as far as is consistent with efficient administration the actual direction of research in the three spheres should be brought under the control of the three Advisory Councils.

In so far as separate research under the direction of any other Department may be thought desirable, it should be incumbent on the Department first to submit its proposals to the appropriate Advisory Council and to submit their report to the Treasury when seeking authority for the necessary expenditure. In this way the Treasury would have before them the views of scientific experts, fully familiar with the issues involved and well informed of the facilities already available both under Government and private auspices to secure the result desired. Moreover the very fact that such prior consultation had to take place would permit of discussion in the early stages when the proposal was in process of formation. It is at that period that the fullest and most effective co-ordination can be brought about.

283. In making this suggestion we recognise that in the case of the Defence Forces there are secret investigations that admit of no such consultation with the civil Departments mentioned. These would be definitely excluded from any such arrangement. But in the formation and development of research organisations of the Defence Forces the closest co-operation with the Advisory Councils should be maintained. With a view to preventing possible overlapping all programmes of research should be as far as practicable on similar lines with the objectives clearly stated and such programmes should be circulated annually to all Departments concerned. (This procedure operates at present between the Department of Scientific and Industrial Research and the Services).

284. It may be difficult at times for the department proposing a new or extended research service to determine whether any particular project falls within the purview of one rather than another of the three Advisory Councils we mention. If the three Councils are in proper association with each other, and we have no reason to doubt that this will be the case, consultation between the Secretariats of the Advisory Councils will ensure that the appropriate Council or Councils are consulted. But to secure the fullest opportunity for effective consultations, arrangements should be made whereby the Secretaries of the three Advisory Councils should meet regularly, say at three monthly intervals. Where matters of major importance are to be discussed, the Chairmen of the three Councils should be present.

285. Our conclusions on this head may therefore be summarised thus. No proposal involving the future establishment or extension of activities involving the creation or addition of scientific research accommodation or staff or the payment to some outside agency for research services should be submitted by any Department of State to the Treasury for approval without a report from the appropriate Advisory Council concerned with Agriculture, Medicine or Scientific and Industrial Research, unless, in cases where National Defence is concerned, the respective Service is satisfied that

the research is of a secret nature or the arrangement is for any other reason impracticable. Even where the funds to be used for the purpose intended are derived from sources other than those normally voted by Parliament, the same procedure should be followed if there is any likelihood of charges falling upon the national exchequer for its continuation or its natural development. In a number of cases the report of the appropriate Advisory Council may well indicate that the proposed activity can best be controlled and financed directly by the originating Department and this is likely to be the case where development work as opposed to research work proper is concerned.

(b) *Financial Control of Research.*

286. The foregoing proposals should be effective in securing a proper consideration of research activities and in preventing wasteful duplication. The maintenance of a due correlation between the expenditure on research and the benefits to be derived therefrom is a much more difficult matter. This difficulty is acute even in the simple case of research carried on by industrial firms where the benefit can only come in the form of increased profits on the firm's products. A complete solution of the problem is almost impossible in the national sphere where economic benefit may be obtained in many different ways. There must, of course, be an optimum figure for the national expenditure on each of the three main branches of research, above which increased expenditure fails to bring an adequate return, but opinion will differ widely as to what the figure should be. We do not feel that we can do more than recommend—

- (i) that meetings of the Advisory Councils for industrial and agricultural research should be attended by a Treasury representative when matters of financial importance are under discussion and
- (ii) that as a general rule State aid should not be given to research which, even if successful, would seem to hold out little prospect of general benefit.

287. We do not extend these recommendations to the third Research Council (viz. the Medical Research Council) for the reasons that the element of economic benefit in this field is not as a rule capable of assessment and that the Government contribution represents but a small part of the total effort now being made in the field of medical research. The State makes at present an inclusive grant to the work of the Council, leaving the Council entirely free as to the disposal of the money, and we think that this arrangement should continue.

288. The object of limiting State aid to industrial and agricultural research which will be of definite benefit to the general community is to maintain the incentive to individual manufacturers to embark on research which will be of direct benefit to themselves.

2. THE ROAD FUND.

289. The Road Fund, or as it was first termed, the Road Improvement Fund, was instituted under the Development and Road Improvement Funds Act 1909 to provide a continuing fund out of which grants might be made for the improvement of roads. It was fed by the produce of excise duties on car licences and a customs duty on petrol. Both assignment of revenue and grants were interrupted during the war but in 1920 the Fund was reconstituted on a much wider basis. The petrol duty, which had during the war been transferred to the Exchequer, was abolished and the licence duties on motor cars were greatly increased, the scope of the Fund being at the same time widened to include the maintenance as well as the improvement of roads and certain ancillary services in addition.

290. The development of serious unemployment soon after the reconstitution of the Fund led to the launching of a series of special programmes of road works with assistance from the Fund to provide employment. The following table shows the revised estimates of the cost of these programmes to the Road Fund and the Exchequer up to 31st March, 1930 :—

—	Road Fund.	Exchequer.	Total.
	£	£	£
1920-21 Programme	2,820,564	832,005	3,652,569
1921-22 Programme	3,987,776	563,000	4,550,776
1922-23 Programme	5,157,622	—	5,157,622
1923-24 Programme	7,495,688	—	7,495,688
1924-25 Programme	15,556,040	—	15,556,040
Totals	£ 35,017,690	1,395,005	36,412,695

The total estimated cost of the schemes to which these contributions have been offered amounts to approximately £56,500,000 and, as shown above, the contribution from public funds is approximately £36,400,000, the balance being found by local authorities.

The schemes included in these programmes did not differ in essential character from road work that was being aided under the normal operations of the Fund: the main difference lay in the magnitude of the schemes and in the high proportion of the cost met from the Road Fund. From 1925 to 1929 the practice of earmarking special schemes as unemployment works was discontinued, but it has been resumed and greatly extended by the present Government. We refer to this later.

291. The heavy liabilities contracted under the above programmes were slow in maturing and on the 31st March, 1926 the Fund had a cash balance of £19,512,000; outstanding commitments at the same date being £30,174,000. The Budget of 1926 made substantial changes in the finance of the Fund. On the one hand the licence duties on certain types of vehicles were increased. On the other, one-third of the proceeds of the duties on private motor cars and cycles was permanently assigned to the Exchequer as being of the nature of luxury taxation, the two-thirds allocated to the Road Fund being regarded as an appropriate charge for road user. At the same time £7,000,000 of the accumulated balance was transferred to the Exchequer to assist in meeting the exceptional budget difficulties of the year and the Fund assumed the liability for grants that had been made for roads by the Unemployment Grants Committee, then roughly £1,000,000 per annum.

292. On the 31st March, 1927 the balance to the credit of the Fund stood at £12,259,000 with total commitments estimated at £27,187,000. Owing to the fact that roughly two-thirds of the revenue of the Fund is received in the last quarter of the financial year (i.e., the first quarter of the calendar year) a balance of this amount was not in excess of cash requirements. Nevertheless, Budget difficulties being still acute, a further £12,000,000 was transferred to the Exchequer, the Treasury undertaking at the same time to make any necessary advances required to finance the Fund each year until its revenue came in.

293. Still further breaches were to follow in the system under which motor taxation was to be applied towards meeting the cost of roads. In 1928 a Customs duty of 4d. a gallon was imposed on petrol in connection with the great scheme of rating reform of that year, the proceeds of the duty being allocated to the Exchequer to assist in meeting the heavy cost of the scheme. That scheme substituted a system of block grants based on such general considerations as population, rateable value, etc., for a number of the existing percentage grants, including the grants theretofore made from the Road Fund towards the maintenance of classified roads in London and the County Boroughs and non-classified roads in other areas. An amount equal to the discontinued grants was charged upon the Road Fund as a contribution towards the block grants and in addition the Fund was required to contribute £3,000,000 per annum towards the increased grants that were being made to local authorities to allow for the growth of the block-granted services. The total amount so charged on the Road Fund is £6,475,000 per annum. Finally in the current year the Customs duty levied on petrol for general revenue purposes has been increased from 4d. to 6d. a gallon.

294. The following table summarises the receipts into and payments out of the Road Fund for the years 1921 to 1930 omitting loan and agency operations :—

	Year commencing 1st April.									
	1921.	1922.	1923.	1924.	1925.	1926.	1927.	1928.	1929.	1930.
	£000.	£000.	£000.	£000.	£000.	£000.	£000.	£000.	£000.	£000.
RECEIPTS.										
Issues from the Consolidated Fund (Motor Taxation Receipts).	10,795	11,772	14,090	15,563	17,455	17,373	19,666	21,131	21,881	22,866
Interest and Profit on Investments and Loans	582	353	351	505	613	609	360	82	200	120
Miscellaneous	1	—	1	—	—	1	—	—	1	2
Total Receipts£	11,378	12,125	14,442	16,068	18,068	17,983	20,026	21,213	22,082	22,988
PAYMENTS.										
Administration and Miscellaneous Expenses	121	125	110	132	151	171	184	188	234	243
Cost of Collection of Motor Taxation (Expenses of Local Authorities).	301	289	275	288	340	354	387	412	446	450
Payment towards General Exchequer Contribution under Local Govt. Acts 1929.	—	—	—	—	—	—	—	—	—	5,071
Other Statutory Charges	40	28	35	36	40	43	47	54	72	129
Net Payments under Grants	8,106	11,726	12,603	14,742	16,165	16,975	18,743	17,015	19,784	22,012
Miscellaneous Payments	100	111	—	5	—	—	—	—	—	—
Transfers to the Exchequer under Finance Act, 1926, and Finance Act 1927.	—	—	—	—	—	7,000	12,000	—	—	—
Payment to Irish Free State	—	—	—	—	—	—	200	—	—	—
Total Payments£	8,668	12,279	13,023	15,203	16,696	24,543	31,561	17,669	20,536	27,905
Balance in Fund at end of year ...£	16,011	15,857	17,276	17,035	19,512	12,952	1,417	4,460	6,035	1,119

294A. We have already referred to the revival by the present Government of special unemployment programmes of road works. Two main programmes have been announced

(i) Five years' programme of works costing £27,500,000;

(ii) Trunk roads programme of works costing £21,000,000

with grants from the Road Fund in both cases usually of 75 per cent. or more of the net cost. These grants are additional to any liabilities that have been accepted in connection with London schemes, particularly for cross river traffic. The total commitments outstanding under all these various schemes amounted on 31st March last to roughly £60,000,000.

295. In view of the long recital of decisions almost without exception tending to impair the solvency of the Fund, it is not surprising to find its finances now in a most unsatisfactory state. The following table supplied by the Ministry of Transport shows the estimated position under existing policies over the five years 1931-1936, but we observe that it makes no provision for interest on the outstanding debt. If this be included, every year of this quinquennium shows a deficit, the debt rising to over £30,000,000. It should be made clear also that this table includes nothing for the Charing Cross Bridge Scheme which with its approaches is estimated to cost the Road Fund over £10,000,000.

ROAD FUND.

ESTIMATED RECEIPTS.

	1931/2.	1932/3.	1933/4.	1934/5.	1935/6.
	£000.	£000.	£000.	£000.	£000.
Motor Taxation	23,350	24,000	24,750	25,500	26,250
Interest on Loans and Investments	100	25	10	—	—
Loan Repayments	30	20	10	—	—
Road Traffic Act Receipts ...	150	155	160	165	170
£	23,630	24,200	24,930	25,665	26,420

ESTIMATED PAYMENTS.

	1931/2.	1932/3.	1933/4.	1934/5.	1935/6.
	£000.	£000.	£000.	£000.	£000.
I. Administration	435	450	460	470	480
II. Other Statutory Charges ...	535	545	560	570	580
III. General Exchequer Contribution.	6,475	6,475	6,475	6,475	6,475
IV. Maintenance Grants ...	9,350	9,350	9,200	9,200	9,200
V. 1920-25 Unemployment Programmes.	2,000	1,250	200	—	—
Carried forward ...	18,795	18,070	16,895	16,715	16,735

	1931/2.	1932/3.	1933/4.	1934/5.	1935/6.
Brought forward ...	£18,795	£18,070	£16,895	£16,715	£16,735
VI. London Cross River Schemes	1,500	2,100	2,500	2,200	350
VII. 5 years programme (including 2 years schemes).	4,000	4,000	4,000	3,000	2,000
VIII. Trunk Roads ...	3,000	4,000	4,000	3,000	2,000
IX. Other Grants ...	5,400	5,500	4,700	3,900	3,800
X. Loan Charge Grants taken over from the Unemployment Grants Committee.	700	670	640	600	560
£	33,395	34,340	32,735	29,415	25,445

			£	
Surplus, 31st March, 1931 ...	...	...	1,120,000	
Estimated Deficit 31st March, 1932	...	...	8,645,000	
" " 1933	...	...	18,785,000	
" " 1934	...	...	26,590,000	
" " 1935	...	...	30,340,000	
" " 1936	...	...	29,365,000	

296. As it is now being administered, this Fund has become a liability on the national finances and in our view drastic action is necessary to remedy the position. First among the steps we recommend is the abolition of the Fund and placing expenditure on road grants on the annual votes of Parliament. The old arguments in favour of the existence of a separate Fund have mostly lost their force. There is no longer any clear cut division between road finance and the general budget either on the revenue or on the expenditure side: the term "Self-supporting Service" is now clearly a misnomer: but what impresses us most of all is the wholly inadequate financial control that is being exercised over road expenditure. It is far easier to get £1,000,000 spent on roads than £100,000 on any service requiring express Parliamentary sanction. We do not blame the Treasury for this state of affairs, though Treasury sanction is necessary for all expenditure from the Road Fund. Rather do we regard it as the natural consequence of a system that allocated a rapidly expanding revenue to a particular service irrespective of the needs of the service and with no power reserved to Parliament to check its growth. The Road Fund has come to be regarded by successive Governments as a convenient means of financing grandiose projects without the inconvenience of obtaining Parliamentary approval and providing for the cost in the annual budget.

In recommending that expenditure on roads be brought under Parliamentary control we recognise that much of it is necessary expenditure required to provide for the economic development of the country, but we cannot shut our eyes to the evidence on every

side of heavy outlay on what we have termed "amenity development," development largely serving the needs of pleasure traffic in so far as it is required at all by present traffic.

297. But it is not enough merely to bring road finance under Parliamentary control: the budgetary position demands that that control should be rigidly exercised to eliminate unessential schemes where possible and in other cases to slow down the rate of expenditure to something more nearly approaching what we can afford. The estimated expenditure for 1932 is £34,340,000, including £6,475,000 for the contribution to the Block Grant. This £6,475,000 would under our proposal be voted in future as part of the General Exchequer Contributions to Local Revenue in Class X Votes 1 and 2 of the Civil Estimates. We recommend that the balance of the Road Fund estimate viz. £27,865,000 be reduced at least to £20,000,000 for each of the next two years. We contemplate that the estimate for road grants in future would be generally on the lines of the estimates given in the table above but with separate details as in the Public Works Estimates for major services; showing for each service, total approved estimate, expenditure to the previous 31st March, the amount required for the year and an estimate of the further amount required for completion.

298. A limitation of the Vote to £20,000,000 for the next two years will involve the postponement of many schemes already approved in principle and the slowing down of many others. It should also involve some lowering of the present very high standard of maintenance. As regards new commitments for the future we recommend a very cautious policy, at any rate until existing liabilities are well on the way to being liquidated. In particular we should regard an expenditure of £12,500,000 on a New Charing Cross Bridge with a further £2,000,000 or more on improving the access to it on the northern side, as unwarrantable in present financial circumstances. And an expenditure of £1,850,000 on improving the traffic facilities at the Elephant and Castle, which is only one—although an important one—of a hundred congested points in London seems to us hardly more justifiable. We cannot afford to deal with London traffic at this rate of expenditure. It is high time that a more extended view were taken of the future finance of London traffic facilities.

3.—DEPARTMENT OF OVERSEAS TRADE.

299. The activities of the Department of Overseas Trade fall under four main heads:—

- (a) Headquarters Staff.
- (b) Commercial Diplomatic Service.
- (c) Trade Commissioner Service.
- (d) Exhibitions and Fairs.

The expenditure of the Department in 1924 and the estimated expenditure for the current year under each head are as follows :—

	Expenditure in	
	1924.	1931. (Estimated).
	£	£
Headquarters	125,452	145,877
Commercial Diplomatic Service	105,445	133,315
Trade Commissioner Service	52,868	79,096
Exhibitions and Fairs	40,054	144,169
Miscellaneous	1,458	17,500
	<hr/>	<hr/>
Gross total ...	325,277	519,957
<i>Appropriations in Aid.</i>		
British Industries Fair ...	13,579	61,500
Grants from Empire Marketing Board	—	29,575
Other	4,912	4,375
	<hr/>	<hr/>
	18,491	95,450
	<hr/>	<hr/>
Net Total ...	306,786	424,507
	<hr/>	<hr/>

300. This vote includes £29,575 for trade exhibitions in the United Kingdom and other publicity activities on behalf of the Empire Marketing Board. This expenditure is recovered as an appropriation in aid and will be dealt with later under the heading "Empire Marketing Board." The policy of the Department is to recover also the whole expenditure on the British Industries Fair except the special grant of £25,000 a year for publicity, but no recoveries are made in respect of the cost of the main intelligence organization which has increased considerably since 1928. The activities of the Department have been reviewed on several occasions since its establishment shortly after the war, and the general conclusion reached was that it should be made self-supporting if it were continued at all. On any principles of rationalisation an organization covering all trade and all countries should be able to give better value for money than a private trader, or even an association of traders, is able to obtain by its own representatives. And

there is advantage in maintaining the closest possible touch between our trade intelligence service and our diplomatic service.

301. We recommend therefore that a policy of recovering the cost from those who benefit should be adopted and steadily pursued. If traders and manufacturers are not prepared to pay for the services they obtain it seems to us self-evident that they do not consider the Department of material benefit to them and no justification exists for its continuance.

302. A similar policy of making the Department self-supporting should be kept in mind in connection with the British Industries Fair and other exhibition activities.

4. RELIEF OF RATES ON INDUSTRY AND AGRICULTURE.

303. Under the Local Government Act, 1929, agriculture was entirely relieved of rates, and other rateable hereditaments, used primarily for purposes of productive industry or of freight transport, had their assessment to rates reduced by three-fourths at a total estimated cost to the Exchequer of about £26,000,000 p.a. These reductions were intended greatly to reduce the adverse effects of rates on industry and were coupled with extensive changes in local government administration and with a radical reform of a large part of the system of Exchequer subventions to local authorities. The relief to agriculture only came into effect on 1st April, 1929, and that to industry generally on 1st October, 1929, and the rapid development of the economic depression in 1930 has made it impossible as yet to form any estimate of their effect on industry in this country. We doubt, however, whether anyone would now suggest the reimposition of the rate burden even if this course were still practicable. As a matter of fact the financial arrangements under which the cost of this relief has been assumed by the Exchequer are so interwoven with other changes under the Local Government Act and form so integral a part of the elaborate new system of general Exchequer Contributions to Local Revenues that any reversal of the policy of the Act in this respect would be a matter of the greatest difficulty. This new system of State subventions to local authorities raises wide issues which are most conveniently dealt with in Chapter VII.

5. MINISTRY OF AGRICULTURE AND FISHERIES.

304. The expenditure of the Ministry of Agriculture and Fisheries (excluding the Beet Sugar Subsidy) has increased since 1924 as

shown below. The table also gives provisional forecasts prepared by the Ministry of the expenditure in 1932 and 1933 :—

	1924 (Expen- diture).	1931 (Estimate)	1932 Pro- visional Forecast.	1933 Pro- visional Forecast.
	£	£	£	£
General Services	490,493	595,780	603,600	609,600
<i>Agricultural Education and Research.</i>				
Education	257,902	363,950	424,500	487,300
Research	258,054	360,785	408,100	381,600
	515,956	724,735	832,600	868,900
<i>Live Stock.</i>				
Diseases of Animal Acts	39,005	120,500	124,000	124,000
Live Stock Improvement	42,428	61,385	62,785	64,285
	81,433	181,885	186,785	188,285
<i>Land Settlement, Drainage, etc.</i>				
Small Holdings and Settlements ...	902,180	862,010	875,010	890,010
Land Drainage, etc.	4,178*	254,225	343,250	423,250
	906,358	1,116,235	1,218,260	1,313,260
<i>Miscellaneous—Agricultural.</i>				
Kew Gardens	48,554	59,985	60,800	61,800
Marketing	—	79,085	85,000	90,000
Agricultural Credits and Co-operation.	26,170	17,000	18,000	19,000
Wages Regulation	9,540	14,145	14,150	14,150
Other Services	4,012	18,325	9,510	9,510
	88,276	188,540	187,460	194,460
<i>Fishery Services.</i>				
Administration	55,772	63,608	64,400	65,150
Research, etc.	12,846	76,310	36,900	36,900
Other Services	11,165	10	10	—
	79,783	139,928	101,310	102,050
Services arising out of the War ...	15,714	2,510	2,510	2,510
Gross Totals	2,178,013	2,949,613	3,132,525	3,279,065

*In 1924-5 grants for unemployment drainage schemes were provided on the Vote for the Relief of Unemployment.

	1924 (Expenditure).	1931 (Estimate)	1932 Pro- visional Forecast.	1933 Pro- visional Forecast.
	£	£	£	£
<i>Appropriations in Aid.</i>				
<i>Grants from Development Fund.</i>				
Agricultural Education	20,780	30,800	62,800	112,800
" Research	237,460	296,825	343,575	318,975
Fishery Research	15,528	17,411	18,450	18,450
Other Grants	17,337	29,635	20,085	20,125
	291,105	374,671	444,910	470,350
<i>Grants from Empire Marketing Fund.</i>				
Agricultural Research	—	31,925	22,200	18,100
Marketing	—	109,500	156,300	166,300
Other Services	—	11,358	11,700	11,700
	—	152,783	190,200	196,100
<i>Other Receipts</i>	176,718	112,007	111,487	111,712
Total Receipts	467,823	639,461	746,597	778,162
Net Total Expenditure ...£	1,710,190	2,310,152	2,385,928	2,500,903

It will be observed in the first place that a large proportion of the expenditure of the Ministry is financed by grants from the Development Fund and the Empire Marketing Fund. While it is true that the expenditure is set out fully in the estimates presented to Parliament, the existence of the large appropriations in aid naturally tends to soften criticism on this Vote. On the other hand when the lump sum grants to the Development Fund and the Empire Marketing Fund are under consideration no information is available on the estimates as to the purposes to which the money will be applied and detailed criticism is hardly possible. The whole arrangement seems to us prejudicial to financial control. We revert to this point later when discussing these two Funds. For present purposes we will deal with the gross expenditure.

305. This shows an increase of £770,000 since 1924 and a further increase of nearly £200,000 is anticipated next year and over £100,000 the year after, apart from the cost of new legislation now before Parliament. If allowance be made for unemployment drainage grants, met from another vote in 1924, the increase since that year is reduced to £560,000. With this correction, the largest increases have occurred in agricultural education, research and

improvement of livestock (£100,000 each), including in the last case animal diseases (£80,000—an uncontrollable variation), agricultural marketing (£80,000) and fishery research (£54,000).

Agricultural Education.

306. **In present circumstances we are opposed to any further extension of this service and we consider that without contraction of existing facilities some reduction might be effected on the Exchequer charge.** The grants for agricultural education average 67 per cent. of the net expenditure, some services attracting a percentage grant of 80 per cent. We regard any percentage grant in excess of 50 per cent. as specially open to objection and we recommend that it should be the maximum grant in future for agricultural education. In view of the reduction in the general level of teachers' salaries recommended in Chapter III the present moment is specially suitable for the change as the reduction in educational salaries will go some way to compensate local authorities for the loss of grant. In this connection we would refer to our recommendation in the following chapter in regard to the elementary education grants.

Agricultural Research.

307. Pending review of this field of expenditure by the new Research Council we make no recommendation for a reduction in expenditure, although a lower level of educational remuneration will tend to reduce expenditure. **We are, however, strongly of the opinion that the existing provision should be made to suffice for the next few years, the cost of any necessary new schemes being met out of savings on existing schemes.**

Live Stock Improvement.

308. Expenditure on livestock improvement now amounts to £61,000 per annum. **In so far as the expenditure is directly profitable to the industry it either ought not to be incurred by the State or it should be recovered from the industry.** The passing of the Licensing of Bulls Bill should facilitate the considerable reduction on this charge which we think justifiable.

Land Drainage, Water Supply, etc.

309. Prior to 1920 the State made no grants for arterial or field drainage, but acted on the principle that the land benefited must pay the cost. Since 1920, however, the position has gradually evolved that the State is expected to contribute, not only to arterial drainage, but also to local field drainage and water-supply schemes, which are ordinary landowners' improvements. These are the successive stages of evolution :—

(a) For unemployment purposes, temporarily, the Ministry were authorised in 1920 to make grants to drainage authorities, towards approved schemes of arterial drainage. These, or

similar grants, have since been continued as part of the policy of reducing unemployment by State schemes of expenditure. The grants were at first 75 per cent. of the net cost, but were subsequently reduced to 50 per cent. of the net total cost or 75 per cent. of the wages bill in each instance.

(b) In 1926, for the first time, the Government started a system of drainage grants, not for unemployment purposes, but for the sake of productivity, on the ground that water-logged land impedes production and that the landowners and land occupiers could no longer afford to pay the full cost of drainage works. In 1926 the Government of the day promised, *inter alia*, £1,000,000 over the next five years for grants to drainage authorities for approved arterial drainage schemes. The grants were fixed at first at 33½ per cent. of the net cost. (Later, in the special case of the Ouse a 50 per cent. grant of £1,250,000 was promised; but the necessary Ouse Bill was defeated in Committee, on local grounds, and no new Ouse scheme has yet been approved.)

(c) Two years later, in order to encourage authorities to employ "transferred labour" from the depressed areas, it was arranged that the grants under (b) should be 50 per cent. in special cases where the prescribed proportion of transferred labour was employed.

The estimated cost of existing schemes under (a), (b) and (c) in 1931 is £132,000.

(d) As part of the Autumn programme of 1929 for dealing with unemployment, temporary grants were given to landowners, for the first time in England, towards the cost of approved schemes of local field drainage, water-supply, etc. Those grants still continue and are normally 33½ per cent. of the net cost, but 50 per cent. is paid where transferred labour is employed. The estimated cost in 1931 is £60,000.

(e) Finally, in 1930, a new Land Drainage Act, which created Catchment Boards for all the main catchment areas, gave rise to a fresh type of grant towards the cost of arterial drainage schemes. Previous grants had been temporary grants, either for unemployment purposes or for productive purposes (with, in this last case, a fixed total money limit). The grants now promised to Catchment Boards towards the capital cost of new schemes are, in effect, a normal and permanent part of the grant system. Despite the fact that arterial drainage in the past has been self-supporting, and that the 1930 Act eases the financial difficulties of the owners and occupiers of flooded land by creating new powers of rating the whole catchment area, including the "uplands", the new authorities have been promised a regular system of grants in future, where the need is established, towards approved Catchment

Board schemes in future. The rate of grant is not fixed but is to be determined with due regard to the rateable value of the area and to local burdens. £58,000 is provided for these grants in the 1931 Estimates; and, as schemes involving many millions of pounds may develop in the course of the next ten years, the future potential burden on the Vote is very heavy.

We recommend:—

(a) that the scheme for grants to landowners should be terminated forthwith,

(b) that the grant to any drainage schemes promoted by a drainage authority should not normally exceed 25 per cent. of the cost, this representing the estimated saving to the State in the maintenance of the unemployed. In this connection we would refer to our remarks below on the grants of the Unemployment Grants Committee. This would necessitate the abolition of the existing limit in section 22 (2) of the Land Drainage Act, 1930, on the amount chargeable on the rates, and

(c) that special consideration be given to Catchment Areas in which, owing to low rateable value, the cost of a necessary major improvement would impose an excessive burden.

Agricultural Marketing.

310. The total estimated cost of agricultural marketing in 1931 (including Administration provided for in Subheads A and B of the Vote) is £131,000, of which amount £113,000 is to be met from the Empire Marketing Fund. £76,000 is to be spent on marketing work and £55,000 on "foreground" publicity. The latter sum falls really on the Exchequer, and not on the Empire Marketing Fund, as a special addition is made to the Fund for the purpose, over and above the general lump sum provision which the Marketing Board spend at their discretion. This "foreground" publicity has served to familiarise the public with the national mark scheme, and we think that this expenditure may now be discontinued—except in so far as the producers are prepared to meet the cost.

311. We consider that by proceeding on the general lines indicated above it should be possible to reduce the provisional forecast of the gross expenditure of the Ministry for 1932 by not less than £500,000. As the provisional forecast for 1932 is £183,000 in excess of the estimate for 1931 this would represent a gross total of £317,000 below that for the current year.

Land Settlement.

312. We have reserved till last the difficult question of land settlement, as the existing charge in the Vote for this service is contractual in character and any alteration of policy can only affect future

growth: moreover the position is complicated by the new legislation at present before Parliament. Three schemes have been operated up to the present:—

- (1) The pre-War scheme under the Small Holdings and Allotments Act, 1908.
- (2) The post-War scheme under the Land Settlement (Facilities) Act, 1919.
- (3) The current scheme under the Small Holdings and Allotments Act, 1926.

1. *Small Holdings and Allotments Act, 1908.*—County Councils were first empowered to provide small holdings under the Small Holdings and Allotments Act, 1908. Money for capital expenditure was provided from the Local Loans Fund at 3½ per cent. interest. Schemes were to be self-supporting, and in order to facilitate this the Ministry could pay (i) the costs (i.e. legal, etc.) of acquiring land and (ii) half the costs of ascertaining the demand. If in fact losses were subsequently incurred the Ministry could pay half the losses, the other half falling on County funds. This arrangement continued in force up to 1919, when by the Land Settlement (Facilities) Act of that year the Ministry was authorised to recoup all losses reasonably incurred by Councils in the administration of the Acts. The sums paid by the Ministry under these provisions in respect of the period 1st January, 1908 to 31st March, 1919, were as follows:—

	£
Half losses on Schemes	3,644
Costs of acquisition	267,678
Half cost of ascertaining demand	13,712
	285,034
Additional payments made under the Act of 1919	111,244
	£396,278

To the extent to which there were losses or profits in subsequent years these were merged in the deficit under the post-war Land Settlement Scheme. According to returns furnished by Councils at 31st March, 1926 (the latest date for which separate figures are available), the expenditure incurred and the holdings provided under the Act of 1908 were as follows:—

Area acquired and let or sold for small holdings at 31st March, 1926:—

	<i>Acres.</i>
Acquired by purchase	137,212
Acquired by lease	49,206
	186,418
No. of men settled and still in occupation ...	12,340
Approximate capital expenditure	£5,350,000
Approximate average capital expenditure per man settled	£433

2. *Land Settlement (Facilities) Act, 1919.*—The post-war scheme was designed to settle ex-service men on the land. The necessary funds were advanced out of national revenue to the County Councils as agents of the State which assumed liability for all losses. Owing to the high cost of building and the high rates of interest charged on the loans (about 6½ per cent.) these losses have been very heavy. In order to give the County Councils an interest in efficient management reimbursement to them since 1st April, 1926, has been on the basis of loan charges, etc., less estimated net income from the holdings averaged over a period of 60 years or more. Payments during the last four years have been as follows :—

	£
1927	886,000
1928	876,000
1929	849,000
1930	845,000

The payments will gradually decrease in amount up to about the year 2000 by reason of the termination of leasing schemes and the repayment of loans. The principal facts of the scheme may be summarized as follows :

Area acquired and let or sold in small holdings at 31st March, 1926 :—

	<i>Acres.</i>	
Acquired by purchase	223,000	
Acquired by lease	33,000	
	<hr/>	256,000
Approximate No. of men settled and still in occupation		16,000
Approximate capital expenditure		£15,250,000
Approximate average capital expenditure per man settled and still in occupation ...		£953
Present annual loss per man settled (approx.)		£53

In order to show the part played by high interest charges in the loss it may be mentioned that a reduction of 1 per cent. in the rate of interest would have reduced the average annual loss from £53 to £45 per annum.

Under Section 18 of the Act of 1919, Councils were empowered to make or guarantee loans to their tenants to assist in the purchase of livestock, fruit trees, seeds, fertilisers, and implements. The loans were repayable with interest and the position at 31st March, 1926, was as follows :—

No. of loans guaranteed	1605
	£
Amount of loans guaranteed	175,838
Amount repaid by tenants	81,965

Of the balance of £93,873 no less than £75,000 or 42 per cent. of the amount guaranteed had been written off by 1926. These losses were in great part attributable to two facts :—

(a) that a large proportion of the tenants entered into possession of their holdings and purchased their stock when prices were at their highest, and these men lost a great part of their capital as a result of the heavy fall in prices during the next few years :

(b) that many men, including a number who were partly disabled, were accepted as tenants although their qualifications were below the standard that would ordinarily be required.

3. *Small Holdings and Allotments Act, 1926.*—Under the scheme now current the Ministry is empowered to contribute not more than 75 per cent. of the annual losses incurred by councils in the provision of small holdings under the Act, the contributions to be fixed in advance on the basis of proposals and estimates submitted to and approved by the Ministry. The remainder of any annual loss is borne by the Councils. The following statement indicates the position up to the 31st March, 1931, as regards schemes for the acquisition of new land either definitely approved or under consideration :—

	<i>Acres.</i>
Area	20,710
Holdings to be created	735
Estimated capital cost	£997,000
Estimated capital cost per holding	£1,356
Estimated annual loss	£22,201
Estimated annual loss per holding (average)	£30
Ministry's annual contribution	£16,577
Ministry's annual contribution per holding (average)	£22

Loans for capital expenditure under the Act may be advanced from the Local Loans Fund and are repayable with interest at the current rate, such repayments being taken into account in arriving at the estimates of annual loss. In practice, however, most councils have hitherto obtained their advances from other sources.

The comparatively high average capital cost per holding under the Act of 1926, as compared with the earlier schemes, is entirely due to the fact that the holdings provided by Councils since 1926 have been mainly of the fully equipped self-supporting type, whereas under the Acts of 1908 and 1919 a much larger proportion of the holdings consisted of small areas of bare land let without equipment to men resident in the locality. The average size

of the holdings provided up to 1926 was about 15 acres; since that date the average, as indicated by the above figures, has increased to about 28 acres. Under the Acts of 1908 and 1919 the proportion of equipped holdings was only 30 per cent. and 46 per cent. respectively; under the Act of 1926 the proportion is 70 per cent. These increases account for the increased average capital cost of the holdings, despite which the average loss per holding is lower than it was under the Land Settlement Scheme owing (a) to decreased cost of building generally, and (b) to the lower rate of interest on loans.

The total capital expenditure under the three schemes above mentioned is as follows :—

	£
Act of 1908	5,350,000
Act of 1919	15,250,000
Act of 1926	997,000
	<hr/>
Total	£21,597,000
	<hr/>

4.—*Agricultural Land (Utilisation) Bill.*—Yet another scheme of land settlement has recently been proposed to Parliament in the *Agricultural Land (Utilisation) Bill*. This scheme is intended to empower the Government itself to provide small holdings and allotments for unemployed persons. The existing powers and duties of local authorities are not curtailed but power is given to the Minister to provide small holdings and cottage holdings for ordinary applicants where the County Council is not adequately meeting the demand. The financial memorandum attached to the Bill estimates the average capital cost of the ordinary small holding at £1,100, and the net return on this investment at about 3 per cent. As regards the provision for the unemployed it is contemplated that the holdings will be of the poultry or market garden type, being provided in the neighbourhood of a man's present home. On this basis the average capital cost is put at £640, yielding an estimated return of 2 to 2½ per cent. In addition a maintenance allowance averaging £40 a case is allowed for the initial period and provision is made for loans of working capital estimated to average £275 a holding—making in all a total capital provision of £955. In so far as any of these loans has to be written off the very low return on capital indicated above will be still further reduced.

313. We find great difficulty in making any precise recommendations on the subject of small holdings. On the one hand we appreciate the great importance to the economic life of the country of in-

creasing the agricultural population and the home production of food : on the other hand the nation cannot afford investments that only bring in a return of 2½ or 2 per cent. or less. Above all else we would emphasize the importance of making the holdings as nearly economic as possible. The first and most important step to this end is the selection of suitable men whether now in employment or not for settlement. Secondly, the holding should be adapted to the kind of farming promising the best returns under modern conditions. At a time when arable production in other countries is tending towards greater and greater units with increasing mechanisation it would be throwing money away to endeavour to compete in the grain markets with units of 20 or 30 acres. Thirdly, granted the right types of holding, the size and the capital expenditure should be adjusted to those types to give the maximum possible return on the capital. Fourthly, the success of a holding of the type that we have in mind is wrapped up with efficient co-operative marketing that will secure to the small holder as large a share as possible of the retail price of the product.

314. We recognize that it is easier to make such generalisations as the foregoing than to put them into practice ; we believe that the best lines of development in this matter will be arrived at by a process of experiment. For this reason, and also because of the very unstable price conditions, we are opposed to any spectacular development of small holdings at the present time. Rather would we advise a policy of careful and judicious experiment on a scale wide enough to yield reliable results. One essential to success is a proper adaptation of plans to local conditions which vary so widely over the country. From this point of view we would deprecate any policy tending to centralise the administrative responsibility for small holding development in the hands of the Government. If it should be deemed essential to take power for the Government to act in default of a county council, a course somewhat opposed to British conceptions of local government, such action should only be at the cost of the defaulting council ; otherwise small holding development everywhere will tend to be left to the Government.

315. One final comment we would make on another aspect of the Agricultural Land (Utilisation) Bill. At a time when there is grave danger of land going out of cultivation owing to the low prices of agricultural produce, the greatest caution should be used in spending the national resources in endeavouring to bring back into cultivation land which was found to be unprofitable even under the more favourable conditions of previous years. In our view land should only be acquired for reconditioning or reclamation where there is clear evidence that it can be subsequently sold without loss.

6.—DEPARTMENT OF AGRICULTURE (SCOTLAND).

316. The following table shows the expenditure of the Scottish Department of Agriculture in 1924, the estimate for the current year and provisional forecasts for 1932 and 1933.

	1924. Expendi- ture.	1931. Estimate.	1932. Provl. Forecast.	1933. Provl. Forecast.
	£	£	£	£
General Services	131,173	154,090	155,850	158,550
<i>Education and Research.</i>				
Agricultural Education	65,195	93,831	127,600	115,900
„ Research and Experi- ments.	28,650	61,745	65,700	58,800
Empire Marketing Fund Schemes	—	8,872	9,500	8,600
	93,845	164,448	202,800	183,300
Live Stock Improvement	34,282	34,413	34,400	34,300
<i>Land Settlement and Drainage, etc.</i>				
Agriculture (Scotland) Fund ...	83,394	269,000	267,000	264,000
Arterial Drainage	—	24,000	25,000	25,000
Land Drainage	— *	29,950	29,950	29,950
Land Reclamation, etc.	1,709	125	90	90
	85,103	323,075	322,040	319,040
Piers, Roads and Drifter Services†	—	19,000	14,000	14,000
Supply of Seed Oats and Potatoes	103,888	—	—	—
Marketing	—	11,832	10,000	10,000
Miscellaneous	7,531	16,785	17,955	17,955
Gross Total Expenditure ...£	455,822	723,643	757,045	737,145
<i>Appropriations in Aid.</i>				
From Development Fund	24,966	97,026	129,650	109,710
„ Empire Marketing Fund ...	—	21,904	20,600	19,700
Other Receipts	33,552	32,400	42,450	42,390
Total Receipts	58,518	151,330	192,700	171,800
Net Total Expenditure ...£	397,304	572,313	564,345	565,345

* £32,444 spent from Relief of Unemployment Vote.

† Prior to 1926 met from Agriculture (Scotland) Fund.

Since 1924 the gross total of the Vote has increased by about £268,000, but if the abnormal charge in that year for seed oats and potatoes be excluded, and the drainage grants then met from another vote be included the increase has been no less than £340,000. The main increases have arisen on the grant to the

Agriculture (Scotland) Fund (which provides for small holdings) £186,000 Research, £33,000; Education, £29,000, and Arterial Drainage, £24,000.

317. We would refer in this connection to our comments on the expenditure of the Vote for the English Ministry of Agriculture, most of which are applicable also to this Vote, but the item, Arterial Drainage, calls for special comment. The Scottish Drainage Act makes no provision for Catchment Boards with the power to levy on local rates such part of the cost of arterial drainage as cannot be recovered from persons directly benefiting. We can see no ground for such differential treatment. To take a drainage scheme now under consideration as an example, residents in the Kelvin Valley have obviously much greater interest in stopping the flooding by their river than have the rest of the country. We recommend that the Scottish Drainage Act be brought into line with the English Act in this respect. Having regard to this recommendation and to our general comments on the corresponding English Vote we think that the provisional gross forecast for 1932 should be reduced by £75,000, i.e., to £682,000, which is £42,000 below the gross estimate for the current year.

7.—DEVELOPMENT FUND.

318. The Development Fund (like the Road Fund) was established by the Development and Road Improvement Funds Act 1909 in order to provide for grants or loans to Government Departments, other public authorities and associations of persons not trading for profit for any of the following purposes:—

(a) Aiding and developing agriculture and rural industries by promoting scientific research, instruction and experiments in the science, methods and practice of agriculture (including the provision of farm-institutes), the organisation of co-operation, instruction in marketing produce, and the extension of the provision of small holdings; and by the adoption of any other means which appear calculated to develop agriculture and rural industries;

(b) Forestry (including (1) the conducting of inquiries, experiments, and research for the purpose of promoting forestry and the teaching of methods of afforestation; (2) the purchase and planting of land found after inquiry to be suitable for afforestation);

(c) The reclamation and drainage of land;

(d) The general improvement of rural transport (including the making of light railways but not including the construction or improvement of roads);

(e) The construction and improvement of harbours;

(f) The construction and improvement of inland navigations;

(g) The development and improvement of fisheries;

and for any other purpose calculated to promote the economic development of the United Kingdom.

Such grants were to be made by the Treasury on the recommendation of an independent body of five Commissioners each appointed for ten years, one retiring every two years.

319. In 1919 the powers and duties of the Commission in regard to forestry were transferred to the Forestry Commission established under the Forestry Act 1919 and in the same year its transport functions (except in regard to fishery harbours) were assigned to the newly created Ministry of Transport.

320. Under the Act of 1909 grants to the Development Fund at the rate of £500,000 per annum were to be made in 1910-11 and in each of the next four years, out of the Consolidated Fund. In addition £400,000 was provided on Parliamentary Votes in 1910-11. No further Vote was made until 1921, when, under the Corn Production Acts (Repeal) Act 1921, a special grant of £850,000 was made to the Fund for the purpose of aiding and developing agriculture in England and Wales in the manner specified in paragraph (a) of the original Act, quoted above. At the same time a similar grant of £150,000 was made to the Agriculture (Scotland) Fund. The following table shows the receipts and payments during the last eight years:—

Development Fund.

