

# SPENDING

OR  
THE ECONOMICS OF  
'ECONOMY'

*By*  
G. D. H. COLE

"Saving, not spending, we lay waste our powers"

Published by  
THE NEW STATESMAN AND NATION  
10 Great Queen Street, London, WC2

34140 CONTENTS

	<i>Page</i>
I—THE FRUITS OF PANIC .. .. .	3
II—WHAT ECONOMY MEANS .. .. .	13
III—THE ECONOMICS OF 'ECONOMY' .. .. .	25

TWO OTHER PAMPHLETS

THE  
**CRISIS**

What it is: How it arose:  
What to do.

By G. D. H. COLE and  
ERNEST BEVIN

*48 pages: Sixpence*

*Manchester Guardian* says:—"An admirably lucid account of the international causes of the crisis, the working of the gold standard, and the reasons for its breakdown."

*Daily Herald* says:—"One of the most clearly expressed reviews of the events leading up to the crisis, the crisis, and how to avoid crises in the future, that I have seen so far."

**WAR DEBTS  
& REPARATIONS**

What they are: Why  
they must be cancelled.

By G. D. H. COLE and  
R. S. POSTGATE

*40 pages: Sixpence*

*Financial News* says:—"The best short statement of the problem of war debts and reparations that we have seen."

*Times Literary Supplement* says:—"Mr. G. D. H. Cole and Mr. R. S. Postgate have done a real service in presenting the facts of the Reparations and War Debts problem in a short, impartial and intelligible form."

*Daily Herald* says:—"One of the most valuable reviews of war debts and reparations from their inception ever published."

Obtainable from any newsagent or bookstall;  
or post free from the Publishers

**NEW STATESMAN AND NATION**  
10 GREAT QUEEN STREET, LONDON, W.C.2

## I.—THE FRUITS OF PANIC

**A**MID the excitements of the financial crisis of 1931, the cry went up that the nation must economise. Were we not spending, as a nation, at the rate of £880,000,000 a year, compared with only £200,000,000 before the war? Was there not, according to the conclusions of the May Committee, the danger of a real deficit of £120,000,000 by the end of the financial year? Clearly the nation, as a nation, must be living beyond its means. Taxation, which absorbed only 11½ per cent. of the national income in 1914, was already taking at least 25 per cent. before the slump began; and now, with the national income falling, the proportion must be already even higher. The country, we were told, was threatened with ruin; and amid the panic scurrings of the electorate, the 'National' Government was returned to power with a mandate to save us from public bankruptcy and disgrace.

The 'National' Government had other mandates too. It was to save the country from the menace of inflation, and keep the pound securely anchored to gold. It had a 'doctor's mandate' to rescue trade and industry from the slough into which they had fallen, and to restore national prosperity as well as national credit. But its first business was to deal with the immediate crisis; and it began, quite wisely but wholly against what it had promised, by going off the gold standard—a feat which was applauded loudly as the salvation of industry by the very persons who had been most vehement a week or two before in denouncing the perils of inflation.

Thereafter the new Government set out to save industry and agriculture, to redress the unfavourable 'balance of trade' by the imposition of tariffs, and to rescue the national credit by drastic doses of public 'economy'. We were to import less and export more. We were to spend less, out of the public purse, and so free resources for the revival of industry. Extravagance, we were told, was at the root of all our troubles: by parsimony and abstinence had our forefathers piled up wealth, and if we would but live after their glorious example all things else should be added unto us. Private, as well as public, parsimony was held up to us as the chief of virtues; and men sacked their under-gardeners in a glow of patriotic righteousness.

All over the world, much the same things were being done. For years, the financial experts of the League of Nations and the Central

Banks had been adjuring the spendthrift debtor nations to economise, to balance their budgets at a lower level, and to reduce their expenditure in order to meet their debts. In the new world crisis, these efforts were redoubled. Financial advisers flitted about the world, shedding Spartan schemes for the establishment of budgetary equilibrium; and almost every nation began to take serious stock of the condition of its finances, and to consider in what spheres it could best achieve a drastic curtailment of expenditure. Naturally enough, most of these countries hit upon much the same devices as ourselves, though the more unfortunate were compelled to apply them with far greater ruthlessness. There were, in one country after another, drastic cuts in public wages and salaries, big reductions in the sums distributed to the unemployed, or spent on public works for the provision of employment, severe retrenchments in the social services of health, housing and education—but not, strangely it may seem, in the sums spent upon national armaments; for the political insecurity of the world increased with every addition to its economic distress.