Statement of actual receipts and payments during the financial years 1924 to 1930, with estimates for the year 1931.

Financial year.	Receipts.				Payments.
	Balance at beginning of year.	Parliamentary Vote.	Profits on Investments and casual receipts.	Total.	
	£	£	£	£	£
1924 ...	(a) 320,595 (b) 661,399	200,000 —	18,605 28,776	539,200 690,175	314,628 152,695
1925 ...	(a) 224,672 (b) 537,481	140,000 —	52,037 46,685	416,709 584,166	268,930 216,386
1926 ...	(a) 147,679 (b) 367,780	200,000 —	18,188 19,738	365,867 387,518	262,707 262,171
1927 ...	(a) 103,160 (b) 125,347	250,000 —	14,126 5,052	367,286 130,399	253,270 130,399
1928 ...	(a) 114,016	400,000	26,856	540,872	363,354
1929 ...	(a) 177,618	300,000	52,541	530,159	444,217
1930 ...	(a) 85,849	625,000	25,102	735,951	589,133
1931-32 (estimated)	(a) 146,818 (actual)	500,000	35,000	681,818	709,807

(a) Ordinary Fund.

(b) Special Fund provided by the Corn Production Acts (Repeal) Act, 1921.

321. The following table analyses as far as is practicable the advances made on the recommendations of the Commissioners during these years according to the main purposes :—

Approximate allocation of advances made from the Development Fund.

Financial Year.	Agriculture and Rural Industries.	Fisheries and Harbours.	Land Reclamation and Drainage.	Administrative Expenses of the Commission.	Total.
	£	£	£	£	£
1924 ...	322,858	55,316	231	10,145	{ 78,773*
1925 ...	420,198	54,666	—	10,452	{ 388,550
1926 ...	455,076	59,056	171	10,575	{ 485,316
1927 ...	319,087	51,143	3,552	9,887	{ 383,669
1928 ...	308,663	44,876	500	9,315	{ 363,354
1929 ...	361,107	74,485	—	8,625	{ 444,217
1930 ...	420,844	159,065	600	8,624	{ 589,133

* This sum of £78,773 was a special payment to the Government of the Irish Free State in respect of allocation of Capital of Development Fund, *less* agreed value of certain loans transferred and therefore not included under the separate headings.

Agricultural Education and Research.

322. We have dealt on the Votes of the two agricultural departments with the grants paid by the Development Commission through these Votes. Our recommendations in that regard will have their reaction on this Vote for next year and any savings involved have already been taken into account. As there stated we do not consider this system of payment of grants out of a lump sum Vote through the Votes of other Departments conducive to sound financial control. The establishment of the Advisory Council for Agricultural Research will no doubt lead to the whole matter coming again under review in the near future. We would favour the association of a small executive branch with the Advisory Council to take entire charge of agricultural research including the responsibility for aiding research institutes. It should be the first duty of the new Council to review all the expenditure of the institutes in order to ascertain what savings, if any, can be effected in the large grants now voted for this service, whether by the abolition of any redundant institutes or otherwise. Agricultural education might remain within the purview of the Ministry of Agriculture and Fisheries, being entirely charged to that Vote without any appropriation in aid from the Development Fund.

Fisheries (including harbours).

323. This leaves practically only fisheries and fishery harbours within the sphere of the Development Commission, and highly as we appreciate the valuable services rendered by the Commission up to the present, we doubt whether it would be justifiable to maintain a separate organization for them alone. Fishery research is already the administrative responsibility of the two Fishery Departments and any expenditure that is necessary might remain a final charge on their respective Votes. Fishery harbours are a transport facility and would naturally fall within the purview of the Ministry of Transport.

These harbours have recently become very costly to the State, grants and loans for capital improvements at Scottish fishery harbours alone having amounted to £140,000 in 1929, and £85,000 in 1930. These figures include part of the cost of a general scheme of minor repairs and free dredging, estimated to cost £21,000 in 1931. We recommend that this scheme should be terminated forthwith and that commitments in respect of these harbours be kept as low as possible in future, any necessary maintenance work being provided for by the local harbour authorities with the aid of the local municipality as in England.

8.—BEET SUGAR SUBSIDY, GREAT BRITAIN.

324. The Beet Sugar (Subsidy) Act, 1925, provided for the payment of a subsidy on sugar and molasses manufactured in Great Britain during the period between the 30th September, 1924, and the 1st October, 1934, from beet grown in Great Britain, and at the same time reimposed the Excise Duty on sugar and molasses manufactured in Great Britain and Northern Ireland from home-grown beet. The rates of subsidy are on a diminishing scale, being at the full rate for four years, and then falling by one-third for the next three years with a further reduction of one-third for the last period of three years. The figures are as follows:—

	Manufacturing Seasons.		
	1924-28. Rate per cwt.	1928-31. Rate per cwt.	1931-34. Rate per cwt.
Sugar :	s. d.	s. d.	s. d.
Exceeding 98 degrees of polarisation.	19 6	13 0	6 6
Molasses :			
50-70 per cent. of sweetening matter.	8 10.9	5 11.3	2 11.6

The rates are reduced for lower degrees of sugar polarisation and percentages of sweetening matter in molasses.

STATEMENT OF EXPENDITURE.

Year.							Expenditure.
							£
1924	...	...	...	...	...	...	492,040
1925	...	...	...	...	...	...	1,066,090
1926	...	...	...	...	...	...	3,225,859
1927	...	...	...	...	...	...	4,309,260
1928	...	...	...	...	...	...	2,854,239
1929	...	...	...	...	...	...	4,229,730
1930	...	...	...	...	...	...	6,022,972
1931 (Estimated)	...	...	...	...	...	...	2,150,000
1932 (Estimated)	...	...	...	...	...	...	2,000,000
1933 (Estimated)	...	...	...	...	...	...	2,250,000

325. Since the subsidy was started in 1924 the price of sugar has fallen to less than one-third of 1924 average :—

Annual Average Price of Raw Sugar *ex-Duty, c.i.f. United Kingdom, from 1921 to 1930 inclusive, compared with the average of 1909-13. †

Year.							Average Price
							per Cwt.
							s. d.
1909-13 (Average)	...	...	...	...	...	...	11 11½
1921	...	...	...	...	...	...	18 3½
1922	...	...	...	...	...	...	15 3½
1923	...	...	...	...	...	...	25 9
1924	...	...	...	...	...	...	21 9
1925	...	...	...	...	...	...	12 9
1926	...	...	...	...	...	...	12 3
1927	...	...	...	...	...	...	13 9
1928	...	...	...	...	...	...	11 7½
1929	...	...	...	...	...	...	9 2
1930	...	...	...	...	...	...	6 8

326. By improvements in technique and greater through-put manufacturing costs were reduced on the average by 5s. 6d. per cwt. between 1924-5 and 1929-30, but this has not been adequate to meet the difficult situation resulting from the latest reduction of the subsidy coinciding with an unprecedentedly low price of sugar and the Government has agreed to make a loan up to 1s. 3d. per cwt. on 300,000 cwt. of sugar per factory for 1931-2 subject to the loan plus the price of sugar not exceeding 7s. 9d. a cwt. This loan is estimated to cost £225,000 this year.

* On the basis of 96 degrees polarisation.

† The figures in the above Table for the years up to 1928 are taken from the "World Sugar Situation" Report by the Economic Committee of the League of Nations, dated July 4th, 1929, C.303.M.104.1929.II. The figures for 1929 and 1930 are the average of market quotations.

327. If allowance be made for the value of duty preferences as well as direct subsidies, the total State assistance given to the British Sugar Beet Industry up to 31st March last is estimated at £29,710,000.

During the operative year 1930-1, 3,060,498 tons of beet were grown by 40,413 farmers on 343,920 acres and the output of the factories reached 418,000 tons of white sugar and 105,300 tons of molasses, the total cost to the Exchequer being £2,670,000 in duty preferences and £6,140,000 in subsidy—a total of £8,810,000. The amount of employment in field and factory provided by the industry for every 100 acres of beet is estimated at $8\frac{3}{4}$ man-years thus :—

Field about... ..	7 $\frac{1}{2}$ Man-Years
Factory about	1 $\frac{3}{4}$ Man-Years
	8 $\frac{3}{4}$ Man-Years
	—

The total State assistance to the industry during the year 1930-31 works out at nearly £300 per man. If the direct subsidy only be taken into account the cost for each worker was about £200 a year and with the reduction of the subsidy this year this rate has now been halved (leaving out of account the temporary loan of £225,000 previously referred to). It cannot be claimed that this was entirely additional employment; on the other hand allowance must be made in any balances of accounts for the value of the beet crop as a preparation for other crops.

328. The State is obviously under contractual obligations to continue existing arrangements until they are due to expire in 1934.

9. FORESTRY COMMISSION.

329. The Forestry Commission was set up in November 1919 under the Forestry Act 1919. Its objectives were broadly to get re-constituted the woodland areas cleared during the war, and by afforestation, to provide a reserve of timber growing in the country. The scale of operations was based on the Acland Report (Cd. 881) which recommended :—

(a) The maintenance of the existing woodland area, 3 million acres, in a state of productivity.

(b) The afforestation with conifers of 1 $\frac{3}{4}$ million acres at the rate of 1,180,000 acres in the first 40 years including 150,000 acres in the first decade.

(c) The establishment of a Forestry Fund with financial provision for the first decade (1919-29) of £3,500,000 plus working receipts.

330. The recommendation of the Geddes Committee that the State afforestation be discontinued was not accepted by the Government of the day but the rate of planting was greatly reduced.

331. In July 1924 the new Cabinet approved an expansion of the afforestation programme and the establishment of forest workers' holdings. A supplementary estimate of £275,000 was accordingly presented and a larger programme embarked upon. The restriction of the service which had followed the recommendations of the Geddes Committee was abandoned, and in the end £3,364,012 in addition to the revenue from the sales of forest products, which rose from £33,000 in 1920 to £147,000 in 1928, was spent in the 10 years 1919-28 inclusive.

138,279 acres were planted by the Commissioners, 76,736 acres by corporate bodies and private individuals under a system of planting grants and 558 forest holdings were established in the same period. The amounts voted either direct for the Forestry Commission or on the Relief of Unemployment Vote for forestry grants were as follows :—

	<i>Forestry Commission Vote.</i>	<i>Relief of Un- employment Vote.</i>
	£	£
1919	99,000	—
1920	379,000	—
1921	200,000	250,000
1922	20,000	50,000
1923	153,000	100,000
1924	453,000	30,000
1925	300,000	—
1926	385,000	—
1927	595,400	—
1928	485,600	—
1929	600,000	—

332. In July, 1928, the then Government undertook to ask Parliament to vote as grants in aid of the Forestry Fund over the ten financial years 1929 to 1938 the aggregate sum of £5,000,000 on the understanding that annual Votes should be kept as low as possible in the first years of the decennium. This provision, coupled with an estimated revenue from forest products of £1,400,000 was expected to be sufficient to provide for the afforestation of 225,000 acres (as against the "Acland" programme of 150,000 acres Government planting in the first decennium) in addition to replanting of 12,000 acres of existing State forests and £140,000 for grants to corporate bodies and private owners, equivalent to about 47,000 acres of private planting. It also included £1,000,000 for forest

workers holdings. The whole matter was again reviewed by the Select Committee on Estimates who reported in April 1929 that, on the basis of calculations made by the Forestry Commission, about 60 per cent. of their expenditure might in certain circumstances be expected to yield a net return up to 3.7 per cent.; the remaining 40 per cent. would yield no return or but a small return. It was not possible, moreover, they said, to draw a firm conclusion that 3.7 per cent. is the true return, even on the capital directly involved and securing an appreciable return, because:—

(a) Part of the expenditure on forest workers holdings and on education and research should be debited against the afforestation scheme;

(b) The calculation of maintenance costs was *prima facie* too low;

(c) Figures taken for acquisition costs needed reconsideration in the light of the latest data available.

They added that:—

(1) Whilst under present conditions of costs and prices afforestation could not prove a remunerative investment for public funds, there was a probability of its becoming one at some future date:

(2) from the point of view of providing employment the results obtainable from the policy of afforestation (say up to 3 men per 100 acres) were disappointing.

333. In September 1929 in view of the growing unemployment the present Government decided that the £5,000,000 programme for the second decade should be increased to £9,000,000 to be provided as shown in the table below which also gives the area to be planted each year. New acquisition was to proceed at the annual rate of 60,000 acres plantable land and 2,500 acres of cultivable land, the latter to provide for an additional 3,000 forest workers' holdings.

Year.	Estimated Parliamentary Grant.	To be afforested.	To be replanted.	Total.
	£	acres.	acres.	acres.
1929	784,000	22,000	3,000	25,000
1930	842,000	22,000	3,000	25,000
1931	880,000	25,000	3,000	28,000
1932	925,000	30,000	2,000	32,000
1933	951,000	33,000	2,000	35,000
1934	941,000	36,000	2,000	38,000
1935	921,000	39,000	2,000	41,000
1936	940,000	40,000	2,000	42,000
1937	958,000	41,000	2,000	43,000
1938	973,000	42,000	2,000	44,000
Total for Decade	£9,115,000	330,000	23,000	353,000

The total expenditure over the decade was estimated at £11.3 million, made up as follows :—

				£
Exchequer grants	...	...	...	9,115,000
Working receipts	...	...	...	2,160,000
				Total ...
				£11,275,000

334. As events have proved, the Forestry Commission's requirements for the first three years of the second decade have fallen considerably short of their programme figures :—

				<i>Voted.</i>	<i>Programme figure.</i>
				£	£
1929	...	...	...	600,000	784,000
1930	...	...	...	837,800	842,000
1931	...	...	...	665,000	880,000
				2,102,800	2,506,000

i.e., a difference of £403,000 over three years. This difference is principally due to delays in acquisition. In the 12 months ended September, 1930, the Commission acquired less than half their programme area of 60,000 acres. This has affected not only planting but also the provision of forest workers' holdings.

335. The estimated expenditure for the current year is £1,049,380 gross and £890,000 net. It was expected that the balance on the 1st April last would be £225,000 and an estimate for £665,000 has accordingly been submitted to Parliament as the grant in aid for the current year.

336. The action taken by this country in connection with afforestation since the War is an admirable illustration of that alternation between expansion and retrenchment referred to in our opening chapter. As an investment of the national resources an estimated return of from 2 per cent. to 2½ per cent. has no attractions. As against the prospect of higher prices of timber in the remote future we would urge the probability :—

- (1) of substitutes for timber being developed; failing which
- (2) of forestry development in other lands where it can be carried out much more cheaply than in this country.

337. As a safeguard for this country in time of war we naturally find some difficulty in forming any idea of war conditions half a century or more hence, if unfortunately war is then still the ultimate resort of disputing nations. The probable development of timber substitutes has also to be borne in mind.

338. Finally, if afforestation be considered as a means of settling the unemployed on the land we would point out that an expenditure of £140 per annum is required to find full-time work for one man and that the capital cost of providing a forest worker's holding wherein he can find part-time employment to supplement his work in the forest is estimated at from £400 to £600. In the great majority of cases the creation of a forest worker's holding is not required to secure the necessary labour for the forests, these being usually within easy range of existing labour supplies.

339. After weighing up all these considerations we recommend that no fresh acquisitions of land be made for the present and that no more forest workers holdings be created, but that afforestation proceed at the rate of 20,000 acres per annum for 5 years on the land already acquired. This course is estimated to save £478,000 next year and £560,000 per annum in subsequent years as compared with the present policy.

10. EMPIRE MARKETING BOARD.

340. The Empire Marketing Board was established in 1926 with a ministerial assurance that an income of £1,000,000 per annum (£500,000 in the first year) would be provided as a grant in aid of a Fund, from which assistance might be given towards the marketing of Empire products (including home products) in this country. The full sum has not been provided since the first year and the actual grants to the Board have been as follows:—

	£
1926	500,000
1927	400,000
1928	500,000
1929	550,000
1930	612,500
1931 (Est.)	659,000

341. The table below shows how the Board spent its money :—

	1926.	1927.	1928.	1929.	1930 (Esti- mated.)	1931 (Esti- mated.)
	£	£	£	£	£	£
Salaries, Wages and Allowances	11,592	31,271	35,880	28,999	45,000	50,000
Rent, Rates, Light, etc. ...	—	3,583	2,766	3,123	3,600	4,000
Postage, Telegrams and Tele- phones.	101	604	928	962	900	1,000
Stationery, Furniture, &c. ...	1,732	3,784	5,129	4,599	5,500	6,000
Travelling and Incidental Expenses.	829	5,233	6,757	6,341	6,000	9,000
Research and Marketing :—						
(i) Grants administered by Govt. Depts.	11,079	41,085	96,773	113,151	247,373	171,369
Do. do. (Agency)...	—	28,426	68,315	45,156	60,903	20,000
(ii) Grants made direct from Empire Marketing Fund.	19,629	51,768	66,531	95,788	151,000	207,766
(iii) Provision for further schemes.	—	—	—	—	16,724	25,865
Publicity by the Empire Mar- keting Board :—						
(i) Exhibitions, Fairs and Shopping Weeks.	18,884	42,263	61,786	33,724	45,000	29,000
(ii) Press Campaign ...	46,911	77,200	106,066	59,401	90,000	5,000
(iii) Poster Campaign ...	23,597	103,885	92,714	57,040	72,000	43,000
(iv) Cinema Activities ...	—	5,768	2,055	16,641	25,000	20,000
(v) Lectures ...	—	8,117	10,545	10,403	5,000	1,500
(vi) Miscellaneous (Special Publicity).	450	892	5,248	8,002	10,000	6,500
Publicity for Home Agriculture by Government Departments.	—	—	—	—	62,500	59,000
Unallocated ...	—	—	—	—	16,000	—
TOTAL ...	£ 134,804	403,879	561,493	483,330	862,500	659,000

342. After giving careful consideration to the work of the Board we feel bound to recommend its abolition. As far as grants for home purposes are concerned, the objections we have already raised to the existence of a separate Development Fund apply with even greater force to the present Fund, because it fulfils no useful restraining or co-ordinating purpose. Rather does it lead in many cases, in our opinion, to a measure of Government assistance being granted to a service through two, sometimes three, different channels greater than would be accorded if the whole were set out on a single Vote. But apart from this, we regard the continuance of the Board as unjustifiable in existing financial circumstances. In so far as any of its activities involve definite commitments or are such as to justify continued State assistance for the benefit of home industries they should be provided for on the Vote of the appropriate department. We estimate that the abolition of the Board will involve a saving of about £400,000 in 1932 additional to the savings already allowed for on the gross expenditure of the two departments of agriculture.

11. COLONIAL DEVELOPMENT FUND.

343. The Fund was established under the Colonial Development Act, 1929, to enable advances to be made from the Imperial Exchequer to develop agriculture and industry in non-self governing Colonies and Mandated Territories and thereby to promote commerce with or industry in the United Kingdom. Advances from the Fund are made to the Governments of the territories concerned by the Treasury with the concurrence of the Secretary of State for the Colonies (or the Secretary of State for Dominion Affairs in certain cases), and on the recommendation of an Advisory Committee. The advances may take the form of loans and grants and may be applied by the Government to which they are made either directly or through any person or body of persons.

344. The Fund is fed from moneys voted by Parliament, which must not exceed £1,000,000 in any one year. All sums received by way of interest on, or repayment of, advances made by way of loan from the Fund are to be paid into the Exchequer, and not into the Fund. The sum of £750,000 was voted for 1930-1. For 1931-2 Parliament is being asked to vote £750,000 which, with the estimated unexpended balance of the £750,000 voted for 1930-1 was calculated to permit of advances from the Fund up to a total of £1,000,000 in the year ending 31st March, 1932.

345. Up to 31st March, 1931, the Committee had recommended assistance towards various schemes totalling £2,904,374, spread over a period of years. Of this sum, £989,935 represents free grants of capital, £1,084,909 direct loans from the Fund, and £829,530 free grants of interest upon moneys borrowed by Colonial Governments to meet expenditure on approved schemes. According to the preliminary estimates furnished by Colonial Governments when submitting their applications the total assistance recommended, £2,904,374, would have been distributed as follows:—

	£		£		£
1930 ...	934,506	1933 ...	443,743	1936 ...	42,600
1931 ...	675,065	1934 ...	103,639	1937 ...	34,000
1932 ...	562,620	1935 ...	48,200	1938 ...	10,000

There has, however, been a considerable postponement of expenditure from 1930-1 to 1931-2 and the amounts likely to be called for in respect of schemes already approved will tend to be increased except in so far as savings may be found possible on the original estimates. We understand that in the absence of any new decision of policy the liability for 1932 and subsequent years is likely to reach the limit of £1,000,000.

346. On reviewing the schemes which have so far been assisted we find that in a fair number of them the element of benefit to the trade and industry of this country which is an essential condition of advances under the Act, is somewhat remote. Under existing

financial conditions this country cannot afford to adopt a policy of mere subsidy by relieving the local government of its obligation to provide a decent and reasonable standard of administration in the matter of public health, housing, transport, etc., nor yet a policy of developments which will bring no appreciable benefit to this country for a long time ahead. We recommend that the grant to the Fund be limited to £750,000 p.a. in future and that the schemes to be aided therefrom should be those that will give the greatest and speediest benefit to this country in the near future. This will effect a saving of £250,000 per annum.

12. COLONIAL AND MIDDLE EASTERN SERVICES.

347. The services provided for in this Vote fall into two main groups.

I.—Grants for Colonial Services.

1. Grants in Aid of Local Revenues, etc.

	£	£
Cyprus	92,800	
Nyasaland	119,500	
Somaliland	91,000	
St. Helena	7,000	
Dominica	40,045	
St. Lucia	5,000	
Antigua	6,000	
British Guiana	80,000	
	<hr/>	441,345
2. Unemployment Grants to West Indies		166,000
3. Miscellaneous		90,741
Total Colonial Services		<hr/> 698,086

II.—Middle Eastern Services.

	£	£
<i>Iraq</i>		
Defence	224,000	
High Commissioner, etc.	49,150	
Grant to Iraq Army	61,000	
Maintenance of Iraq Levies	189,000	
	<hr/>	523,150
<i>Palestine and Trans Jordan</i>		
Defence	173,250	
Grant for Frontier Force	141,000	
Trans Jordan Administration	92,500	
	<hr/>	406,750
<i>Arabia</i>		
Aden		60,000
Telegrams		4,000
		<hr/> 993,900
Total Middle Eastern Services		993,900
Grand Total		<hr/> 1,691,986

		£
Appropriations in Aid		
Contribution by Palestine Government towards Defence	55,000	
Contribution of India towards expenditure in Aden	13,500	
Other receipts in Aden ...	12,770	
	81,270	
Net Total		1,610,716

348. We have included this Vote in the present chapter because it should in our opinion be looked at primarily from the point of view of development though we recognise that as regards Middle Eastern Services the dominant consideration at the moment is Empire Defence. There has at times in the past been a tendency to call on the British tax-payer to help other parts of the Empire in their difficulties irrespective of any return to this country. Now this country itself is facing serious difficulties and we feel that a much stronger case is required to justify subsidies.

349. We are informed that the economic position of British Guiana and of the West Indian Islands now in receipt of grants is being examined locally by financial Missions. A similar Mission has lately visited Palestine and all opportunities for local economies are being explored in Somaliland and Aden. Pending receipt of the reports of these various enquiries we make no recommendation in respect of these grants beyond stressing the need of this country for the maximum possible relief from its burdens. As regards Cyprus and St. Helena we are satisfied that no reduction of the present subsidy is practicable. It is hoped that the financial position of Nyasaland will have improved sufficiently by 1934 to permit of a reconsideration of present arrangements. Our liabilities in the Middle East—as already stated—are dominated by considerations of Empire defence. Some reduction may be expected in Iraq when she is admitted to the League of Nations and the recent treaty with this country comes into force.

350. The expenditure falling on the British taxpayer in the past has been enormous and we trust that no further engagements will be entered into involving this country in additional financial commitments in the Middle East.

351. The world depression naturally bears with particular severity on colonies which depend mainly on primary products and have not been able to build up reserves large enough to carry them through a long crisis; and we are concerned lest it should be found necessary to ask the British Exchequer to come to the rescue of

other administrations besides those already in receipt of assistance from this vote. We are glad to learn that the Colonial Office are keeping in close touch with the Treasury in all cases where there might be a risk of this happening if the depression should continue; and we feel sure that in such cases the responsible authorities will not hesitate to take all possible steps to economize before it is too late.

13. UNEMPLOYMENT GRANTS COMMITTEE.

352. The Unemployment Grants Committee was originally appointed by Treasury Minute of 20th December, 1920, to make grants towards works of public utility carried out by local authorities other than road and housing schemes. The Committee were to select the schemes to be assisted and the amount of help to be given within a maximum of 30 per cent. of the wages of additional men taken on for the work and a total limit of grant of £3,000,000. In January, 1921, the maximum rate of grant was raised to 60 per cent. of wages and the Committee were allowed to assist roads not receiving grants from the Road Fund.

In October, 1921, the Committee was invited to undertake the administration of a new scheme for the relief of unemployment. Financial assistance was to be given by the State to authorities putting in hand or accelerating works of public utility for the relief of unemployment on the following basis :—

(a) In the case of non-revenue producing works, grants equivalent to 65 per cent. of the interest and sinking fund charges on loans raised to meet expenditure on approved schemes for a period of half the term of the loan, subject to a maximum period of 15 years' grant.

(b) In the case of revenue producing works, grants equivalent to 50 per cent. of the interest for five years on loans raised to meet expenditure on approved schemes.

Both categories of grants were conditional on the work commencing before the 1st January, 1922, and being completed before the 31st March, 1923.

An additional condition was attached to these further schemes under which a reduced rate of wage of 75 per cent. of the Local Authority's rate for unskilled labour should be paid to unskilled men where the Local Authority carried out the work by direct labour.

The previous scheme of grants of 60 per cent. of wages was continued for works financed out of revenue.

Since October, 1922, these conditions of grant and both time and money limits have been revised on many occasions and almost

every revision has resulted in their being made more generous. In December, 1925, in connection with the review of expenditure then being made by a Cabinet Committee it was decided to limit the scheme to areas with heavy unemployment and to exclude all roads from the purview of the Committee, but in January, 1929, these limits were again removed in an attempt to effect the transference of surplus labour from the depressed areas.

353. It is unnecessary for us to set out all the changes in rates and conditions of grant that have taken place in the past 10 years. The story is one of recurrent pressure from the central government on local authorities to put in hand works of a capital character with offers of ever increasing grants and easier conditions. The present rates of grant are as follows :—

A.—Schemes of Work Financed by Way of Loan.

Non-Revenue producing Schemes.

Seventy-five per cent. of the interest and sinking fund charges on any loan raised to meet approved expenditure for the first half (up to 15 years) of the loan period, and 37½ per cent. of interest and sinking fund charges for the remainder (up to 15 years) of the loan period.

Revenue Producing Schemes.

(i) Normal Grant.

Fifty per cent. of the interest on any loan raised to meet approved expenditure for 15 years or for the period of the loan, whichever is the shorter, or, if the Authority prefers, 100 per cent. of the interest for five years or for one-third of the period of the loan whichever is the shorter.

(ii) Special Grants for Works exceeding £100,000 and requiring more than 18 months.

One hundred per cent. of the interest during construction on any loans raised as required to meet approved expenditure, and 50 per cent. of the interest after that date for the remainder of a period not exceeding 15 years in all in respect of each loan.

(iii) Special Grants for selected schemes for Rural Water Supply, Public Baths, &c.

One hundred per cent. of the interest for the first seven years of the period of the loan and 50 per cent. of the interest for the remainder of the period or eight years whichever is the shorter.

B.—Schemes of Work financed otherwise than by way of Loan.

(i) In areas where the average monthly rate of unemployment among adult males during the 12 months ended 31st March, 1931, exceeded 15 per cent., 90 per cent. of the wages of the unemployed men taken on for the work.

(ii) In other areas, the rate of grant will be 75 per cent. of the wages of the unemployed men taken on for the work.

354. The total estimated cost of the schemes approved by the Committee since 1920 now amounts to £187,000,000. In many cases the State liability for grant has already been discharged in whole or in part either by payment of a lump sum or by the annual contribution to loan charges. At 30th June, 1931, the estimated capital value of the State liabilities was nearly £40,000,000 for schemes charged on the Relief of Unemployment Vote in addition to about £5,000,000 for road schemes transferred to the Road Fund. The annual payment now being made in respect of the former by the Ministry of Labour is £3,000,000 and that from the Road Fund, £740,000. The Ministry of Labour charge in respect only of schemes approved up to 31st March, 1931, is estimated to increase to £3,690,000 in 1932, £3,890,000 in 1933, £3,850,000 in 1934, £3,880,000 in 1935, £3,870,000 in 1936; and then gradually to decline to £2,690,000 in 1940, £1,600,000 in 1945, £640,000 in 1950, £370,000 in 1960.

But these figures take no account of any liabilities incurred since last March. At 31st March the Unemployment Grants Committee had 1,014 schemes to the estimated value of about £16,000,000 under consideration and local authorities had just been invited to submit further schemes to be put in hand next winter. Since 31st March 464 schemes at an estimated cost of roughly £7,000,000 have been approved and 996 schemes estimated to cost some £16,000,000 are now under consideration.

355. The circular of March last expressed the desire of the Government "that there shall be no departure from the present policy that the works shall be fully justified on grounds of public utility and economic development apart from their value as relief works and shall show substantial acceleration." To take first the latter stipulation—of substantial acceleration—we cannot but reach the conclusion that after 10 years of working this scheme has largely resolved itself into giving grants—now of large amount—to local authorities and others to carry out their normal responsibilities. If works appropriate to 1933 are carried out in 1931, those appropriate to 1934 in 1932 and so on, the whole scheme becomes a mere grant in aid of capital expenditure by local authorities without many of the limitations usually attached to Government grants.

356. How far the works are justifiable on grounds of public utility and economic development apart from the value of relief works is a difficult question to answer. We append a statement as to the

nature of the schemes approved between 1st June, 1929, and 31st March, 1931 :—

Class of Scheme.	No.	Amount.	Approximate Present Value of Exchequer Grant.
		£	£
Docks	54	6,256,000	1,914,000
Water	496	7,325,000	2,200,000
Electricity	164	13,279,000	4,032,000
Gas	97	1,039,000	291,000
Sewerage	839	20,002,000	9,848,000
Land Development, Drainage and Reclamation.	132	1,997,000	899,000
Sea defence	56	1,472,000	853,000
Roads	1,077	8,851,000	5,313,000
Parks	565	2,527,000	1,317,000
Civic Buildings	57	2,535,000	1,100,000
Sanitation	45	666,000	399,000
Baths	53	1,228,000	354,000
River Improvement	55	1,497,000	914,000
Cemeteries	21	115,000	49,000
Trams	5	69,000	18,000
Miscellaneous	—	48,000	29,000
Totals	3,716	£68,906,000	£29,530,000

357. The total for electricity schemes was exceptionally increased by two schemes of the Central Electricity Board for the standardisation of frequency (£9,000,000) and the extension of the " Grid " (£1,000,000) in the North East Coast area. Apart from these two schemes one half of the whole is in respect of sewerage and road schemes. The value of this expenditure depends on the date at which the new works will be needed, but looking at the large amount of similar expenditure in previous years and the fact that a State grant worth over 60 per cent. of the capital cost had to be offered before these schemes came forward, we are inclined to regard much of the expenditure as unwise in that it has been incurred considerably in advance of requirements. Many of the other items in the table clearly represent amenity developments and the fact that they also have not been put forward earlier suggests that they do not rank very high as amenities.

358. We cannot endorse a policy of great expenditure on capital works, irrespective of their economic value, as a means of providing work. It is too expensive. On the usual calculation of 4,000 man years of labour, direct or indirect for £1,000,000 expenditure it costs £250 to keep a man in work for one year. The saving on maintenance of the man is usually put at about £60 a year. Thus, proceeding on this basis, unless the man's work is worth at least

£190 to the nation when it is done, the nation loses economically by carrying it out.

How is compliance with this condition to be secured? It is difficult for the Unemployment Grants Committee even with the aid of Government Departments to select suitable schemes for assistance. If waste is to be avoided the authorities directly concerned should themselves weigh up the merits of a scheme against its total cost and in order to secure this effectively the Government grant should not exceed the saving in the cost of maintenance of the men who find work directly or indirectly under the scheme. This may be interpreted in practice as limiting the Government grant in each case to not more than 25 per cent. of the cost and we recommend that this course be adopted as regards all schemes to which the Government has not already definitely promised grants on a more generous basis. As far as is practicable the grant in respect of revenue producing undertakings even within this limit, should not be allowed to exceed the extra cost to the undertaking of putting capital works in hand in advance of the normal date.

359. We recommend also that the Committee in future should not make grants towards road and bridge improvements. These are the concern of the Ministry of Transport and it is undesirable to have two Departments making grants for the same purpose.

14. DEVELOPMENT (PUBLIC UTILITY) ADVISORY COMMITTEE.

360. This Committee was constituted in 1929 under Part I of the Development (Loan Guarantees and Grants) Act, 1929. Part II of the same Act gave statutory recognition to the Unemployment Grants Committee (referred to in the preceding section). The latter Committee had been able since 1923 to make grants to Public Utility Undertakings carrying on the same class of work as local authorities subject to certain conditions as to limitation of dividends during the time that loans or advances from the Government were in operation. Under the Act of 1929 the responsibility for recommending grants to Public Utility Undertakings carried on for profit was assigned to a new Committee appointed by the Treasury.

361. Assistance under Part I of the Act may take one of two forms, viz. :—

(i) Guarantees may be given in respect of the principle and/or interest of loans raised and applied for the purpose of meeting capital expenditure on the schemes eligible. Any payments that may have to be made in fulfilment of such guarantees will be met from the Consolidated Fund.

(ii) The interest on such loans may be defrayed in whole or in part for a period not exceeding 15 years; in cases where the

capital expenditure is met from revenue or accumulated funds assistance may be granted as if a loan had been raised at such rate of interest as the Treasury may determine.

362. Instructions were issued for the guidance of the Advisory Committee by Treasury Minute of 11th September, 1929, (published in the Appendix to Command Paper 3449 of 1929). The main purport of these instructions is that assistance is only to be given to schemes that would not otherwise be undertaken in the near future and that regard is to be had to the value of the schemes as economic development as well as to their employment value. Provisions are also included with regard to the use of British materials on assisted schemes and regulations with regard to the labour engaged.

363. The following table shows the schemes approved for grant on the recommendation of the Advisory Committee up to the 30th June, 1931. The interest grants are at varying rates not exceeding 5 per cent. and for various periods not exceeding 15 years. There is no uniform scale of grants: such grant is recommended as appears appropriate for each work, regard being paid to the estimated additional net charge on the undertaking involved in the acceleration of the scheme. Column 3 gives the present value of these grants, and column 4 states the percentage of the estimated total cost of the scheme represented by the present value of the grants.

Position as at 30th June, 1931, in respect of " Grant Schemes ".

Nature of Undertaking.	Total Estimated Cost of Scheme.	Present Value of Exchequer Grant.	
		Amount.	Percentage of Total Estimated Cost.
	£	£	Per cent.
Railways (excluding Docks) ...	22,541,623	5,239,473	23
Docks (including Railway owned Docks)*	9,066,382	2,280,640	25
Water Companies	860,321	249,833	29
Gas Companies	1,501,045	255,714	17
Electricity	700,931	66,807	10
Canals	455,000	129,526	28
Total£	35,125,302	8,221,993	23

* This figure includes a sum of £1,350,000 for certain Dock schemes which are now understood to be subject to reconsideration.

In addition to the grant schemes set out above it has been agreed to guarantee under Part 1 of the Act a loan of £206,000 for expenditure on an electricity scheme estimated to cost £236,000. The total estimated cost of the electricity schemes approved under Part 1 of the Act is therefore £936,931 and the total for schemes of all classes £35,361,302.

364. It will be observed that except in the case of Water Schemes the grants recommended by the Committee have not on the average exceeded the proportion of 25 per cent. we have recommended as the level for the Committee operating under Part II of the Act. We recommend that that limit should apply also to each scheme assisted by this Committee. It is already the practice of the Committee to have regard to the extra cost falling upon an undertaking by reason of its proceeding with a scheme in advance of the normal date and we recommend that in this case also that limit to the grant be strictly applied as far as is practicable.

CHAPTER VI.

SOCIAL SERVICES.

365. The general review given in our opening chapter of the increase of Government expenditure since 1924 showed that of the total increases on various heads likely to reach about £130,000,000 this year, about £80,000,000 could be ascribed to developments of social services, including both those administered by the Government and those under the direct control of local authorities. As regards the latter class, the State contribution represents only a part of the cost and for a complete picture it would be necessary to look also at the accounts of local authorities. Indeed, as regards some social services a large part is played also by private effort.

But even if we restrict our attention to public charges we are met with the difficulty of demarcation. No clear definition of the category of social services has ever been laid down and we doubt whether it is possible in this matter to do more than give comparative costs of selected services as has in fact been done for some years past in the Annual Parliamentary Return headed "Public Social Services."

366. That return includes War Pensions, but this service differs so much in origin and character from the general class of social services that we have excluded it from this chapter and deal with it in Chapter VII. Excluding War Pensions, the latest issue of this Return shows that even up to 1929 (or, in a few cases, a previous year) the total cost, so far as it comes within the purview of the Government or of local authorities, of the leading social

services had increased as follows from 1911. (We omit two obsolescent items of negligible amount in the published Return, viz., the Inebriates Acts and the Unemployed Workmen Act) :—

Service.	Total Expenditure in Great Britain.	
	1911.	1929.
	£	£
Unemployment Insurance	—	53,848,000
National Health Insurance	—	39,895,000
Widows', Orphans' and Old Age Contributory Pensions.	—	23,827,000
Old Age Pensions (non-contributory)	7,360,000	34,914,000
Education	33,489,000	97,028,000
Reformatory and Industrial Schools	690,000	738,000
Hospitals and treatment of disease	2,231,000	8,470,000
Maternity and Child Welfare	not ascertainable	2,498,000
Housing	888,000	31,642,000
Poor Relief	16,158,000	43,936,000
Lunacy and Mental Deficiency	2,105,000	4,981,000
	£	
	62,921,000	341,777,000

367. These figures relate to the total cost of the services as far as it is known : it is instructive to see to what extent that cost was met (1) by the Exchequer, (2) by local rates and (3) by other receipts, e.g., insurance contributions mainly by the beneficiaries or their employers, rents, fees, endowments, etc., respectively in 1911 and 1929 :—

Receipts.

Service.	From Exchequer.		From Local Rates.		Receipts from Contributions, rents, fees, etc.	
	1911.	1929.	1911.	1929.	1911.	1929.
	£	£	£	£	£	£
Unemployment Insurance	—	12,011,000	—	—	—	41,823,000
National Health Insurance	—	7,630,000	—	—	—	31,682,000
Widows', Orphans' and Old Age Contribu- tory Pensions.	—	4,000,000	—	—	—	23,299,000
Old Age Pensions (non-contributory) ...	7,360,000	34,914,000	—	—	—	—
Education	17,688,000	48,152,000	14,149,000	40,863,000	1,652,000	8,013,000
Reformatory and Industrial Schools ...	309,000	324,000	217,000	325,000	56,000	89,000
Hospitals and Treatment of Disease ...	47,000	2,717,000	2,055,000	5,279,000	129,000	474,000
Maternity and Child Welfare	—	1,021,000	—	1,059,000	—	418,000
Housing	5,000	11,393,000	259,000	2,897,000	624,000	17,352,000
Poor Relief	2,561,000	3,502,000	12,782,000	37,989,000	835,000	3,174,000
Lunacy and Mental Deficiency	362,000	1,179,000	1,372,000	2,440,000	371,000	1,362,000
Totals	28,332,000	126,843,000	30,814,000	90,852,000	3,667,000	127,686,000

368. Thus between 1911 and 1929 the total cost of these services grew to more than five times its former figure, the charge on rates was trebled, and the charge on the Exchequer was multiplied four and a half times. It is, however, satisfactory to note how very great has been the extension in this period of the policy of requiring contributions towards the cost of social services from those who benefit from them, directly or indirectly.

Since 1929 there has been a further increase of roughly £70,000,000 in the gross cost of unemployment insurance and a steady growth of most of the other items in the table, and it is roughly correct to say that the above services in the current year are costing the country in one form or another about seven times what they cost in 1911. An increase of this charge on the country's productive capacity would have been a serious matter, notwithstanding the change in the value of money, had our trade continued to develop as in the years immediately prior to the war. Under the difficult conditions of the post war period, the increase of burden has been a grave handicap, and we cannot shut our eyes to the fact that the enormous increase in the Exchequer charge for these services has been the prime cause of the present crisis in the national finances.

369. Had it been possible to make sufficient reductions in other fields of expenditure we would gladly have been content with comparatively minor adjustments in this field. No such alternative is open and we cannot escape the conclusion that, under existing conditions and bearing in mind the rapid downward tendency in the price level with its inevitable reactions on the cost of living and wages, the rapid growth of this expenditure should be stopped and a large reduction made in the existing charge on the Exchequer.

I.—UNEMPLOYMENT INSURANCE.

370. The whole question of the Unemployment Insurance Scheme is at present being considered separately by a Royal Commission. Nevertheless, we have felt bound to include the financial aspects of the matter within the scope of our enquiry in view of their outstanding importance to the National Exchequer. That Commission has recently issued an interim report setting out the main financial features of the present scheme and dealing with the more urgent aspects of their enquiry.

371. Under existing conditions, the cost of the Unemployment Insurance Scheme in 1932 is estimated (on the basis of a live register of 2,500,000) at £119,000,000, made up as follows:—

	£
Insurance Scheme	84,000,000
Transitional Benefit Scheme	35,000,000
	<hr/>
Total ...	£119,000,000
	<hr/>

372. We are in entire agreement with the majority of the Commission that " borrowing on behalf of the Fund should as nearly as possible cease and that the liabilities, as such, should be restricted to those which can substantially be met from its current income," and we agree also that for this purpose an average level of unemployment of 2,500,000 may be assumed. We have already indicated in the earlier part of this report our considered opinion that it would be unwise for this country to count on any substantial improvement in its financial and economic position for some time to come.

373. The Commission recommend alterations in the existing scheme which on the basis of a live register of 2,500,000 are estimated to have the following financial effect :—

<i>The Insurance Scheme</i> (excluding transitional benefit).		<i>Financial effect.</i>
		£
1. Increase of contributions (in the case of men* to 9d. a week for the man, employer and the Exchequer)		9,000,000
2. Reduction of benefits by 11.7 per cent. on the average		8,700,000
3. Special provisions for particular classes, reducing the cost by about 7½ per cent.		5,000,000
4. Limitation of benefit to 26 weeks in a period of 12 months, representing an estimated saving of 15 per cent.		9,100,000
		<u>31,800,000</u>
Thus reducing the deficit in a full year from ...		<u>39,450,000</u>
to		<u>£7,650,000</u>
<i>Transitional Benefit</i>		£
Estimated cost for a full year		35,000,000
Addition, due to 26 weeks' limit, (4) above		9,100,000
		<u>44,100,000</u>
		£
5. Reduction of benefits	3,700,000	
6. Amendment of qualifying contribution conditions	3,300,000	
7. New conditions as to need in certain cases	3,100,000	
		<u>10,100,000</u>
Reduced cost of transitional benefit		<u>£34,000,000</u>

* For women, young persons and children proportionately lower rates of contributions would be payable. To avoid complication reference is made only to the men's rate in this report.

374. On this basis while the estimated rate of borrowing is reduced from £39,450,000 per annum to £7,650,000 per annum, the direct Exchequer charge given in the original estimates for 1931 as £45,000,000 is increased to:—

	£
Contribution to Insurance benefit	18,000,000
Cost of transitional benefit	34,000,000
	<hr/>
Total	£52,000,000
	<hr/>

375. We approach this question from a somewhat different angle from the Royal Commission and in the course of our inquiry we have probably obtained a fuller appreciation of the grave difficulties confronting the Exchequer. After giving full consideration to the views of the Commission we regret that we cannot regard their recommendations as adequate to meet the situation. In our view a large reduction in the present Exchequer charge, as well as the practical elimination of borrowing for this service, are essential, and looking at the matter in the light of our other recommendations we are of opinion that these objects might reasonably be achieved on some such lines as the following. We give these general indications of our views in order to show that we are fully alive to the seriousness of the issues involved, and to the extent of the sacrifices that are necessary to achieve the object we have in view. Their elaboration into a proper scheme would necessarily involve us in detailed investigations which the Royal Commission is far better able to undertake.

The Insurance Scheme.

376. The estimated cost of the Insurance Scheme proper in 1932-3 is made up as follows:—

	£
Benefit	74,500,000
Administration	5,000,000
Interest on debt	4,500,000
	<hr/>
	£84,000,000
	<hr/>

Towards this expenditure of £84,000,000 and the further payments amounting to £35,000,000 under the transitional benefit scheme the beneficiaries are at present contributing at the rate of about

£14,000,000 per annum or only 12 per cent. Under the recommendations of the Commission the expenditure on the Insurance Scheme is reduced to £61,200,000, and the income is increased to £53,550,000.

377. While we concur in the proposed limit of 26 weeks on benefit, we have come reluctantly to the conclusion that on each of the other heads further action is necessary. Dealing first with expenditure, it is not generally realised how greatly the benefits under the scheme have improved in recent years. The original rate under the Act of 1911 was 7s. a week for men and women alike and on the extension of the scheme in 1920 this was increased to 15s. for men and 12s. for women. No special provision was at that time made for dependents. In November, 1921, when dependents were first admitted to benefit, the total benefit for a family of four (man, wife and two children) was raised to 22s. a week. In 1925 it was raised to 27s.; in 1928 to 28s. and in March, 1930, to 30s. The present equivalent in purchasing power (on the basis of the Ministry of Labour index of the cost of living) of the rates of benefit paid in previous years is shown in the following table:—

Year in which rates have been fixed.	Actual rate of benefit then fixed.	Rate of benefit now required to give the same purchasing power.
	s. d.	s. d.
1911	7 0	10 6
1920	15 0	8 10
1922	22 0	14 4
1925	27 0	22 7
1928	28 0	24 10
1930	30 0	27 11

. Thus a rate of benefit of 14s. 4d. a week at the present time would have the same purchasing power in terms of commodities as the benefit of 22s. a week actually paid in 1922.

In the light of these figures we do not regard an average reduction, during the continuance of existing conditions, of 20 per cent., i.e., for the above typical case from 30s. to 24s. a week, as excessive. On this basis the benefit would be worth more than the benefit deemed suitable in 1925 and only 10d. a week less than that paid as recently as 1928.

378. The adjustment of benefit conditions raises many intricate questions which it is not necessary for present purposes for us to pursue beyond saying that a reduction of 10 per cent. might be made by the application of special provisions to classes of beneficiaries who are at present making unfair demands upon the Fund.

379. The effect of these adjustments on the expenditure of the Insurance Scheme would be as follows:—

	£
Cost of benefit on existing basis	74,500,000
Reduction of 20 per cent. in the average rate of benefit	14,900,000
	<hr/>
	59,600,000
Reduction of 10 per cent. by new regulations as to beneficiaries	6,000,000
	<hr/>
	53,600,000
Limitation of benefit to 26 weeks (15 per cent.)	8,000,000
	<hr/>
	45,600,000
Interest on debt	4,500,000
Administration (say)	4,500,000
	<hr/>
Total expenditure on Insurance Scheme ...	£54,600,000

Before discussing the method of meeting this expenditure it will be convenient to deal with the scheme of transitional benefit.

Transitional Benefit Scheme.

380. The Royal Commission submit interim recommendations in regard to this scheme which have the effect of bringing the cost (which would be increased from £35,000,000 to £44,100,000 by the operation of the 26 weeks limit in benefit) down to £34,000,000. **These recommendations include the introduction of a condition as to need in regard to certain special categories. We are, however, of the opinion that this condition should apply to all applicants for benefit who have exhausted their insurance rights.**

381. Government Departments have not the machinery for inquiring into personal circumstances and to set up special machinery for this purpose would be a wasteful duplication of the reconstructed machinery now operating under the County and County Borough Councils as Public Assistance Authorities. At the same time we recognise the strength of the feeling against any immediate outward and visible differentiation against those who have fallen out of insurance. Subject to the assessment of need by the public assistance authority we suggest that it might be possible, in the case of an intermediate class of persons who are still suitable for employment to arrange for any necessary allowances to be paid by the Employment Exchanges as agents for the local authority.

382. A considerable measure of State assistance to local authorities would at the same time be needed if an oppressive increase of burden is not to fall on the rates in many areas. Under existing

arrangements local authorities have received an extensive relief, not contemplated when the great increase of Exchequer contributions to local authorities was granted under the Local Government Acts of 1929, and in areas with very light unemployment we see no need for attaching any State grant to the arrangements now suggested. But assistance on a scale rapidly rising with the degree of local unemployment will be necessary in other areas and we suggest that in order to leave financial responsibility with the local authorities it should take the form of a capitation grant for persons transferred to the public assistance authorities, to be continued for such period as they are qualified to remain in the intermediate class. The capitation payment might be on a scale which had due regard to the percentage of persons in this category to the local population. We consider that these grants to the local authorities should be charged on the Insurance Fund and that the whole cost of maintaining the fund in solvency should be borne in equal shares by the employer, the employed and the Exchequer. This arrangement, while providing an equitable division of the burden, would serve incidentally to maintain some further connection for persons in this intermediate grade with the Insurance Scheme. On the best information we have been able to obtain, the imposition of a needs test under efficient local administration would probably reduce the cost of benefit to the present transitional benefit class to approximately one-half the present cost. On this basis it would be reasonable to fix the scale of capitation payments to the local authorities to cost about £12,000,000, thus bringing the total cost of both schemes up to £66,600,000. Dividing this among the three parties would involve a weekly contribution (in the case of men) of 11d. each by the State, the employer and the employed person.

The Extension of the Scheme.

383. While we entertain no doubt that in the present difficult world conditions an increase of contributions even to this extent would be less damaging to the national interests, considered as a whole, than an increase of general taxation, we are anxious if possible not to raise contributions above 10d. which was the amount paid by employers prior to 1925. Two alternatives are open :—

- (1) to allow borrowing ;
- (2) to extend the area of contribution.

384. Contributions on the 10d. scale for all three parties would produce roughly £60,000,000 leaving some £6,000,000 or £7,000,000 to be borrowed with the live register as high as 2,500,000. We should prefer to reserve any borrowing against the contingency of unemployment rising above this level for any considerable period, and we turn therefore to the possibility of strengthening the scheme by bringing within it a wider field of steady employment hitherto excluded.

385. There are three directions in which extension is possible to the advantage of the Fund :—

(a) by bringing back within the ordinary operation of the scheme the Banking industry and the Insurance industry which were allowed to contract out of the main scheme under special schemes made under section 18 of the Unemployment Insurance Act 1920. This power to make special schemes was suspended in 1924 and abolished in 1927 without prejudice, however, to the position of those who had previously contracted out of the main scheme ;

(b) by bringing within the scheme certain classes of workers who have hitherto been specially excepted as not being subject in any serious degree to the risk of unemployment, e.g., State and municipal workers (including school teachers), employees of public utility companies, especially the railways ;

(c) by raising the income limit for the inclusion of non-manual workers from £250 per annum to say £350 or £400 per annum.

The main ground for the inclusion of persons in the first two categories is that they are themselves largely immune from the risks of unemployment and should come to the help of their less fortunate fellows. The same argument would normally apply also to persons in receipt of an income above the present limit, for non-manual workers, of £250 per annum. We must not, however, lose sight of the fact that one-third of the whole cost of the scheme is being borne by the Exchequer and that the main ground of principle for this charge is that it brings to the assistance of workers who are subject to unemployment a large measure of assistance—far larger than would be represented by weekly contributions at the flat rate—from the more fortunately placed body of direct taxpayers. The average married man does not, however, make any appreciable contribution to direct taxation until his income reaches £350 or £400 per annum, and it would not be unreasonable that the exemption limit should be raised to this figure. There appears to us, therefore, to be a good *prima facie* case for bringing within the ordinary scheme all the three classes of persons referred to above.

386. There is little information on which to base any sort of estimate of the effect of such extensions and we give figures with all reserve. Such information as there is leads us to think that contributions by the State, employer, and employed at the rate of 10d. would produce about £7,500,000 per annum while the cost of benefits and administration might be put at £1,500,000 to £2,000,000. On this basis the total expenditure of our combined scheme would be raised to, say

and the total revenue with contributions 10d.	...	...	...	...	...	£68,500,000
(men) to	...	...	...	...	...	£67,500,000
leaving a deficiency of	...	...	...	...	...	£1,000,000

The Government contribution would be one-third of the total contributions, viz., £22,500,000.

387. The Exchequer charge for 1932 would thus be reduced:—

	from £	to £	Reduction. £
Budget charge ...	50,000,000	22,500,000	27,500,000
Loan charge ...	40,000,000	1,000,000	39,000,000
Total ...	£90,000,000	£23,500,000	£66,500,000

388. We regret very much that it should be necessary at a time like this to increase the burden on industry, even to the limited extent we suggest, but after giving the matter most careful thought we have been unable to find any practicable alternative open to less serious objections. Even as we have presented it, the scheme barely balances on the basis of 2,500,000 unemployed and with the prospect of a material excess over this figure during the next few months, we should be sorry to see the scheme carried on without any strengthening on the revenue side. Yet if the contributions of employers are left unaltered it will be very difficult to increase those of the workers alone, while as regards the Exchequer any excess over the one third ratio, while departing from a basis of division hitherto accepted as fair, would expose the Exchequer to charges which it cannot bear. To leave all the rates of contributions unchanged would reduce our estimated revenue by no less than £17,000,000 per annum, and we must dismiss this possibility as fundamentally unsound.

389. It is not that we regard the extra 2d. on employers as a serious charge in itself; it represents a very small fraction on the cost of production: it is rather the psychological effect of any addition to existing burdens at this moment. On this point, however, we would make this—to our minds very relevant—observation. No small part of the present financial difficulties of the Exchequer is to be attributed to the extensive rating relief granted to industry under the Local Government Acts, 1929. That relief is costing the Exchequer £26,000,000 per annum, whereas the additional 2d. a week represents over the whole field of contributions—extended as we suggest—only £4,500,000. As the charge of £4,500,000 is spread over a much wider field of employment than the relief of £26,000,000 it is clear that the amount of the extra charge falling on productive industry will be considerably less on the average than one-sixth of the rating relief that it is enjoying. And it should be borne in mind that the rating relief is permanent, whereas we trust that the increase in unemployment insurance contributions will be temporary.

390. We repeat the recommendation in our opening chapter that borrowing for the Unemployment Insurance Scheme should be discontinued after this year. This means that any deficit on the Scheme (including the cost of transitional benefit) would have to be made good by the Exchequer i.e. until the existing debt of the Fund had been substantially reduced.

2.—NATIONAL HEALTH INSURANCE.

391. The sums payable to the National Health Insurance Funds from the Exchequer represent mainly the statutory Exchequer proportion of the expenditure on medical, sickness disablement, maternity, and additional benefits, and expenses of administration under the National Insurance Acts, this proportion being fixed in the National Health Insurance Acts, 1924-28.

The total expenditure in Great Britain in the year 1930 out of National Health Insurance Funds was approximately as follows :—

	£
Sickness and Disablement Benefits	16,800,000
Maternity Benefit	1,750,000
Medical Benefit	10,500,000
Additional Non-cash Benefits	3,000,000
	£32,050,000
Approved Societies and Insurance Com- mittees Administration expenses	4,400,000
	£36,450,000

Of this expenditure £6,370,000 was derived from the Exchequer, representing a grant of 1/7th of the expenditure in the case of men and 1/5th of the expenditure on women. In addition the cost of central administration to the amount of £1,000,000 was charged on Parliamentary Votes of which only £100,000 was recovered from insurance funds, leaving a further net liability on the Exchequer of £900,000.

392. The total expenditure for the years 1921-30 and the portion thereof derived from the Exchequer are shown in the following table :—

Calendar Year.	Total Expenditure out of Insurance Funds (including Exchequer Grants). (1)	Exchequer Grants. (2)
	£	£
1921	28,368,000	10,271,000
1922	28,577,000	7,296,000
1923	28,308,000	5,984,000
1924	29,898,000	6,114,000
1925	31,378,000*	7,121,000
1926	36,041,000*	6,069,000
1927	39,882,000	6,645,000
1928	36,598,000†	6,242,000
1929	38,842,000	6,676,000
1930	36,400,000	6,370,000

* Additional benefits provided out of surpluses declared available on the second valuation came into operation partly in July, 1925, and partly in July, 1926.

† As from January, 1928, persons aged 65-70 ceased to be entitled to sickness and disablement benefits.

393. The decrease in the amount of Exchequer Grants since 1921, in spite of the increase in expenditure, is due mainly to:—

(a) The reduction in the rate of ordinary State Grant from 2/9ths of the expenditure to 1/7th for men and 1/5th for women, under the provisions of the Economy (Miscellaneous Provisions) Act, 1926, as from 1st January, 1926.

The reduction in the grant on the estimated expenditure for the current year amounts to £2,000,000.

(b) The cessation as from 1st April, 1922, of Special Grants to meet the additional cost of medical benefit (including administration) over the amount payable under statute out of benefit funds.

Under the 1920 Act a sum of 10s. a year per member was payable out of benefit funds, the remainder (2s. 6d. to 3s. per member) being met by Special Exchequer Grants up to 31st March, 1922. From that date up to 31st December, 1926, the additional cost was met under the provisions of the National Health Insurance Act, 1922, and the National Health Insurance (Cost of Medical Benefit) Act, 1924, out of Insurance funds, partly out of benefit funds and partly out of unclaimed contributions and the Investment Account Reserve. Under the Economy (Miscellaneous Provisions) Act, 1926, a sum not exceeding 13s. a year per member was made payable out of benefit funds. This reduction in Exchequer grants amounts at present to approximately £2,150,000 a year.

(c) The cessation as from 1st January, 1922, of the Special Grant to the Women's Equalisation Fund.

The provisions of the National Health Insurance Act, 1918, under which this Fund was constituted, as a charge on the Exchequer, for the purpose of assisting Approved Societies to meet their liability in respect of the sickness claims of women, were repealed by the National Health Insurance Act, 1922. The amount provided was £350,000 a year.

(d) Since 1921 the Special Grant of £142,000 to the Central Fund has been suspended. This Fund is constituted under Section 68 of the National Health Insurance Act, 1924, its purpose being to make good deficiencies found on the valuation of Approved Societies which cannot be made good from the Society's Contingencies Fund. The proviso to Section 68 (1) provides that the grant shall be reduced proportionately with any reduction in the levy out of contributions. The levy has been wholly suspended since 1921, but owing to the increase in claims on the Fund it may have to be re-imposed in the near future.

394. The course of health insurance finance for the five years ending 31st December, 1929, is summarised in the following table of the receipts and payments for all Approved Societies in Great Britain, as well as Deposit Contributors, members of the Navy,

Army and Air Force Insurance Fund and Exempt Persons. Complete figures for 1930 are not yet available but we understand that the general results of the year will be similar to those of 1928.

Receipts.

	1925.	1926.	1927.	1928.	1929.
	£	£	£	£	£
Contributions	27,722,000	24,456,000	26,381,000	25,979,000	26,005,000
Parliamentary Votes and Grants.	7,121,000	6,069,000	6,645,000	6,242,000	6,676,000
Interest and Other Receipts.	5,643,000	5,967,000	5,572,000	5,612,000	5,676,000
Total	40,486,000	36,492,000	38,598,000	37,833,000	38,357,000

Payments on Benefits and Administration.

	1925.	1926.	1927.	1928.	1929.
	£	£	£	£	£
Sickness Benefits* ...	10,339,000	12,543,000	13,034,000	11,304,000	13,265,000
Disablement „ * ...	5,104,000	6,183,000	7,174,000	6,125,000	6,395,000
Maternity „ * ...	1,704,000	1,757,000	1,738,000	1,743,000	1,742,000
Medical „ ...	9,428,000	9,555,000	9,784,000	10,091,000	10,323,000
Additional (non-cash) Benefits.	937,000	1,961,000	3,980,000	3,054,000	2,771,000
Admin. Exs.	3,955,000	4,127,000	4,261,000	4,376,000	4,444,000
Total	31,467,000	36,126,000	39,971,000	36,693,000	38,940,000

* Includes Additional Benefits estimated at £2,100,000, £3,000,000, £3,600,000, £3,100,000, £3,500,000.

Total Funds.	At 1st January, 1925.	At 31st December 1929.
	£	£
Invested with National Debt Commissioners...	69,502,000	67,663,000
Invested by Approved Societies (or by the Minister on their behalf).	44,623,000	55,100,000
Cash at Bank	432,000	149,000
Cash in hands of Approved Societies and Insurance Committees.	2,062,000	2,873,000
£	116,619,000	125,785,000

NOTE.—The rates of contributions were reduced as from January, 1928, on the reduction of the age limit for (sickness and disablement) benefits from 70 to 65, under the Widows', etc., Pensions Act, 1925.

395. In explanation of these large invested funds we should explain that the Health Insurance Scheme rests on the financial basis of the contributions being appropriate to persons entering insurance at the age of 16. A scheme of this nature when it had reached a normal state of affairs, would necessarily possess large reserve funds representing the excess value of the contributions made by each person in his early years over the benefits received by him. When the scheme began in 1912 these reserves were provided by paper credits in the books of societies and in the 20 years that have elapsed, these credits have in great measure been replaced by cash reserves. We understand that the ultimate figure required for the scheme on its present basis is in the neighbourhood of £140,000,000.

396. Quinquennial valuations are made of the assets and liabilities of each Approved Society and where a disposable surplus is revealed the society is able to declare additional benefits. The results of the first two valuations are summarised below and the estimated payments made in respect of additional benefits are shown in the five years summary above.

	Valuations showing surplus.		Valuations showing deficiency.	
	No. of Societies and Branches.	Total Amount.	No. of Societies and Branches.	Total amount.
First Valuation as at 31st Dec., 1918 (including Ireland) (Cmd. 1662, pages 11 and 22).	9,755	£ 17,273,887 Disposable 9,184,087	407	£ 80,919
Second Valuation as at 31st Dec., 1922, and 31st Dec., 1923 (including N. Ireland) (Cmd. 2785, pages 16 and 24).	8,001	42,413,319 Disposable 26,619,161	134	91,675

397. The third valuations as at 31st December, 1927, 1928 or 1929 of the 7,500 Approved Societies and branches with over 16 million members are now nearing completion. The results thus far show that there is considerable reduction in the disposable surpluses as compared with the previous valuations which must lead to some reduction in the additional benefits payable over the next five years.

We understand that certain Societies will need assistance from the Central Fund to enable them to pay the statutory benefits over the next five ^{course of}

398. The 31st December *Fund*, which is a United Kingdom fund, as the receipts and purpose in 1918, stood at 31st December, 1929, Britain, as well as it is fed as required by a levy of about 3d. a year

per member on approved societies and an Exchequer grant of £142,000 a year, but both levy and grant have been suspended since 1921 owing to the size of the balance. With the continuance of heavy unemployment and the heavy sickness benefit claims which have been a feature of the last few years there is, however, considerable prospect of this fund needing replenishment at no distant date.

399. A considerable measure of assistance towards meeting losses arising from unemployment is also afforded to approved societies by the *Unclaimed Contributions Account* for Great Britain. To this account is credited the proceeds of sales of stamps which for one reason or another are never submitted to the Department on insurance cards. Under the Insurance Act, 1928, the moneys available on this account are to be applied in credits to approved Societies towards meeting the cost of benefits to members, in arrears owing to unemployment, for a maximum period of about two years and nine months from the termination of employment.

400. It was estimated that the balance standing to the credit of the account together with the yearly accumulation of unclaimed stamps money and interest would enable a sum of £500,000 to be distributed amongst Approved Societies for the next four or five years. Owing to the abnormal rate of unemployment, however, the annual losses incurred by Societies in the excusal of arrears due to unemployment are now very largely in excess of the money available.

401. A third way in which special provision has been made by Parliament for members suffering from prolonged unemployment is seen in the National Health Insurance (Prolongation of Insurance) Act, 1930. This Act provides for the payment from the Exchequer of 36 contributions for each Approved Society member who would otherwise, by reason of prolonged unemployment, have ceased to be insured during 1931. The estimated cost is £100,000 to £150,000 for the year, but no decision has been arrived at as to the action to be taken after this year.

402. We have dealt with the present situation in regard to the Health Insurance Scheme somewhat fully in order to bring out the curious situation which is developing. **While the income of the scheme as a whole is just about sufficient to finance a continuance of the present rate of expenditure (including any additional benefits that are being provided out of the surpluses of Societies) notwithstanding the serious loss of contributions from unemployment, the separate financial units comprising the scheme are showing at each valuation increasing disparities. The richer societies are becoming able to increase their additional benefits still more and even in a few cases refund to their members their proportions of the contributions, while those at the other extreme are in increasing danger of being unable to maintain even the statutory rates of benefit. Such disparities of fortune might perhaps be**

defended if it could be shown that they arise from good or bad administration. This element does undoubtedly enter into the matter, but by far the most weighty factors are the differing health and unemployment risks of the members in separate societies.

403. We are fully aware that the freedom of insured persons with favourable risks to form their own societies and in time to obtain special advantages for themselves was held out at the inception of the scheme as one of its great attractions and was the answer to complaints of the inequality of charging uniform rates of contributions to all persons. This argument, pushed to its logical conclusion, is however destructive of national insurance in any field, and indeed strikes at the basis of all insurance, viz., the pooling of risks. However careful the selection these can never be equal for all participants in the pooling. A small element of pooling as between societies is already present in the working of the Central Fund. There is therefore no new departure of principle involved in a further measure of pooling and as long as it still leaves considerable variations in the rates of benefit offered by societies the expectations held out at the inception of the scheme are substantially met. In our view the present situation demands an extended application of this principle of pooling, sufficient (1) to prevent well administered societies from failing to maintain the statutory rates of benefit and (2) to enable societies to give special treatment to men suffering from prolonged unemployment to the extent provided by the National Health Insurance Act, 1928. These arrangements are so generous that we can see no adequate ground for extension of the Prolongation of Insurance Act beyond this year in so far as it concerns health insurance.

404. There are many ways in which this pooling can be effected. One would be by reimposing and increasing the levy for the Central Fund and by using that fund as expended to meet the charges we have in mind. Another would be by a direct levy on the disposable surpluses of societies. A discussion of the relative merits of these would take us into intricate details which we are anxious to avoid. Suffice it to say that such pooling as is necessary should in our view be effected without any additional charge falling upon the Exchequer.

405. The Exchequer grant of £142,000 to the Central Fund is open to serious objection as going to meet expenditure which will itself attract the normal State proportion. As far as finance of the scheme permit the general policy for the future should be to limit Exchequer assistance rigidly to this proportionate grant, all central administrative expenditure being charged to the scheme. The non-extension of the Prolongation of Insurance Act and the elimination of the grant to the Central Fund removes a contingent liability of about £250,000 per annum.

406. We have considered whether some reduction might not be made in the expenditure of the scheme as a whole to enable it to meet the cost of central administration now falling on the Exchequer to the extent of £900,000 per annum.

407. We do not recommend any reduction in the statutory rates of cash benefits :—

Sickness benefit 15s. man and 12s. woman.

Disablement benefit 7s. 6d.

Maternity benefit 40s.

408. It is to be noted that no additional allowances are paid in respect of dependents under this scheme. The allowance to approved societies for administrative expenses shows an increase of 32 per cent. over the pre-war figure and the existing arrangements as to drugs enable a revision to be made after next year if prices have then fallen.

409. We are however of the opinion that the payments to the doctors are too high in present circumstances. These consist of a flat capitation allowance of 9s. per annum for every insured person in a doctor's list in addition to mileage allowances in rural areas, amounting in the aggregate to £250,000 and equivalent on the average over the whole of the medical panels to about 4d. per insured person. It is common knowledge that the standard of remuneration of the medical profession has been greatly increased as a result of the Health Insurance Scheme and there has been growing difficulty in filling salaried medical posts under the Government and the local authorities at rates of pay corresponding to those in other classes of public service. In present circumstances we should not regard a reduction of the capitation rate to 8s. as unreasonable. This would represent a saving to the scheme of about £750,000 and enable it to meet the cost of central administration to this additional amount.

410. The total reduction in this field is thus brought up to about £1,000,000.

3.—MATERNITY SCHEME.

411. In connection with the National Health Insurance Scheme we have had our attention called to a development of the maternity service, at present provided thereunder, which has been under consideration for some time. Under the Health Insurance Scheme a sum of £2 is paid on the confinement of an insured woman or the wife of an insured man. In the case of a married woman who is or has recently been herself an employed contributor (some 25 per cent. of the whole) a total sum of £4 is paid. Out of this provision

she is free to make her own arrangements as regards the attendance of doctor or midwife at confinement. Medical benefit under the insurance scheme covers attendance before confinement or not less than 10 days thereafter and sickness benefit may be drawn by an insured woman except for a period of four weeks following confinement.

412. The total provision for maternity benefit made from insurance funds is about £1,950,000 per annum and the present expenditure is about £1,530,000 per annum, thus leaving a margin to approved societies of about £420,000 per annum. Under the new scheme it is proposed to halve the present maternity benefit and to divert half the provision (i.e. £975,000) to an extended maternity service to be provided by the local authorities. This service would cover

(1) Provision in every case of the services of a qualified midwife to act either as midwife or maternity nurse;

(2) provision in every case of a doctor to give ante-natal, natal and post-natal attention as may prove necessary to all cases showing any abnormality;

(3) provision of a consultant when desired by the doctor in attendance;

(4) provision of hospital beds for such cases as need institutional care;

(5) provision of certain ancillary services (e.g. transport, sterilised equipment, laboratory facilities).

413. The scheme would be operated by county and county borough councils, subject to a power to the county council to delegate all or any part of it, with prior approval of the Minister of Health, to a county district council which is a maternity and child welfare authority. The local authority would be under statutory obligation to render the above services free to insured persons but would have complete discretion in other cases as to the service to be rendered and as to the charge, if any, to be made therefor.

414. The terms of service of doctors and midwives (and possibly also consultants) would be negotiated centrally with representative bodies. Such terms would include provision for securing proper service under appropriate penalty; the contract of service thus arranged to be with the local and not the central authority, as in the case of the National Health Insurance Medical Service contract. A panel of doctors, midwives (and possibly consultants) would be established for each county and county borough area to work the scheme in that area. A woman would have power to

select doctor and midwife to attend on her, subject to their concurrence.

415. We understand that it is contemplated that services (4) and (5) above would, in view of the increase of grants under the Local Government Act, 1929, be provided wholly out of rates and that any receipts from uninsured persons under the scheme generally would be retained by local authorities. The cost of (1) (2) and (3) in excess of the amount diverted from insurance funds would be an Exchequer charge. Pending negotiations with the medical profession, any estimate of the cost of these services is given with reserve, but the total figure is put by the Ministry of Health at about £2,500,000 for Great Britain of which £975,000 would fall on insurance funds leaving about £1,500,000 as the probable Exchequer charge.

416. No one can dispute the desirability of taking action to reduce the serious loss of life and health in connection with maternity and we do not doubt that it would be a definite advantage from this point of view to substitute, in considerable measure, services of attendance for the present cash payment of maternity benefit. At the same time we cannot but regard this scheme as unduly ambitious in scope; it introduces into local government administration for the first time the very undesirable principle of differentiation between those who belong to the State insurance scheme and those who do not; but most serious of all is the proposed additional charge of £1,500,000 per annum upon the Exchequer. **In present financial circumstances, the Exchequer cannot afford to assume this liability and in our view improvement of this service should be sought without any extra State grant.**

4.—OLD AGE PENSIONS AND BLIND PERSONS PENSIONS (NON-CONTRIBUTORY).

417. The Old Age Pensions Act, 1908, with effect from the 1st January, 1909, first introduced the scheme of non-contributory old age pensions, the broad principles of which have, with certain modifications, remained in force ever since.

The grant of a pension was made subject to age, means, nationality and residence tests, and the maximum rate was fixed at 5s. a week if the means did not exceed £21 a year. Lower rates of pension were payable if the means did not exceed £31 10s. a year.

418. In view of the increase in the cost of living during the war, an Additional War Allowance of 2s. 6d. a week was added in 1916, and as from 2nd January, 1920, under the Old Age Pensions Act, 1919, this was merged in an increase of the normal rate of pension

to 10s. a week. That Act fixed the rates of pension in relation to means as follows and this scale has remained in force ever since :—

<i>Yearly Means.</i>			<i>Pensions.</i>	
			s.	d.
Not exceeding £26 5s.	...	...	10	0
Exceeding £26 5s. but not exceeding £31 10s.	...	...	8	0
„ £31 10s.	„	„ £36 15s.	6	0
„ £36 15s.	„	„ £42	4	0
„ £42	„	„ £47 5s.	2	0
„ £47 5s.	„	„ £49 17s. 6.	1	0

The same Act introduced the present method of calculating annual means from capital, viz., the first £25 is disregarded, the next £375 is assessed at 5 per cent. and any surplus at 10 per cent., this being a rough estimate of the annuity value of the capital. For a married couple living together the means of each is assumed to be one half of the total means.

419. The Old Age Pensions Act, 1924, introduced with effect from the 7th August, 1924, an important alteration in the calculation of means by providing for a deduction not exceeding £39 a year (or £78 a year in the case of a married couple living together), from means other than earnings. This alteration was made in order to meet the plea that the means limit penalised thrift and to discourage old people from competing in the labour market. Thus it is now possible for a married couple to draw the full pensions of 10s. a week each if they have already total means (otherwise than from earnings) amounting to £52 10s. + £78 = £130 10s., thus giving them a total income of £182 10s. per annum.

420. Apart from the alterations in the old age pension position introduced by the contributory scheme instituted in 1925 (which is dealt with in the following section), the only other important change since the War was the reduction of the age of qualification for blind persons from 70 to 50 years of age under the Blind Persons Act, 1920.

The cost of Old Age Pensions since the War.

421. The following table shows the costs of old age pensions (including blind persons pensions) in Great Britain for each year since 1921, together with the expenses of administration. Since 1926 an increasing proportion of pensioners have established a title under the contributory scheme, and are therefore not subject to the means limit. Separate figures of cost for non-contributory and contributory pensioners over 70 are not available but a rough estimate is given in note (c) below. These figures are, of course, quite different from the extra cost of old age pensions due to the Contributory Pensions Scheme, i.e., of pensions to persons who would otherwise

be disqualified on the ground of means. No part of the cost of pensions over 70 given below is chargeable against contributions under this scheme:—

Year ended 31st March.	Expenditure on Pensions (borne on the Old Age Pensions Vote).	Expenses of Local Pensions Committees (borne on the Old Age Pensions Vote).	Estimated Other Administrative Expenses (borne on the Votes of the Government Departments concerned).		Total Expenditure. (b)
			(a)	(b)	
	(1)	(2)	(3)		(4)
	£	£	£		£
1921	20,696,029	54,397	751,650		21,502,076
1922	21,939,563	49,552	854,032		22,843,147
1923	22,362,993	54,206	743,991		23,161,190
1924	23,221,415	49,503	749,201		24,020,119
1925	24,905,668	66,130	827,977		25,799,775
1926	27,017,955	56,773	878,294		27,953,022
1927	29,984,344(c)	51,371	839,341		30,875,056
1928	32,829,796(c)	43,087	833,917		33,706,800
1929	34,052,321(c)	41,749	822,918		34,916,988
1930	34,918,142(c)	39,370	827,099		35,784,611
1931 (approx.)...	36,700,000(c)	38,000	830,000		37,568,000
1932 (Estimated)	38,200,000(c)	37,000	786,841		39,023,841

(a) Customs and Excise, Post Office, Ministry of Health, Department of Health, Scotland, Exchequer and Audit Department, Registrar-General's Office and Stationery Office.

(b) These figures do not include the costs incurred by the Ministry of Health and the Department of Health, Scotland, in administering the over-70 Contributory Pensions paid out of the Old Age Pensions Vote, as these costs are chargeable to the respective Pensions Accounts.

(c) *Estimated* cost of pensions paid to pensioners registered as over-70 "Contributory Pensioners," included in above figures of expenditure.

				Approx. £
1926-27	...	...	...	2,600,000
1927-28	...	...	...	6,000,000
1928-29	...	...	...	8,575,000
1929-30	...	...	...	10,550,000
1930-31	...	...	...	13,050,000
1931-32	...	...	...	15,600,000

(d) *Blind Pensions*.—The cost of Blind Pensions, which is included in the above figures as from 10th September, 1920, has risen gradually from approximately £255,000 in 1921-22 to £585,000 in 1930-31.

The Future Cost of Old Age Pensions.

422. We are advised by the Government Actuary that the problem of estimating with accuracy the future cost of old age pensions is

rendered especially difficult at the present time by reason of the fact that the population in various age-groups, as now estimated, depends upon the enumerated numbers at the Census of 1921. Pending the issue of the detailed figures for this year's Census, he estimates that the numbers of persons in Great Britain aged over 70 years in 1930-31, 1935-6 and 1940-1 will be as follows :—

<i>Date.</i>	<i>No. of persons over age 70 in Great Britain.</i>
30th September, 1931	1,811,000
30th September, 1936	2,031,000
30th September, 1941	2,242,000

423. The proportion of the population over 70 who have been in receipt of an old age pension in recent years is shown in the following statement, from which persons receiving "blind" pensions have been excluded.

Year. (as at 30th June).	Percentage of population over 70 in receipt of Old Age Pension (Great Britain).		
	Men.	Women.	Total.
1921	47·2	62·3	56·1
1922	48·2	62·8	56·8
1923	49·0	62·6	57·0
1924	50·1	63·2	57·8
1925	55·8	67·5	62·7
1926	57·5	68·6	64·0
1927	69·0	72·3	71·0
1928	72·6	75·5	74·3
1929	74·3	76·4	75·5
1930	76·7	78·7	77·8

By 31st March, 1931, the number of old age pensioners (excluding blind) in Great Britain had risen to 1,409,000, representing approximately 79 per cent. of the population over 70.

It will be seen that there was a sharp increase in the proportion of pensioners from 1924 to 1925; this is mainly attributable to the Old Age Pensions Act of 1924, the effect of which continued to be felt in 1925-26. The large increase in 1926-27 is due to the Contributory Pensions Act of 1925; here again a considerable period elapsed before the full number of claims under the Act emerged, and this accounts mainly for the further rise in 1927-28. Precise information is not available as to the number of pensions awarded under the Pensions Act of 1929, but it is thought that approximately one-third of the increase in the proportion of pensioners since July, 1929, may be attributed to this Act.

424. While changes in legislation are clearly responsible for certain large and well-marked increases in the proportion of pensioners

they do not appear to account fully for the persistent tendency towards an increase in the proportion which can be observed throughout the period under review. In this connection the progress of the percentages for men and women separately is of interest. Whereas, in 1921, the proportion of men over 70 in receipt of pension was nearly 25 per cent. less than the corresponding proportion of women, in 1930 the proportion was practically the same for both sexes. In part this feature is the result of the grant of pensions at 70 by virtue of the provisions of the Contributory Pensions Act of 1925, but to some extent also it may probably be attributed to the growing economic stress of the past few years which has presumably made it increasingly difficult for an elderly man to obtain a livelihood.

425. Having regard to the position as indicated briefly in the foregoing paragraphs, it was assumed for the purpose of the Parliamentary estimates for 1931-2 that the average proportion of pensioners during that year would amount to 80 per cent. (excluding "blind" pensioners). The estimate of £38.2 millions makes provision accordingly. After careful examination of such material as is at present available the Government Actuary thinks it improbable that the proportion of the aged population becoming entitled to old age pensions will reach 85 per cent. He assumes that the saturation point will be reached at 82½ per cent. in about five years time.

Addition for blind pensioners.

426. The addition to be made to the cost of old age pensions to include those payable to blind persons aged between 50 and 70 is a somewhat speculative matter. The number of such persons has grown considerably in recent years, as will be seen from the following table:—

Year. (31st March). (1)	Number of persons in receipt of "blind" pensions in Great Britain. (2)	Column (2) expressed as a percentage of the population over age 70. (3)
1921	8,900	0.6
—	—	—
1927	17,100	1.0
1929	20,700	1.2
1931	23,500	1.3

427. The marked and continued increase in these numbers may indicate, in some small measure, an increase in industrial blindness. It appears mainly, however, to reflect the growth of activity on the part of the local authorities who administer the Blind

Persons Act to 1920 and have, in the last few years, tended to give generous financial and other assistance to blind persons who register themselves. In this connection it is important to note that the statutory definition of blindness for the purpose of the Act, viz. that the person is "so blind as to be unable to perform any work for which eyesight is essential" is not altogether satisfactory, and as a result the development of an easy standard in the test for qualification, together with the lack of expert examination in many cases, may bear some responsibility for the increase.

On the figures given above it was assumed that the proportion of blind pensioners to the population over age 70 would have grown to 1½ per cent. by 1935 and to 1¾ per cent. by 1940.

Cost of pensions in next decennium.

428. On the basis described above, and making suitable adjustments for pensions payable at a lower rate than 10s. 0d. a week, it is estimated that the number of pensioners and annual cost of pensions in the next decennium will be as follows:—

<i>Financial year.</i>		<i>Average number of pensioners during year.</i>	<i>Annual cost of pensions. £</i>
1931-2	... ..	1,478,000	38,200,000
1935-6	... ..	1,705,000	44,200,000
1940-1	... ..	1,889,000	49,000,000

When submitting estimates in connection with the Widows', etc., Pensions Bill, 1925, the Government Actuary put the total cost of Old Age Pensions over 70 for the same years at:—

					<i>£</i>
1931-2	...	...	...	...	36,400,000
1935-6	...	...	...	...	40,600,000
1940-1	...	...	...	...	46,300,000

so the financial outlook for the scheme has become appreciably more serious in the past six years. But even on the lower level of costs then adopted the total burden was estimated to increase continuously as far as the estimates were carried, i.e., up to 1965-6, for which year the cost was put at £64.4 millions. Other estimates given at the same time showed that the growth of this charge would practically neutralise the large reduction in the War Pension charge over the same period.

429. Apart from the action to be taken in connection with the Contributory Pensions Scheme we do not consider that it is practicable at the present time to make any reduction in this liability. As time goes on and more and more pensioners establish a title under the Contributory Scheme, the means limit will become less important. If any substantial reduction of burden were essential,

it would in our view be necessary to reduce the basic rate of 10s. a week. As far as adjustments in respect of the altered value of money are concerned it is relevant to point out that the present rate is 100 per cent. over the pre-war standard, that it was fixed in 1919 when the cost-of-living index also was about 100 per cent. above the pre-war level, and that the increase in this index has fallen to 45 per cent. We cannot, however, overlook the change in public opinion in regard to such pensions that has occurred since the Scheme started in 1909 and the movement in favour of a more extended scheme of retirement pensions. In our view a reduction of the basic rate of 10s. could now only be effected as part of a general scheme of sacrifice all round.

5.—WIDOWS', ORPHANS', AND OLD AGE CONTRIBUTORY PENSIONS.

430. Under the scheme approved by Parliament on the Widows', Orphans', and Old Age Contributory Pensions Act, 1925, provision was made for

(a) pensions for widows and dependent children, and

(b) old age pensions commencing at the age of 65 instead of 70 and passing, on the attainment of the age of 70, into pensions under the Old Age Pensions Acts, freed from the restrictions and disqualifications at present applied to such pensions.

Subject to the fulfilment of the statutory conditions, which involve a minimum period of insurance and the payment of a minimum number of contributions by the person on whose insurance a claim to pension under the Act is based, the following are the benefits normally payable:—

(a) Widows' Pensions.—10s. a week for the widow of an insured man who dies after the 4th January, 1926, and was under 70 years of age at that date, with an additional allowance for children up to the age of 14 (or 16 if remaining under full-time instruction in a day school) at the rates of 5s. a week for the eldest such child and 3s. a week for each of the other children.

(b) Orphans' Pensions.—7s. 6d. a week for each child of an insured man, being a married man or a widower, or of an insured widow, payable up to the age of 14 (or 16 if the child remains under full-time instruction in a day school).

(c) Old Age Pensions.—10s. a week to insured men and insured women between the ages of 65 and 70, and 10s. a week to the wives between the ages of 65 and 70 of insured men who are themselves entitled to pensions.

431. Provision was also made by the Act of 1925, subject to certain conditions, for pensions at the ordinary rate to widows and children of insured men who died before the commencement of the Act. A widow in this class was not, however, eligible for a pension unless there was living at the commencement of the Act at least one child of the marriage, or of a former marriage of either parent, under the age of 14. Her pension ceased six months after the youngest child attains 14. An orphan's pension is similarly payable to the orphan children while under the age of 14 (or 16 if under full-time instruction in a day school) of an insured man (being a married man or a widower) or an insured widow who died before the commencement of the Act.

As from 2nd July, 1926, pensions under the Old Age Pensions Acts, 1908 to 1924, at the full rate of 10s. a week became payable by virtue of the Widows', Orphans' and Old Age Contributory Pensions Act to insured persons on attaining 70, without the application of the means test. The same rights were given to the wives of insured men.