Moreover, almost every country, alarmed by the development of the 'unfavourable balance of trade', had the bright thought of exporting more and importing less, or, when this proved to be impossible, at least of curtailing its imports more than its exports in order to meet the mounting burden of charges for its external debts, which of course grew heavier and heavier as world prices continued to fall. The restriction of imports was brought about in part by higher tariffs, and in part by all manner of quotas and prohibitions, and regulations on the supply of foreign exchange; and, as imports fell off, the need of States for additional revenue provided a supplementary and constantly growing inducement to the imposition of higher tariffs. World trade was strangled more and more by these devices; and by the end of 1931 the total value of world imports had fallen by 41 per cent., and of world exports by 43 per cent., in comparison with the totals of 1929.

Even the world's statesmen could not be unaware that every sale implies a buyer as well as a seller, and that it is accordingly impossible for all countries simultaneously to sell more and buy less. But to the politicians of each distressed State it appeared necessary that in their case at any rate the thing must be done; and the more any particular country restricted its imports and strained every nerve to expand its exports the greater seemed the need for all the others to do the same. Restrictions, quotas, higher tariffs in country A begat similar defensive and retaliatory measures

in countries B, C, and D; and these in turn provoked country A to still more drastic measures of regulation. It was easy enough to get the statesmen, when they met together in international conference, to agree that these vexatious restrictions ought to be abolished or relaxed. But no one was prepared—no one dared—to be the first to relax them: indeed, almost every country was continuously making them more severe.

It was often argued that the fault lay, not with the debtor countries, which were compelled to build up a favourable trade balance in order to meet the claims of foreign creditors, but rather with the creditor countries, which would not buy enough of the debtors' exports to balance the account. Especially it was urged that the United States, instead of keeping up and raising still higher an already mountainous protective tariff, ought, if she wished to be paid by her debtors, to take down her tariff wall and accept payment in an ever-increasing flood of imports. But in fact imports into the United States fell off even faster than exports to most other countries—their value in 1931 being only 48 per cent. of their value in 1929; and yet America, because her exports also fell off sharply—by 54 per cent. over the same period—saw her favourable trade balance shrink to a fraction of what it had been before the slump. It was 818 million dollars in 1929, and only 286 million in 1931. The United States suffered more from unemployment than most European countries: the American budget showed the most monstrous deficits of all; and American manufacturers were in no mood, if they could help it, to throw open the home market, which alone remained to them, to a deluge of imports from Europe. Instead, the United States Congress clamoured for Europe, in some unspecified way, to meet its contractual debts to the American taxpayer, and so relieve his burdens without throwing the American artisan out of work.

Thus all the world restricted and 'economised'; and still the world situation grew steadily worse. For everywhere national economy ran a losing race with trade depression. Budgets could not be balanced, because, whatever efforts were made to reduce expenditure, revenues persistently fell faster still. The most any country could claim was that by its restrictions and economies it was to some extent protecting itself against the consequences of the restrictions and economies imposed by the rest. The world seemed to be heading for a climax when the last factory left working in any country would at least be able to boast of the relative prosperity of having outlived all the others.

But, it will be objected, though the nations have admittedly gone tariff mad and trade is everywhere being strangled to death with quotas and restrictions of every conceivable sort, surely 'national economy' at least is a good, and a salutary discipline for mankind. For budgets ought to be balanced, and it is certainly no better for States than for individuals to live beyond their incomes. Agreed—with certain very important reservations. The first of these is that if all States had since 1929 by mutual consent lived beyond their incomes in agreed and suitable proportions, and met the consequent deficits simply by printing additional money, the world would not be suffering to-day from the calamitous fall in prices which has actually occurred, and at the least the effects of the slump could have been considerably mitigated. Observe that this would have been the case only if the countries of the world had embarked in concert on an agreed and limited programme of international inflation, and not if only the needier countries had inflated their currencies, while the others pursued a majestic policy of monetary deflation. It was not open to the debtors alone to follow this course; for to do so would have swollen past endurance the burden of external debts payable in deflated foreign currencies. That is why most of the distressed nations of Europe, from Germany to Bulgaria, have clung desperately to the gold standard throughout the crisis.