432. The scheme is on a contributory and compulsory basis and is interlocked with the scheme of health insurance, combined contributions being made, as a rule, towards both on the same insurance card. The relation of the contributions to the benefits is based upon the principle by which the contributions have been determined in the case of National Health Insurance, viz., that the contributions are equal in value (as actuarially ascertained) to the benefits granted to persons entering into insurance at the age of 16, special arrangements being made by which, in effect, the State provides for the extra liability, over and above the provision made by the contributions, arising in respect of persons entering into insurance at all ages between 17 and 70. In applying this principle to the present case regard has been had to two considerations peculiar to a scheme of this kind, namely, (i) that the major part of the benefits consists of pensions for widows and allowances for children, and (ii) that the wife of an insured man will be entitled, equally with himself, to a pension when both have reached the age of 65. Insured women (who for the most part are young and unmarried) are therefore required to contribute to the scheme on a wider basis than is represented by the slight probability that they will themselves continue in insurance to the age of 65 and then become entitled to a pension in their own right, their weekly contribution being fixed at one-half of the rate payable for insured men. The effect is that during the period of their employment women (with their employers) will make a contribution towards the benefits to which they will be entitled either in their own right or as the wives and widows of insured men.

433. On this basis the appropriate weekly contributions from the age of 16 for the benefits granted by the Act up to age 70 were 10d.

for a man and 5d. for a woman. The initial rates were fixed at 9d. and 4½d., respectively, equally divided between employees and employed, but having regard to the unconditional right to old age pensions after 70 conferred by the Act, it was provided that from 1936, 1946 and 1956 the rate contributions should be increased by 2d. (1d. for women) on each occasion thus bringing the total eventually to 1s. 3d. representing the full equivalent, in the case of the person entering at 16, of all the benefits of the Act.

434. As already stated the excess cost of the benefits for entrants over 16 was accepted as a liability on the Exchequer, which had in addition to meet the extra cost of the rights granted to voluntary contributors over and above their contributions, the cost of granting pensions without any contributions to existing widows and children and the extended rights granted to Old Age Pensioners at 70. The capital value of the liability so assumed by the Exchequer was summarised by the Government Actuary as follows :—

	£
For employed persons entering compulsory insurance when over 16 years of age	566,000,000
For Voluntary Contributors	12,000,000
For Widowed Mothers and Children ...	42,000,000
For extended rights to Old Age Pensions at 70	126,000,000
Total	£746,000,000

435. Contrary to the principle adopted under the Health Insurance Scheme, no provision has been made in this scheme for building up reserve funds which would in time represent the accumulated surplus of contributions by persons entering at 16 years of age. From the outset contributions have been applied as received to defray current expenditure. The actual net charge falling upon the Exchequer in any year, over and above contributions received, is therefore a gradually rising figure and for the first decennium was estimated to average only £4,000,000 per annum. The Exchequer grant was accordingly fixed at this figure by the Act of 1925 up to 31st March, 1936.

436. In 1929 a new Act was passed extending the scheme to include :—

(a) pensions to widows over the age of 55 of men of the insurable class who died before the 4th January, 1926, and to widows of men who, though they survived the 4th January, 1926, were then over 70;

(b) prolongation of right to widows' pensions under the 1925 Act, until the youngest child attains the age of 16 in the case where the husband died before 4th January, 1926;

(c) Old Age Pensions to the wives between the ages of 65 and 70 of men who were over 70 on 2nd January, 1928, and were entitled to old age pension under the Old Age Pensions Acts, 1908 to 1924, and to widows over 70 who, had they been under 70, would have been qualified for widows' pension.

437. The total cost of these concessions (of which (a) was by far the most expensive) in the period to 31st March, 1936, was estimated at £47,300,000, averaging about £8,000,000 per annum. For the next decennium the extra charge was £5,000,000 per annum, falling gradually thereafter to a minimum of £600,000 per annum. As contributions were unaltered this necessitated an increased Exchequer grant and in order to provide this and also to smooth out the sudden increase that was to have taken place under the original scheme in 1936, the new Act fixed the charge at £9,000,000 for 1930-31 rising by £1,000,000 per annum to a maximum of £21,000,000 in 1942-3. This relates to the expenditure charged on the Treasury Pensions Account and does not include the additional cost of Old Age Pensions over 70 resulting from the Contributory Pensions Acts. The following table gives the estimated revenue and expenditure of the scheme up to 1946. As far as can be foreseen the liability after 1946 is not considered likely to rise above the sum of £21,000,000 per annum.

Financial Year.	Receipts from Contributions.	Interest.	Exchequer Contribution.	Total Income.	Total Expenditure.	Balance in Treasury Pensions Account at end of year.
	£	£	£	£	£	£
1929-30 ...	23,400,000	1,900,000	4,000,000	29,300,000	27,300,000	44,800,000
1930-31 ...	23,700,000	1,900,000	9,000,000	34,600,000	35,400,000	44,000,000
1931-32 ...	23,800,000	1,800,000	10,000,000	35,600,000	39,700,000	39,900,000
1932-33 ...	23,900,000	1,500,000	11,000,000	36,400,000	41,000,000	35,300,000
1933-34 ...	24,000,000	1,200,000	12,000,000	37,200,000	42,400,000	30,100,000
1934-35 ...	24,100,000	1,000,000	13,000,000	38,100,000	43,800,000	24,400,000
1935-36 ...	25,600,000	800,000	14,000,000	40,400,000	45,100,000	19,700,000
1936-37 ...	29,700,000	700,000	15,000,000	45,400,000	46,700,000	18,400,000
1937-38 ...	29,800,000	600,000	16,000,000	46,400,000	48,000,000	16,800,000
1938-39 ...	30,000,000	600,000	17,000,000	47,600,000	49,100,000	15,300,000
1939-40 ...	30,000,000	500,000	18,000,000	48,500,000	50,300,000	13,500,000
1940-41 ...	30,100,000	400,000	19,000,000	49,500,000	51,400,000	11,600,000
1941-42 ...	30,100,000	300,000	20,000,000	50,400,000	52,200,000	9,800,000
1942-43 ...	30,200,000	200,000	21,000,000	51,400,000	53,100,000	8,100,000
1943-44 ...	30,300,000	200,000	21,000,000	51,500,000	53,800,000	5,800,000
1944-45 ...	30,300,000	100,000	21,000,000	51,400,000	54,400,000	2,800,000
1945-46 ...	31,700,000	—	21,000,000	52,700,000	54,900,000	600,000

438. The above table embodies the estimates made by the Government Actuary at the time the Act of 1929 was before Parliament. The actual outturn of the two years that have elapsed has been more favourable to the extent of £2,400,000 :—

	1929-30.			1930-31.		
	Estimate.	Actual.	Surplus or Deficit.	Estimate.	Actual.	Surplus or Deficit.
INCOME.						
Receipts from contributions.	£ 23,400,000	£ 24,080,000	£ 680,000	£ 23,700,000	£ 23,470,000	£ -230,000
Exchequer payment ...	4,000,000	4,000,000	—	9,000,000	9,000,000	—
Interest ...	1,900,000	2,000,000	100,000	1,900,000	2,200,000	300,000
Total ...	29,300,000	30,080,000	780,000	34,600,000	34,670,000	70,000
EXPENDITURE.						
Widows' and Orphans' Pensions.	10,600,000	10,620,000	20,000	16,700,000	16,880,000	180,000
Age 65-70 Pensions ...	15,600,000	14,730,000	-870,000	17,500,000	16,370,000	-1,130,000
Administration Expenses	1,100,000	1,100,000	—	1,200,000	1,350,000	150,000
Total ...	27,300,000	26,450,000	-850,000	35,400,000	34,600,000	-800,000
Balance in Accounts at end of year.	44,800,000	46,330,000	1,530,000	44,000,000	46,400,000	2,400,000

439. We are advised that the bulk of the excess of £680,000 in the contribution income for 1929-30 was due to the fact that the growth in the insured population during the latter half of 1928-29 and during 1929-30 was greater than anticipated. A relatively small part of the excess is to be accounted for by an improvement in the sickness experience which resulted in a smaller loss of contributions. As regards 1930-31 the contribution income cannot be considered in relation to the insured population, figures for the latter being not yet available. It is clear, however, that the excess in the contribution income which would otherwise have occurred in that year as a result of the abnormal increase in insured population in the preceding period was more than counter-balanced by the rapid growth in the rate of unemployment.

440. It is not possible to state with any authority the manner in which the above mentioned increase in the number of insured persons has affected the age and sex distributions of the population. There are grounds however for thinking that the increase has arisen as a result of a diminution in the number of persons leaving insurance rather than an increase in the number of new entrants. Each such additional person remaining in insurance represents a liability for benefits which will, in due course,

probably exceed the additional amount of contributions paid on his account in the future. The excess income derived from this source cannot, therefore, pending further information, be regarded as a surplus available for disposal.

441. The diminution in the contribution income which occurred in 1930-31 as a result of the rise in the rate of unemployment must be regarded as an irrecoverable loss. During that year the average rate of unemployment among persons insured against unemployment was about 18 per cent. The present rate is nearly 21 per cent. and it is thus to be feared that unless a rapid recovery occurs in the economic position of the country the loss of contributions due to this cause in 1931-32 will exceed that of the preceding year.

442. The difference between the actual and estimated costs of age 65-70 pensions appears to be due to two causes. First, it was necessary, in the absence of knowledge of the effects of the new conditions regarding termination of insurance introduced by the Pensions Act of 1925 and the Insurance Act of 1928, to make assumptions regarding the proportions of the population which would be qualified for pension in future years. So far, only two-thirds of the increase allowed for in this respect has materialised. The non-emergence of the remaining third accounts for about £750,000 of the difference which arose in each of the two years. Secondly, the Pensions Act of 1929 relaxed the conditions as to the contributions test in the case of certain persons. On the basis of an examination by the Ministry of Health of the rejected applications in their possession provision was made for 20,000 awards under this head, of which some 90 per cent. consisted of age 65-70 pensions. So far the bulk of these additional cases do not appear to have emerged. It is estimated that the non-emergence of this class accounted for about £100,000 of the difference in 1929-30 (quarter year's charge) and about £400,000 in 1930-31.

443. While it is clear that the two causes mentioned above have so far resulted in a surplus of some £2,000,000 in the Pensions Accounts, it would not be justifiable to assume, on the experience of the two years' working of the new benefits, that surplus of this dimension will emerge in future years. In the first place the relaxation of the contributions test covered a diminishing class since, at the outset, provision was necessary for the whole of the class concerned then aged between 65 and 70. In fact, the amount provided up to the 31st March, 1936, amounted only to £2,100,000 in total and thereafter to a relatively small annual sum. Further, experience shows that there is usually a considerable lag in applications for a new or an extended benefit, presumably due to the slow appreciation of the position on the part of the insured persons concerned. Thus it may well be that the

proportion of claims in respect of both of the classes referred to in paragraph 442 will yet show a substantial increase.

444. The foregoing considerations suggest that, at the moment, the Pensions Account appears to be suffering a loss of contribution income of at least £1,000,000 per annum as a result of the present heavy unemployment and that this loss is approximately counter-balanced by the surplus provision made for the two classes of age 65-70 pensioners referred to above. The excess of £2,400,000 in the balance in the Pensions Accounts as at 31st March, 1931, probably does contain a surplus, but it is thought that its amount is not in excess of £1,000,000 and this sum is at present not being added to. Further, if the present heavy rate of unemployment continues for long, and if, as is by no means improbable, the lag in applications for age 65-70 pensions is reduced, it is likely that this surplus of £1,000,000 will rapidly be replaced by a deficiency. It seems clear, therefore, that it would be imprudent to reduce the annual State contribution to the Pensions Account at the present time, but we are of the opinion that the situation should be reviewed again in two years' time in the light of the further information then available.

445. Apart from the question of a possible over-estimate of the Exchequer liability the only possibility of a substantial reduction of this rapidly growing charge for pensions lies in a reduction of the basic rate of 10s. a week. This rate is obviously linked with the rate of the non-contributory old age pension, and is therefore subject to the observations made in the previous section. It may in addition be urged against any reduction of benefits under the contributory scheme that there is an actuarial relation between benefits and contributions. We do not, however, feel that there would be great force in this contention until contributions had reached the eventual maximum of 1s. 3d. a week (men) contemplated under the Act of 1925. We would merely add that if existing pension rates are maintained it is in our view essential to the proper regulation of this serious charge on the Exchequer to bring the increases in contribution duly into operation. Should any margin on the estimates eventually emerge it should, we consider, be applied to reducing the Exchequer charge and not used either to increase benefits or to defer the increases of contributions by 2d. a week each as from 1936, 1946 and 1956, provided for in the Act of 1925. Notwithstanding these increases it would appear that the Exchequer must look forward to a steady increase in its total liability for old age pensions of all kinds and for widows' and orphans' pensions to over £80,000,000 a year in 30 years' time, truly a serious prospect.

6.—HOUSING.

A.—ENGLAND AND WALES.

446. The Estimates of the Ministry of Health for the current year make the following provision for housing subsidies :

	£
(i) Housing and Town Planning Act of 1919	6,855,000
(ii) Housing Act, 1923	2,510,000
(iii) Housing (Financial Provisions) Act, 1924	3,160,000
(iv) Housing (Rural Workers) Act, 1926 ...	10,000
(v) Housing Act, 1930	200,000
	£12,735,000
Total	£12,735,000

(i) HOUSING AND TOWN PLANNING ACT, 1919 (£6,855,000 IN 1931).

447. Apart from a comparatively small charge of £81,000 per annum in respect of 50-year subsidies to Public Utility Societies and Housing Trusts, this sum represents the annual deficit on local authorities' building under this Act in excess of 1d. rate which was the limit of the liability of the local authority. Owing to excessive cost, the scheme was limited in July, 1921, to 176,000 houses. The average capital cost per house built under this scheme was £1,011 and the total capital cost approximately £178,000,000, of which £5,000,000 is attributable to the houses built by County Councils, Public Utility Societies and Housing Trusts.

The total amount paid by way of subsidies up to the 31st March, 1931, was £69,598,656, made up as follows :—

	£
Local Authorities	67,681,892*
County Councils	126,439
Public Utility Societies and Housing Trusts	1,790,325
	£69,598,656

448. It is anticipated that Exchequer subsidy will continue to be paid until the loans for building (the loan sanction period for which is 60 years) have been finally repaid. These loans will expire during the period 1980-1985. Before that period is reached, however, there will be a reduction in the amount of subsidy payable as other loans are finally extinguished, the loan periods for fencing, roads, and sewers being 15, 20 and 30 years, respectively. These loans amounting to approximately £330,000, £8,500,000 and £4,000,000 are expected to expire during the periods 1934-37,

* Includes £172,689 for slum clearance schemes including rehousing.

1940-45 and 1950-55, respectively. The following shows roughly the effect of the repayment of loans on Exchequer subsidy :—

1933-1937, £6,720,000 decreasing to £6,690,000.
 1937-1940, £6,690,000.
 1940-1945, £6,690,000 decreasing to £5,940,000.
 1945-1950, £5,940,000.
 1950-1955, £5,940,000 decreasing to £5,640,000.
 1955-1980, £5,640,000.
 1980-1985, £5,640,000 decreasing to nil.

449. Three other factors, however, affect the position :—

(a) Assuming no alteration is made in the present basis of rating, the produce of the penny rate contribution of the local authorities may be expected to increase, thus decreasing the amount of the loss falling upon the Exchequer. During the past few years the average increase in rateable value and therefore in the rate contribution has been approximately 2 per cent., due to new constructional works, etc. This rate of increase is not likely to be maintained, but assuming an average increase of 1 per cent. the effect will be as follows :—

Year.	Total Estimated Rate Contribution.	<i>Estimated increase in Rate Contribution and decrease in subsidy compared with 1931-32.</i>	
		£	£
1931-1932	...	930,000	—
1934-1935	...	958,000	28,000
1944-1945	...	1,058,000	128,000

(b) Another factor to which reference should be made is the fluctuations in interest rates. The average annual charge on loans raised to meet capital expenditure has been 6.56 per cent. (interest 6.08 per cent., annual sinking fund for repayment of loan 0.48 per cent.). While approximately 50 per cent. of the loans in connection with the scheme have been raised for the full loan period, at a fixed rate of interest, the balance was raised by the issue of Stock, Local Bonds and Short Term Mortgages, for periods varying from three years to 20 years and upwards. Further savings may be expected to accrue in this way, and it is calculated that, on the basis of re-borrowing at $4\frac{1}{2}$ per cent., they will amount to an average of about £15,000 per annum during the next four years (total £60,000) to an average of about £45,000 per annum during the succeeding five years (total £225,000), and in the year 1940, in respect of Stocks then maturing, a further saving of £350,000 will probably accrue, i.e., a total reduction on the present subsidy of £635,000 per annum.

(c) Rents are fixed in accordance with certain Rules incorporated in the Regulations and are dependent to some extent upon the economic conditions of the working classes and upon the existing level of rents of pre-war houses. During the last seven years the average rental has fallen from 9s. 8d. per week (exclusive of rates) to 9s. 4d. per week. Any future variation in rents will affect the amount of Exchequer subsidy *pro tanto*.

(ii) HOUSING &c. Act, 1923 (£2,510,000 IN 1931).

(a) *Housing Schemes*.

450. Section 1 (1) of this Act authorised the Minister of Health to pay Exchequer contributions in the form of annual payments for 20 years of £6 per house towards expenses incurred by a Local Authority :—

(a) in promoting by assistance to private enterprise, the construction of houses of specified type and size completed before 1st October, 1925. (This date has been extended by the Housing (Financial Provisions) Act, 1924, to 1st October, 1939) :

(b) in the provision of such houses by the Local Authority themselves.

The Act (Section 3) also provided for direct payment by the Minister of contributions of like amount towards expenses incurred in the construction of houses provided under approved schemes by societies, bodies of trustees or companies, which do not trade or profit, or which pay interest or dividends limited to rates prescribed by the Treasury.

451. Under the Housing Acts (Revision of Contributions) Orders 1926 and 1928, made under Section 5 of the Housing (Financial Provisions) Act, 1924, the contribution payable by the Exchequer for houses completed after the 30th September, 1927, and before 1st October, 1929, is at the rate of £4 per annum, and no contribution is payable for houses completed after 30th September, 1929.

452. The assistance to private enterprise towards which Exchequer contributions are payable could be given by Local Authorities in any of the following ways specified in section 2 of the Act, viz. :—

(a) lump sum payments after completion of the house ;

(b) annual payments for 20 years to the person by whom the rates on the houses are payable ; or

(c) the provision during a specified period of any part of the periodical sums payable by way of interest on or repayment of loans raised to meet the cost of construction.

453. The amount of the assistance given by the local authority is within their discretion but the Exchequer contribution towards such assistance is limited to the amounts stated above. In a large

proportion of cases the assistance has been in the form of lump sum payments varying from £50 to £100. Before approving schemes for promoting the building of houses by private enterprise, the Minister is required to be satisfied that the need for such houses cannot be met without assistance.

454. By the 30th September, 1929, when contributions ceased to be payable in respect of further houses, 351,232 houses had been erected under private enterprise schemes assisted by Local Authorities, 73,895 under schemes carried out by Local Authorities themselves, and 11,506 by Public Utility Societies, etc., assisted directly by the Exchequer, making a total of 436,633 houses provided under the Act. The annual Exchequer commitment in respect of these houses is approximately £2,366,000, continuing until 1943 and then gradually falling until 1949.

(b) *Slum clearance Schemes.*

455. Section 1 (3) of the Act provided for an annual contribution not exceeding one-half of the estimated average annual loss likely to be incurred by the Local Authority in carrying out slum clearance re-housing schemes. This provision has been repealed by the Housing Act, 1930, in respect of all schemes not approved before the commencement of the Act. Under the conditions approved by the Treasury under this section, the Exchequer contribution payable each year during the construction period is one-half of the reasonable deficit arising during the year, and after completion of each scheme is one-half of the estimated average annual deficit as approved by the Minister arising on the scheme from the year of completion to the year in which the building loans are finally redeemed.

456. Of the 124 slum clearance schemes in progress since the war, 110 are assisted under this Act, 11 being assisted under the Housing, Town Planning, &c., Act, 1919, and three being carried out by Local Authorities without assistance. Of the 110 schemes under the Act of 1923, 44 were completed at 1st January, 1931. At that date 10,151 houses had been erected as rehousing in respect of the 110 schemes.

457. The total capital expenditure on completion of the 110 schemes assisted under the 1923 Act is estimated at roughly £8,400,000. The annual Exchequer contribution is estimated at £90,000 for 1931-32, at £100,000 afterwards until about 1984, then being gradually extinguished in the ensuing 10 years.

The cost of the 11 schemes assisted under the Act of 1919 is included in the figures regarding housing under that Act.

(iii) HOUSING (FINANCIAL PROVISIONS) ACT, 1924.

(£3,160,000 in 1931.)

458. This Act provides that in respect of schemes approved after the passing of the Act, annual Exchequer contributions at the rate

of £9 for 40 years (or £12 10s. if the house is in an agricultural parish as defined by the Act), shall be given in lieu of the contributions authorised by the Housing Act, 1923, for houses provided by Local Authorities themselves or under schemes promoted by them for the erection of houses by private enterprise or by Public Utility Societies, &c., provided that the Local Authority (or Public Utility Society) undertake that certain special conditions (including a restrictive condition as to rents) will be observed.

459. Under the Housing Acts (Revision of Contributions) Order, 1926, made under Section 5 of the Act, the contribution payable by the Exchequer for houses completed after 30th September, 1927, and before 1st October, 1929, is at the rate of £7 10s. per annum for 40 years, or in agricultural parishes, £11 per annum. The Housing Acts (Revision of Contributions) Order, 1928, made provision for a further reduction of the contributions for houses completed after 30th September, 1929, to £6 per annum (£9 10s. in agricultural parishes), but this provision did not come into force, as the Housing (Revision of Contributions) Act, 1929, restored the rates of £7 10s. and £11 for houses completed after 30th September, 1929. Under Section 43 of the Housing Act, 1930, a further review will take place after 1st October, 1933, of the contributions to be made for houses completed after a date to be specified.

460. By the 31st March, 1931, 336,282 houses had been erected by Local Authorities themselves, 5,823 by private enterprise assisted by Local Authorities, and 1,534 by Public Utility Societies assisted directly by the Minister, giving a total of 343,639 houses provided under the Act. In addition definite arrangements had been made for construction of a further 48,414 by Local Authorities, 1,475 by private enterprise, and 274 by Public Utility Societies.

The annual Exchequer commitment in respect of houses completed by 31st March, 1931, is approximately £2,860,000 continuing until 1965 and then gradually decreasing until 1971.

(iv) HOUSING (RURAL WORKERS) ACT, 1926. £10,000 IN 1931.

461. Under this Act Local Authorities are empowered, where applications are received before 1st October, 1931, to give assistance towards the cost of reconstruction or improvement of houses or buildings in order to provide housing accommodation for agricultural workers and others of like economic condition. Assistance may be given by way of lump sum grant or of annual payments for a period not exceeding 20 years. The value of the grant must not exceed either two-thirds of the estimated cost of the work, or £100 in respect of each dwelling. The application for assistance must under the Act have been made before the 1st October, 1931, but it is proposed under the Bill at present before Parliament to extend the period for a further five years.

Where assistance is given by way of grant, the Minister is authorised to pay contributions equal to one-half of the estimated annual payments falling to be made by the Local Authority in respect of charges on loans raised for the purpose or which would have fallen to be so made if loans had been raised.

462. Up to the 31st December, 1930, assistance had been promised by Local Authorities by way of grants in respect of 4,024 dwellings to a total of £312,329. Work had been finished on the same date of 2,998 dwellings and grants paid to a total of £224,930. Assuming that a further 400 dwellings were completed during the quarter ended 31st March, 1931, and further grants to an amount of £30,000 paid, the annual Exchequer commitment in respect of the dwellings finished at 31st March, 1931, is approximately £10,000 for 20 years.

It may be assumed that further grants amounting to £200,000 will be paid under the Act after 31st March, 1931, which will increase the Exchequer liability under the Act to a total of £18,000 per annum for 20 years.

463. Extension of the operation of the Act for a further five years, will involve an estimated additional Exchequer liability of about £30,000 per annum for 20 years.

(v) HOUSING ACT, 1930—(£200,000 IN 1931).

464. Under this Act Exchequer contributions may be paid in the form of annual payments for 40 years towards expenses incurred by a Local Authority in connection with action taken by them under the Act for dealing with unhealthy areas or for the demolition of insanitary houses or for the closing of parts of buildings, and in connection with the provision and maintenance of housing accommodation rendered necessary by such action.

465. The annual contribution is normally at the rate of £2 5s. for each person displaced by action taken under the Act, in so far as suitable accommodation in new houses has been made available. Increased contributions of £2 10s. per person are payable in the case of persons displaced from agricultural parishes and of £3 10s. per person where rehousing accommodation is provided in tenement buildings of more than three storeys on the site of a cleared area, or on other sites the cost (or in certain case, value) of which exceeds £3,000 per acre. Payment of the contributions is contingent on the observance of certain special conditions as to letting and as to restriction of the rents to be charged in respect of the new houses.

466. No payments have yet been made under this Act. A sum of £200,000 has been provided in the estimates for 1931-32 in respect of Exchequer subsidy.

Total house-building in recent years.

467. The following table shows the total number of houses erected since 31st March, 1924.

Year ended 31st March.	Houses built with State assistance.			Houses built without State Assistance.*	Total No. of houses built.
	By local authorities.		By private enterprise.		
	Under the Acts of				
	1919 and 1923.	1924.†			
1925 ...	18,151	2,473	47,045	69,220	136,889
1926 ...	17,318	26,900	62,769	66,439	173,426
1927 ...	15,003	59,090	79,686	63,850	217,629
1928 ...	13,981	90,053	74,548	60,332	238,914
1929 ...	5,069	50,654	49,069	64,740	169,532
1930 ...	5,631	54,614	50,125	91,691	202,061
1931 ...	—	52,514	2,565	128,728	183,807

468. The large increase shown for the year ended 31st March, 1928, was due to special efforts made to complete houses before the reduction of subsidy on the 1st October, 1927, under the Acts of 1923 and 1924. The increase in the year ended 31st March, 1930, similarly was due to the desire to complete houses before the termination on the 30th September, 1929, of subsidy under the Act of 1923. The number of State-assisted houses under construction on the 31st March, 1929, 1930 and 1931, respectively were as follows. Information is not available as to the number of unassisted houses under construction :—

Number of houses under construction.	On 31st March		
	1929.	1930.	1931.
By local authorities	30,281	27,113	34,504
By private enterprise	25,704	1,064	1,024
Total	55,985	28,177	35,528

* NOTE.—The great bulk of these houses were built by private enterprise. In the year ended 31st March, 1931, the number of houses built without State assistance by local authorities was 3,360. Returns for earlier years did not distinguish houses built by local authorities.

† Including in 1931 16 houses under the Housing Act, 1930.

Future Liability.

469. An estimate has been prepared of the capital value (on a 4½ per cent. basis) at 31st March, 1931, of the outstanding Exchequer liabilities under the various Housing Acts, and we append it together with a statement of the number of houses covered in each case :—

Housing Act of	Capital Value of liabilities at 31st March, 1931.	Number of houses built.
	£	
1919	111,625,000	176,000
1923	27,215,000	436,633
1924	49,672,000	343,639
1926	127,000	3,398
Total	£188,639,000	959,670

470. These figures relate of course to houses already built. Any estimate of the future growth of the annual charge is necessarily very speculative. The following figures have been submitted to us by the Ministry of Health on the basis of surveys prepared by local authorities under the Act of 1930, but with housing subsidies at the present high level they may well be exceeded.

Year.	Housing Act of					Total.
	1919.	1923.	1924.	1926.	1930.	
	£	£	£	£	£	£
1931-2 ...	6,855,000	2,510,000	3,160,000	10,000	200,000	12,735,000
1932-3 ...	6,835,000	2,466,000	3,685,000	16,000	575,000	13,577,000
1933-4 ...	6,825,000	2,466,000	4,210,000	22,000	950,000	14,473,000

471. We view with deep concern this steadily growing charge upon the Exchequer, and the similar though smaller charges on local rates, for the housing of the working classes. There is serious danger of the nation, gradually and without forethought, finding itself committed to the principle that a man's wages are not normally intended to enable him to pay fully for his housing. In our view such a development would be a grave mistake from every point of view, and we can see no ground of principle why it should stop at housing. We regard the principle embodied in the Housing Act, 1924, of a subsidy gradually declining with the cost of housing as thoroughly sound, and we can only regret that the Act has not been applied in accordance with the clear intentions of its authors. We submit a table showing (i) the average cost

of non-parlour houses for each quarter since 1925, (ii) the capitalised value of the subsidy payable under the Act of 1924 in urban areas, and (iii) the rate charged by the Public Works Loans Board for housing loans. In explanation of the last column we would point out that the rate of interest to be paid on the capital has an important bearing on the economic rent necessary to pay for a house and therefore in the need for subsidy. On a house costing £400, repaid over 60 years, a reduction from 5 to $4\frac{1}{2}$ per cent. in the rate of interest is equivalent to a capital subsidy of about £17.

Quarter ended	Average estimated all-in cost per non-parlour house.*	Exchequer subsidy.		Local Loans Rate for Housing.
		Rate per annum for 40 years.	Capital value at 5 per cent.	
	£	£ s. d.	£	Per cent.
31st December, 1925 ...	509	9 0 0	155	$4\frac{1}{2}$
31st March, 1926 ...	513	9 0 0	"	5
30th June, 1926 ...	513	9 0 0	"	"
30th September, 1926 ...	511	9 0 0	"	"
31st December, 1926 ...	503	9 0 0	"	"
31st March, 1927 ...	512	9 0 0	"	"
30th June, 1927 ...	518	9 0 0	"	"
30th September, 1927 ...	494	9 0 0	"	"
31st December, 1927 ...	481	7 10 0	129	"
31st March, 1928 ...	473	7 10 0	"	"
30th June, 1928 ...	477	7 10 0	"	"
30th September, 1928 ...	438	7 10 0	"	"
31st December, 1928 ...	436	7 10 0	"	"
31st March, 1929 ...	430	7 10 0	"	"
30th June, 1929 ...	424	7 10 0	"	"
30th September, 1929 ...	409	7 10 0	"	"
31st December, 1929 ...	419	7 10 0	"	$5\frac{1}{2}$ (15th Oct.)
31st March, 1930 ...	413	7 10 0	"	5 (21st Mar.)
30th June, 1930 ...	419	7 10 0	"	"
30th September, 1930 ...	405	7 10 0	"	"
31st December, 1930 ...	406	7 10 0	"	$4\frac{1}{2}$
31st March, 1931 ...	410	7 10 0	"	"
30th June, 1931 ...	423	7 10 0	"	"
30th September, 1931 ...	419	7 10 0	"	$4\frac{1}{2}$ (3rd July)

* Based on prices of contracts let six months earlier, plus £70 for land, roads and sewers.

472. It will be seen that by the autumn of 1927, when the subsidy was reduced in value by £26, the cost of building had fallen by practically the same amount. In the following two years the average cost showed a further fall of over £60, and on this basis, notwithstanding some increase in the rate of interest, the further reduction of about £26 in the subsidy, which was to be made by

the Housing Acts (Revision of Contributions) Order, 1928, would have been fully justified. Before that Order could come into operation, however, the proposed reduction of subsidies under the Act of 1924 was cancelled by the Housing (Revision of Contributions) Act, 1929 (26th July, 1929), and it is significant that since September, 1929, there has been no fall whatever in housing costs in England and Wales (except in the rate of interest), and this in spite of the facts (1) that the prices of raw commodities generally have fallen heavily and (2) that there has been materially less pressure on the building industry generally during this period than in previous years. **We find it difficult to resist the conclusion that the high rates of subsidy have played a part in keeping up the cost of house building.**

473. Be that as it may, the clear need of the moment seems to us to place the housing subsidies on a basis of principle that shall lead to their entire abolition as regards ordinary working class housing (i.e. apart from slum clearance schemes and special provision for exceptional classes) when building costs (including rates of interest) have fallen to a level reasonably related to the general cost of living for the working classes. Taking as our standard type for this purpose the ordinary non-parlour house, now costing in England and Wales about £410, we are advised that a similar house would have cost just before the war about £250. The Local Loans rate of interest for housing loans was then $3\frac{1}{2}$ per cent. If we take the appropriate rent of such a house (after allowing 20 per cent. for repairs, empties, etc.) as £12 10s. 0d. per annum and assume a rise in the general standard of working class rents of say 40 to 45 per cent., i.e. to about £18, we find that this rent would be sufficient (assuming repairs etc. at 20 per cent. of rent and repayment of loan over 60 years) to provide an economic return on a house costing £327 when interest had fallen to 4 per cent. We suggest that these should be adopted as the standard conditions which should be held to justify the complete withdrawal of subsidies for ordinary house building and that a steady policy of adjustment of the subsidy should be followed with this end in view.

474. The above rent of £18 per annum would suffice to give an economic return :—

	£
With interest at 4 per cent. on	327
" " $4\frac{1}{4}$ "	312
" " $4\frac{1}{2}$ "	298
" " $4\frac{3}{4}$ "	285
" " 5 "	273
" " $5\frac{1}{4}$ "	262

475. In the initial period of the Wheatley Act the average all-in cost of the non-parlour house was £510 and the Local Loans rate was $4\frac{1}{2}$ per cent. On the above table the appropriate subsidy would have been £510 - £285 = £225. The actual capital value of the subsidy at that time was :—

	£	s.	d.
Exchequer grant	155	0	0
Local rates (not exceeding)	77	10	0
	<hr/>		
Total (not exceeding)	£232	10	0
	<hr/>		

which shows that the above assumptions are in close agreement with the financial basis of the Wheatley Act.

476. In the Autumn of 1929 with an average cost of £419 and interest at $5\frac{1}{2}$ per cent. the appropriate total subsidy would have been £419 - £262 = £157. If this had been divided between the Exchequer and local rates in the original proportions, the Exchequer charge would have been £105 or almost exactly that contemplated in the Housing Order of 1928. (£6 per annum for 40 years at 5 per cent. = £103.)

477. At the present time with the interest rate again at $4\frac{1}{2}$ per cent. and total costs at £419, the appropriate subsidy would be £419 - £298 = £121 of which the Exchequer share would be £81, equivalent to a grant of £4 $\frac{1}{2}$ for 40 years. In our view therefore there is ample ground for a reduction of the housing subsidies by £2 10s. per annum and we suggest that this should be applied to all houses completed after the 30th April next, i.e. to £5 in urban areas and £8 10s. in rural areas. A corresponding reduction should be made in the rates of grant under the Housing Act, 1930, which are based upon the subsidies payable under the Wheatley Act. It will readily be gathered from this recommendation that we should find it difficult on any of our principles of housing finance to justify an increase, instead of a decrease, in the Exchequer subsidies for housing in rural areas as contemplated in the Bill now before Parliament.

478. We recommend that further revisions of the subsidies under the Acts of 1924 and 1930 should be made at two yearly intervals, the first with effect from 1st October, 1933, on the basis set out above.

B.—SCOTLAND.

479. The estimate of the Department of Health for Scotland for housing for the year 1931-32 is £1,808,381, made up as follows :—

	£
(i) <i>Housing, Town Planning, &c. (Scotland Act), 1919.</i>	
(a) On Housing Schemes by Local Authorities and Public Utility Societies	976,000
(b) On Slum Clearance—payments from £5,000 Pool	4,986
(ii) <i>Housing &c. Act, 1923.</i>	
(a) On Housing Schemes by Local Authorities and private enterprise	137,855
(b) On payments to Local Authorities by way of Slum Clearance Grant	115,014
(iii) <i>Housing &c. Act, 1924.</i>	
On Housing Schemes by Local Authorities and private enterprise	492,649
(iv) <i>Housing (Rural Workers) Act, 1926.</i>	
On Schemes for the conversion and improvement of dwellings	16,850
(v) <i>Housing (Scotland) Act, 1930.</i>	
On Housing Schemes by Local Authorities	20,000
(vi) <i>Rosyth Housing Scheme.</i>	
On 1,702 houses erected at Rosyth for Admiralty employees	55,027
	£1,818,381
<i>Less (vii) Steel Houses.</i>	
Receipts in respect of 2,552 houses erected on behalf of the Government by the Second Scottish National Housing Company (Housing Trust) Limited	10,000
	£1,808,381

480. Housing since the War has followed much the same course in Scotland as in England. In the main the legislation has been the same for both countries and we need only refer therefore to special Scottish features.

(i) *Housing and Town Planning Act, 1919.*

481. The number of houses erected under this Act was limited to 25,550 costing on the average about £900 each. £8,951,748 had been paid in subsidy up to 31st March last and the present annual charge of £976,000 is expected to fall to £954,663 in 1932-33 and to decrease to about £850,000 by 1945 as a result of repayment of loans and increase of the rate deduction. 78 per cent. of the loans are for periods of 3, 5 and 7 years and have already been renewed at lower rates of interest.

(ii) *Housing &c. Act, 1923.*

482. The Exchequer grant under this Act, as in England, was originally £6 per annum for 20 years. Owing to the slower progress of housing in Scotland and to the somewhat higher cost of building no reduction was made either under this Act or under the following Act of 1924 when the first abatements were made in England in 1926 but under the Housing Acts (Revision of Contributions) Order, 1928, made under Section 5 of the Housing (Financial Provisions) Act, 1924, the contribution payable by the Exchequer for houses completed after 30th September, 1929, was reduced from £6 to £4 per annum.

(a) *Private enterprise.*

483. As far as private enterprise is concerned the general practice of local authorities in Scotland is to make the payment by way of a lump sum. Before the reduction of the Exchequer contribution the amount of assistance offered by local authorities varied from £75 (the capital equivalent of the Exchequer contribution) to £150 per house. After the reduction of the Exchequer contribution in 1929, the lump sum offered by the local authorities has varied from £50 to £75 or thereabouts. The amount of grant paid by local authorities in excess of the Exchequer contribution is met out of local rates.

484. The position of building by subsidised private enterprise (including Public Utility Societies) at 31st March, 1931, was as follows:—

Houses completed	...	...	...	...	19,409
„ under construction	...	...	...	...	1,424
„ approved, but not yet begun	...	...	...	...	1,122
Total	...	...	...	...	<u>21,955</u>

The annual Exchequer contribution for 1931-32 is estimated at £113,657. Houses are being built at the rate of 1,400 per annum.

(b) *Local Authorities.*

485. Building by local authorities under this Act has ceased, as they prefer to build with the aid of the larger subsidy under the Housing (Financial Provisions) Act, 1924. Altogether local authorities have built 4,033 houses under the Act of 1923 (excluding slum clearance houses, to which reference is made in the next paragraph).

(c) *Slum Clearance.*

486. Section 1 (3) of the Act provided for an annual contribution not exceeding one-half of the average loss incurred by local authorities in providing houses for persons dispossessed consequent upon slum clearance schemes. This grant has been superseded by the grant under the Housing (Scotland) Act, 1930, but will continue to be paid in respect of commitments entered into by the Department with local authorities prior to the coming into force of the Act of 1930. The position of building under this scheme at 31st March, 1931, was as follows :—

Houses completed	12,972
„ under construction	1,762
„ approved, but not yet begun	256
„ not yet approved	2,626
Total	<u>17,616</u>

(iii) *Housing (Financial Provisions) Act, 1924.*

487. Under the Housing Acts (Revision of Contributions) Order, 1928 (the Order of 1926 did not apply to Scotland) made under Section 5 of the Act, the contributions payable by the Exchequer for houses completed after 30th September, 1929, were to be reduced to £7 10s. per house per annum for 40 years, or in rural areas to £11 per house per annum. This revision, however, did not come into force, as the Housing (Revision of Contributions) Act, 1929, restored the original rates.

At 31st March, 1931, the position of building was as follows :—

	<i>By local authorities.</i>	<i>By private enterprise.</i>	<i>Total.</i>
Houses completed	49,314	3,093	52,407
„ under construction	5,336	152	5,488
„ approved, but not yet begun	2,781	1,241	4,022
Total	<u>57,431</u>	<u>4,486</u>	<u>61,917</u>

(iv) *Housing (Rural Workers) Act, 1926.*

488. Up to 31st March, 1931, assistance had been promised by local authorities by way of grants in respect of 7,662 dwellings to a total of £662,973, or at the rate of £85 per house. The annual Exchequer contribution in these cases was approximately £26,600, or nearly £3 10s. per house per annum. The Exchequer contribution in respect of houses covered by applications estimated to be received by 30th September next and approved for grant is £33,000. If the Act is extended for a further five years as now proposed, it is estimated that a further 15,100 houses will be improved in Scotland with the aid of grants as from September, 1931, to September, 1936. On the basis of the present grants, the average additional Exchequer liability will be about £10,000 for each of the additional five years. On these estimates, the total increase of Exchequer liability at the end of five years will be approximately £50,000 per annum, making, with the estimated annual liability of £33,000 at the end of September, 1931, a total annual liability of £83,000, declining from 1947 onwards as the loans of the local authorities are repaid. The charge on local rates will be equal to that on the Exchequer.

(v) *Housing (Scotland) Act, 1930.*

489. No payments have yet been made under this Act. A sum of £20,000 has been provided in the estimates for 1931-32 in respect of Exchequer subsidy.

(vi) *Other Housing Schemes.*

490. No further houses are now being built under the Rosyth Housing Scheme (1,702 houses) or the Steel Houses Scheme (2,552 houses). Little variation in the present liability is possible, so we need not enter into the details of the arrangements.

Total House-building.

491. The following table shows the total number of houses built in Scotland in recent years :—

Year.	With State assistance.	Without State assistance.	Total.
1926	13,592	1,212	14,804
1927	20,158	2,017	22,175
1928	18,096	2,147	20,243
1929	18,240	1,275	19,515
1930	11,056	1,361	12,417

Future Liabilities.

492. The following table gives the estimated expenditure under the various Acts during the three years 1931, 1932 and 1933 :—

Year beginning 1st April.	Housing Act of					Rosyth Housing Scheme.	Govern- ment Steel Housing Scheme.	Total.
	1919.	1923.	1924.	1926.	1930.			
	£	£	£	£	£	£	£	£
31 ...	980,986	252,869	492,649	16,850	20,000	55,027	—10,000	1,808,381
32 ...	959,649	275,469	604,849	23,400	188,000	55,000	—15,000	2,096,367
33 ...	957,149	286,369	717,049	39,600	356,000	55,000	—15,000	2,396,167

493. The capitalised value as at 31st March, 1931, of the balance of Exchequer subsidies due in respect of assisted housing schemes was :—

	£	No. of houses built.
<i>Housing, Town Planning, &c. (Scotland) Act, 1919</i>	17,808,000	25,550
<i>Housing, &c., Act, 1923.</i>		
General	1,490,007	23,442
Slum Clearance	2,068,572	12,972
<i>Housing (Financial Provisions) Act, 1924.</i>		
General	8,014,985	52,407
<i>Housing (Rural Workers) Act, 1926</i>	311,555	7,662
	<u>£29,693,119</u>	<u>122,033</u>

Cost of Building in relation to Subsidy.

494. The following table gives the average cost of all subsidised houses quarter by quarter since 1925 and the percentage of total cost represented by the subsidy under the Wheatley Act (1924) which has remained unaltered throughout at £9 per annum for 40 years—capital value £155.

Period.	Average Total Cost.	Percentage of Cost defrayed by State Subsidy.
1925—	£	
1st Quarter	466	33·0
2nd " 	491	31·4
3rd " 	471	32·7
4th " 	444	34·7

Period.	Average Total Cost.	Percentage of Cost defrayed by State Subsidy.
1926—	£	
1st Quarter	447	34.4
2nd "	461	33.4
3rd "	447	34.4
4th "	465	33.1
1927—		
1st Quarter	433	35.6
2nd "	443	34.8
3rd "	449	34.3
4th "	436	35.3
1928—		
1st Quarter	418	36.8
2nd "	406	37.9
3rd "	424	36.3
4th "	389	39.6
1929—		
1st Quarter	370	41.6
2nd "	393	39.2
3rd "	380	40.5
4th "	380	40.5
1930—		
1st Quarter	372	41.4
2nd "	356	43.3
3rd "	361	42.7
4th "	357	43.1

495. Comparing this table with that on page 182 it will be observed that these figures of cost have throughout been some £50 less than the average for the English non-parlour house.

496. The proportion of cost represented by the subsidy in England is now about 31 per cent. We are aware that the difference in cost is attributable to the fact that the typical Scottish house is rather smaller than the typical English house, and that the English type would actually cost somewhat more to build in Scotland. But this does not in our view warrant the present differentiation in favour of Scotland, neither can we see any good reason for giving Scotland more favourable treatment because her local authorities may have been somewhat slower in taking advantage of the facilities available.

497. In our view this disparity of treatment should be brought to an end as soon as this can conveniently be arranged. We recommend that the Scottish rates of subsidy under the Housing Acts of 1924 and 1930 should be reduced in respect of houses completed

after April next by the same amounts as in England, that the subsidy under the Act of 1923 should then be entirely withdrawn, and that as from 1st October, 1932, all subsidy rates in Scotland should be brought down to the rates applicable to houses completed after that date in England.

7.—EDUCATION.

498. The total net expenditure of local education authorities in England and Wales on elementary and higher education within the purview of the Board of Education has increased since 1913-14 from £30,010,000 to £83,690,000 (estimated) for the current year. In 1921-22 the total reached a maximum of £73,146,000: it then declined to £67,602,000 in 1923-24. In the last eight years therefore, there has been an increase of £16,000,000 and apart from the raising of the school-leaving age (which was estimated to involve an additional expenditure of £6,250,000 in the first full year rising to £8,000,000 in the year 1935-36) it is estimated that the total net expenditure of local education authorities will have increased by a further £3,500,000 by 1932.

499. This is by no means the whole cost of education in this country. Assistance is given both by the State and by local authorities to university education and by the State to a large number of schools managed by governing bodies and the total charge on public funds for 1913-14 and for each year since 1922-23 is shown in the following table:—

Year beginning 1st April.	Total population of State-aided schools.	Amount falling on Rates.	Amount falling on Taxes.	Total	Total Average Cost per Child.	Pro-portion met from Taxes.
		£	£	£	£	Per cent.
1913 ...	6,234,710	16,212,000	15,599,000	31,811,000	5·1	49·0
1922 ...	6,167,148	31,925,000	43,606,000	75,531,000	12·2	57·7
1923 ...	6,055,263	29,853,000	42,861,000	72,714,000	12·0	58·9
1924 ...	5,953,256	30,841,000	43,595,000	74,436,000	12·5	58·6
1925 ...	5,927,186	31,872,000	44,244,000	76,116,000	12·8	58·1
1926 ...	5,946,347	32,543,000	44,532,000	77,075,000	12·9	57·8
1927 ...	5,968,513	32,898,000	45,244,000	78,142,000	13·1	57·9
1928 ...	5,948,746	34,965,000	44,603,000	79,568,000	13·4	56·1
1929 ...	5,899,278	36,824,000	45,540,000	82,364,000	13·9	55·3
1930 (Est.)	5,921,218	37,474,000	46,874,000	84,348,000	14·2	55·6
1931 (Est.)	5,931,786	38,977,000	49,855,000	88,832,000	15·0	56·2

500. The table shows that the total cost of this service to public funds has nearly trebled since 1913-14 and that whereas the amount falling on rates has risen by 140 per cent. the amount falling on taxes has increased 220 per cent.

501. Many causes have conduced to this rapid expansion not the least of which has been the great transference of charge from the administering authorities to the Exchequer and the placing of a powerful lever in the hands of the Board of Education in the form of percentage grants. In using this lever to urge on local authorities the Board have admittedly had behind them a weighty force of public opinion. Educational progress has been a popular plank in election platforms since the war and we fear that a tendency has developed to regard expenditure on education as good in itself without much consideration of the results that are being obtained for it and of the limits to which it can be carried without danger to other, no less vital, national interests.

502. Since the standard of education, elementary and secondary, that is being given to the child of poor parents is already in very many cases superior to that which the middle class parent is providing for his own child, we feel that it is time to pause in this policy of expansion, to consolidate the ground gained, to endeavour to reduce the cost of holding it, and to reorganise the existing machine before making a fresh general advance.

503. First among the changes that we consider necessary in the interests of efficient administration we would place the reduction in the number of authorities by the concentration of all educational functions, as far as local authorities are concerned, in the hands of the county and county borough councils. There are 317 Local Education Authorities for elementary education and 146 Local Education Authorities for higher education. The authorities for elementary education consist of London, 62 counties (excluding London), 83 county boroughs, 131 boroughs and 40 urban districts, making a total of 317. The Authorities for higher education consist of London, 62 counties (excluding London) and 83 county boroughs, making a total of 146.

504. The local bodies which are Local Education Authorities for elementary but not for higher education are now 131 boroughs which, according to the Census of 1901 had populations of more than 10,000, and 40 urban districts which had populations of more than 20,000. (These are commonly known as "Part III Areas" because their duties are primarily those imposed upon them by that part of the Education Act, 1902.) Consequently the 62 counties which are authorities for elementary education do not comprise the same areas as the 62 counties which are authorities for higher education, because they only administer so much of the areas as remain after the 131 boroughs and the 40 urban districts have been taken out of them. As authorities for higher education, however, the 62 counties comprise the whole area within the county boundaries excepting only that of the county boroughs. We do not question the high efficiency in their limited sphere of many of the minor authorities now exercising powers over some part

of the educational field, but the service is now developing under the recommendations of the Hadow Committee in a manner which is rapidly breaking down the old distinction between elementary and higher education. The dividing line of the future will be less between elementary and higher education than between education under and over 11 years of age. As long as the Part III areas remain there will be overlapping jurisdiction, competition and confusion in the education of the older children. Another important tendency in educational progress is towards the development of more specialised services which it would be wasteful for many of the smaller units to provide. We would further point out that the present division of the administration of the elementary education service among 317 authorities inevitably means that many of these areas contain abnormal communities, some especially wealthy and some so poor as to require an exceptional measure of State assistance. Of the 29 areas receiving the Necessitous Areas Grant (referred to below) no less than 22 are Part III areas. The action which we recommend in regard to this service with a view to increasing efficiency and reducing rate inequalities would be in complete agreement with the general policy of the Local Government Act, 1929, in regard to other services of national importance.

505. It would be an essential part of this reform that the county councils and county borough councils should take over from the Board of Education the entire responsibility for supervising and helping, where necessary, private educational effort in their areas.

These changes would remove the chief obstacles to bringing this service within the block grant system set up under the Local Government Act. Under that system the element of local responsibility would be increased and the Board of Education would be able to substitute a general advisory supervision of the service for its present meticulous control.

506. We realise however that such reforms will take a considerable time to effect and we accordingly submit recommendations for such temporary adjustments as seem to us desirable in the meanwhile.

1. *Elementary Education.*

507. The existing main grant for elementary education is given by the formula :—

- (a) 36s. a child in average attendance;
- (b) 60 per cent. of teachers' salaries;
- 50 per cent. of special services, maintenance allowances, and, as regards the period 1st September, 1929 to 31st August, 1932, loan charges and other expenditure on reorganisation and development;
- 20 per cent. of remaining expenditure;

(c) From the sum of (a) and (b) is subtracted the produce of a rate of 7d. in the £ for the area;

(d) If the result is less than 50 per cent. of the net expenditure the grant is made up to this proportion.

This formula originated with the proposals of the Kempe Committee of 1914, but the percentage element in the formula recommended by that Committee was limited to 40 per cent. The increase to 60 per cent. in the case of teachers' salaries was given in order to induce local authorities to increase the general standard of teachers' remuneration. That object has not only been fully achieved but in our view there is now urgent need for a reduction. We recommend in Chapter III of this report that this reduction should be not less than 20 per cent. Inasmuch as the increase of teachers' salaries was made the occasion for raising the percentage grant towards such expenditure we now recommend that the benefit of this reduction should be secured to the Exchequer by reducing the grant to 50 per cent.

At the same time the special increase of grant in respect of loan charges and expenditure on reorganization and development incurred during the three years 1929-32 should be withdrawn forthwith subject to the honouring of existing commitments.

508. Were the existing minimum limit of grant of 50 per cent. (under (d) above) to continue in force, these recommendations would be inoperative in the wealthier areas of the country, because any reduction of grant thereunder in these areas would be made up under the guarantee. This would be quite unjustifiable. We understand that the 50 per cent. minimum formed no part of the Kempe Committee's recommendations. It does in fact tend to defeat one of the most important objects of the formula recommended by that Committee, viz., the differentiation of the grant between rich and poor areas, and we recommend that it be withdrawn.

509. In making these recommendations, which involve loss of grant to the richer authorities and the loss of a possible saving to all, we have taken into account the fact that the reduction of the produce of the rate of 7d. in consequence of the derating of industrial and agricultural property under the Local Government Act did in fact result in an increase of about £1,000,000 in the education grant, which we understand was entirely additional to the relief intended to be given to local authorities as set forth in the financial memorandum attached to the Local Government Bill.

510. Another exception to the plain working of the elementary education grant formula is afforded by a limited group of necessitous areas. Prior to 1930, areas which after receipt of the formula grant would have had a rate burden for this service exceeding 3s. 6d. in the £ were given an extra grant of 50 per cent. of the excess; the

amount so distributed in 1929 being £250,000. Thus any additional expenditure attracting the ordinary formula grant of 50 per cent. or 60 per cent. fell as to 75 per cent. or 80 per cent. on the Exchequer. It is not surprising to find that under this strong incentive to expenditure the cost of education in many of these areas has risen to a very high figure. Owing to the alterations made by the Local Government Act this basis of distribution is no longer workable and pending the formulation of a new scheme the distribution has been stereotyped on the 1929-30 basis with an addition of 20 per cent. We have already pointed out that many of these areas are financially too weak to form suitable independent units of administration and the majority would be merged in larger areas under the reforms recommended above. **Pending this—in our opinion the only proper remedy—we recommend that any revised basis of distribution should avoid the strong incentive to expenditure contained in the old scheme.** We recognize that in so doing it will in all probability be necessary to widen the field of distribution of the grant and on this account we have allowed for some increase of the existing amount of £300,000.

2. Higher Education.

511. Higher Education comprises a wide field of activities. In so far as these are carried on by local authorities the State contributes one half of the cost that would otherwise fall on the rates. To other bodies the State makes various grants on a capitation basis. Complete information as to the cost of higher education in this country is not available. The net expenditure of local education authorities in recent years is shown on page 196.

HIGHER EDUCATION.

Net Expenditure of Local Education Authorities over a series of years.

Year beginning 1st April. 1.	1913-4.	1921-2.	1922-3.	1923-4.	1924-5.	1925-6.	1926.	1927.	1928.	1929.	1930.	1931.	
	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	L.E.As. October Ests. 12.	Assumed for Board of Educa- tion Est. 13.	
	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	£'000.	
1. Colleges etc. for the Training of Teachers.		457	378	324	330	325	317	309	288	282	332	320	
2. Secondary Schools	Details	5,295	4,912	4,496	4,743	4,980	5,029	5,568	6,176	6,471	6,894	7,200	
3. Technical, etc., Schools ...		3,670	3,153	2,938	3,143	3,368	3,334	3,610	3,733	3,967	4,196	4,300	
4. Loan Charges	not	640	717	720	718	751	832	956	1,110	1,250	1,483	1,660	
5. Administration and Inspection.		672	648	605	664	714	726	735	703	712	751	750	
6. Aid to Students	avail-	1,383	1,571	1,589	1,621	1,695	1,769	1,870	1,982	2,099	2,257	2,320	
7. Other Expenditure		334	276	194	195	202	231	191	261	252	442	450	
8. Employers' Pension Contributions.	able.	—	—	—	—	—	—	—	*276	*271	*293	400	
9. TOTAL		4,403	12,451	11,655	10,866	11,414	12,035	12,238	13,239	14,529	15,304	16,648	17,400

* These contributions are in respect of teachers in Maintained Institutions only, and exclude any aid given by Local Education Authorities to non-Local Education Authority Institutions to meet the cost of such contributions.

512. Prior to the war the Exchequer contribution towards this expenditure was in the main on a capitation basis but under the Education Act, 1918, it was placed on a 50 per cent. basis. Up to 31st March, 1930, £807,000 of the grant was paid through the Local Taxation Account, the balance being provided on the Board of Education Vote, but since that date the whole amount has been so provided.

513. The Geddes Committee commented on the "extreme rapidity" with which this expenditure was expanding at the time of their enquiry, the preliminary estimates for 1922-3 being as high as £16,200,000. The national movement in favour of economy brought the actual expenditure for that year down to £11,655,000, and it was not till 1927 that the expenditure of 1921 was exceeded. Since then the growth has averaged £1,000,000 a year. Part of this growth has been the result of the transfer of schools from the category of those aided directly by the Board of Education to that of schools aided by the local authority (with the assistance of a State grant). This transfer followed the recommendation of the Geddes Committee that no school should receive grant through both channels, and was effected over a period of years as is shown by the table below of grants for higher education to bodies other than local education authorities:—

Grants for Higher Education to Bodies other than Local Education Authorities.

Financial Year.	Training of Teachers.	Secondary	Technical	Grants in respect of Employers' Contributions under Teachers (Super-annuation) Act, 1925.	Central Welsh Board.	Total.
	£	£	£	£	£	£
1913-14 ...	Figures not available.					
1921-22 ...	803,261	1,089,188	107,920	—	—	2,000,369
1922-23 ...	723,677	1,278,380	103,366	—	—	2,105,423
1923-24 ...	675,805	1,154,812	113,473	—	—	1,944,090
1924-25 ...	721,887	1,141,132	110,098	—	—	1,973,117
1925-26 ...	665,972	1,140,352	107,570	—	—	1,913,894
1926 ...	669,494	1,193,025	116,424	—	—	1,978,943
1927 ...	698,739	822,587	103,548	—	4,600	1,629,474
1928 ...	695,222	506,121	105,481	35,254	4,993	1,347,071
1929 ...	731,823	508,930	111,735	42,265	4,925	1,399,678
1930 ...	787,054	605,800	118,600	42,500	5,000	1,558,954
(Estimate)						
1931 ...	822,170	602,250	130,500	42,500	7,200	1,604,620
(Estimate)						

514. Under the operation of the percentage grant to local education authorities the Exchequer will obtain one half of the saving in teachers' salaries (resulting from our recommendation in Chapter III) as far as their own institutions are concerned. Steps should be taken to secure a similar saving to the Exchequer as regards institutions aided by local education authorities. Grants to bodies other than local education authorities are mainly on a capitation basis. We recommend that the rates of grant be revised to give the Exchequer the benefit of one half of the saving to be anticipated on teachers' salaries in these cases also. The total Exchequer saving to be made in the field of higher education from the reduction of teachers' salaries we estimate at about £950,000.

515. In addition we consider that steps should be taken to slow down the rapid growth of expenditure from public funds on secondary education resulting both from the provision of additional schools and also from the steady increase in the proportion of free places in such schools. Since 1920 the number of free places in secondary schools has practically doubled, while the number of fee payers has shown little change. The following table shows the position up to October 1930, the latest date for which figures are available :—

Date.	Pupils paying fees.	Pupils paying no fees.	Total.
31st March, 1920	206,891	101,375	308,266
" " 1922	221,584	133,372	354,956
" " 1924 ...	215,128	134,013	349,141
" " 1926 ...	217,261	143,242	360,503
" " 1928 ...	217,187	160,353	377,540
" " 1929 ...	217,739	169,254	386,993
1st October 1930 (estd.)	218,961	198,024	416,985

Plans for new schools already approved and in course of erection are estimated to bring the above total up to about 440,000, of which roughly one half will be free places.

516. Taking into account the very large provision for secondary education made in institutions not aided from public funds and the certainty of a marked decline in the number of children of secondary school age in the near future owing to the heavy fall in the birth-rate since 1920, we consider that this provision should in present financial circumstances be regarded as adequate.

517. We are further of the opinion that a large proportion of the total expenditure can and should be met from fees charged to parents who can afford to pay them. The present system under which certain local authorities have been allowed to free their schools entirely—and, through the percentage grant, to throw one half the cost of this local benefit on to the country generally, which has not adopted this policy—seems to us inequitable.

This situation will be fully met by the general reform of educational administration and grants recommended above, but in the meantime we think that the existing policy in regard to fees should be reviewed. While local authorities should be free to charge, or not to charge, fees as they choose, we suggest that the State grant to any area with an average fee income per scholar below the national average for the preceding year should be based on the assumption that that average fee income is in fact received. **We recommend further that the grant of a free place should be conditional on the parent being able to show that he cannot afford even a modified fee.** In other cases the scale of fees should be increased more nearly to the standard of what the parent would be willing to pay to a private school. In these ways we consider that it should be possible to increase the total income from fees by not less than 25 per cent., or roughly £1,000,000, of which one half should be secured to the Exchequer by the operation of the 50 per cent. grant or by an alteration in capitation rates.

518. Finally, reference must be made to the fact that on existing policy the Exchequer charge in respect of education is estimated to be about £2,250,000 more in 1932 than in 1931, and that amount, with a proportionate increase for Scotland, has been included in the forecast on page 9. £350,000 of this will be required for the rapidly growing charge for teachers' pensions and a considerable further sum may be needed to meet other unavoidable commitments, but we trust that if local authorities recognize the urgent need for economy at the present time, the increase will be limited to £1,000,000.

519. The financial effect of the foregoing recommendations may be summarized as follows :—

England and Wales	£
1. Abolition of 50 per cent. minimum limit of grant	1,450,000
2. Reduction of teachers' salaries by 20 per cent. and of the grant in respect of teachers' salaries from 60 per cent. to 50 per cent. after allowing for reduced pension contributions, and increase of grant to poor areas	7,800,000
3. Reduction of grants for higher education in consequence of	
(1) 20 per cent. reduction of teachers' salaries	950,000
(2) increase of school fees	500,000
4. Reduction of growth of education expenditure in 1932	1,250,000
Total for England and Wales ...	£11,950,000

£

5. The grant for education in Scotland varies with the corresponding grant for England in the ratio of 11: 80. The corresponding saving in Scotland will therefore be ...	1,640,000
making a total of	£13,590,000
	say £13,600,000.

This represents the total reduction in the first full year. As, however, the education grants are paid as to 90 per cent. on account each year, the balance being adjusted in the following year, the saving in 1932 would be only 90 per cent. of this sum, but we trust that the general effect of our recommendations would be to effect a greater reduction than £13,500,000 as compared with the expenditure that would otherwise have been incurred in subsequent years. The amount is large because the growth of expenditure has been large. None of the reductions we recommend involves the withdrawal of any educational facility now being afforded.

Grants to Universities.

520. The State grants to universities are made on the recommendation of a Treasury Committee from a Special Vote. In 1922 the total sum available for distribution (which had been increased from £1,250,000 to £1,500,000 in 1920) was reduced on the recommendation of the Geddes Committee to the previous figure of £1,250,000, but the increase of £250,000 was again made on a review in 1925. On the next quinquennial review in 1930 the total sum was further increased to £1,750,000 for the next 5 years. We understand that in so far as the increased grants have been applied by universities to recurrent needs they have gone largely to increase salaries. Having regard to our recommendations in other fields of education we consider that this extra £250,000 should be discontinued.

521. We are informed that no small part of the growing needs of the universities represents the maintenance of additional institutions provided out of capital benefactions. In some cases, we understand, the rule has been adopted of only accepting capital benefactions where a suitable portion of the amount has been allocated as an endowment fund, and we commend this rule for general adoption.

CHAPTER VII.

MISCELLANEOUS.

1. WAR PENSIONS.

522. Pensions in respect of service in the Fighting Forces in the war are payable by the Ministry of Pensions established in 1916. Pensions to merchant seamen and fishermen payable under the War Risks Compensation Schemes set up in 1915 are charged to a separate Vote—Merchant Seamen's War Pensions—administered by the Board of Trade. The expenditure from these Votes for the last ten years has been as follows :—

Year.	Ministry of Pensions.	Merchant Seamen's War Pensions.
	£	£
1921	95,304,757	504,930
1922	80,126,694	502,679
1923	72,109,690	486,439
1924	69,460,194	479,048
1925	66,856,268	464,494
1926	63,131,867	451,402
1927	59,744,312	430,689
1928	56,707,700	409,129
1929	54,080,383	391,897
1930 (Est.)	51,850,000	375,392
1931 (Est.)	50,039,000	357,488

The general principles of administration of the Merchant Seamen's Schemes closely follow those adopted by the Ministry of Pensions from time to time in regard to the main scheme and it will be convenient to restrict detailed consideration to the latter.

523. The table below indicates the probable course of expenditure on the Ministry of Pensions in the immediate future :—

Head of Expenditure.	Estimated 1931-32.	Estimated 1936-37.	Estimated 1941-42.
	£	£	£
Administration	1,039,500	860,000	710,000
Pensions, etc.	47,024,500	39,980,500	35,224,000
Medical Treatment	1,505,000	1,057,000	720,000
Treatment Allowances (excess over pension).	470,000	290,000	190,000
Miscellaneous	22,000	10,500	5,000
Gross Total£	50,061,000	42,198,000	36,849,000
Appropriations in Aid	22,000	15,000	10,000
NET TOTAL£	50,039,000	42,183,000	36,839,000

Estimates prepared by the Government Actuary in connection with the Widows' Orphans' and Old Age Pensions Scheme in 1925 showed that the charge would not fall to one half of the present amount for twenty years and that even in 1965 the country would still be paying £10,000,000 for pensions for a war fought nearly half a century before. These forecasts are necessarily based on the assumption that the general principles on which the liability of the State for compensation is determined remain in substance unimpaired. The creation of any new class of pensioner or relaxation of the existing standards of title to pension would at once throw out these estimates, and might indeed convert a slowly diminishing expenditure into an increasing one.

Expenditure on administration.

524. At the time of the Geddes Committee on National Expenditure (1922) the cost of administration was £5,524,100, which was equivalent to 1s. 2½d. per £ of benefit expenditure. For the current year the expenditure is estimated at £1,039,500, representing 5½d. per £ of benefit expenditure. Some further contraction in the cost of administration should still be effected as the volume of the Ministry's work is reduced.

Medical Treatment.

525. The medical expenditure of the Ministry has shown a substantial decline and is still decreasing. The decrease of expenditure follows on the diminished demand for medical treatment, of which the most costly portion is, of course, hospital treatment. At the time of the Geddes Committee, 1921-22, the hospital treatment accounted for £5,750,000 out of a total expenditure on medical treatment of £7,300,000; in the current year it is estimated to amount to not more than £1,130,000. The latter sum is made up of:—

	£
Hospitals and clinics controlled by the Ministry ...	265,000
Red Cross, and other voluntary institutions, including Public Civil Hospitals	370,000
Sanatoria for Tuberculosis	100,000
Public Mental Hospitals	395,000
	<hr/>
	£1,130,000
	<hr/>

The number of the Ministry's own hospitals has been substantially reduced. In 1921-22 the Ministry were controlling and maintaining 67 hospitals with a bed accommodation of 13,970 and 115 clinics. In the current year Ministry institutions number 16 hospitals with a bed accommodation of 2,349 and 24 clinics, and by the end of the year two, and possibly three, of these hospitals will have been closed.

The Ministry have been able to utilise the accommodation of a number of Red Cross and other Voluntary Hospitals as well as public civil hospitals, the accommodation of which is paid for usually by a capitation fee per case, and the Ministry have found it of advantage to use these in view of the general decline in the need for treatment in preference to maintaining institutions of their own. We understand that a close watch is accordingly kept upon hospital accommodation and Ministry institutions are closed where their continued maintenance is no longer justified.

526. Some further concentration of hospital accommodation may be expected, but a nucleus of hospitals, properly distributed with regard to the needs of various parts of the country, will be necessary for some years to come. There will be for some time a number of wound and injury cases, of severe neurasthenic and quasi-mental cases and some other special classes whose condition will periodically require treatment and who can be more advantageously dealt with in institutions where their case history is known.

Pensions and Treatment Allowances.

527. The annual decline in the cost of pensions and treatment allowances is a net figure representing the balance between the known factors of decrease and increase. The former comprise deaths among all classes of pensioners (at present about 22,000 annually) : remarriages of widows (a diminishing number) : children ceasing to be of dependent age (16) and entitled to allowances (a substantial but rapidly diminishing factor, which will disappear by 1936-37) : and reduction of pension (a diminishing factor, though never wholly disappearing) and in the amount of medical treatment required. The factors of decrease are known and can be estimated with tolerable accuracy. The factors of increase are more uncertain, as for example fresh grants of pension to widows and dependants (at present about 2,000 a year) : fresh grants in cases of late claims for disablement—a comparatively small number, which will probably diminish : increase of pension on re-assessment (an uncertain factor liable to be affected by climatic conditions, unemployment, etc.) : and minor grants of various kinds needed for education, sickness, etc.

528. One factor which the Geddes Committee contemplated as operating to reduce the cost of pensions was a reduction of the rates of pension in accordance with the fall in the cost of living.

529. The improved rates of pensions made effective by the Royal Warrant of 1919 were deemed to be based on the cost of living for that year (average index figure of Ministry of Labour 115.25) and Article 24A provided that such rates should be subject to increase or decrease in accordance with the increased or decreased cost of

living as compared with that for 1919. For this purpose a certificate was issued by the Minister of Labour in January of each year showing the cost of living for the previous year as compared with the year 1919. The cost of living is defined to be the general cost of living of working class families.

530. It was further provided that no re-adjustment of rates should take effect before the 1st April, 1923, and then only if the cost of living for 1922 differed from that for 1919 by at least 5 per cent. of the cost of living in 1919, and similarly, subsequent annual adjustments would be made only if the variation in the cost of living since the previous re-adjustment amounted to 5 per cent. of the cost of living in 1919. Certain minimum rates, below which reduction should not be made, representing generally the rates of pension in force before the Warrant of 1919, were scheduled in the Warrant. These minimum rates are equivalent approximately to the pensions payable under the terms of Article 24A when the Ministry of Labour index figure stands at 72.

531. The cost of living for the year 1922 was certified by the Minister of Labour to be 85 per cent. of that in 1919 so that on the 1st April, 1923, a re-adjustment of rates to the extent of 15 per cent. was indicated, but in November 1922, in reply to a question asked in the House of Commons, the Minister stated that the Government had decided that no revision of pension under Article 24A of the Royal Warrant on account of the fall in the cost of living should be made within a period up to three years after the 1st April, 1923. During this interval the practicability of a settlement of pension rates on a less fluctuating basis than that provided under Article 24A was engaging the attention of the Government. In June 1925, in the House of Commons, the Minister announced that as a temporary measure, pending a more permanent settlement, the Government had decided to extend the period of immunity from reductions in respect of the declining cost of living until at least March 1927.

532. At the end of July 1925 (when the index figure of the cost of living stood at 73) this question was again raised in the House and in reply the Minister, at somewhat greater length, reviewed the essential facts from the date of the Warrant of 1919 and explained that it was always the view of the Government that the operation of the Warrant in regard to rates should, in the interests of pensioners, be conditional on a reasonable stability being reached in the cost of living. After full consideration of all the known factors the Government of the day decided that a substantially larger measure of security than had already been announced could

be given to the pensioner and that no change in the rates then current would be made so long as the average cost of living remained between 60 per cent. and 115.25 per cent. in excess of the pre-war cost of living and furthermore, to give still further security to the pensioner, the cost of living would be on an average over three years instead of one year and that such average would not operate before 1929.

533. In July 1928 a further step was taken. The index figure of the cost of living stood then at 65 and looked like being fairly stabilised at or about that figure. The Government considered it desirable to remove both the uncertainty felt by pensioners and also, a recurrent subject of political contention, by settling finally the rates of pension. The Minister accordingly made public the Government's decision that existing rates should be stabilised so far as they were dependent on the cost of living. It was, however, made a condition of the maintenance of these rates that should any substantial change be made in the principles of pension administration involving the admission of new classes of pensioners, to whom the existing high rates of pensions would automatically become applicable, the Government of the day must be free to review the rates of pension in the light of its aggregate liability.

534. Were the adjustment in respect of the fall in the cost of living now brought into effect the saving on the Vote for this year would we are informed be no less than £6,250,000. While it is true that at the time that the announcement in July 1928 of stabilisation was made by the late Government no one anticipated a further large fall in the cost of living we nevertheless feel that the announcement in July 1928 prevents any re-opening of this question except as part of any comprehensive scheme of reduction of pension charges of all kinds. We refer to this aspect of the matter in our concluding chapter. We must however stress the qualifying condition governing the promise of stabilisation viz. that there should be no substantial change in the principles of pension administration.

2.—BRITISH BROADCASTING CORPORATION.

535. The agreement between the Post Office and the British Broadcasting Corporation dated 1st January, 1927, provides (clause 18) that, subject to the provision of funds by Parliament, the Post Office shall pay annually to the Corporation the following percentages of the gross revenue derived from wireless receiving licences

issued in the preceding year, after deducting $12\frac{1}{2}$ per cent. for cost of collection and administration :—

	<i>Per cent.</i>
On the 1st million licences	90
On the 2nd million licences	80
On the 3rd million licences	70
And on all licences over 3 millions	60

536. The agreement also provides that the Postmaster General will consider any application made by the Corporation after 1st January, 1929, for an increase in these payments on the ground that they are insufficient for the performance by the Corporation of its obligations under its Charter and Licence.

537. By a Supplementary Agreement dated 11th June, 1931, the percentage deducted for cost of collection was reduced from $12\frac{1}{2}$ to 10 and provision was included for the payment, subject to the approval of Parliament, to the Corporation of an additional grant of £17,500 a year in aid of a subsidy to the Grand Opera Syndicate.

538. The principle of the financial arrangements with the Corporation is that it has no legitimate claim upon the whole or any specified part of the revenue derived from wireless licences but that it should be supplied with adequate funds for maintaining the broadcasting service. For this purpose the sliding scale based upon the number of licences was framed and accepted by the Corporation as a convenient formula to secure them an income which would expand as their clientele of listeners increased.

539. We understand that at the time that the main agreement was under discussion it was generally contemplated that a revenue of about £800,000 per annum would meet requirements. The rapid growth shown in the following table was not then anticipated :—

—		Collected.	Post Office Percentage.	Paid to B.B.C.	Balance accruing to the Exchequer.
		£	£	£	£
1927	...	1,234,898	$12\frac{1}{2}$ per cent. 154,362	824,237	256,299
1928	...	1,358,187	" " 169,773	887,616	300,798
1929	...	1,537,377	" " 192,172	963,171	382,034
1930	...	1,812,656	" " 226,582	1,069,648	516,426
1931	...	2,050,000 (estimated.)	10 per cent. 205,000 (estimated.)	1,248,834 (actual being based on previous year.)	596,166 (estimated.)

540. The Corporation expenditure and income during the past four years have been as follows :—

INCOME.

—	1927.	1928.	1929.	1930.
	£	£	£	£
Receipts from Post Office	800,959	871,800	944,301	1,043,023
Publications	93,686	120,600	138,852	160,209
Interest	6,980	10,100	14,184	21,122
£	901,625	1,002,500	1,097,337	1,224,354

EXPENDITURE.

—	1927.	1928.	1929.	1930.
	£	£	£	£
Programmes	487,728	538,990	548,676	580,304
Engineering	131,036	160,455	178,942	192,720
Standing Charges (rates, rent, light, heat, etc.).	63,252	77,999	59,025	90,686
Administration	64,921	70,716	71,199	76,036
Depreciation	26,350	31,150	38,500	48,605
Income Tax	—	—	60,000	50,000
Total £	773,287	879,310	956,342	1,038,351
Capital expenditure incurred other than on regional stations.	10,108	34,167	36,425	4,460
Transfer to Reserve	100,000	100,000	110,000	180,000

541. It will be seen that apart from capital expenditure amounting to £90,000 incurred by the Corporation for purposes other than the regional stations, and excluding depreciation reserve which now stands at about £145,000, the Corporation have accumulated a reserve fund of £490,000.

542. The Corporation are incurring capital expenditure on a considerable scale. It is understood that at present they are either committed to or contemplate the following capital programme :—

	£
Four regional stations at £140,000 each ...	560,000
Broadcasting House, purchase of site and building	650,000
Equipment and furnishing	200,000
Purchase of adjacent site to Broadcasting House	50,000
	1,460,000

543. To meet this outlay they propose to draw in the first instance upon their reserve funds and future revenue surpluses; the balance will be provided by loans, and it is understood they have concluded an arrangement for borrowing of £500,000 for the purpose.

544. One cannot fail to be struck by the contrast between the general state of the national finances and the financial position of this national corporation. We believe it will be generally agreed that measured by any ordinary standards of public entertainment the facilities afforded represent good value for the small annual licence payment of 10s.

545. Here is a service which by virtue of the establishment of a state monopoly enables the State to obtain much needed supplementary revenue without giving rise to the sense of grievance engendered by most taxation. The principle of the State drawing this revenue, whether it be deemed the profits of a monopoly like the earnings of the Post Office from postal services or analogous to the entertainments tax, is already decided. The question we ask ourselves is whether in present circumstances this revenue should not be increased instead of continuing in force the original agreement under which the bulk of the increase in licence fees is being assigned to improvements in the broadcasting service.

546. We recognise that without at the same time a reduction of facilities, any substantial benefit can only accrue to the Exchequer if the Corporation are enabled by some form of statutory guarantee to spread their present heavy capital expenditure over a period reasonably comparable with the anticipated effective life of the asset. As the charter of the Corporation is due to expire in December, 1936, it cannot offer security for repayment of any loan after that date. We consider that as part of the revised allocation of revenue suggested below a statutory guarantee of payment of loan charges might properly be given in respect of capital expenditure approved as reasonable by the Postmaster General.

547. On the above figures of licence duties collections the payment to the British Broadcasting Corporation in the next year is likely to reach £1,380,000. In addition the Corporation have a depreciation reserve of £145,000 and other reserve funds of £490,000 which are rapidly being added to. If capital expenditure were provided for by a definite loan charge, the interest on these funds and the revenue from publications seem likely to bring next year's revenue to about £1,600,000, and there is no indication as yet of a slackening off in the rate of growth.

548. On the expenditure side a maintenance of expenditure at the 1930 level would require about £1,040,000. Even if one assumes that capital expenditure to the whole extent adumbrated above were approved, amortisation of the loans on London property over 30 years and on equipment and furnishing for the four regional stations over 15 years would only require about £120,000, or a total outgoing of £1,160,000. This amount is nearly 50 per cent. in excess of the income of £800,000 originally contemplated as adequate to meet requirements. On these figures we think that the allocation of a licence revenue to the Corporation might reasonably be reduced next year to £900,000 bringing the total revenue, including £220,000 from publications, etc., down to about £1,120,000. Pending further increase of revenue the invested reserve funds would be available to meet any temporary deficits on annual working.

549. We recommend that the percentages of allocation of revenue to the British Broadcasting Corporation be revised so as to yield this result by making the proportion of net licence duties (after deducting costs of collection as at present) to be paid to the British Broadcasting Corporation as follows:—

On the 1st million licences	...	...	80 per cent.
On the 2nd million licences	...	...	60 per cent.
On the 3rd million licences	...	...	40 per cent.
all in excess of 3 millions	...	...	20 per cent.

This scale calculated on the 4,100,000 licences estimated for this year would yield next year a licence revenue just over £900,000. The gain to the Exchequer would be about £475,000 for the year rising with any further growth in the licence duties.

3. EXCHEQUER CONTRIBUTIONS TO LOCAL REVENUES.

550. Provision is made in the Civil Estimates (Class X Votes 1 and 2) for the payment to Local Authorities in Great Britain of Exchequer Grants on the basis prescribed by Part VI of the Local Government Act, 1929, and Part III of the Local Government (Scotland) Act, 1929. By these Acts important alterations were made in the financial relations between the Exchequer and Local Authorities and in the administration of Local Government. The principal alterations were:—

(i) Boards of Guardians in England and Wales and Parish Councils in Scotland were abolished and the administration of the Poor Law was transferred to the Councils of Counties and County Boroughs (in Scotland—large Burghs) as from 1st April, 1930. (16th May, 1930, in Scotland.)

(ii) The administration of all highways in Rural Districts and of certain highways in Boroughs and other Urban Districts forming part of Administrative Counties (other than London) (in Scotland—small Burghs) was transferred to the County Councils as from the same dates.

(iii) In Scotland the administration of education was transferred at the same time from *ad hoc* authorities to the councils of counties and large burghs and there was a large measure of consolidation of the public health activities of minor authorities in the hands of these Councils.

(iv) Part V of the English Act and Part II of the Scottish Act contain what are popularly known as the "derating provisions" to which reference has already been made in Chapter V, page 110.

(v) Finally the old system of Assigned Revenues was abolished and the percentage grants from the Exchequer for health services as well as certain maintenance grants from the Road Fund were discontinued as from 31st March, 1930, (or 15th May, 1930), and a new system of Exchequer grants towards local government expenses came into operation.

551. It is unnecessary for us to set out the whole of the elaborate arrangements governing the distribution of these grants but we would refer to the basis on which the aggregate is determined from time to time.

(a) *General Exchequer contributions.*

552. Each year there is to be provided by Parliament, for distribution to Local Authorities in each country, a sum of money called the General Exchequer Contribution. This contribution is fixed, in accordance with a scheme set out in the Act, for a series of years, each such series being called "a fixed grant period".* The annual amount of the General Exchequer Contribution for the first fixed grant period is the total of the following amounts:—

(i) An amount equal to the total "losses on account of rates" arising from the derating provisions of the Act in the standard year, 1928-9.

(ii) An amount equal to the total "losses on account of grants" arising from the discontinuance of the grants referred in (v) above; this also being measured by the payments for the standard year.

(iii) An additional amount (specified in the Act) of £5,000,000 (England and Wales), £750,000 (Scotland).

* The first fixed grant period is a period of 3 years from 1930; the second period is a period of 4 years from 1933; each subsequent fixed grant period covers 5 years.

553. The amount of the annual General Exchequer Contribution during the first fixed grant period, i.e., the period of three years from 1st April (or 16th May), 1930, is provisionally estimated as follows :—

—	England and Wales.	Scotland.	Total.
	£	£	£
Losses on account of rates ...	22,600,000	3,295,780	25,595,780
Losses on account of grants ...	16,300,000	2,039,459	18,539,459
Additional Money	5,000,000	750,000	5,750,000
Total annual General Exchequer Contribution for the first fixed grant period.	£ 43,900,000	6,085,239	49,985,239

(b) *Additional Exchequer Grants.*

554. Provision is made for Additional Exchequer Grants to ensure that as compared with the standard year (1928-29) each County or County Borough or Large Burgh area obtains from the new grants a minimum advantage by reason of the Act equivalent to 1s. per head of population in 1928. The amount of the Additional Exchequer Grants was provisionally estimated at £550,000 for the first fixed grant period in England and Wales and £7,814 in Scotland.

(c) *Supplementary Exchequer Grants.*

555. As part of the gradual process by which the financial changes provided for in the Act are to be brought into operation, there are provisions designed to mitigate any increase of rate poundage which might otherwise arise during the first 19 years in which it is in force and provisionally estimated to cost £1,100,000 per annum in England and Wales and £184,695 in Scotland for the first five years.

556. Thus the total liability under this legislation for the first fixed grant period is estimated provisionally at :—

—	England and Wales.	Scotland.	Total.
	£	£	£
(a) General Exchequer Contribution.	43,900,000	6,085,239	49,985,239
(b) Additional Exchequer Grants	550,000	7,816	557,816
(c) Supplementary Exchequer Grants.	1,100,000	184,695	1,284,695
	£ 45,550,000	6,277,750	51,827,750

Of this amount £6,473,638 is at present charged upon the Road Fund under the two Acts, leaving a net amount of £45,354,112 to be voted. The actual provision in the Estimates for 1931 differs slightly from this figure by reason of it including partial payments in respect of two years.

(d) The Revision of the General Exchequer Contribution.

557. The Acts prescribe that for each fixed grant period subsequent to the first the additional amount of £5,000,000 and £750,000 included in the General Exchequer Contribution is to be replaced by such sum as Parliament may determine, provided that the additional amount for the second and any subsequent fixed grant period shall be such that the proportion which the amount of the annual General Exchequer Contribution for that fixed grant period bears to the total amount of rate and grant-borne expenditure incurred by all authorities for the last year but one of the preceding fixed period shall never be less than the proportion which the annual General Exchequer Contribution for the first fixed grant period bore to the total amount of rate and grant-borne expenditure of the first year of that period. The amount of the General Exchequer Contribution for 1933 onwards and again for 1937 onwards will therefore depend upon the extent to which the expenditure of local authorities as a whole for the year 1931 and 1935 respectively exceeds the expenditure of local authorities for the year 1930. Broadly speaking, under these arrangements strictly applied, the total Exchequer contribution will rise or fall at the periodical revisions by about one-fourth of the variation in the aggregate expenditure of local authorities.

558. This establishes a general interdependence of national and local finance additional to that already existing in the grant arrangements applicable to particular services (whether these take the form of percentage grants as with education, police, roads and unemployment schemes, or grants per unit of service as with house-building), and in considering the future course of national commitments we must have regard therefore also to the general trend of local expenditure. Indeed any review of the burden of public expenditure would otherwise be incomplete.