The second reservation is that the public income of a State is not like the private income of an individual. It is a share, variable at the will of the taxing authority, in a total varying with the ebbs and flows of national prosperity. A State may find itself living more beyond its income than before if the effect of its measures of retrenchment is to slow down the economic life of the nation, and so to reduce the incomes out of which its citizens have to pay their taxes, or the processes of exchanging goods and services on which it levies toll. This is true whether the predominant forms of taxation are direct or indirect; and it is also true in either case that the less a tax is bringing in, on account of economic depression, the harder it will be to raise it and the less productive any increase in its rate will be. The interest of States, as tax-gatherers, is far more in increasing wealth and taxable capacity than in keeping the absolute amount of taxation down to a minimum, regardless of the effects of its 'economies' on the volume and profitableness of production.

There is also a third reservation. States meet their expenditure partly out of tax revenue and partly out of loans. Normally, the proceeds of loans are used—except where budget deficits have actually arisen—only to finance expenditure that can reasonably be

regarded as productive, in some sense not as a rule very accurately defined. It is easy enough to see that the cost of building a State railway, or harbour, or electricity station, can reasonably be defrayed out of loans, only interest and a sufficient sinking fund being borne on the annual accounts, because such undertakings are destined to be directly productive of revenue out of which the loan charges can be met. A State borrowing money for such purposes is only in the same position as a joint stock company raising capital for the development of a productive undertaking. It is, moreover, generally admitted that, when the State or a local authority undertakes some constructional work, such as building a school, which is to last for a long period of years, the capital charge may reasonably be spread, by loan and sinking fund, over a corresponding period, or rather, for safety, over a period rather shorter than the anticipated life of the undertaking. But, at the edges, it is not easy to draw the line between undertakings which can properly be financed by way of loans and those which ought to be paid for wholly out of current revenue.

What, however, is clear is that the obligation upon a State—save under the conditions contemplated above—to balance its budget does not involve the same attitude to public borrowing for capital expenditure as to public spending out of revenue for non-reproductive purposes. For, in the first place, the times when the taxes are least productive and the demands for ‘economy’ most pressing—i.e. times of economic adversity—are also usually times, at all events in the richer countries, when money can be borrowed for both long and short terms at the cheapest rates, so that capital works can at such times be carried through at the lowest cost. This is so, not only because direct charges for interest are reduced, but also because contractors and other suppliers are willing to work at a lower margin of profit, materials can be bought at cheaper rates, and almost everything costs less than in more prosperous times. The capital burden on the future is thus kept low; and, if the enterprise is rightly planned, there is more than the ordinary prospect of the investment turning out well in the long run. Secondly, when the State gives orders for works of construction to be carried out, it not only helps directly to make industry less depressed than it would otherwise be, but also relieves itself of some part of the burden of maintaining the unemployed. Its expenditure is not, even from the narrowest point of view, a net cost; for men who are paid wages no longer need ‘doles’; and the money spent in employing them does not stop in their pockets, but continues to

circulate from them to the tradesmen from whom they buy goods, and so to manufacturers and to other workmen in an endless series of transactions.

This argument holds good, of course, only if the productive activity called into being by the enterprise of the State is a real addition to the current volume of enterprise, and not a mere diversion to use by the State of funds that would otherwise be used, and used no less well and productively, by others. For if every project of capital expenditure launched by the State causes a corresponding reduction in the volume of capital applied to productive investment by private individuals, there is no assurance of any real addition to the quantity of production or employment, and no advantage unless the State spends the money more wisely than it would be spent through the ordinary capital market. In normal times, the case for State spending on capital account can rest, under the present economic system, only on the contention that the State will spend the money to better advantage, in the public interest. But in abnormal times of acute business depression, another highly important consideration enters in. *For it is highly probable that, unless the State does take the responsibility for spending the money, it will not be spent at all.*