559. The net revenue expenditure of local authorities in England and Wales (charged on rates and Exchequer grants) reached a peak of over £243,500,000 in 1921 and then under the influence of the national pressure for economy fell rapidly. In 1924 a move-

ment in the reverse direction set in. The following table gives the figures up to 1927-8 :—

<i>Year.</i>							<i>Expenditure falling on rates and grants.</i>
							£
1921	...	...	...	...	...	...	243,566,250
1922	...	...	...	...	...	...	223,245,786
1923	...	...	...	...	...	...	220,446,843
1924	...	...	...	...	...	...	229,145,023
1925	...	...	...	...	...	...	240,574,710
1926	...	...	...	...	...	...	258,622,012*
1927	...	...	...	...	...	...	249,567,156

Detailed figures are not available for later years for the whole country but we have been furnished by the County Councils' Association with valuable statistics showing an increase in the gross expenditure of County Councils (other than the London County Council) from £53,658,000 in 1923 to £67,680,000 in 1929, the last year before the extensive changes caused by the Local Government Act. This is an increase of 26 per cent. in the space of 6 years. Estimates of the amount raised by rates, or contributed by the State in the form of increased grants under the Local Government Act, have recently been published showing an increase between 1927 and 1930 of over £11,000,000. In addition the Exchequer grants to local authorities for education, roads and police were all increased during these years.

560. This rapid growth of local expenditure since 1923 has occurred notwithstanding that (owing no doubt to the operation of the Unemployment Insurance Scheme) the number of persons in receipt of poor relief fell from :—

on 31st March, 1922	...	...	...	1,465,599
and on 31st March, 1923	...	...	...	1,345,634
to on 31st March, 1928	...	...	...	1,183,088
on 31st March, 1929	...	...	...	1,106,673
on 31st March, 1930	...	...	...	1,047,026
and on 31st March, 1931	...	...	...	1,029,114

561. Moreover, as in the case of the national expenditure, the revenue account does not show the full seriousness of the position. Between 31st March, 1921, and 31st March, 1928, the total capital indebtedness of local authorities in England and Wales (after deducting amounts standing to the credit of sinking funds) rose from £595,500,000 to £1,051,500,000, an increase of £456,000,000, or an average of £65,000,000 a year. This represents the net excess of

* Poor-law expenditure in 1926 was exceptionally heavy owing to industrial disputes.

increased capital expenditure over repayments of loans. The amount actually spent on capital account in 1927 was £120,000,000. We recognise that the debt of local authorities is very different in character from the national debt in that it is offset in far greater degree by valuable assets. One-fifth of the increase of £456,000,000 was in respect of trading services; housing accounted for well over half the increase and the gross indebtedness of local authorities under this head alone (including £39,400,000 advanced to other parties) stood at £383,000,000 on 31st March 1928.

This figure of course includes the estimated future capital liability of the State in respect of housing schemes given on pages 181 and 189. We have no reason to think that the growth of local authorities' indebtedness has proceeded at any reduced rate since 1927. Such information as is available points rather to an acceleration.

562. We view with grave concern this rapid rise of expenditure of local authorities both on the capital and on the revenue side during a period of falling prices and small growth of the population. We recognise that in certain areas the movements of population have caused heavy demands on the local authorities for increased expenditure on municipal services and we do not question the necessity for the increased expenditure in such cases. We are also aware of the pressure that has been put upon local authorities in recent years by the Central Government to increase their expenditure on certain services. Nevertheless taking the country as a whole the fact remains that in the local as in the national field we have been piling up public burdens. We have been appointed only to review the national expenditure. At the same time we are glad to learn that some local authorities, recognising the seriousness of the position, have appointed similar committees to survey their own expenditure and recommend reductions where possible. We would earnestly commend this policy to the attention of every authority in the country.

563. Notwithstanding the extent to which increased State assistance to local authorities has contributed to the present difficulties of the Exchequer, we have endeavoured throughout our search for economies to avoid a mere transference of burden from taxes to rates, realizing full well that rates represent on the whole a less equitable impost than the national taxes. In a few cases, in order to achieve the object we had in view, we have been unable to avoid throwing some extra charge upon the rates, but such charges should be trivial in any but the wealthier areas and we do not doubt that if local authorities undertake a careful review of their expenditure suggested above, the net result will be a substantial relief to the ratepayer with beneficial reactions in the national exchequer.

CHAPTER VIII.

SUMMARY OF RECOMMENDATIONS AND CONCLUSION.

1. Summary of Recommendations.

564. In our opening chapter, we came to the conclusion that the anticipated borrowing in 1932 on behalf of the Unemployment Insurance Fund and the Road Fund should be regarded as a revenue liability, and on this basis we estimated that to produce a properly balanced budget in 1932, including the usual provision for the redemption of debt, a deficiency of £120,000,000 had to be made good by new taxation or by economies.

564A. We now summarise the financial effect of our more important recommendations and indicate how far they suffice to bridge this gap.

We divide our list into two parts. In the former we show the financial effect of those which will effect a reduction in charges expected under existing policy in 1932. The full effect of our recommendations will not be felt in all cases in that year. Nevertheless we think it better to give the saving which will be realised in the first full year of their operation. In the second part of our list, we give those recommendations whose effect will be to limit future increases of expenditure rather than to secure immediate reduction. In most cases in the latter list it is impossible to express the saving to be expected therefrom as a definite figure.

Major Recommendations involving immediate saving.

	<i>Saving to Exchequer in a full year.</i>
	£
Chapter III. Pay and Pensions.	
Abolition of preferential bonus paid to Government Industrial employees in the Dockyards and Ordnance Factories (paragraph 91)	325,000
Introduction of 1925 rates of pay for all personnel of the Fighting Services (paragraphs 111 and 112)	2,199,000
Introduction of revised cost of living deduction for officers of the Fighting Services (paragraph 114) ...	400,000
Reduction of pay of police by 12½ per cent. less rateable deductions towards cost of pension (paragraph 131). Exchequer share	925,000
Reduction of pay of teachers by 20 per cent. (paragraph 155). The saving from this reduction is incorporated below under Education grants ...	—

	<i>Saving to Exchequer in a full year.</i>
	£
Introduction of revised cost of living deduction from pensions of officers of the Fighting Services (paragraph 162)	190,000
Abolition of grant of marriage gratuities in the Civil Service (paragraph 166)	167,000

Chapter IV.—Defence.

General.

Reduction of expenditure on Research and Technical Development by 12½ per cent. (paragraph 210)	300,000
Reduction of Education Votes by 10 per cent. (paragraph 219)	150,000
Reduction of Inspection costs by 10 per cent. (paragraph 222)	100,000
Stabilisation of Works Votes over a period of years (paragraph 226)	150,000
Reduction of Clothing Allowances by 10 per cent. (paragraphs 237, 247, and 258)	154,000

Navy.

Further saving to be obtained from the introduction of Royal Marine Police at Dockyards (paragraph 236)	50,000
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Army.

Discontinuance of subsidies for Mechanical Transport (paragraph 245)	20,000
Discontinuance of Light Horse Breeding Scheme (paragraph 246)	30,000

Air Force.

Abandonment of New Programme of Research in Civil Aircraft (second year's instalment of a total of £40,000) (paragraph 265)	25,000
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Chapter V.—Development.

<i>Road Fund.</i> —Postponement and slowing down of schemes and lowering of the present very high standard of maintenance (paragraphs 297 and 298)	7,865,000
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*Saving to
Exchequer
in a full
year.*

£

<i>Ministry of Agriculture and Fisheries.</i> —Reduction of Agricultural Education grants to 50 per cent., limitation of grants for research, expenditure on livestock improvement to be recovered or discontinued, reduction of land drainage grants, cessation of "foreground" publicity (paragraphs 306 to 311) involving in all reduction of the gross forecasted expenditure for 1932 by	500,000
<i>Department of Agriculture, Scotland.</i> —Reduction on lines similar to proposals as regards England and Wales and modification of Scottish Land Drainage Act (paragraph 317)	75,000
<i>Forestry Commission.</i> —Cessation of land acquisition and restriction of planting and provision of forest workers' holdings (paragraph 339) ...	478,000
<i>Empire Marketing Board.</i> —To be abolished (paragraph 339) involving a saving, in addition to savings already allowed for on the gross votes for the Department of Overseas Trade and the Agriculture and Fisheries Departments of	400,000
<i>Colonial Development Fund.</i> —Limitation of annual grant to £750,000 (paragraph 346)	250,000

Chapter VI.—Social Services.

<i>Unemployment Insurance.</i> —Reductions of benefits by 20 per cent., increase of weekly contributions to 10d. each for workers, employers, and the State in the case of men, extension of scheme to include certain classes now outside it, application of needs test by public assistance authorities to all applicants who have exhausted their insurance rights, but are still within the industrial field. Reductions of State liability less Government grant to local authorities (paragraphs 370 to 389)	66,500,000
<i>National Health Insurance.</i> —Reduction of the capitation payment to doctors, National Health Insurance (Prolongation of Insurance) Act, not to be extended, revival of State grant to the Central Fund to be avoided by a greater measure of pooling among Approved Societies (paragraphs 403 to 405 and 409)	1,000,000

*Saving to
Exchequer
in a full
year.*
£

Education :—

Abolition of 50 per cent. minimum limit of grant, reduction of teachers' salaries by 20 per cent. and of the grant in respect of teachers' salaries from 60 per cent. to 50 per cent., reduction of grants for higher education in consequence of 20 per cent. reduction in teachers' salaries and increase of school fees, reduction of growth of education expenditure in 1932, and proportionate reduction for Scotland (paragraphs 498 to 519)	13,600,000
Reduction in grants to Universities and Colleges (paragraph 520)	250,000

Chapter VII.—Miscellaneous.

<i>British Broadcasting Corporation.</i> —Reduction of percentages of wireless licence receipts paid to the British Broadcasting Corporation (paragraph 549)	475,000
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Total	£96,578,000
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Major Recommendations whose effect is to limit future increases of expenditure.

Chapter III.—Pay and Pensions.

An age limit for voluntary retirement in the police forces to be imposed (paragraph 168).

The whole subject of police pensions to be reviewed to determine conditions of service for new entrants which will effect a saving in the present high non-effective cost (paragraph 169).

The 1930 scales of pension to be applied in the Fighting Services on re-engagement or re-enlistment to all men now serving (paragraph 172).

The whole scheme of pensions of officers in the Fighting Services to be immediately examined in the light of its extremely expensive character. All age limits for retirement under 60 in the Non-Executive Branches to be raised by 5 years pending such enquiry (paragraph 182).

Chapter IV.—Defence.

The distribution of the burden of Empire Defence to be examined when the financial situation of the Empire is more favourable (paragraph 203).

Before the next Naval Conference, the Government to appoint a representative Committee to enquire into the whole subject of naval design and to consider whether any modifications might be adopted, either with or without international agreement, which would lessen the cost of naval defence without endangering national security (paragraph 233).

The establishment of the Ordnance Factories to be reviewed and the question whether orders should be placed in excess of the amount required to keep the nucleus establishment fully employed, and if so, in what proportion such orders should be distributed between the trade and the factories to be considered in the light of respective costs (paragraph 250)

The Air Ministry to consider whether some reduction of the present number of firms competing for the supply of aircraft is not possible (paragraph 254).

The Air Ministry to consider the practicability of a reduction in the number of different types of aeroplane and engine in daily use (paragraph 256).

The organisation of the Air Ministry to be examined on lines similar to the enquiry made in 1923 into the Admiralty and War Office establishments (paragraph 267).

Chapter V.—Development.

Road Fund.—To be abolished, the proceeds of all motor taxation being left in the Exchequer and all grants being provided on Annual Parliamentary Votes. Reconsideration of expensive London schemes necessary (paragraphs 296 to 298).

Department of Overseas Trade.—A policy of recovering the cost of the department from those who benefit to be steadily pursued (paragraphs 301 and 302).

Agriculture.—The provision of small holdings under the Agricultural Land (Utilisation) Bill to be restricted to careful and judicious experiment on a scale wide enough to give reliable results. Centralisation of administrative responsibility in the hands of the Government is to be deprecated (paragraph 314).

The acquisition of land for reconditioning or reclamation to be restricted to cases where there is clear evidence that the land can subsequently be sold without loss (paragraph 315).

Unemployment Grants Committee and Development (Public Utility) Advisory Committee.—The scale of grants towards works put in hand to relieve unemployment to be restricted to 25 per cent. of the cost and in the case of revenue producing works not to exceed the extra cost of putting capital works in hand before the normal date if less than 25 per cent. (paragraphs 358 and 364).

Chapter VI.—Social Services.

Maternity Scheme.—The contemplated development of the maternity service at a cost to the State of £1,500,000 not to proceed. Improvements to be sought without any extra State grant (paragraph 416).

Housing.—The aim of re-establishing economic housing for the working classes to be kept steadily in view; as a first step, subsidies in England and Wales and Scotland under the Act of 1924, both in urban and in rural areas, to be reduced by £2 10s. per annum for houses completed after 30th April next; corresponding reductions to be made in subsidies under the Act of 1930. Subsidies in Scotland to be brought down to English rates after 1st October, 1932 (paragraphs 471, 477 and 497).

Education.—The number of education authorities to be reduced and educational functions concentrated as far as local authorities are concerned in the hands of county and county borough councils; this step to be followed by the introduction of a block grant for all education services (paragraph 505).

2. Conclusion.

565. In submitting these recommendations for reductions of expenditure we have proceeded on three general principles which it may be convenient to summarize here :—

(1) that the rise in the value of money in recent years provides a strong *prima facie* case for the revision of money obligations fixed under other conditions. In considering the emoluments of public servants we have also had regard to the principle of "fair wages".

(ii) that existing financial difficulties make it necessary for the nation like the private individual to consider seriously what it can afford and not merely what is desirable. Reviewed from this standpoint much expenditure is unwarrantable at the present time, which, under more favourable conditions, we should deem justifiable and even a wise investment of the national resources.

(iii) that only by the strictest regard to economy and efficiency over a long period can the trade of the country be restored to its pre-war prosperity and any substantial number of the unemployed be re-absorbed into industry.

566. We believe that the whole of our recommendations are in accord with these principles and in the terms of the resolution of the House of Commons we regard them as "practicable and

legitimate reductions in the national expenditure consistent with the efficiency of the services". Many of them are clearly interdependent: even the more drastic will, we think, be accepted as fair if the whole programme be carried into effect. But if a policy of selection be adopted, if economies are only attempted where little opposition is anticipated, if certain classes are called upon in the national interest to suffer serious reduction of emoluments while large unprofitable expenditure goes on unchecked in other fields, resentment and opposition will be aroused and the eventual result in savings will be negligible; the object of our appointment will remain unfulfilled.

567. What are the alternatives to the reductions we suggest? The nation can continue as at present borrowing to meet current requirements and deluding itself that by still showing a sinking fund item in the national accounts it is not only meeting its liabilities but actually paying off debt. **This course will lead inevitably to an intensification of the financial difficulties until the day comes when far greater sacrifices than those we suggest are forced upon the country.** The other method is to endeavour to right the position solely by means of additional taxation, but to achieve a truly balanced budget next year in this way the extra taxation would need to be very heavy and we fear the consequences. The margin of safety is already narrow. Who knows whether the future may not have further troubles in store for us that will make that reserve of financial strength of inestimable value?

568. Even under our proposals the risk of additional taxation is not entirely obviated. We set ourselves the task of covering a prospective deficiency next year of £120,000,000. The savings arising from our recommendations only total about £96,500,000 for the first year of their full operation. While their general reactions should lead to a greater saving in later years, even this amount of £96,500,000 would not be wholly available in 1932 owing to the inevitable delay in making some decisions fully operative.

569. How the gap of £20,000,000—£30,000,000 is to be bridged is a difficult question raising issues so much beyond our sphere that we cannot submit any definite recommendation. If in view of the present economic position it were possible to arrange that all classes of the Community should suffer an all round reduction of income, whether derived from earnings, in order to bring costs of production down to a lower level, or investments, we should have no hesitation in proposing that all public Servants and pensioners, Municipal as well as State, of whatever grade or kind, old age pensioners, widows and war pensioners, should share in the reduction, including those whose pay had already been reduced in

accordance with our recommendations. **We cannot however justify the singling out of public servants and pensioners from the rest of the community for special sacrifice.**

570. Failing the economy from an all-round reduction of incomes, therefore, the alternative is some additional taxation. We do not favour imposing any further burden on productive industry (beyond the small increase in the contributions for unemployment insurance) as this would impede trade recovery, but we are not without hope that the sum required can be found by revisions of general taxation which are free from this objection. In one way or the other we trust that it will be found possible to supplement the economies we recommend sufficiently to surmount immediate financial difficulties.

571. Our chief concern however is for the future. If action is limited to these adjustments of expenditure or income, experience since the War does not allow us to hope for that sustained effort for national economy which we regard as essential to the restoration of prosperity. Some further action is needed if retrenchment is not soon to give way once more to expansion as has happened twice in the short period since the War. We have no recommendations to make for improving the machinery of Treasury control. The procedure of Parliament and the relation of Parliament to the Executive are matters rather outside our province and in any case are being examined by a Select Committee. We think however that it would be of definite advantage if a comprehensive review of the financial position could be given to Parliament and through it to the nation, more frequently than on the opening of the annual budget. Particularly is such a review desirable shortly before the dissolution of a Parliament and soon after the assembly of a new House of Commons. These reviews should cover not merely the current financial year but should take account of the next few years, giving full information also as to the growth of long term commitments. A statement of future obligations of the State distinguishing between liabilities in respect of capital expenditure already incurred e.g. grants for housing, roads, unemployment works, etc. and liabilities in respect of continuing pension schemes including pensions to public servants and national pension schemes would be a valuable addition to the tables presented to Parliament in connection with the Budget Statement.

572. In the case of the Cabinet we suggest that in the detailed and exhaustive consideration which has to take place before items of Government policy can be put into force financial implications should have greater weight. At present the Chancellor of the Exchequer seems alone among his colleagues to be regarded as charged with responsibility for financial policy. While no doubt

he is able to enlist some support within the Cabinet no organised machinery exists whereby he can be assisted in his difficult task. We suggest that on the analogy of the Committee of Imperial Defence which is working successfully to secure full co-ordination in matters affecting the national defence, **there should be a standing Finance Committee of the Cabinet** (such as we understand existed under the Coalition Government) which would be kept fully informed of the state of national revenue and expenditure and would examine all schemes submitted to the Cabinet, which involved serious outlay, not merely on their individual merits but from the wider point of view of their bearing on national finance. We have in mind that the Committee would, like the Committee of Imperial Defence, be elastic in its constitution to permit the calling into council of any advisers it thought fit, and that it would normally consist of the Prime Minister and Chancellor of the Exchequer and a small number of Ministers selected not so much by reason of the offices they hold as of their aptitude for the difficult task of financial appreciation and criticism.

573. But the best devised machinery of financial control will be of little avail if the will to control be absent. The root cause of our financial difficulties since the war is that the machinery has been largely nullified in its operation. It has secured the utmost regularity in Government accounting and high standards of administration and organisation, but as regards major items of policy—where the real expense of Government lies—the machinery of control has again and again been put out of action before it has had any chance of functioning.

574. We referred in our opening chapter to the political developments since the war which have resulted in Members of Parliament and Governments being returned to Westminster pledged in advance to vast and expensive schemes. The electoral programme of each successive Party in power, particularly where it was formerly in opposition, has usually been prepared with more regard to attracting electoral support than to a careful balancing of national interests. When the time comes to put that programme into force, matters which had formerly appeared easy and attractive are found to involve such grave questions as whether the proposals are administratively possible, whether they will have the desired results, whether the country can bear the cost; whether, in short, they are really in the national interest. It is almost inevitable that a new Cabinet should find itself driven to the conclusion that many of its promised reforms ought not to proceed, but it has a difficult course to steer before it can persuade its supporters in the House to recognise this in view of their pledges so freely given to the electorate. The problem is a serious one and it is hardly for us to suggest a solution: yet a solution has to be found if democracy is not to suffer shipwreck on the hard rock of finance.

575. In the course of our work, we have been much impressed by the ability and courtesy of all the permanent officials who have so freely given us their assistance.

We must particularly thank our Secretary, Mr. B. W. Gilbert, for his able work and we desire to place on record our high appreciation of his ability and zeal. Sir Alfred Hurst has been invaluable to us and we are very grateful to him.

We also wish to refer to the great help we have received from Mr. Waterfield, Mr. Morris and other Treasury officials.

We have the honour to be,

Sir,

Your obedient servants,

G. E. MAY (*Chairman*).

P. A. COOPER.

M. WEBSTER JENKINSON.*

PLENDER.

T. ROYDEN.

B. W. GILBERT,

Secretary.

24 July, 1931.

* Subject to the reservation on page 225.

Reservation by Sir Mark Webster Jenkinson.

I differ from the views expressed by my colleagues in Paras. 22 and 574 that "the root cause of our financial difficulties since the War" is due to "political developments . . . which have resulted in Members of Parliament and Governments being returned to Westminster pledged in advance to vast and expensive schemes", and that "the electoral programme of the Party in power . . . has usually been prepared with more regard to attracting electoral support than to a careful balancing of national interests".

It is true that during recent years a tendency has grown up among all classes to rely upon the State to subsidize projects of varying National importance, and that the zeal of those who advocate expensive schemes of social reform may outrun their knowledge of the financial ability of the country to bear the burden.

At the same time I have sufficient faith in Parliament to believe that no Party entrusted with the reins of Government would *deliberately* jeopardize the National Finances merely to honour "the lavish promises contained in election addresses".

The following causes have, in my view contributed to the present position:—

(1) Successive Governments have, without true appreciation of the economic position of the country and the financial problems arising from the war and from world conditions, embarked upon expenditure on Social reforms; granted concessions to various classes of State employees; undertaken obligations to local authorities; and followed a course of increased National Expenditure, failing to take into account the *cumulative* financial effect of their action.

(2) The rapid growth in the activities and expenditure of certain Government Departments is partly attributable to the natural desire of those responsible for the policy and administration of those Departments to attain the maximum of accomplishment irrespective of financial considerations; and as results in a Government service can only be measured by achievements and not, as in a commercial concern, by profits earned, there is no incentive to economy.

(3) Although Parliament has the opportunity to review the annual estimates in the House—which estimates are submitted in the greatest detail—instead of examining the expenditure proposed with a view to reduction, the occasion is used to urge the Government to further expenditure or to ventilate grievances.

The control of the National Expenditure is vested to-day in :—

- (a) The Treasury
- (b) The Government
- (c) The House of Commons

but the supreme control rests with the last named.

No Chancellor of the Exchequer, no Government Department, no Committee on National Expenditure, can secure that measure of economy that financial considerations now render so imperative unless the House of Commons is determined that the necessary savings shall be effected.

M. WEBSTER JENKINSON.

MINORITY REPORT.

To the Rt. Hon. PHILIP SNOWDEN, M.P.,
Chancellor of the Exchequer,
Whitehall, S.W.1.

SIR,

1. Having regard to the measure of our disagreement with the majority of the Committee on several important aspects of public expenditure, we regret we are unable to sign the main report and feel it incumbent upon us to set forth in a separate report the reasons for these divergencies of opinion.

2. We consider that in any proper estimation of the possible and actual results of the Committee's work, its genesis cannot be entirely overlooked. The appointment of the Committee arose out of the acceptance by the Government on the 11th February, 1931, of an amendment to a direct motion of censure on the subject of public expenditure moved by the major Opposition, and the House of Commons passed by 468 to 21 the following resolution:—

“That this House consider that, having regard to the present burden of Taxation in restricting industry and employment, the Government should at once appoint a small and independent committee to make recommendations to the Chancellor of the Exchequer for effecting forthwith all practicable and legitimate reductions in the national expenditure consistent with the efficiency of the services.”

3. From a reading of the debate which preceded this resolution it is apparent there was considerable doubt in the minds of many Members of Parliament as to the possibility of a Committee effecting any large measure of economy; and at an early stage in the work of the Committee it became abundantly clear that these doubts were well founded and accurately adumbrated the limitations upon securing economy in expenditure unless the enlarging policies of successive Governments and Parliaments were to be severely modified or abandoned. Since the appointment of the Committee, Parliament has approved further measures calling for additional expenditure of varying orders of magnitude. Thus the road to reduced expenditure is largely closed by policies to which the country is committed and outside that domain there remains only the narrow field of administrative and like expenditure.

4. The differences apparent amongst those who comprise the House of Commons as to the sources available for effecting real

national economy were not absent from the Committee, and they involve fundamental questions of principle and of social policy to which regard must be paid if proper consideration is to be given not merely to the measure of expenditure, but equally to the manner in which it is being utilised and the extent to which it is being applied for the general well-being. Viewed from that standpoint, it is to us a matter of profound satisfaction to find that of that part of the national expenditure coming within our terms of reference there has been a growing tendency towards the application of an increasing proportion to purposes of the highest social and economic value, and with what care and efficiency on the whole the public services are being administered.

5. While we fully share the desire of our colleagues to secure means for the proper control and wise expenditure of public funds, we entirely disagree with the implications contained in their review of the course of national finance since the War as set forth in section 4, of chapter 1, of the main Report under "Factors, Political and Economic, in the Present Situation." We do not question the need for caution in undertaking financial commitments of a continuing or other character, but we consider that their picture is over-painted and would represent a condition of financial irresponsibility which in fact does not exist. So far as their strictures concern the principle of ultimate financial responsibility, what they regard as "undesirable," we view as consistent with the right and proper course of democratic government and progress. How otherwise shall the people obtain legislative redress of social and economic injustice except through those who seek their suffrage?

6. The results arising from the past inequitable distribution of the national income were not generally recognised until the nation became involved in a disastrous war, when the whole resources of man-power and of material had to be strained to the utmost to enable the country to meet a grave crisis, and when it was discovered that despite the rapid growth of wealth and prosperity, the human factor had attained to nothing more than what was described as a C3 standard. It is a matter for gratification that in the post-war years, and despite the difficulties existing, all political parties in different degrees have recognised an obligation in this respect, and that each in turn has been anxious in varying measure to show appreciation of the necessity for utilising a larger proportion of the national income for the purpose of remedying the evil results of past neglect. Much remains to be done, and much more might be done now but for the dead-weight burden of war debt which absorbs so large a share of the national income and the heavy expenditure involved in the apparent necessity for providing against future wars. Allowing for these, it may be truly said that in the main State policy has been one of a wise use of the funds collected by taxation.

7. Public expenditure has ample justification when it rests primarily upon the necessity for re-adjusting the use of the national income in such manner as to transfer expenditure from less essential or desirable channels into those which are designed to mitigate social injustices, or those which improve the economic structure of the nation. The growth of social services is a natural corollary to the development of industry and commerce and it cannot be denied that these have profited materially from services often narrowly regarded as amenities, and it is not an overstatement of the case to say that improved health and sanitation, better education, wider and cleaner roads, quicker communications and even open spaces and playing fields are essential to modern large scale industry.

8. In this connection, it is arguable that the drift of the newer industries to the less congested South is not unrelated to the fact that these social services are more generally available at less cost than in older industrial districts still handicapped by the neglect of the past or the accumulated cost of remedying that neglect. In consequence of the re-settlement of industry now taking place and the world changes particularly affecting the basic industries of this country, a new intersection of the nation is becoming apparent, dividing on lines of comparative poverty and wealth the distressed industrial North and other parts from the more prosperous South. It is a matter for serious consideration whether money now being spent in improving facilities in the South would not be more profitably employed in reviving districts already possessing industrial equipment, but lacking those services and facilities which render the better designed and more spaciouly planned South so powerful an attraction to those establishing new industries in this country.

9. The existing social services have been slowly built up with the general approval of all citizens of goodwill and vision, and their essential value is perhaps most clearly demonstrated in the fact that their existence has materially assisted this country to withstand the shock of the unparalleled economic depression, better, perhaps, than any other country in the world. Their true worth in this connection will probably only be accurately appreciated when the present period of depression has passed, and it will be possible to view in proper perspective the course of present economic troubles. We can see no special reason why a period of economic difficulty should necessarily be required to bear its own financial burden at the price of scaling down social services, and we do not share the pessimism that discerns signs of only remote recovery. We cannot ignore the fact that the cost in recent years of organised development in the social, as also indeed in the industrial life of the country, largely represents the accumulated liability of an unwise economy of the past, and is only now beginning in any appreciable degree, to eradicate the disastrous consequences of neglect, and of the mal-adjustment of the national wealth during and following the

industrial revolution of the nineteenth century ; and, in our considered judgment, to enter afresh upon a policy of cutting down expenditure which would require this and succeeding generations to pay a like tribute to the cost of the industrial revolution now proceeding would be to add to the burdens of the nation and not to reduce them.

10. Much of the national effort is to-day being absorbed outside the realm of public control in forms of wasteful and uneconomic expenditure or in the provision of various forms of luxury which, as regards the latter, while permissible in times of prosperity, cannot be disregarded in the consideration of means to meet the present time of stress.

In any event, we are satisfied that as a principle of sound national economy, before any sacrifice can be called for in a reduction of the social services which represent absolute necessities to the workless citizen, the sick and infirm and the aged, before any action is taken to curtail the provision of decent housing conditions for the people or to retard the educational progress of the children of the nation, there is ample field of exploration for taxation, and for restriction ✓ of expenditure in other less justifiable directions.

11. During the War many restrictions were applied and accepted as being necessary to the common interest. If to-day another emergency has arisen, then it is incumbent upon Parliament to introduce legislation to secure that the sacrifice necessary to meet it shall be common to all and in proportion to the ability to bear the burden.

With the foregoing considerations in mind, we turn to the task placed upon the Committee.

I. The Field for Economy in National Expenditure.

12. The Committee were appointed on the 17th March, 1931, after consultation between all parties. Their orders of reference, in terms identical with those of the Committee on National Expenditure set up in 1922, and known as the "Geddes" Committee, were as follows :—

"To make recommendations to the Chancellor of the Exchequer for effecting forthwith all possible reductions in the National Expenditure on Supply Services, having regard especially to the present and prospective position of the Revenue. In so far as questions of policy are involved in the expenditure under discussion, these will remain for the exclusive consideration of the Cabinet ; but it will be open to the Committee to review the expenditure and to indicate the economies which might be effected if particular policies were either adopted, abandoned or modified."

13. If, as the Geddes Committee stated, the task assigned to them was one of complexity, that placed upon the present Committee has been even more difficult. The former Committee dealt

with an expenditure which still reflected in a very considerable degree the extravagant policy and ways of the war period, as well as the hopes and expectations of the peace, stimulated by the short-lived boom of the immediate post-war years. No like opportunity has offered itself to the present Committee. Of the £175,000,000 reduction the Geddes Committee were charged to secure, no less a sum than £75,000,000 was provided by Government Departments in response to a Treasury circular on the subject of the restriction of public expenditure, and the fact that the sum so saved was largely in respect of special expenditure on services arising out of the war is an indication of the resources of saving available at that time. With regard to the £100,000,000 which remained to be found, close on £60,000,000 was recommended as being available from the Defence Forces, the expenditure on which had been enormously swollen by the war.

14. Since 1922, and apart from the continuous survey by the Select Committee on Estimates and the Public Accounts Committee, other Special Committees have examined many branches of national expenditure. These include the Anderson Committee of 1923 "to enquire into the present standard of remuneration and other conditions of employment of the various classes of State servants employed in the Civil Service and in the three Fighting Services". The Standing Cabinet Committee, set up by the Chancellor of the Exchequer in 1925 "to review the estimates of national expenditure with a view to making a substantial reduction in the charges on the tax payer". (The recommendations of this Committee formed, we understand, the basis of the Economy (Miscellaneous Provisions) Act, 1926). The Colwyn Committee, appointed in 1925 to investigate the expenditure falling upon the navy, army and air force, and this Committee appointed another body to examine into the administration of the Royal Dockyards. The Colwyn Committee subsequently investigated expenditure on education. In 1926 and 1927 the Standing Cabinet Committee continued its researches, which resulted in certain departmental economies. In 1927 the Committee under Lord Chalmers considered Police expenditure.

15. In addition to the special investigations made by these *ad hoc* Committees, our enquiries show that provision has been made for a continuous check upon administrative expenditure throughout the various Departments, with the result, we are satisfied, that effective measures are in general taken to secure the most economical administration consistent with the efficient execution of the duties and responsibilities devolving upon the Departments.

16. It will thus be seen that the field of economy in State expenditure is a much trodden one, and our general conclusion is that as regards the particular classes of expenditure coming within the purview of this Committee to effect any serious decrease is

impracticable, except by measures which are solely in the control of Parliament itself.

Even so information was before us which showed that the position of national expenditure in relation to revenue is one of exceptional difficulty, and that the situation calls for careful scrutiny and supervision.

17. Without detracting from our previous remarks as to the general high standard of supervision of expenditure, we think it may well be found that within the wide and complex framework of national administration and development there are places where, by reorganisation of particular services, duplication of administrative costs and possibly of actual expenditure in certain directions may be eliminated without injury to the service itself or its designed object; but as regards the general limitation and reduction of expenditure it seems to us that other and wider considerations arise.

18. National expenditure is not necessarily wise or unwise by reference only to its amount, nor to the fact that it is public as distinct from private expenditure. The former, like the latter, must be considered not only from its quantitative but also from its qualitative aspects. It seems to us that real economy in expenditure is much more than a simple process of "lopping-off", regardless of the loss to the well-being of the nation, and without estimation of whether the amount thus figuratively saved may not be exceeded in lessened national efficiency, on the one hand, or the necessity for future expenditure of an enlarged order, on the other. Thus our dissent from the general point of view expressed by our colleagues in their Report rests upon a conviction that, taking the long view, their recommendations in many respects would not, if carried into effect, achieve real national economy, although they might for the time being secure an actual reduction of expenditure.

19. Turning now to an examination of the national expenditure, we find that the sum estimated to meet requirements for the current year amounts to £884,900,000, or excluding self-balancing services, £803,400,000. Of this, £312,300,000, being the sum charged on the Consolidated Fund, chiefly in respect of interest and management of the national debt, and £52,050,000 Sinking Fund, are outside the Committee's order of reference, leaving £439,016,000 of supply expenditure to be considered.

2. Post-war National Expenditure compared with pre-war.

20. The introductory chapter of the main Report deals somewhat fully with the amount and character of post-war expenditure. We do not, however, feel that a proper perspective can be obtained by a comparison only of one post-war year with another. The following classification of the several heads of expenditure in comparison with the relative expenditure in 1913 will serve to indicate the directions in which large increases have taken place.

National Expenditure.

<i>Services.</i>	1913-14	1931-32 (Estimated)	+ Increase or - Decrease	Percentage of Increase 1931-32 over 1913-14.	1931-2 reduced to 1913-14 (145 : 100)
Total	£000. 195,800	£000. 884,900	+ 689,100		£000. 610,300
Less self balancing ...	25,700	81,500	+ 55,800		56,200
	170,100	803,400	+ 633,300	= 372·31	554,100
				Distribu- tion of Increase £000. 633,300 = 100.	
<i>Debt, War Pensions, etc.</i>					
Debt Interest and Man- agement.	16,900	302,900	+ 286,000		208,896
War Pensions... ..	—	50,396	+ 50,396		34,756
Imperial War Graves... ..	—	602	+ 602		416
	16,900	353,898	+ 336,998		244,068
<i>Add Sinking Fund ...</i>	7,600	52,100	+ 44,500		35,931
	24,500	405,998	+ 381,498	60·24	279,999
<i>Defence Services.</i>					
Navy	49,078	52,181	+ 3,103		35,987
Army (including Ord- nance Factories).	29,000	40,794	+ 11,794		28,133
Air Force	—	18,437	+ 18,437		12,715
	78,078	111,412	+ 33,334	5·26	76,835
<i>Social Services.</i>					
National Health Insur- ance.	3,966	6,491	+ 2,525		4,476
Unemployment Insc.	602	45,108	+ 44,506		31,109
Old Age Pensions ...	9,805	38,197	+ 28,392		26,343
Widows', etc., Pensions	—	10,000	+ 10,000		6,897
Health Service Grants	209	188	— 021		129
Housing Grants ...	—	14,543	+ 14,543		10,030
	14,582	114,527	+ 99,945	15·79	78,984
<i>Education.</i>					
Grants	16,504	56,767	+ 40,263	6·35	39,150

<i>Services.</i>	1913-14.	1931-32.	+ Increase or - Decrease	Percentage of Increase 1931-32 over 1913-14.	1931-2 reduced to 1913-14 (145 : 100)
<i>Development.</i>					
Agriculture, etc. ...	390	5,428	+ 5,038		3,743
Exports Credits, etc.	—	1,867	+ 1,867		1,287
Scientific Research ...	452	1,263	+ 811		871
Unemployment Grants	054	3,585	+ 3,531		2,473
	896	12,143	+ 11,247	1.78	8,374
<i>Police and Prisons.</i>					
Police	440	11,950	+ 11,510		8,241
Prisons... ..	851	1,032	+ 181		712
	1,291	12,982	+ 11,691	1.85	8,953
<i>Tax Collection.</i>					
Customs and Excise ...	2,118	4,346	+ 2,158		2,997
Inland Revenue ...	2,104	7,170	+ 5,066		4,945
	4,292	11,516	+ 7,224	1.14	7,942
<i>Grants to Local Revenues.</i>					
Taxation and Tithe ...	7,922	46,246*	+ 38,324	6.04	31,894
<i>Other Services.</i>					
Foreign and Colonial...	1,498	2,834	+ 1,336		1,954
Works, Buildings, and Stationery.	2,943	5,536	+ 2,593		3,818
Oversea Settlement ...	—	265	+ 265		183
Training Unemployed	—	563	+ 563		388
Civil Superannuation...	786	1,927	+ 1,141		1,329
General Administration, etc.	4,888	10,018	+ 5,130		6,909
Miscellaneous Grants...	425	889	+ 464		613
Irish Services	10,700	9,800	- 900		6,759
	21,240	31,832	+ 10,592	1.67	21,953
Amount deducted from pre-1928 expenditure to adjust to present basis.	800	—	- 800	-0.12	
Totals ...	170,105	803,423	+ 633,318	100	554,084

* Includes £26,000,000 in respect of rating relief given to industry and agriculture under the Local Government Act, 1929.

21. From the foregoing table, it will be seen that out of a total increase of £633,318,000, no less than £381,498,000 (60.24 per cent.) is on account of Debt, War Pensions, etc., and if there be added the increase in respect of Defence Services £33,334,000 as being generally related to like purposes, the increase is £414,832,000, namely 65.50 per cent. of the total increase. Next in order of increase are the Social Services. To the sum of £99,945,000 there has to be added £12,324,000 increase under grants to local Revenues (i.e. £38,324,000 less £26,000,000 for de-rating), showing a total increase of £112,269,000, namely 17.73 per cent. The increase on Education is £40,263,000, namely 6.35 per cent.

22. In any appreciation of 1931-32 figures with those of 1913-14 regard must be paid to the present lower value of money, and the figures given in the above table of 1931-32 expenditure expressed in 1913-14 prices permit of a more accurate comparison. The degrees in which specific classes of national expenditure are responsive to changes in price levels necessarily vary with their different constituents. One fact, however, emerges, and it is, that by far the largest single item, namely that in respect of Debt Interest and Management, amounting to £302,900,000, remains (subject to actual reduction of debt and conversion operations) fixed in terms of money and its burden increases with any fall in price level.

23. Our colleagues comment upon the degree to which national taxation now absorbs the national income as compared with pre-war years, and seek to relate this to the post-war policy of Parliament in matters of expenditure.

This, in our judgment, must tend to carry a wrong impression as to the nature of the burden of taxation and its causes.

The following table shows:—

- (a) the percentage distribution of Government expenditure under the various heads for 1913/14, 1929/30, and 1931/32, and
 (b) the proportion of various heads of Government expenditure to national income for 1913/14 and 1929/30.

<i>Services</i>	Per Cent. of Total.			Per Cent. of National Income.	
	1913/14.	1929/30.	1931/32.	1913/14 £2,300 mills.	1929/30 £4,000 mills.
<i>War Debt, Pensions, etc.</i>					
Debt Interest and Management.	9.94	41.23	37.71	74	7.80
War Pensions ...	—	7.20	6.27	—	1.36
Imperial War Graves	—	.07	.07	—	.01

<i>Services.</i>	Per Cent. of Total.			Per Cent. of National Income.	
	1913/14.	1929/30.	1931/32.	1913/14 £2,300 mills.	1929/30. £4,000 mills.
Add Sinking Fund ...	9.94 4.47	48.50 6.30	44.05 6.48	.74 .32	9.17 1.19
	14.41	54.80	50.53	1.06	10.36
<i>Defence Services.</i>					
Navy	28.85	7.48	6.50	2.14	1.42
Army (inc. Ordnance Factories)	17.05	5.50	5.08	1.25	1.04
Air Force	—	2.27	2.29	—	.43
	45.90	15.25	13.87	3.39	2.89
<i>Social Services.</i>					
National Health Insur- ance.	2.33	.83	.80	.17	.16
Unemployment Insur- ance.	.35	2.56	5.62	.03	.49
Old Age Pensions ...	5.76	4.61	4.75	.43	.87
Widows, etc., Pensions	—	.53	1.25	—	.10
Health Services Grants	.12	.55	.02	—	.10
Housing Grants ...	—	1.69	1.81	—	.32
	8.56	10.77	14.25	.63	2.04
<i>Education.</i>					
Grants	9.70	6.37	7.06	.72	1.21
<i>Development.</i>					
Agriculture, etc. ...	.23	1.09	.68	.01	.21
Export Credits, etc. ...	—	.11	.23	—	.02
Scientific Research ...	.27	.18	.16	.02	.03
Unemployment Grants	.03	.26	.44	—	.05
	.53	1.64	1.51	.03	.31
<i>Police and Prisons.</i>					
Police ... ..	.26	1.11	1.49	.02	.21
Prisons ... ..	.50	.14	.13	.04	.03
	.76	1.25	1.62	.06	.24
<i>Tax Collections.</i>					
Customs and Excise ...	1.29	.59	.54	.10	.11
Inland Revenue ...	1.24	.93	.90	.10	.18
	2.53	1.52	1.44	.20	.29
<i>Grants to Local Revenues</i>					
Taxation and Tithe ...	4.66	4.16	5.76	.34	.79

<i>Services.</i>	Per cent. of Total.			Per cent. of National Income.	
	1913/14.	1929/30.	1931/32.	1913/14. £2,300 mills.	1929/30 £4,000 mills.
<i>Other Services.</i>					
Foreign and Colonial	.88	.29	.35	.06	.06
Works, Buildings and Stationery.	1.73	.64	.69	.13	.12
Oversea Settlement ...	—	.11	.03	—	.02
Training Unemployed	—	.10	.07	—	.02
Civil Superannuation...	.46	.24	.24	.03	.05
General Administration, etc.	2.87	1.36	1.25	.21	.26
Miscellaneous Grants	.25	.24	.11	.01	.04
Irish Services	6.29	1.26	1.22	.50	.23
	12.48	4.24	3.96	.94	.80
Amount deducted from pre-1928 expenditure to adjust to present basis.	.47	—	—	.03	—
TOTALS	100.00	100.00	100.00	7.4	18.93

It will be seen that the proportion of expenditure to national income has risen from 7.4 per cent. in 1913/1914 to 18.93 per cent. in 1929/1930, an increase of 11.53 per cent. The principal increases are :—

Debt Interest and Management ...	7.06 per cent.
Sinking Fund ... ..	.87 per cent.
War Pensions	1.36 per cent.
Social Services	1.41 per cent.

The first three items together account for 9.29 per cent. On the Defence Services the proportion has fallen by .5 per cent. If this item be deducted, then the total increase taken into account in respect of all other services is but 2.74 per cent. On Education the increase is .49 per cent.

On a fair consideration of these figures as well as of those which give the distribution of expenditure we cannot accept the view implicit in our colleagues' arguments that there has been an excessive increase in the proportion of the national income applied to social services and education or that they absorb an undue share of the proceeds of national taxation.

It is abundantly clear, therefore, that no appreciation of the measure of post-war national expenditure, whether in relation to national income or to national taxation, can be valid which does not take full account of the preponderate proportion of such expenditure which arises from the war.

24. The following table shows the cost of interest on the internal portion of the National Debt in relation to Budget receipts for the

year 1913/1914, and for each year since the war. It will be noted that although the actual interest charges fell from £308,664,000 in 1920/21 to £272,995,000 (estimated) in 1931/32, the percentage of budget receipts which it absorbs has risen from 22.42 per cent. to 33.02 per cent., and that approximately one-third of all the revenue raised is required for the payment of interest on debt internally held.

Internal Debt Interest in Relation to Budget Receipts.

Year.	Budget Receipts.	Internal Debt Interest.	Per cent of Col. 2 to Col. 1.
	(£000)	(£000)	per cent.
1913-14 ...	173,636	16,728	9.63
1919-20 ...	1,295,421	283,780	21.90
1920-21 ...	1,376,485	308,664	22.42
1921-22 ...	1,068,480	285,562	26.73
1922-23 ...	864,155	265,671	30.43
1923-24 ...	787,358	269,914	34.28
1924-25 ...	749,056	272,777	35.08
1925-26 ...	758,112	273,655	36.42
1926-27 ...	750,801	283,291	37.73
1927-28 ...	786,024	282,154	35.90
1928-29 ...	779,235	280,446	35.98
1929-30 ...	756,071	280,503	37.10
1930-31 ...	798,761	262,967	32.92
1931-32 ... (Estimate).	826,850	272,995	33.02

25. Another aspect of this heavy charge is made plain by the figures given in the further table, which show that although the actual payments of interest on the internal debt fell from £308,664,000 in 1920/21 to £272,995,000 (estimated) in 1931/32, a reduction of £35,669,000, the real cost to the nation in terms of goods and services has risen by £93,970,000, and if the reduction in the annual payment be taken into account then the burden of financing the internal debt has increased by the equivalent of £114,658,000, or 73 per cent. :—

Internal Debt Interest adjusted in Relation to Price Levels.

—	Actual Cost.	Cost of Living (June). (July, 1914=100).	Cost adjusted on cost of living proportions.
	£000		£000
1920/21 ...	308,664	250	179,025
1925/26 ...	273,655	172	230,706
1931/32 ... (Estimate)	272,995	145	272,995

Adjustment.

	£000		£000	
1920/21. Actual Cost ...	308,664	Adjusted Cost ...	179,025	
Reduced for comparison to	272,995,	giving comparative		
		adjusted cost ...	158,337	
Adjusted cost for 1920/21	...	...	158,337	
Adjusted cost for 1931/32	...	...	272,995	
Increase of real cost due to rise in value of money...			114,658	
			or 73 %	

26. The consideration of the national expenditure relating to Debt Interest, etc., was outside the purview of the Committee's work; but, having regard to the large degree in which this charge absorbs national revenue, we have felt justified in making some reference to it, and to the increasing burden which it imposes on the nation as a consequence of the fall in price levels.

3.—CIVIL SERVICE ADMINISTRATION.

(Chapter II. Main Report.)

27. We agree with the general summary of facts and the conclusions arrived at. We have been impressed by the efficiency of the various administrative departments and the degree of control exercised to secure reasonable economy.

4.—PAY AND PENSIONS.

(Chapter III. Main Report.)

28. We are in agreement with this part of the main report subject to the following reservations:—

A. Civil Service.

Industrial Employees.

In the light of the facts and circumstances ascertained we are in accord with the view of our colleagues that the Award of 1924 relating to the employees in the Royal Dockyards and Ordnance Factories should be reconsidered, **provided this is carried out through the recognised procedure of negotiation.**

29. We cannot, however, accept their conception of the "fair wages" basis when applied to the employees in question by a comparison with the outside engineering industry—a matter which also concerns employees of similar occupations in the public services. The general practice appears to be to regard outside rates as minima; and the "fair wages" principle, as we conceive it in its application to employment by the State, is that the State as a model employer should offer such terms as will secure the best service available, the comparison with private employment being

in relation to what the "best" employers in private industry are able to offer for equal service, regard being paid to security of employment and other factors. Further, it appears to us to be essential that the possibility of friction between the State and its servants should be avoided by the existence wherever practicable of an authoritative but impartial tribunal to secure that the "fair wages" principle is equitably applied.

30. Judged by the foregoing criteria, we feel it is open to serious question as to whether the outside engineering industry under present arrangements with its policy of *force majeure* as the ultimate means of disposing of questions of wage payment is satisfactory as providing a "fair wages" basis applicable to State employment.

31. We would, however, add another and general consideration, which is, that State employment implies a sense of civic responsibility which should reflect itself in the relationship between the State and its employees, and that if the State adopts a more liberal policy in the treatment of its servants when the national resources make this practicable, it may reasonably expect that such a policy will find a reciprocal attitude on the part of those it employs in times of national stress such as now exists.

B. Teachers.

32. While we agree with the view that an adjustment of the salaries of teachers is justified, we are unable to accept some of the arguments adduced and certain of the conclusions arrived at.

33. It appears to us to be perfectly reasonable that the State, being so largely concerned in the results of the settlement of teachers' salaries, should be a party to the negotiations to the extent of placing before the negotiators "the important national financial considerations which arise", and is entitled to expect that such considerations should be paid full regard to by the negotiating body. With regard, however, to the suggestion of our colleagues that the pay of teachers, like that of the police, should be fixed by the State, we can see no grounds of justification for determining the joint machinery of negotiation called into existence for the purpose of dealing with the pay and conditions of service of the teachers and which appears in the whole to have worked satisfactorily. The conditions of employment of the police are not closely comparable with those of the teachers, having regard to the different functions they perform, and we consider that the requirements of the case would be adequately met if provision were made within the existing machinery for the proper representation of the large financial interest of the State in the pay of teachers.

34. While we appreciate that in the recommendations of our colleagues for reducing teachers' salaries it is contemplated that

they will still retain an equivalent to more than double the pre-war average, we think it necessary to comment upon the latter to the extent of saying that an average remuneration of £97 per annum (the pre-war figure) to a profession charged with the responsibility for the instruction of the children of the nation, even when regard is paid to the contribution made by the State to the training of the teachers themselves, is an impossible basis from which to decide what is an equitable salary to be paid and to secure "an orderly and progressive solution of the salary problem in Public Elementary Schools by agreement".

The duties are both exacting and responsible, and in the case of certificated teachers require a training and qualifications of a standard certainly not lower than is expected of those ranks of the Civil Service who are in receipt of measurably comparable salaries.

35. While it is difficult to make a close comparison between the teaching profession and other branches of public employment, it seems reasonable to take the average salary as a basis of consideration as in the case of the Civil Service. A comparison of all certificated teachers' salaries with the third group of employees in the Civil Service (Executive and Clerical) gives results distinctly favourable to the Civil Service, namely £279 as against £281 4s. We do not, however, overlook the fact that the Civil Service is still subject to the cost of living index figure. On the other hand, the teachers contribute 5 per cent. of their salary to pension provisions. **A fair examination of the whole position, with due regard to the "fair wages" principle, would appear to justify consideration of an adjustment of teachers' salaries in the region of 12½ per cent. The actual figure, however, is one to be decided through the joint negotiating machinery existing for that purpose.**

36. In the degree that the existing salaries of secondary and fully employed technical teachers are related to the salaries of elementary teachers, a corresponding adjustment would fall to be made.

5. DEFENCE.

(Chapter IV. Main Report.)

37. We are in agreement with the Main Report on the general conclusions arrived at with regard to the Army, Navy and Air Force and ancillary services; but in respect of the Naval Dockyards we cannot accept the view of our colleagues as expressed in paragraph 239 on the question of the execution of naval construction work. While it is reasonable that in considering whether such work be undertaken in the Dockyards comparison should be made with the cost if carried out by private firms, any proper comparison designed to secure savings must not overlook the fact that to the extent that construction work ceases to be done in the Dockyards the proportion of fixed overhead charges falling to be borne by the

repair work will rise, and an apparent saving in the one direction may be more than offset in the other. Moreover, the importance in case of emergency of keeping the Dockyards reasonably fully employed must not be overlooked, and if the high standard of efficiency essential in Naval establishments is to be maintained, a policy which seems to contemplate the casualisation of employment in the Dockyards ought not lightly to be entered upon by reason only that from a narrow comparison of particular costs savings may appear to lie in that direction.

6. DEVELOPMENT.

(Chapter V. Main Report.)

38. We differ from our colleagues' point of view in regard to expenditure on development. We do not question that this expenditure must be fairly judged from the standpoint of economic benefit, but we disagree with the opinion implicit in their arguments that economic benefit is possible only if the "test of profit" in the sense used by them be present, or that operations are necessarily wasteful where the measure of State assistance exceeds the direct saving in respect of the maintenance of the unemployed. In our opinion, it is impossible to approve or disapprove expenditure on development by reference to these two factors alone. Other, and, to us, no less important considerations exist.

39. We would ourselves judge development expenditure by the broad test of whether it is designed to add to the Capital equipment of the country, to improve its technical and industrial efficiency, and whether having satisfied this desideratum it also provides employment for persons who otherwise would be idle. Nor do we exclude in this connection the improvement of what are often deprecatingly referred to as "amenities". The provision of swimming baths, of roads, which, among other purposes, may facilitate holiday traffic, can be justified as conducing to economic development—even on a strict utilitarian test—as satisfactorily as can much of the nation's private expenditure in other directions, although this latter may easily discharge the requirement of commercial profitability. Nor can the value of development works be narrowly assessed on the basis of immediate or early calculable direct financial return. On the contrary, it may well be that schemes of development requiring several years to carry out and the return from which may be even more remote, will be found to be of the most nationally profitable character.

We are of opinion, therefore, that expenditure on development can be justified when devoted to the removal of industrial or social defects or the creation of new capital assets and equipment which will inure to the general betterment of the economy of the nation.

40. The figures of this expenditure as given in the Main Report show it to be large and varied, embracing both Home and Empire Development, and our considered view is that on the whole it is wise expenditure of definite economic benefit. It appears to us that it is especially the time when, as now, much of the resources of the nation both of money and of man-power is compulsorily idle by reason of the disequilibrium in world industry and commerce, that the nation should utilise both money and men for the purpose of renewing its capital equipment and of improving its industrial and social structure.

41. A comparison of the cost of maintaining on a bare subsistence basis an unemployed man in idleness with the cost to the State of providing or accelerating work is incomplete and defective unless the value of the work as an addition to or an extension of the nation's equipment be taken fully into account.

Moreover, the idle man is not only a dead loss to the productive power of the community but there is the human waste in morale and self-respect arising from long periods of idleness, the effect upon his domestic economy and the reaction upon his dependants—all of which must be placed in the scale.

42. We do not overlook the limitations which exist of providing employment in this way, nor that they are inherent in the present economic system which is itself unable in times of industrial change and readjustment to provide employment for many who seek it, but we cannot subscribe to the doctrine that development in the sense used here must remain in abeyance unless and until it can be carried out on terms of commercial profitability. On the contrary, the renewal, the remodelling and the re-planning of the economic and social structure of the country is essentially a task which the State, in association with the local authorities and other large organisations, should undertake and, if this be so, it can hardly be doubted that the most favourable occasion is when money and man-power are readily available and can be utilised without the disturbing effects of the withdrawal of either from its normal employment in industry.

43. We consider that the "burden" upon industry of State expenditure for these purposes is commonly overestimated, and whilst the pressure upon State finances as at present regulated may be considerable, the objective and creative character of the expenditure must not be overlooked, nor the additional yield of taxation resulting from the increased volume of employment provided and the lessened demand upon the State for contributions to the maintenance of the unemployed.

44. We have referred earlier in our report to the benefits which industry draws from the provision of social services, and it draws

no less benefits from national development. Moreover, money spent in both cases passes through industry, employs industry, fructifies industry, and there appears to us no sufficient evidence that the money so spent would, in the economic conditions existing since the war, have been utilised for purposes on the whole more beneficial to industry.

45. Accordingly, we are not in favour of restricting expenditure on development by reference to the tests sought to be applied by our colleagues. We are, however, inclined to the view that advantage would result from a greater measure of co-ordination of the many activities of the State particularly related to development; that steps should be taken to remove overlapping or duplication of effort, and where, as is the case with the Road Fund, administrative policy is altered or normal programmes are accelerated in order to provide employment in development work, these emergency activities should be kept separate and distinguishable from the ordinary working of the service. Indeed, it appears to us that all such activities might with material advantage both of control and of wise economy be co-ordinated into one definite service.

46. With these general appreciations of the place of development in the nation's activities, we record our comments upon the several recommendations of our colleagues upon particular development services :—

1.—Research.

47. We are in agreement with the conclusions in the Main Report so far as these are designed to secure the co-ordination of Research work and improved financial control. We also agree with the desirability of stimulating industry and agriculture to develop their own research activities.

2.—The Road Fund.

48. We are unable to concur in the recommendation that the Road Fund should cease to be treated as a separate self-contained fund, and henceforth be voted as part of the supply expenditure. The advantages claimed for the proposal appear to us to be more theoretical than real. A fully documented report and Statement of Accounts of the fund is annually presented to Parliament: the accounts are subject to audit by the Comptroller and Auditor General and also to the scrutiny and criticism of the Public Accounts Committee.

49. The receipts into the fund arise from taxation originally imposed in 1909 for specific expenditure designed to facilitate the use and development of the vehicles taxed and not in aid of the general

revenue of the country. The fact that in 1926 and 1927 the cash balances were "raided" to the tune of £7,000,000, and £12,000,000, respectively, for the general relief of the Exchequer did not alter the character or object of this special vehicle taxation, but rather served to emphasise it and to afford Parliament and the country an opportunity of observing that the revenues of the fund were being diverted from their intended purposes. The appropriation of these sums clearly cannot be disregarded in any consideration of the present necessity of borrowing for the fund, the need for which borrowing arises as a consequence of a definite policy of acceleration of works in relief of unemployment. In addition to these raids, one-third of the taxation on ordinary motor cars and motor-cycles, amounting this year to nearly £5,000,000, has from March, 1926, been taken as general Exchequer revenue, on the basis, presumably, of a luxury tax upon the owners of such vehicles. Of the remaining revenue, a large proportion is now allocated under Statute (the Local Government Act, 1929, in particular) or is, in effect, charged for maintenance grants, etc., to local highway authorities.

50. Both the local highway authorities and the payers of motor vehicle taxation regard—and having in mind the origin and nature of this taxation are, in our view, entitled to regard—the Road Fund as an allocated fund for highway and cognate purposes, and would properly object to its diversion into the general revenue receipts of the Exchequer. As a supply service, any future excess of income over expenditure would, *ipso facto*, be applied annually in relief of general expenditure not related to road and like improvements, and thus, *pro tanto*, the fund would be systematically raided in relief of general taxation. That these raids would automatically take place as part of normal budgetary operations, and would, therefore, for the most part be unnoticed, does not seem to us to make the proposal any less a fundamental departure from the purposes for which this special taxation was originally levied and is now paid.

51. Furthermore, the separate existence of the Road Fund enables the Minister of Transport, subject to exceptional circumstances, to make reasonably long-term arrangements with the local highway authorities and to encourage the "Programme" policy. If the fund becomes a supply service it will, presumably, be the subject of annual review and argument between the Treasury and the Minister. This, we think, would be bad from the point of view of good administration in the Roads Department: would involve uncertainties in the minds of local highway authorities: would militate against well-thought out highway policy, and would not result in ultimate economy.

52. As to the proposal for a limitation of expenditure in immediate future years, we are inclined to the view that because, as

we understand, road and like expenditure has been regarded as affording means of providing a greater measure of employment more rapidly than other works, the promotion and acceleration of road programmes has been looked at too much from that aspect and too little, perhaps, from that of present need or of immediate cost. While we think it would be difficult to designate any particular road as serving pleasure, more than other, traffic; or, if it were possible, to say that the cost of such road is therefore uneconomic, we feel that there are substantial grounds for the general opinion that the development of arterial roads has reached a point where, in present financial circumstances, a slowing down might take place without serious disadvantage. The degree in which this may be possible is necessarily related to present commitments and the merits of particular schemes. It appears to us that the rapid acceleration of the trunk roads programme and the Five Year programme of works may be found to have intensified the problem of road congestion in the large Cities and Towns and their adjoining Urban areas, thus accentuating the need for street improvement in those areas, with consequent earlier, if not, additional expenditure. We are aware that the employment capacity is much less on improvement schemes than on main road schemes in relation to the total cost, because of the large compensation generally to be paid in respect of the former; but we cannot help feeling that the problem of improving traffic facilities would be assisted by a reconsideration and re-alignment of the present policy with special regard to congested areas.

53. We have considered the information placed before us as to the present standard of maintenance, and we are unable to conclude that it is generally higher than is necessary. We understand that the expenditure on road maintenance is carefully checked, and every effort is made to reduce the cost within the limit of avoidance of subsequent additional expense. We doubt, therefore, whether the general lowering of the standard of maintenance of the roads would, in the long run, prove to be economical.

54. Whilst we agree with our Colleagues that a more extended view should be taken of the future finance of London traffic facilities, we do not share their outlook that what can be afforded is necessarily related to a given rate of expenditure. The London traffic problem has reached a state when the direct and indirect loss arising from congestion is such as to require full enquiry whether its continuation can long be afforded. We do not ignore the fact that London's problem in this respect is not only that of London's traffic. With respect to the Charing Cross Bridge Scheme, this we think must be viewed as a part of the whole problem, but if it can be shown that the contemplated outlay could be used to greater economic advantage, whether in relation to London's traffic problem or otherwise, the Ministry of Transport and the

Treasury will have the opportunity, if and when the scheme is again submitted to Parliament, of dealing with the expenditure aspect of it, and we do not doubt that the requirements of the present financial position as well as other factors will be taken into account in the consideration by those Departments as well as by Parliament itself.

55. We appreciate that in regard to the Charing Cross Bridge Scheme, the preponderate proportion of its cost will be on account of compensation and not of works, and that under existing circumstances compensation is inescapably a large contributory factor in the cost of London street improvements.

(3) Department of Overseas Trade.

56. We agree that it is reasonable that those who utilise the services of the Department upon matters of direct and particular interest to themselves should pay for such. We understand that where the cost is capable of approximate ascertainment an appropriate charge is made, and it may well be that this policy is capable of extension, or that the charges now made could be fairly increased, and if so, we consider such should be done. We are in some doubt, however, as to whether the general services, the increasing value and extent of which is more and more being realised and acknowledged by the trading interests of the country, could effectively be put upon a charge basis, or that, if they were, the revenue resulting would be sufficient to make the Department self-supporting. Bearing in mind the large measure of support and assistance given by competitive countries in the direction of fostering the trade of their nationals and the need in this respect, as well as in others of placing the traders and manufacturers of this country as nearly on a parity as is possible, we are unable to agree that it would be wise to discontinue the Department on the grounds *only* that it cannot be made self-supporting.

(5) Ministry of Agriculture and Fisheries.

57. We agree with our colleagues' conclusions and recommendations with the following exception:—

(1) *Land Drainage and Water Supply, etc.*

Recommendation (b).—We regard the proposed normal limitation of grant to the estimated saving to the State in the maintenance of the unemployed as an impossible basis of fixing State aid to drainage schemes. Nor do we think it would, if desirable, prove to be practicable.

6. Department of Agriculture (Scotland).

58. Bearing in mind that the Scottish Drainage Act was passed as recently as 1930, when the necessity for this differential treat-

ment was doubtless justified on the facts, and as no sufficient evidence has been submitted to us to show that the situation has since changed, we find ourselves unable to support the recommendation.

7. Development Fund.

59. We agree with the main Report on this matter.

8. Beet Sugar Industry—Great Britain.

60. Having regard to the contractual obligations under the Beet Sugar (Subsidy) Act, 1925, which does not expire until 1934, we can only concur in the comments of our colleagues and express the hope that the whole matter may then be fully and exhaustively reviewed.

61. We are unable to resist the feeling that the very considerable State assistance given by way of subsidy and duty preferences to this particular industry has failed to achieve commensurate results. While it may be that this is in some degree due to the steep fall in the world price of sugar, we consider that the reason is to be found more in the manner in which the assistance has been given and the large extent to which it has been applied towards the liberal remuneration of capital, when other important basic industries of the country have had to be content with a much lower return or no return at all.

Home grown beet sugar in 1930 represented only about 20 per cent. of the total consumption of the United Kingdom, whilst about one-third was cane sugar from Empire sources. And it ought not to be overlooked that at the same time as the State, by large subsidies, is stimulating the production of home-grown beet sugar, the national finances are also being called upon to provide assistance to certain cane sugar producing Colonies, where, owing to the contraction of the markets for their sugar, distress is so prevalent that local revenues, unaided, are unable to cope with it. The competition of home-grown beet sugar, assisted by large annual subsidies and other reliefs, is a factor, though perhaps a small one, in this state of affairs, and is we feel worthy of attention.

9. Forestry Commission.

62. This is particularly one of those forms of development which must necessarily be done by the State if serious attention is to be given to it at all. Its value cannot be judged from a purely commercial standpoint, and the Commissioners have ample justification for the attitude they have adopted towards their functions when they state that "the object of afforestation is not to provide a remunerative investment for State funds, but to meet certain deficiencies in the economic organisation of the country which otherwise would not be made good."

63. It was represented to the Committee that one of the considerations in mind when the present scheme was started was the bulky nature of timber as an import and its consequent heavy demands on tonnage. As a factor to be taken into account in the event of war, the necessity to import timber would be a serious consideration having regard to past experience, which showed that as much tonnage had to be devoted to timber as to food imports.

64. Another important feature, however, is that excessive forest depletion is at present going on in most parts of the world without adequate replacement by new planting, and considerable concern is felt as to the future of supplies. In Great Britain, with the break-up of estates, woods are being felled and not replanted. That process is likely to be accelerated and the work of the Commission remained as one of the few efforts to reconstitute rural Britain.

While the unplanted land already held by the Commission is 173,000 acres, in spite of this reserve their present programme of planting could only be carried on if further lands were acquired. In the absence of new acquisitions, their planting programme must fall from 25,500 acres in 1931 to 17,000 acres in 1936.

The Commission are obtaining land on favourable terms and they do not anticipate that there is any prospect of a further fall in value which on that ground would make it economic to avoid further purchases at the present time.

65. On the request of the Committee the Commissioners submitted various schemes indicative of the effect of limiting in varying degrees their activities over the next five years' period in comparison with the present scale of operations. The recommendations in the Main Report would, it appears, involve the gradual abandonment of any considered forest policy, and we are unable to support the same. Further, while we agree that from the point of view of providing direct employment the results obtainable from afforestation are not very substantial, it is a consideration that under the recommendations of our colleagues 1,700 workers would be paid off and to a great degree must become chargeable upon the National Insurance funds. Moreover, in that connection it must not be overlooked that this country imports timber products to a value of between £40,000,000 and £50,000,000 per annum, a large amount of which is finished material.

66. The Commissioners state that the outlook with regard to production from privately-owned woods has become appreciably worse and is likely to deteriorate still further, and while we have some doubt as to the wisdom of any modification of the 10 years' scheme now in process, **we recommend that afforestation and the necessary acquisition of plantable land should continue as at present, but that the provision of holdings should be restricted to**

not more than twenty-five per annum. This it is estimated will effect a saving of £182,000 next year, or over the period 1932-36, a reduction of net expenditure by 18 per cent. as compared with the present programme.

10. Empire Marketing Board.

67. We are in agreement with the main Report on the recommendation to abolish this Board and with the reasons given as justifying that course.

11. Colonial Development Fund.

68. The establishment of this Fund appears to have resulted from the recognition of the necessity for raising the economic and social level of the indigenous populations of non-self-governing Colonies and Mandated Territories, by assisting the provision of works designed to increase productivity, and to provide and to improve health, education and other services in these countries and thus to promote and increase the trade and industry with the U.K. These areas can no longer, in the present economic organisation of the world, be looked at only as resources of raw material, but must also be considered as potential markets for the manufactures of this country. A reciprocal balance of trade is thus being aimed at by efforts to raise the economic level of the population, to increase their purchasing power and to extend the range and measure of their wants. This end is sought in aiding by grant or loan the construction of capital works, the provision of health services, education, transport, etc., which otherwise could not be done. The Fund was established *as recently as* 1929, and the Colonial authorities have been urged to utilise the financial resources thus made available in undertaking necessary and desirable schemes of development; and, in our opinion, to reduce by £250,000, i.e., 25 per cent., the grant to the Fund, would result in discouragement to those charged with the duty of formulating and promoting schemes; would lead to widespread uncertainty as to what are the intentions of H.M. Government; would diminish the value of efforts already made, and may largely nullify the results expected from money already spent.

69. We are satisfied that the Advisory Committee exercises a wise discretion in the use of money placed at its disposal and we can see no sufficient grounds for suddenly restricting the pursuit of a considered policy entered upon as recently as two years ago.

70. We would add that to regard the grants and loans from this Fund as going to relieve local government of its obligations is, in our opinion, to misinterpret entirely the distinctive object of the Fund and the declared policy which led to its establishment.

13. Unemployment Grants Committee.

71. We have already set forth our views on the question of the economic value of public expenditure for providing work for the unemployed, and we feel it unnecessary, therefore, to say more under this head, except that we disagree with our colleagues' proposals for the limitation of grants, as well as with the basis upon which they seek to apply such limitation.

72. While we agree that care should be taken to secure that the schemes submitted have both economic and social value, no evidence was before us to show that proper discrimination is not exercised in that respect, or that the authorities directly concerned have, because of the measure of grant, been lacking in all necessary efforts to avoid waste or excessive cost.

73. We agree as to the undesirability of two Departments making grants towards road and bridge improvements, and that as these are properly the concern of the Ministry of Transport, the Committee should discontinue making grants for such purpose.

7.—SOCIAL SERVICES.

(Chapter VI. Main Report.)

74. Earlier in our report we have expressed our views on the question of expenditure in relation to social services. We here record the extent of our agreement with or dissent from our colleagues' recommendations with regard to the following :—

1.—Unemployment Insurance.

75. We take the view that the Royal Commission on Unemployment Insurance is the appropriate body to advise the Government on this matter. The Commission have had the advantage of hearing evidence on the various aspects of the question and from many interested parties, including the Treasury and the Minister of Labour; they have been sitting almost continuously for some months and they have now issued an interim report.

While we fully appreciate that under its terms of reference the Committee are entitled to consider and report upon Unemployment Insurance, we have felt that for the Committee to do so upon a comparatively limited knowledge of the facts and of the issues involved, and in duplication of the work of a body appointed for that specific purpose, might well hinder, rather than help, the Government in any steps they might be recommended or desire to take.

76. While it may be that the Royal Commission are limited in their consideration of national expenditure to that arising from Unemployment Insurance, whereas this Committee have been charged with the duty to review the whole field of supply expenditure in

relation to the national revenue, present and prospective; yet, having regard to the evidence tendered by the Treasury and the Ministry of Labour and the knowledge as to the national finances generally available from the successive statements made by the Chancellor of the Exchequer and otherwise, we cannot share the view that the Members of the Royal Commission on Unemployment Insurance are not fully aware of the whole position in these respects, or that due weight has not or will not be given thereto in any recommendations they have made or may make.

For the rest, we are not in agreement with our colleagues' recommendations, nor with many of the statements upon which they are based.

2.—National Health Insurance.

77. We are in general agreement with the recommendations of our colleagues.

We share their views that provision should be made from within the insurance fund itself to enable societies to maintain the statutory rates of benefit and also to retain in benefit members suffering from prolonged unemployment where, from reasons of the heavy incidence of sickness and/or unemployment, societies would otherwise be unable to do so. We cannot, however, agree that the rights of unemployed members should, after the end of this year, be limited to the extent provided by the National Health Insurance Act, 1928.

78. The present position of the unemployed member is that normally he retains his membership rights to full benefits for a period of eighteen months: that under the National Health Insurance Act, 1928, he is given a further period of twelve months at half-sickness benefit with medical and pension benefits; that at the expiration of this latter period he would have ceased to be insured but for the provision made by the National Health Insurance (Prolongation of Insurance) Act, 1930, under which the Exchequer undertook, at an estimated cost of £100,000 to £150,000 to pay thirty-six contributions for each Approved Society member who would otherwise, by reason of prolonged unemployment, have ceased to be insured during 1931: his rights under the Act of 1928 are thus continued for this year. We understand that no decision has yet been come to as to what action should be taken after the end of this year. If, as is recommended by our colleagues, the Prolongation of Insurance Act be not renewed, the effect will be that about 120,000 persons who have been continuously unemployed for more than two years and nine months will cease to be entitled to Health Insurance and Pension Benefits some time during 1932, and thereafter all insured persons unemployed for that period would automatically fall out of Insurance and Pension Benefits.

79. It seems to us that the money required to continue this emergency provision can be found from within the insurance fund without any unfair call upon the resources of societies whose members are more happily placed so far as employment is concerned. The inability of members to pay contributions as a consequence of long unemployment does not arise from any moral obliquity on their part, but from circumstances and causes beyond their control which fall unevenly and inequitably upon the membership of some of the societies; and this risk, as well as the higher sickness risk, both of which, it appears, are at one and the same time being felt with increasing severity by certain societies, should be shared by all insured persons either by a re-imposition and, if necessary, an increase of the original levy for the Central Fund, or by a direct levy upon disposable surpluses of societies. Had it been the case that instead of members being grouped in separate societies they had been aggregated into one whole these risks would, in the circumstances which have arisen, have been spread over the whole field of the assured and would have been so borne. In our view, it would be inequitable in the extreme if, at one end of a national insurance scheme some societies, more fortunately circumstanced, should be able to continue, and even to increase, additional benefits to their members, whilst at the other end less fortunate societies should be faced with the prospect of having to reduce benefits to below the statutory rates and at the same time to see a growing number of their members without title to any benefits at all.

80. We feel that surpluses, which for the most part arise from differential risks, should in the first place be available to mitigate inequalities of this character. **We are of opinion, therefore, that no society should, as a consequence of actually ascertained higher sickness risks, be forced to reduce benefits below the statutory rates, and that members suffering from prolonged unemployment who would, but for the provisions of the National Health Insurance (Prolongation of Insurance) Act, 1930, cease to be insured, should be retained in benefit as provided by that Act; and that the funds necessary for both purposes should be obtained by a direct levy on the disposable surpluses of societies.** We consider that a direct levy on disposable surpluses possesses advantages over the proposed re-imposition and increase of the levy for the Central Fund; the former method would, in our submission, be more equitable and would partake more of the real principle of insurance, namely, of pooling exceptional and abnormal risks. We do not, however, exclude consideration of both methods being used conjointly.

81. It has been represented to us that a direct levy on disposable surpluses would present serious administrative difficulties involving, perhaps, recasting the existing Additional Benefits Schemes. We would not minimise these difficulties, but we do not feel that they

should be insurmountable. However, should they prove to be so, then we would prefer, rather than to resort *only* to the re-imposition and increase of the levy, that the whole question of the widening inequalities between societies should be dealt with by the method of partial pooling of all surplus funds recommended by the Royal Commission on National Insurance in their report published in 1926.

3.—Maternity Scheme.

82. We have carefully examined the proposed scheme for the development of the maternity service in relation to its financial obligation upon the Exchequer, and bearing in mind the purpose of this Committee we have experienced some difficulty in fairly balancing the exigencies of the present financial position against the indisputable claims, alike on national as well as individual grounds, for the immediate provision of services which will lessen the very serious loss of life and of health in connection with maternity. This may, perhaps, be regarded as a case where the need for economy may be thought to exclude all question of the extension of a social service, however desirable such may be: that inasmuch as the nation has up to the present done without it, then its inauguration must wait over until better times. Pertinent as these considerations may be from the point of view of expenditure, we have been constrained to ask ourselves whether it is in the cause of wise economy in any real sense to allow over 3,000 women to die each year, and the health of many thousands more to be seriously damaged, as a result of childbirth or causes associated therewith: whether the heavy loss to the nation of lives, upon which under existing social services much money may already have been expended, or the cost in terms of future expenditure necessitated by the seriously impaired health of many of those who survive the hazards of childbirth, is not, leaving aside all other considerations, greater than the annual sum of £1,500,000 estimated to be necessary as a State grant to provide the contemplated extension of maternity services.

83. In coming to our decision, we cannot overlook the very disturbing facts revealed in the recently issued Interim Report of the Departmental Committee on Maternal Mortality and Morbidity, and especially the statement that of the 2,000 cases of maternal mortality investigated by the Committee their finding was that *not less than one-half were preventable*. The Departmental Committee detail the services they consider essential in order to lessen the toll of maternity upon the womanhood of the nation, and we find that they generally coincide with those the scheme proposed by the Government is designed to provide. The Committee, further, indicate that they are convinced that many preventable deaths can be, in fact, prevented by such services.

84. Having regard to these weighty statements and after considering the facts of the matter from the broad aspect of national well-being, no less in terms of ultimate financial economy than of human life and health, we have come to the conclusion that the proposed scheme for the extension of maternity services is an urgent necessity, is overdue, and ought not to be delayed on any grounds of temporary and, in our view, illusory economy. It appears to us abundantly clear that so far from the scheme being unduly ambitious in scope, it represents the bare minimum of requirement of any adequate attempt to avoid loss of life and injury to health known to be preventable.

85. We should have wished that ways and means to provide these additional services were available without further charge upon the national finances, but if this be not the case, we cannot think that it would be wise or desirable economy on that account to postpone the provision of facilities known to be capable of appreciably lessening the hazards and discomforts of childbirth.

86. We would add that under the Economy (Miscellaneous Provisions) Act, 1926, the Exchequer grants to National Health Insurance Funds were reduced by a sum substantially larger than the annual additional charge estimated to be necessary to provide these maternity services; and that this relief to the Exchequer resulted in an annual loss to the National Health Insurance Funds which, we understand, the Royal Commission on National Health Insurance in 1926, indicated would have been sufficient to finance maternity services similar in character to those now proposed.

4. Old Age and Blind Persons Pensions. (Non Contributory).

5. Widows', Orphans' and Old Age Contributory Pensions.

87. With regard to these sections of the main Report we only wish to observe that consideration of the rates of pension now paid can hardly be related to any fall in the cost of living either present or remotely prospective, and we feel the country generally would hesitate to contemplate making any reduction.

6. Housing.

(a) England and Wales.

88. We are not in agreement with our colleagues' recommendation that the existing State subsidy under the Housing (Financial Provisions) Act, 1924, of £7 10s. in urban areas, and £11 in rural areas, should be reduced to £5 and £8 10s. respectively, and that corresponding reductions should be made in the grants provided by the Housing Act, 1930.

89. It is unhappily the fact that even with the present rate of State subsidy and corresponding contribution from the rates, local authorities still find it difficult, if not impossible, to provide houses for those most needing them, owing to the comparatively high

rents they are compelled to charge. The Housing Act, 1930, was at once a recognition of this and an attempt to meet the minimum requirements of those still living under conditions which are an affront to common decency and every standard of civilisation; and any proposal likely to hinder the provision of decent housing accommodation for the many thousands urgently in need of it would, in our considered view, be the reverse of sound economy—whether national or local. Under the Housing Acts (Revision of Contributions) Order, 1926, the contributions payable by the Exchequer were reduced from £9 in urban areas, and £12 10s. in rural areas, to £7 10s. and £11 respectively, for houses completed in England and Wales after the 30th September, 1927, and it cannot be doubted that this reduction resulted in a serious slowing down of house building by local authorities, with very questionable economy on any long-range view. The following table shows, the total number of houses erected by local authorities with State assistance under the various Acts since 31st March, 1924 :—

Houses built with State assistance by Local Authorities in 1925-1931. (England and Wales.)

Year ended 31st March.	1919 Act.	1923 Act.	1924 Act.	1930 Act.	Total
1925	2,898	15,253	2,473	—	20,624
1926	1,087	16,231	26,900	—	44,218
1927	882	14,121	59,090	—	74,093
1928	196	13,785	90,053	—	104,034
1929	10	5,059	50,654	—	55,723
1930	32	5,599	54,614	—	60,245
1931	—	—	52,498	16	52,514
TOTALS	5,105	70,048	336,282*	16	411,451

* In addition, 5,823 houses were built by Private Enterprise and 1,534 by Public Utility Societies under the 1924 Act. The total built under the 1924 Act was therefore, 343,639.

90. The increase shown for the year ended 31st March, 1928, is partly accounted for by the special efforts made by local authorities to complete houses, before the operation of the reduced subsidies under the 1923 and 1924 Acts, as from the 1st October, 1927. But the even greater rate of increase in 1927 over 1926 would seem to show that this factor may easily be over-estimated. If, in fact, it were a large contributory factor, then it seems to us open to grave question whether the rapid acceleration of housing programmes chiefly to secure unreduced subsidies is likely to have conduced to economy, either in the planning or preparation of schemes or in the actual cost of the houses; and it may not be incorrect to assume that the increase in the average all-in cost per non-parlour house from £503 in the quarter ended December,

1926, to £518 in the quarter ended June, 1927, is closely related to the measure of acceleration that took place. If so, then it appears to us not improbable that many of the additional houses completed in 1927-28 cost from £9 to £15 more than those erected on the basis of contracts placed before the reduction of subsidies was announced in 1926.

91. It is obvious that the economical construction of houses by local authorities is not best achieved by the sudden acceleration of programmes in one particular period, with a subsequent equal or greater deceleration, as a consequence of the alteration in the rates of the State grant. For the three years 1926-28, the total built under the Act was 176,043, whereas in the three subsequent years the number fell to 157,766: over the seven years the average was 48,040 each year. Although the number of houses built from 1926 onwards falls lamentably short of the number assigned to each of the 15 years over which 2,500,000 were to be built under the scheme as devised at the time of the passing of the Act of 1924, and to secure which the financial provisions of the Act were designed, it is reasonable to assume that by 1927 the local authorities were getting into their stride and were planning ahead with the intention of providing houses in increasing numbers, and that for the succeeding years a progressively increasing number would have been built, but for the reduction in the subsidy as from the 1st October, 1927.

92. Consideration of the weight of the financial burden arising from the building of houses under the 1924 Act, as well as a proper estimation of how far the needs of the country, as admitted in 1924, have been met will be assisted by a comparison of the figures given in the foregoing table relative to houses built under the 1924 Act, with the programme of the annual construction in mind when the scheme was promoted and approved by Parliament, as set out in the following table. To the total of 343,639 shown in the preceding table for England and Wales, there should be added 52,407 for Scotland, giving a grand total of 396,046 built under the 1924 Act up to the 31st March, 1931.

Number of houses assigned to each of the 15 years under the 1924 Act Scheme.

<i>Year.</i>	<i>Houses.</i>	<i>Year.</i>	<i>Houses.</i>
1925	90,000*	1933	210,000
1926	100,000	1934	225,000
1927	110,000	1935	225,000
1928	120,000	1936	225,000
1929	135,000	1937	225,000
1930	150,000	1938	225,000
1931	170,000	1939	225,000
1932	190,000		

* Including 40,000 expected to be built under the 1923 Act before it expires.

93. These figures show that the scheme provided for the erection, by the end of 1931, of 835,000 houses, excluding the 40,000 expected in 1925, under the 1923 Act. While this was doubtless a statement of maximum expectations, set as a goal to be aimed at rather than, perhaps, easily attainable, the fact that only 396,046 houses have been built—less than 50 per cent.—is to us a sufficient indication that the State subsidy has not led to the wasteful or extravagant promotion of housing schemes under the 1924 Act. We consider, therefore, that no steps should be taken likely to slow down the building of houses by local authorities; that on the other hand the stimulus contained in the continued payment of the present rates of subsidy under the 1924 Act, and in the special grants for unhealthy areas and insanitary houses available under the Act of 1930, is still desirable; that the lessened housing activities of local authorities which would inevitably result from any reductions would be deplorable, and would prove, in the very short run, not to be wise economy. It ought not to be overlooked that in the working out of the finances of the 15 year scheme under the 1924 Act, the maximum charge on the Exchequer and the local rates was on the assumptions:—

- (a) That the full programme of 2,500,000 houses is carried out;
- (b) That $7\frac{1}{2}$ per cent. of the houses are built in agricultural parishes; and
- (c) That the full subsidy is payable in all cases during the whole of the period,

estimated to be as shown in the following table:—

Year.	<i>Exchequer Charge.</i>		<i>Charge on local rates.</i>
	£		£
1924-25	278,000
1925-26	1,072,000
1926-27	1,905,000
1927-28	2,823,000
1928-29	3,827,000
1929-30	4,946,000
1930-31	6,195,000
1931-32	7,601,000
1932-33	9,180,000
1933-34	10,930,000
1934-35	12,824,000
1935-36	14,761,000
1936-37	16,699,000
1937-38	18,636,000
1938-39	20,573,000
1939-40	22,511,000
			135,000
			521,000
			925,000
			1,371,000
			1,859,000
			2,403,000
			3,010,000
			3,693,000
			4,460,000
			5,310,000
			6,231,000
			7,172,000
			8,113,000
			9,054,000
			9,995,000
			10,936,000

Year.	Exchequer Charge.		Charge on local rates.
	£		£
1940-41 to 1963-64	...	23,156,000*	11,250,000*
1964-65	...	22,828,000	11,115,000
1965-66	...	22,084,000	10,729,000
1966-67	...	21,251,000	10,325,000
1967-68	...	20,333,000	9,879,000
1968-69	...	19,329,000	9,391,000
1969-70	...	18,210,000	8,847,000
1970-71	...	16,961,000	8,240,000
1971-72	...	15,555,000	7,557,000
1972-73	...	13,976,000	6,790,000
1973-74	...	12,226,000	5,940,000
1974-75	...	10,332,000	5,019,000
1975-76	...	8,395,000	4,078,000
1976-77	...	6,457,000	3,137,000
1977-78	...	4,520,000	2,196,000
1978-79	...	2,583,000	1,255,000
1979-80	...	645,000	314,000

* Per annum.