In times of fair business prosperity, such as the capitalist world used to regard as 'normal', the problem of 'idle money' hardly exists; for everyone who has money is eager either to invest it in order to make a profit or to lend it at interest to someone else who sees his way to making a profit by its use. At such times the balances which men keep at their banks are no more than the minimum they feel they must keep ready to meet cash demands; and the banks themselves find no difficulty in lending out at good interest as much money as they feel it safe to create. Long-term funds are speedily invested, and short-term funds readily borrowed and applied to production. The problem is rather that of shortage than of superabundance of capital and credit. But in times of business depression the situation is very different. The owner of capital who is asked to invest in industrial enterprise is more fearful of losing his capital than expectant of making a profit. The attempt to play for safety by lending at fixed interest instead of investing in shares forces down the yield of gilt-edged securities, and correspondingly forces up their stock exchange values, until the buying of them too threatens purchasers with loss of capital in the future—for if business recovers their prices are likely to fall as ordinary shares offer improving prospects of profit. At some point, therefore, the avidity

to buy up gilt-edged securities at high prices diminishes; and some of the owners of money prefer to leave it idle in the banks, even at a very low rate of interest, confident that, as long as the banks themselves remain solvent, their principal is safe, and that, if the banks are seriously threatened, the State will be forced to come to their aid with a guarantee of their deposits. Even impoverished Austria had to do this in the case of the Credit Anstalt, and Germany in that of the Danat Bank. The United States, indeed, with a very different banking system, left the unfortunate depositors to stand the racket of local bank failures; but even individualist America rushed in with the Reconstruction Finance Corporation to save the big national banks as soon as they were in serious danger. Certainly, thinks the depositor, the British Government would never allow one of the 'Big Five' to default.

Bank deposits, then, seem at least relatively safe in an insecure world; and accordingly, amid the deepening depression they tend to pile up unused, largely out of money which would under normal conditions have been applied to long-term investment. This embarrasses the bankers; for, even if they bring down deposit interest to a derisory rate, there is still something to pay, and they cannot make their usual profits unless they can find means of lending out the usual amount of money at a satisfactory rate of interest. But, in the circumstances, borrowers—or at any rate borrowers who seem credit-worthy—are exceedingly scarce. For contraction of capital investment carries with it a contraction in the demand for short-term credit, and bankers cannot maintain their loans in bad times unless they are prepared to run the risk of being 'frozen up' by lending short-term money for long-term uses, as happened in Austria and Germany; and even so the supply of eligible outlets for long-term capital is limited by the depression of industry. Banks consequently suffer from a plethora of unusable money; and rates of interest on such desirable short-term investments as Treasury Bills fall absurdly low.

When conditions such as these are in being, it simply is not true that State borrowing for public investment in capital undertakings diverts an equivalent sum of money from private investment. On the contrary, it results in putting otherwise unused and unusable funds to productive use. It adds to the current volume of production and employment, reduces public spending on 'doles', swells the revenue from taxation by increasing the effective income of the community, and ministers to a general revival of business activity. This is not to say that its influence is omnipotent, or that even the

wisest policy of public capital spending would avail to conquer the present depression. What is claimed is that it would make in the direction of recovery, not that it would avail by itself to bring prosperity to pass.

It is, of course, true that all spending of this sort is in one sense a burden on the future; for it involves interest and sinking-fund charges spread over a number of years. But this is true only in a sense in which the same thing is true of any and every form of capital investment, in private business equally with public enterprise. For every investment of capital constitutes a charge on the future—made in the confidence that this charge will be met because people will go on wanting the things which the investment is to be used to provide. State capital investment stands so far on the same footing as investment in a joint-stock company. It is 'saving' rather than 'spending', in the customary and often misleading use of these terms.

There is, however, a difference. As a rule, the private investor invests in ordinary business, and the entrepreneur promotes it, only in the expectation of making a direct profit by the sale of the goods or services which are to be produced. This is true of some forms of public enterprise—the Electricity Board's, or the Post Office's, for example—but not of all. The State has for the last decade been aiding and subsidising the erection of small houses—on a large though insufficient scale—at a known and accepted direct financial loss. A local authority, when it builds a new school, does not expect the fees, if there are any, to cover the cost. Houses and schools are built in the belief that the community needs them, and that to build them is economic because good housing and good education are necessary elements in national welfare.

But, our economisers object, things such as these are luxuries which, in times of depression and financial embarrassment, the community simply cannot afford. Find us projects that will bring in a safe 5 or 6 per cent. in direct financial return, and we shall be eager—not for the State to undertake them, but to take them in hand ourselves; for that is just the sort of investment we are looking for in vain. But if the State takes on unprofitable investments, on which the returns must be harvested in welfare and not in *sous complaints*, we, the taxpayers, shall be called upon to foot the bill. We refuse. Our profits have fallen off already, and we are overtaxed. We demand, instead of fresh burdens, a remission of those we are now compelled to bear. We insist on retrenchment—on the avoidance of all avoidable expenditure falling on either rates or taxes. It is

all very well to say that public expenditure will provide work. So it will, perhaps; but for us taxpayers, 'doles' come cheaper. Cut down the 'dole' to the lowest point consistent with the May Committee's conception of humanity; but for Heaven's sake go on paying 'doles' and don't spend more money trying to set people to work.