94. The Ministry of Health figures, based on surveys prepared by local authorities pursuant to the Act of 1930, show the following estimates for the next three years of the Exchequer charge under the Act of 1924 :—

	England and Wales.	Scotland.	Total.
	£	£	£
1931-2	3,160,000	492,649	3,652,649
1932-3	3,685,000	604,849	4,289,849
1933-4	4,210,000	717,049	4,927,049
Totals	11,055,000	1,814,547	12,869,547

95. These give a total estimated Exchequer charge for the three years of £12,869,543 as against the original maximum estimate of £27,711,000. In comparing these figures, the reduction of the subsidy from the 1st October, 1927, must be taken into account.

96. We would not, of course, contemplate that, in the altered financial circumstances, it would be desirable, even if it were possible, to stimulate local authorities to build on the scale originally planned for each year: nor would we suppose that the present state of the country's finances could support an annual charge of the order estimated in 1924: neither do we overlook the additional provision since made under the Housing Acts of 1926 and 1930. But we think that the foregoing figures sufficiently show that the housing problem of this country is not being solved at other than a minimum rate each year.

97. It is regrettable, as well as significant, that since September, 1929, there has been practically no reduction in building costs, notwithstanding the very heavy general fall in raw commodity prices, but we consider that this important aspect of the housing problem should be dealt with by measures other than that of reducing the number of houses to be built in the hope that by lessening demand costs can be made to respond more closely to the general fall in the price of prime materials. We feel that other and better methods of reducing building costs should and can be found than one which, in effect, would condemn persons living in unhealthy and unsanitary houses or rooms to remain there in order that economic factors relative to building costs should be forced to operate: such a method seems to us to be intolerable and we cannot persuade ourselves that the resources of alternative action are so exhausted as to make it necessary.

98. As to the fall in building costs since 1927, we consider it will be in the interests of the long-range policy of improvement in housing conditions in this country on economical lines that this should continue to go towards the reduction of the rents charged and chargeable for houses built under the Act, and not in reduction of the State subsidy. We have previously referred to the fact that the comparative high level of rents which have to be charged even with the existing State subsidy and rate contribution is so high as to preclude many of the worst-housed people from occupying the houses which Parliament by the subsidy provisions intended should be available for them. Moreover, the need for reduced rents is becoming more and more pressing as a consequence of the substantial and continuing fall in wages.

99. We would add that any reduction of subsidy cannot fail to have seriously disturbing effects on the five-year programmes (in Scotland three-year) which local authorities have recently submitted pursuant to the Housing Act, 1930, and the steps taken or to be taken to carry out such programmes. It would result in uncertainty and vacillation in the minds of local authorities: would impair their own budgetary provisions for such programmes and would throw once again the whole problem of meeting the shortage of houses into confusion. This cannot lead to sound economy, whether in administration or in expenditure.

100. Finally, in any consideration of the price the country can reasonably be expected to pay for housing, the question of relative need and alternative cost, cannot, it seems to us, be excluded. The accumulating consequences of the bad housing of a vital part of the nation, in impaired health and reduced efficiency, and the cost of both to the country, are large and important countervailing factors, leaving aside all humanitarian aspects. It will surely be of little avail to rationalise industry in its mechanical elements, if the housing conditions of the human element, present and

future, are to remain neglected and unimproved. A policy that would seek an improved industrial equipment for the nation, while leaving large numbers of the working population exposed to the dangers which inescapably arise from bad housing conditions, affecting physical and mental health, and productive and civic capacity would, in our judgment, be the reverse of economy, from whatever standpoint it might be judged.

101. Under Section 43 of the Housing Act, 1930, a review of the contributions to be made by the State will take place after the 1st October, 1933, and we are of opinion that the existing subsidies under the 1924 and 1930 Acts should remain undisturbed until such review has been made.

(b) Scotland.

102. Our remarks as to England and Wales apply equally to the rates of subsidy payable by the State for houses erected in Scotland. We wish only to add that no sufficient evidence has been submitted to lead us to the conclusion that the circumstances which called for the differentiation between the rates payable in Scotland and those payable in England have ceased to exist. We understand that this difference, which has operated as from the 1st October, 1927, when the original subsidies for Scotland remained unreduced, was based upon an ascertained necessity for special treatment by reason of the very low standard of housing in Scotland, even in comparison with that of England, and also because of geographical and other factors. We are not convinced that the higher rate of subsidy in Scotland was continued only for the purpose of stimulating local authorities to the proper performance of their duties.

103. While it may be that the position in Scotland will in the future warrant reconsideration and the adjustment of subsidies nearer to those being paid in England, we feel that the existing rates of subsidy for Scotland, under the 1924 and 1930 Acts, should, like those applicable to England and Wales, remain undisturbed until the general review under Section 43 of the Housing Act, 1930, and Section 25 of the Housing (Scotland) Act, 1930, takes place after October, 1933.

7. Education.

(a) General.

104. We differ fundamentally from the general outlook of our colleagues on the subject of elementary and higher education. Whether the expansion that has taken place since 1913 is properly described as rapid is a matter of approach, but in our submission, the extension of educational facilities is to be approved rather than deprecated, and it is noteworthy that this extension has had behind it the force of public opinion. From the evidence tendered and the

information available to the Committee, we can find no warrant for any doubt that expenditure upon education generally is wisely administered with due consideration to the results obtained or obtainable. The admitted general improvement of the standard of education provided is a sufficient proof of this, and is more an occasion for appreciation than for retardation, whether, as our Colleagues suggest, such standard is in many cases superior to that which the middle-class parent is providing for his own child or not. It is apposite here to state that of the 6,566,900 children in England and Wales of ages 5 to 15 estimated at 31 March, 1930, no less than 5,395,400 were being educated in State-maintained or State-aided elementary schools and the parents of the remaining 1,171,500 children are equally entitled to avail themselves of these schools for the education of their children if they choose. That for reasons of education or otherwise they do not cannot be regarded as affording any proper ground for a policy which would limit the standard of education in State-maintained or aided schools by reference to that obtainable in private schools.

105. Consideration of the present cost of education in relation to what the nation can reasonably be expected to afford by reference only to the statistics of increased expenditure in comparison with early periods is incomplete, unless due weight is given to the necessity for improvement in the character and enlargement of the field of facilities which the additional expenditure was intended to provide. The history of educational development during the last decade has been a conscious and nationally approved policy of levelling out inequalities of educational opportunity and of broadening on well-planned lines the scope, the function and the character of public education; and, it may here be noted, the pursuit of this policy has directly resulted in an appreciable improvement of the standard provided by private schools. In our judgment, it could not in any sense be in the interests of national economy, even in the present time of financial stringency, to seek at this stage to arrest this process; and we cannot agree to recommendations which would tend to restrict the field of educational opportunity of the majority of the children of the nation in order to meet financial necessities arising from causes for which they are not responsible, and the continuing burden of which they will in their turn as adults have to bear; on the contrary, they should be given every opportunity of securing the knowledge and ability that will enable them to shoulder the load, and if not to lighten it, at all events to avoid any augmentation of the existing inequalities of its incidence.

106. Thus apart altogether from the cultural aspects of education, to which all the children of the nation are equally entitled, a policy of limiting educational facilities would ill-equip them as active citizens of the next generation to meet the changing and intensified

economic conditions of the world, and to take their places in the reorganised and rationalised industrial mechanism of the country. It is a truism that in business it is impossible to pause without retrocession, and it appears to us to be not less so in the important business of educating the nation's children. At the same time, any steps to reduce the administrative or other costs of education without injury to its services are not only essential in the financial exigencies of the present, but are desirable at all times; we are, therefore, in accord generally with the recommendation for securing a reduction of the number of education authorities by a concentration of function in the larger local government units. We are not, however, convinced that, having regard to the national character of education, its development through the local authorities would be best continued by the State contribution ceasing to be on the basis of percentage grants and becoming merged in the general block grant system. This is a matter needing very careful consideration with equal regard to the finance of national and local government; and, in any event, it would seem wise, before adventuring upon this fundamental change in the financial relationship between the State and local education authorities, to await a fair period of experience of the working of the general block grant system for health and other services, initiated by the Local Government Act, 1929. We should here state that we do not subscribe to the opinion that the present system of percentage grants necessarily leads, or can be shown in any general degree to have led, to extravagant or careless expenditure on the part of local education authorities.

107. If any appreciable reduction of salaries results from the review now taking place, we agree that there will be grounds for reduction of the State grant in respect of expenditure on salaries; but in any alteration of grants embracing a revision of the present guaranteed minimum of 50 per cent. a wider provision than is proposed by our colleagues should, we think, be made to adjust the incidence of any reduction equitably between the rich and poor authorities. An all-round reduction applicable to rich and poor districts alike would, in our view seriously affect the educational facilities available in just those districts where they are most needed and where owing to the consequences of prolonged industrial depression it is being found increasingly difficult to maintain even the present standard of educational facilities. Special provision should also be made for the necessitous areas at present receiving an additional grant for elementary education.

(b) *Higher Education.*

108. We agree that, subject to our previous comments relative to the revision of grants, appropriate adjustments of grant for higher education should be made in respect of any reduction of teachers' salaries that may take place.

109. We must, however, dissent from the views of our Colleagues relative to the growth of secondary schools and from the recommendations based upon them. Section 14 (4) of the Education Act, 1921, laid down the principle that "children and young persons shall not be debarred from receiving the benefits of any form of education by which they are capable of profiting through inability to pay fees." The equity of the principle thus approved by Parliament is no less in 1931 than it was in 1921, and any proposals for a reduction of national expenditure involving a restriction of the progressive application of this principle would clearly be highly prejudicial to, and inequitable in its incidence upon, the child of poor parents. It should not, however, be concluded that the principle laid down in the Act of 1921 has even yet been translated into practice in any substantial degree, for at March, 1929, the number of full-time pupils in maintained or aided secondary schools did not exceed for England and Wales 386,993, or 9.8 per 1,000 of the estimated population at July, 1928; while of the 477,828 children in England and Wales between the ages of 10 and 11 years in public elementary schools in March, 1928, only 63,055, or 132 per 1,000, were admitted into secondary schools, and of this number only about 40 per cent. secured free places. How many of sufficient mental capacity to profit thereby were denied the opportunity of secondary education because of their parents inability to pay the requisite fees, and also from a lack of accommodation, it is difficult to compute; but it is safe to say it was very greatly in excess of the number who secured entry. The number of free place pupils in secondary schools was on 31st March, 1929, no more than 43.6 per cent. of the whole.

110. Reference to the provision for secondary education made by institutions not aided from public funds seems irrelevant when it is remembered that provision by local authorities became necessary precisely because such institutions have never been, nor are they now, open to the vast majority of children, for obvious economic reasons. These institutions cannot, therefore, be regarded as offering any additional accommodation to meet the needs of the child of poor parents and their existence is not a material factor in the proper consideration of the adequacy of the provision now made by the local authorities.

111. From the information furnished by the Board of Education we very much doubt whether any worth-while economy of public expenditure is likely to be achieved by the proposals of our colleagues to raise the scale of fees at present charged to fee payers. On the other hand, the facts of the case go to show that any such increase would most probably be followed by a falling off in the number of fee-paying pupils with consequent loss of fees otherwise receivable and a corresponding loss to the Exchequer and the local authorities. The fees charged by the different local

authorities vary in amount with the varying social conditions and customs of the respective areas, and unless they are related to these and other local factors there is grave danger that they may fail to attract fee-paying pupils with resultant unoccupied secondary school places. If these vacant places were to become available as free places there might be something to be said in favour, but hardly on the score of economy of the nature to be sought by the Committee. There are, moreover, very good grounds for the statement that at the present time there is a not inconsiderable number of secondary school places unoccupied or occupied by elementary pupils below the age of 11, because either the fees charged are too high to attract sufficient fee-paying pupils or the number of free places is too low, or both. This can hardly be held to be wise economy, and any proposal for a general increase of fees to a standard more closely approximating those charged by private schools, could not fail to accentuate this state of affairs, with loss to the Exchequer, to the local authorities and to the youth of the nation as a whole. **We are unable, therefore, to support such a proposal. We are likewise opposed to the proposal that an income test should henceforth be attached to the grant of free places and that modified fees should be charged to some parents. This would inevitably result in hardship for the child of parents unable to afford even the modified fee; would in effect reduce the number of free places available and therefore add to the already large number of children who, though of mental capacity to profit by secondary education, are excluded from it by reason of inability to pay fees. Notwithstanding the creditable fact that the school-life of free place holders is on the average considerably longer than that of fee-paying pupils, the measure of sacrifice of many parents in expenses and/or loss of earnings is not less, but probably more than, that of the better placed parents who either pay fees for public secondary school education for their children or send them to private schools. It is a matter for regret that in many cases this sacrifice, though at first willingly borne in the interests of the child, often becomes insupportable owing to adverse economic circumstances, with the consequent premature withdrawal of the child from school with a view to becoming a wage earner. The waste of this from every point of view is too apparent to need any amplification. We cannot persuade ourselves that the need for economy in expenditure is such that the nation would wish to raise the existing barrier of means which already completely shuts out from advanced educational opportunity all but a small proportion of children, or that any real or lasting economy is to be found in that direction.**

112. As to the existing free secondary schools, these numbered, on the 1st October, 1930, only 76 out of a total number of 1,365 schools and accommodated 29,507 pupils out of a total of 416,771. These free schools, we understand, are all situated in areas of an

industrial character, and in the majority of them industrial conditions are at the present time notoriously bad. The upper limit for free places was raised in February, 1930, to 50 per cent., and the Board of Education retained power to grant exception in particular cases, the conditions of the exercise of which were agreed by the Treasury; and we are informed that no education authority would now be given permission to introduce free secondary education without special Treasury sanction. From this it would seem that before sanction is given to an increase of free places beyond 50 per cent. or to the introduction of free secondary education, the equities of the case as between the rest of the country and the particular area are sufficiently taken into account by the Board of Education and the Treasury. In any case, any prospective saving from the recommendation of our colleagues in this respect would be of the *de minimis* order and would not seem likely in practice to justify itself.

8. MISCELLANEOUS SERVICES.

(Chapter VII. Main Report.)

1. War Pensions.

113. The general statement under this heading calls for no comment, but with regard to the reference in paragraph 534, that reconsideration of the rates of pension would follow from the adoption of the course referred to in the concluding chapter of the Main Report embracing an all-round reduction of income, in our view due consideration would in that event require to be paid to the fact that disablement is not only related to economic disability but extends largely in many cases into the field of personal and social disability involving onerous restrictions and limitations upon the ordinary enjoyment of the amenities of life which cannot be related to any fall in the cost of living or be regarded as closely comparable with any loss of income to be borne by persons not subjected to such disability.

2. British Broadcasting Corporation.

114. We disagree with the recommendations of the Main Report in that we think the introduction of the principle that the State should guarantee the payment of loan charges in respect of capital expenditure may constitute a dangerous precedent in regard to an undertaking which, on its formation, was intended to be a self-supporting one, and opens up possibilities in our minds that the history of the Road Fund and the raids upon its revenue may, at some future date, be repeated in connection with the Corporation, and that the State may, under its guarantee in respect of capital

expenditure, find it impossible to avoid an extension of its liability, and that calls may arise on the general revenue of the country to meet deficiencies not expected at the moment. We regard the principle underlying the formation of the Corporation as a self-contained and self-supporting service as a sound one, and ought not to be impinged upon as a result of its successful operation and the unexpected growth of licence revenues as a consequence.

115. Whilst it may be that entering upon large capital expenditure in respect of the acquisition of new premises was, in the circumstances that exist, unwise, the Corporation would at all events, under its present financial arrangements, be enabled to meet that capital expenditure out of revenue surpluses as they fell due, and without recourse to a State guarantee as proposed by our colleagues.

116. If the successful operation of State enterprise, on the basis of the Broadcasting Corporation, is to be regarded as a ground for appropriation of a larger measure of its receipts than was originally intended, it cannot make for the general success of this type of State service.

117. Finally, the Charter under which the Corporation at present operates is due to expire in December, 1936, and it seems to us that any revision of the proportion of the licence revenue to be retained by the Exchequer, as also other financial considerations in respect of the service, could most conveniently and appropriately be dealt with at that time rather than at the present time, and this would have the advantage of permitting of a wider appreciation of the financial requirements of the Corporation over a longer period of operation than is now possible.

(3) Exchequer Contributions to Local Revenues.

118. We agree that the general interdependence of national and local finance may have required, in any complete review of national expenditure, some reference to the finance of local authorities; but we would have wished that the Committee could have had the advantage of a fuller enquiry into this matter, including the taking of evidence and obtaining further and more exhaustive information.

119. In the absence of this, we feel bound to say that, in our opinion, their somewhat summary comments upon this important aspect of the nation's expenditure are calculated to convey a wrong impression.

120. Figures of the growth of the loan indebtedness of local authorities must lead to incomplete appreciations and defective conclusions, unless they are considered by reference to the many and varied causes which have led to that growth, and unless there be also taken into account the increased value of the assets possessed by local authorities as a result of that expenditure.

121. The following table gives details of the outstanding debt at 31st March, 1928, related to the principal services in respect of which it has been incurred :—

*Loan Debt of Local Authorities in England and Wales
at 31st March 1928.*

	Distribution of Loan Debt.	
	Total amount outstanding.	Percentage.
	£	
1. Education, Public Libraries and Museums.	51,016,217	4'55
2. Public Health Services	87,292,774	7'79
3. Lunatic and Mental Services	8,078,685	0'72
4. Housing (a)	382,702,233	34'13
5. Poor Relief	8,184,036	0'73
6. Highways, Bridges, Street Lighting, Private Street Works. (b)	98,482,250	8'78
7. Fire Brigades, Police and Administration of Justice.	5,156,404	0'46
8. Small Holdings and Allotments	20,282,291	1'81
9. Markets, Ferries, Waterworks, Gasworks, Electricity, Tramway and Omnibus undertakings, Harbours, Docks, Corporation estates etc.	425,829,080	37'98
10. Cemeteries	2,511,973	0'22
11. Other Specific Services	16,507,625	1'47
12. Unallocated Expenditure	10,428,972	0'93
13. Land Drainage, Embankment and River Conservancy.	4,785,582	0'43
14. Town Planning	843	—
	(c) 1,121,258,965	100'00%

(a) Including £39,408,900, the greater part of which is in respect of advances by Local Authorities to private individuals for the acquisition of houses under the Small Dwellings Acquisition Acts and Housing Acts 1923 to 1925.

(b) Including £1,772,910 on Private Street works and other works of private improvement, a large part of which is recoverable from private frontagers.

(c) This is the *gross* figure before deducting £69,799,407 standing to the credit of sinking funds: the *net* debt was therefore £1,051,459,558.

122. Unlike most of the national debt, the debt of local authorities is represented by capital assets of very great value, including land, houses, schools, hospitals, as well as transport, water, gas, electric light and other trading undertakings. No less than £425,829,080 or 37.98 per cent. of the total represents loan debt on trading undertakings, which in the year ended 1928, earned, taken together, very substantial surpluses, some of which went to the relief of rates.

123. Clearly, no proper appreciation of the growth of local expenditure can be assisted by reference to one item only of expenditure, such as that upon Poor Relief. Against the growth of local

government expenditure there must be set the increase of rateable value, which in so far as it is in respect of new properties coming into rating, is only made possible by previous expenditure, and its continuance assured by subsequent expenditure. The opening up and development of new urban areas as a result of the outward spread of population has called for large expenditure, both on revenue and loan account, in the provision of even the minimum services imposed upon local authorities, not only by Statute, but also by the common requirements of present day society; and a consideration of and judgments upon local government expenditure are incomplete which fail fully to take into account this large contributing factor, as well as the fact that the movement of population to housing estates publicly provided outside Cities and Towns calls for large additional outlay, without any corresponding reduction of expenditure being possible in the congested areas from which they are taken.

124. We are unable, therefore, to subscribe to the view that local authorities, in their own field of public expenditure, have been "piling up the public burdens"; and whilst we agree that in the domain of local finance, as well as in that of national finance, strict supervision and wise economy is desirable, no sufficient evidence was before the Committee to show that in general local government finances are not well-managed, or that the publicly elected persons charged with their administration are not fully sensible of their obligations in this respect.

125. Finally, it cannot be overlooked when considering present local government expenditure, that to a not inconsiderable degree it represents the liquidation of accumulated liabilities arising from an unwise and, as now appears abundantly clear, a very costly past neglect in the field of local government.

9. CONCLUSION.

126. In the introductory pages of our report we indicate that there are wide divergencies of opinion between our colleagues and ourselves as to the value of national expenditure and the grounds upon which it can be justified, as well as to the directions in which effective economy can be equitably sought and imposed; and the measure of our dissent from their recommendations is a reflection of our disagreement with, and the application of, the principles which our colleagues state in their concluding chapter have guided their proceedings.

127. In the diversified and complex task set before the Committee all members endeavoured with goodwill to secure agreement wherever possible, and although we differ fundamentally from our colleagues' point of view on many important aspects of the problem which confronted the Committee, we do not in any sense question

the sincerity of their belief that the proposals they submit are in the interests of the nation.

128. Equally, we have been no less impressed by the need for wise economy; nor have we been less sensible of the requirements of the present and prospective position of the Revenue.

129. We do not, however, agree that the kind of economy contemplated would be conducive to a restoration of trade or increased employment, or that a pre-war standard of prosperity could be accepted as being in any degree compatible with the enormously increased wealth producing capacity of to-day. Moreover, we consider that many of the recommendations of our colleagues would, in their operation, impose an unfair measure of sacrifice upon certain large sections of the community, many of whom are already feeling with considerable and growing severity the effects of what has graphically been described as the "economic blizzard," but would fail to lay under any comparable contribution others more favourably situated, many of whom are enjoying, to the extent of their fixed income, effortless benefits from the increased value of money due to falling prices. These include not only the holders of the National Debt, a large part of which was incurred when price levels were much higher than those which have for some years prevailed or which now prevail, but also the holders of the large post-war issues of Municipal Stocks, Fixed Income Debentures, etc., and of other money claims where, in general, similar factors have operated in varying, but appreciable, degrees.

130. Our conclusion is, therefore, that if sacrifices are to be called for in order to maintain budgetary stability; to restore and to extend the trade of this country, and to re-absorb the unemployed into industry, then such sacrifices should be made by all sections of the community, with proper regard to the relativities of capacity to make and to bear.

131. We take the view that the present financial difficulties of the country and of industry do not arise from any pursuit of wasteful public expenditure or lack of responsible control of such, but are much more closely related to the policy of deflation followed since the war and confirmed by the return to the gold standard, and the subsequent aggravation of the burden in this respect as a consequence of the further fall in world prices; and that to argue that the present budgetary position arises from public expenditure is to confuse cause with effect. The pursuit of this monetary policy and the subsequent accentuation of its effects by world causes has penalised with growing severity the productive and active elements of the nation, and at the same time has conferred fortuitous blessings on those possessed of money claims, protected by contract.

132. We appreciate that the problem of meeting this situation and of securing that the burden arising therefrom shall be equitably distributed is one of great difficulty; and, so far as debt externally

held is concerned, is complicated by important international considerations. To the extent, however, of the internal debt and of the fixed interest bearing investments or other like money claims of those resident in this country, the problem is well capable of equitable treatment within the existing system of taxation, and whilst we do not favour imposing any further burdens upon productive industry, we should, were the matter one falling within the purview of the Committee, feel fully justified in submitting that there is ample scope for securing such additional revenue as would enable budgetary stability to be maintained, by the adjustment of taxation in relation to the uncovenanted benefits now being received by the holders of fixed incomes.

133. Nor do we think that those more fortunately placed citizens in receipt of these benefits would—upon a proper realisation of the nation's financial necessities as set out in the main report—wish to withhold the comparatively slight measure of sacrifice which this additional taxation would involve, especially as it would leave them actually no worse off than they were when their title to the income to be differentially taxed originally arose, but would, perhaps, serve to assure the security of income which might otherwise be jeopardised by a continuance of the disequilibrium in national finances caused by changes of price level.

134. While we do not wholly subscribe to our colleagues' remarks as to the inadequacy of Cabinet control of national expenditure, we feel that their suggestion for setting up a Standing Finance Committee of the Cabinet is worthy of serious consideration.

135. In conclusion, we wish unreservedly to join with our colleagues in expressing warm appreciation of the invaluable assistance ungrudgingly rendered to the Committee by its Secretary, Mr. B. W. Gilbert, and of his unfailing courtesy, and in this appreciation we include, with equal measure, Sir Alfred Hurst who was attached to the Committee. The Committee are also much indebted to Mr. Waterfield and Mr. Morris for their very considerable help in the wide question of Defence and associated matters. To the heads of all Departments our thanks are also due for the ready and helpful way in which they placed at the disposal of the Committee the fullest information.

Finally, we would wish to express our thanks to the other members of the Civil Service who in any way helped forward the labours of the Committee.

We have the honour to be,

Sir,

Your obedient servants,

CHARLES LATHAM.

ARTHUR PUGH.

24 July, 1931.

APPEN
NATIONAL
TABLE A.—

	Details in Table.	1913.	1921.	1922.	1923.
I. GRANT SERVICES.					
		£m.	£m.	£m.	£m.
Services in Great Britain	B	26·9	130·5	94·4	100·7
Irish Services	—	10·7	28·4	14·3	12·8
II. SERVICES NATIONALLY ADMINISTERED.					
Debt Interest and Management	—	16·9	303·9	296·6	304·3
National Pensions and Insurance	C	14·4	134·9	120·8	114·7
Defence	D	78·1	178·3	118·0	112·4
Tax Collection	E	4·3	12·9	10·7	10·0
All Other Services	F	11·4	175·9†	88·0	49·6
TOTAL ORDINARY EXPENDITURE	—	162·7	964·8	742·8	704·5
Statutory Sinking Fund**	—	7·6	25·0	24·7	40·0
Amount deducted from pre 1928 Ex- penditure to adjust to present basis.	G	0·8	4·9	4·7	5·1
Post Office	—	24·2	56·4	50·0	49·3
Excess of Exchequer Issue to the Road Fund over Road Fund Expenditure.	—	·4	2·1	—·5	1·1
Roundings	—	+·1	—	—	—·1
TOTAL PUBLISHED FIGURE	—	195·8	1,053·2	821·7	799·9

NOTE.—The figures in all these tables for the years 1913 to 1927 inclusive are Appropriation Accounts and are subject to audit.

§ Including £2·6m. charged directly on Rating Relief Suspense Account.

* Including £4·8m. interest on National Savings Certificates met by borrowing.

† Including Post Office excess expenditure £9·3 millions.

‡ This total is less by £7·4m. than the sum of the above figures in that the amounts

**The amounts actually applied or available out of Revenue for REDUCTION OF DEAD-WEIGHT DEBT differed from the above figures owing to surpluses and deficits and were as follows :—

	7·7	70·7	126·2	88·3
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DIX I.
EXPENDITURE.
SUMMARY.

1924.	1925.	1926.	1927.	1928.	1929.	1930 Estimates.		1931 Estimates.
						Original	Total.	Original.
£m.	£m.	£m.	£m.	£m.	£m.	£m.	£m.	£m.
102.8 8.8	126.7 9.6	118.9 8.8	117.3 9.0	115.6 9.0	137.5§ 9.5	164.9 9.3	166.3 9.3	172.6 9.8
308.7 115.1 116.9 10.3 34.8	304.3 114.7 121.5 10.7 30.6	314.3 114.9 117.4 10.9 30.5	309.0 115.7 118.6 11.1 26.3	311.5 113.2 115.7 11.6 25.1	312.1* 119.0 115.4 11.5 24.8	304.6 130.7 111.9 12.0 26.3	304.6 141.8 112.7 12.0 27.5	302.9 150.2 111.4 11.5 26.3
697.4 45.0 5.1	718.1 50.0 5.5	715.7 60.0 8.9	707.0 65.0 10.1	701.7 57.5 —	729.8 47.7 —	759.7 55.4 —	774.2 55.4 —	784.7 52.0 —
50.9 .4 +.1	53.9 .8 —	54.7 —2 —	56.8 .1 +.1	57.1 3.5 —	58.7 1.3 +.2	60.3 -4.3 -1	60.3 -4.3 -2	58.2 -10.0 —
798.9	828.3	839.1	839.1	819.8	830.3‡	871.0	885.4	884.9

Audited Expenditure; for 1928 and 1929 the figures show expenditure as given in the

referred to in the notes § and * were not met from revenue.

						Estimate	Actual	
48.7	36.0	23.3	65.0	57.5	33.2	57.6	43.6	—

TABLE B.—GRANT

	1913.	1921.	1922.	1923.
	£000.	£000.	£000.	£000.
Exchequer Contributions to Local Revenues including Local Taxation Accounts and Tithe.	7,922	9,381	10,131	13,323
Education (including Teachers' Pensions) ...	16,504	53,731	47,410	46,269
Agriculture (including Forestry, Development Fund, Beet Sugar Subsidy).	390	24,011†	2,371	5,869
Road Fund Expenditure	936	8,547	12,154	12,913
Health Services	209	4,446	3,565	3,214
Housing	—	9,061	8,049	8,326
Police	440	7,844	7,096	6,689
Unemployment Grants and Loans	54	3,805	2,268	2,971
Coal Mines Subsidy	—	7,049	10	1
Miscellaneous	425	2,627	1,302	1,160
Total Grant Services£	26,880	130,502	94,356	100,735

* Borne directly on Rating
† Including Corn Production
Agricultural District
Land Settlements

TABLE C.—NATIONAL

	1913.	1921.	1922.	1923.
	£000.	£000.	£000.	£000.
War Pensions	—	95,810	80,630	72,596
Old Age Pensions (non-Contributory)	9,805	22,047	22,356	23,213
Widows, etc., Contributory Pensions	—	—	—	—
National Health Insurance	3,966	9,215	5,839	6,084
Unemployment Insurance	602	7,830	12,018	12,821
Total£	14,373	134,902	120,843	114,714

SERVICES.

1924.	1925.	1926.	1927.	1928.	1929.	1930 Estimates.		1931 Estimates.
						Original.	Total.	
£000. 13,627	£000. 14,114	£000. 14,185	£000. 15,726	£000. 16,407	£000. 28,971 *2,570 }	£000. 45,507	£000. 45,707	£000. 46,246
46,615 3,287	47,137 3,841	48,395 5,521	48,657 6,994	47,782 5,583	48,203 8,261	53,468 9,095	53,468 9,785	56,767 5,428
15,071 3,207 9,065 7,106 3,487 — 1,378	16,545 3,460 9,119 7,701 3,620 19,000 2,126	17,372 3,676 10,040 8,066 6,073 4,199 1,409	19,377 4,128 11,125 8,094 1,928 29 1,270	17,481 3,953 12,128 8,299 1,763 — 2,234	20,302 4,175 12,803 8,419 1,938 — 1,841	27,662 488 13,651 11,456 2,450 — 1,115	27,662 488 13,651 11,456 2,950 — 1,115	32,960 188 14,543 11,950 3,585 — 889
102,843	126,663	118,936	117,328	115,630	137,483	164,892	166,282	172,556

Relief Suspense Account.

Guarantee ...	£18,059,000.
velopment Grant ...	£1,000,000.
... ..	£2,647,000.

PENSIONS AND INSURANCE.

1924.	1925.	1926.	1927.	1928.	1929.	1930 Estimates.		1931 Estimates.
						Original.	Total.	
£000. 69,939 24,900 — 7,125 13,148	£000. 67,320 27,012 — 6,850 13,504	£000. 63,583 29,981 4,000 6,447 10,838	£000. 60,175 32,827 4,000 6,681 12,025	£000. 57,117 34,050 4,000 6,290 11,758	£000. 54,472 34,916 4,000 6,241 19,411	£000. 51,976 36,497 9,000 6,730 26,470	£000. 52,225 36,847 9,000 6,730 36,970	£000. 50,396 38,197 10,000 6,491 45,108
115,112	114,686	114,849	115,708	113,215	119,040	130,673	141,772	150,192

TABLE D.—

	1913.	1921.	1922.	1923.
	£000.	£000.	£000.	£000.
Navy	49,078	76,885	58,170	54,748
Army (including Ord. Factories)	29,000	87,433	50,589	46,865
Air Force	—	14,005	9,243	10,752
Total £	78,078	178,323	118,002	112,365

TABLE E.—TAX

	1913.	1921.	1922.	1923.
	£000.	£000.	£000.	£000.
Customs and Excise	2,188	5,667	4,410	4,161
Inland Revenue	2,104	7,268	6,316	5,891
Total £	4,292	12,935	10,726	10,052

TABLE F.—ALL

	1913.	1921.	1922.	1923.
	£000.	£000.	£000.	£000.
Foreign and Colonial Services	1,498	30,930	13,070	17,357
Imperial War Graves Commission	—	527	352	765
Oversea Settlement	—	21	59	428
Export Credits, Empire Marketing, Colonial Dev. Fund and Trade Facilities Acts Payments.	—	1,083	284	91
Prisons	851	1,629	1,148	1,071
Scientific Investigations, etc.	452	1,215	987	974
Currency Note Services	—	373	339	337
Works, Buildings and Stationery	2,943	7,439	5,042	4,909
Civil Superannuation (excluding Revenue Depts.)	786	1,747	1,549	1,440
Training of Ex-Service Men	—	12,200	7,096	4,173
„ „ Unemployed	—	—	—	44
Liquidation of War Commitments	—	86,128	47,146	7,176
Remainder (General Administration, etc.)... ..	4,904	{ 16,551 6,728 (a)	{ 10,956 (b)	10,797
Total £	11,434	166,571	88,028	49,562

(a) Importation of Coal.

(b) Including

DEFENCE.

1924.	1925.	1926.	1927.	1928.	1929.	1930 Estimates.		1931 Estimates.
						Original.	Total.	
£000. 56,341 45,736 14,826	£000. 60,715 45,123 15,708	£000. 57,868 43,947 15,623	£000. 58,841 44,401 15,380	£000. 57,832 41,572 16,364	£000. 56,608 41,612 17,189	£000. 52,395 41,348 18,159	£000. 53,098 41,366 18,178	£000. 52,181 40,794 18,437
116,903	121,546	117,438	118,622	115,768	115,409	111,902	112,642	111,412

COLLECTION.

1924.	1925.	1926.	1927.	1928.	1929.	1930 Estimates.		1931 Estimates.
						Original.	Total.	
£000. 4,145 6,139	£000. 4,257 6,449	£000. 4,355 6,517	£000. 4,371 6,705	£000. 4,356 7,218	£000. 4,449 7,038	£000. 4,547 7,464	£000. 4,549 7,475	£000. 4,346 7,170
10,284	10,706	10,872	11,076	11,574	11,487	12,011	12,024	11,516

OTHER SERVICES.

1924.	1925.	1926.	1927.	1928.	1929.	1930 Estimates.		1931 Estimates.
						Original.	Total.	
£000. 7,637 952 388 50	£000. 7,066 774 494 40	£000. 5,381 1,006 1,074 520	£000. 4,285 545 1,242 567	£000. 2,141 671 1,097 761	£000. 2,233 536 852 868	£000. 2,361 652 833 1,671	£000. 2,824 652 833 1,733	£000. 2,834 602 265 1,867
1,077 1,074 340 5,318 1,532 2,485 151 1,181 12,619	1,098 1,149 360 5,695 1,577 962 213 571 10,580	1,063 1,193 346 5,256 1,648 249 198 706 (10,386 (1,500 (a)	1,070 1,198 364 5,146 1,695 55 192 715 9,238	1,044 1,191 380 4,996 1,742 31 651 585 9,805	1,059 1,331 — 4,829 1,794 27 728 690 9,859	1,089 1,290 — 5,138 1,896 30 1,002 166 10,177	1,089 1,290 — 5,437 1,896 30 1,002 166 10,519	1,032 1,263 — 5,536 1,927 † 563 † 10,453
34,804	30,579	30,526	26,312	25,095	24,806	26,305	27,471	26,342

Importation of Coal.

† Included in Remainder.

TABLE G.—ADJUSTMENTS OF PRE-1923

In 1923 accounting changes were made involving the exclusion from the Budget in order to exhibit a proper comparison with later years the expenditure of the years have been added back to the total expenditure figures in Table A, in order to achieve

	Deducted from	1913-14.	1921-2.
INTEREST on Victory Bonds, etc., and on Ways and Means borrowing from Government Departments.	Debt Interest	£000. —	£000. 3,435
INTEREST on money raised under Un-employment Insurance Acts.	Remainder, Table F ...	—	103
RECEIPTS from FEE STAMPS	Remainder, Table F ...	654	1,194
	Tax Collection, Table E (Inland Revenue).	95	103
	Irish Services, Table A...	86	84
Total Fee Stamps ... .. £	... ..	835	1,381
TEACHERS' SUPERANNUATION CONTRIBUTIONS.	Education, Table B ...	—	—
TOTAL DEDUCTIONS from Audited Expenditure.	... ..	835	4,919

EXPENDITURE TO PRESENT BASIS.

figures of certain items which had hitherto entered into both Revenue and Expenditure. prior to 1928 has been adjusted by deduction of the above items. The amounts deducted reconciliation with the published figures of revenue and expenditure.

1922-3.	1923-4.	1924-5.	1925-6.	1926.	1927.	1928.
£000. 2,695	£000. 3,026	£000. 3,478	£000. 3,887	£000. 4,273	£000. 4,802	£000. —
718	784	406	361	573	1,178	—
1,126	1,120	1,094	1,083	1,094	1,103	—
106	114	109	111	109	121	—
27	31	31	32	34	36	—
1,259	1,265	1,234	1,226	1,237	1,260	—
—	—	—	—	2,779	2,896	7
4,672	5,075	5,118	5,474	8,862	10,136	7

APPENDIX II.

*(See paragraph 259 of Report.)***AIRSHIPS.***Copy of Letter Addressed to the Chancellor of the Exchequer.*

8th May, 1931.

DEAR CHANCELLOR OF THE EXCHEQUER,

In our examination of Air Estimates we have noted that provision has been made in Vote 3 in respect of Airships of £50,000 "on account," pending a decision of H.M. Government as to their future policy. We understand that before taking that decision H.M. Government would be glad to have before them our views on the question of the desirability of incurring further expenditure on this account. We have accordingly obtained from the Air Ministry a statement of the proposals which they intend to lay before the Cabinet, and have taken oral evidence thereon from the Secretary of the Ministry, Mr. Bullock.

The Air Ministry propose to adopt the policy of a "watching brief," including the refitting and recommissioning of R.100 and its use for short experimental flights, at a total estimated cost of £120,000, rising to £140,000 a year. This would involve a Supplementary Estimate of £70,000 this year, and a corresponding increase of expenditure in future years, against which the Air Ministry are unable to suggest any economies under other heads. This liability would continue until the experiments now being made in Germany and the U.S.A. have reached a point when it can be definitely stated either that there is no commercial future for the airship, or that it is worth while for H.M. Government to negotiate with outside interests for the construction and operation of airships on a commercial basis, presumably with the aid of a Government subsidy. We understand that the present Air Council do not contemplate in any circumstances a further programme of construction by the State itself.

After due consideration, we think that this proposal should be rejected, for the following reasons:—

(1) In the first place, we consider that in the present financial stringency an exceedingly strong case would have to be made out before any new service of this magnitude could be sanctioned. In our opinion no such case has been made out in favour of the present proposal.

(2) On the contrary, even if the financial situation were less unfavourable, we should regard further expenditure by the State on Airship development as extremely speculative:—

(a) It has always been open to grave doubt whether Airships can ever be flown under the conditions of safety and regularity which are essential to a commercial service; and this doubt has obviously been increased—to put it no higher—by the R.101 disaster.

(b) There appears to be no means of estimating the cost of operating such a service, including depreciation, or the probable receipts. Viewed as a business proposition, the scheme is a pure gamble; and while it can safely be assumed that a State subsidy would be needed for very many years to come, the amount required is quite uncertain.

(c) H.M. Government already spend £350,000 a year on subsidies to heavier-than-aircraft services, and we understand that plans for additional services are under consideration. At the same time new fast steamship services are being promoted by several companies; while the possibilities of new developments by wireless telegraphy and telephony are almost unlimited. It is at least doubtful whether the amount of fast traffic, both mail and passenger, will be great enough to support the competition of airships, which are unlikely to afford more than a compromise between the rival claims of speed, comfort, regularity and security, with these other forms of service.

(3) The Air Ministry contend that it is worth while to continue to operate the R.100 because it is only by this means that a trained crew can be retained in being and the highly skilled art of airship navigation kept alive in this country. We do not overlook this argument, but we would observe that on the Air Ministry's own showing the importance of this object is relative, not absolute; they are prepared to spend £140,000 a year to secure it, but not £240,000 (if helium has to be provided). If airship development is ever revived in this country as a result of successful experiments abroad, in our opinion it is reasonable to expect that we shall be able to make a friendly arrangement with other Governments for British crews to be given the necessary training on foreign airships. Facilities for training in the R.N. and R.A.F. are commonly provided by H.M. Government for the personnel of other countries and we do not think it necessary to pay £120,000 a year to insure against the risk that such facilities will be denied us, provided that we are willing to pay a reasonable price for the privilege.

(4) Although the Air Ministry inform us that they are determined at all costs to restrict expenditure during the next few years to a maximum of £140,000 a year, we think that it may prove very difficult to adhere to this resolution, especially if, as seems highly probable, public opinion should insist on the substitution of helium for hydrogen in the R.100 as a necessary measure of

safety. The present Council cannot of course bind its successors. Generally speaking, we think that the existence of a nucleus organisation is a standing temptation to expenditure on further developments, which the State is unlikely to be able to afford.

Even under favourable economic conditions, we think that the above considerations are such as would render very great caution necessary before further indefinite commitments were entered into by the State. Under existing financial conditions we regard them as conclusive against the Air Ministry proposal.

We therefore recommend that E.100 should forthwith be sold or dismantled, that expenditure in 1931 be restricted to the £50,000 provided in the Estimates, and that expenditure in future years be kept at least within the limit of £20,000 per annum mentioned by the Air Ministry. Whether it is really necessary to spend up to that limit we have not had time to satisfy ourselves; the details would no doubt be carefully scrutinised by the Treasury.

We think that there may be a good case for retaining Cardington, at any rate until a favourable opportunity occurs for disposal of the property; the question should be brought up for review after say three years.

Yours faithfully,
G. E. MAY.

The Right Hon. Philip Snowden, M.P.