So say the advocates of 'economy', sometimes falsely called the 'economists'; for on this point most of the professional economists are against them. The economist, unlike the 'economiser', knows that the national income is not a fund—a fixed store of value—but a current flow of goods and services. He knows that it cannot pay the community to keep three million—or the world to keep thirty million—workers in idleness, instead of setting them to work to produce goods and services which the world's population sorely needs. He knows too, unless he is of a singularly benighted school of doctrinaires, that national capital is no more capable than national income of being stored up unused without losing its value and its real existence. For the money held back from investment and piled up idle in the banks is in fact being held back out of the current stream of purchasing power. To invest it would be to spend it—on capital goods—and to set it flowing into the incomes of the producers of these goods, who would then be able to buy other goods. Not to invest it, but to leave it lying idle, is to throw men out of work, to set factories idle, to cause business losses, to destroy capital values already invested in the business undertakings on which these losses fall, and so to cancel the act of 'saving' by which these balances in the banks were accumulated. For if A saves £ $x$ , and by refusing to invest it wipes £ $x$  off the capital value of B's machinery-making and C's building business, the net result is the same as if there had been no saving at all—or rather worse; for A might have enjoyed himself, and done some good, by spending the money on champagne and oysters.

Let us go rather more closely into this vital question of idle or hoarded money. The essential idea to grasp is that, while under our present system an individual can save money by hoarding it, this is sheerly impossible from the standpoint of the community as a whole. The individual who puts his money away in a bank or an old stocking, and leaves it there, can at any future time take it out of his hoard and spend it. But this is not to say that either when he hoards it in the first place or when he takes it out of his hoard the money itself has any real existence. It is not a thing in itself, but a claim—a right to command a certain quantity of goods

or services depending on the current level of prices. Now what happens if an individual, having acquired this right to a certain quantity of consuming power, refuses to exercise it for the time being, and leaves his money in the bank? Usually nothing of importance; for the bank is able to lend the idle money—or an equivalent sum which it creates—to someone else who does wish to use it for buying things at once. But in times of depression this may not happen; for there may be too few solvent borrowers wanting to borrow money from the banks to take up nearly all the money they are in a position to lend. In that event, the idle balance left by the individual who does not desire to spend it will not be spent at all.

This sum, however, forms a part of the purchasing power distributed by the productive system. It stands to reason that the total purchasing power distributed in the course of production is equal to the selling prices of all the goods produced.\* If some of this purchasing power is held back, and not used at all, it follows that there will not be enough purchasing power left to buy all the goods at the prices currently asked for them. If this happens, either prices must be reduced or some of the goods must remain unsold. If some of the goods remain unsold, the effect will be to slow down further production, and to throw workers out of employment. What will actually occur is that production will be decreased to some extent, and prices will also fall to some extent.

Decreased production at lower prices will mean less profits. This will make capitalists even more reluctant to invest money in fresh production, and will therefore accentuate the tendency for idle balances of unspent money to pile up in the banks, and set up a fresh wave of falling prices and decreased production.

Moreover, if profits fall, the money value of the capital assets already invested in productive enterprise—represented by the stock exchange prices of industrial shares—is bound to fall too; for this value is in reality simply a capitalisation of expected profits. Accordingly, when A attempts to 'save' his money without investing it, the effect of his action is to decrease the value of the existing invested capital of B, C, D, and a host of other capitalists, probably including himself—for he probably has capital already invested in industry. From the standpoint of the community, his 'saving' of money has been sheer waste; for (a) the community has no more real productive assets than before, and (b) it has not even any more money assets, what is added to A's money assets having been

\* Production here includes transport and distribution.

wiped off the money value of the assets of B, C, and D. In other words, money is fruitful only if it is *spent*: saving without spending is sheer waste. Nay, worse; for saving without spending sets up a disequilibrium in the economic system, forces down prices, creates unemployment, and deepens business depression.

*If money is 'saved' and not 'spent'—on either capital or consumable goods—the effect must be, by withdrawing a part of the purchasing power needed to provide an adequate demand for the output of industry, to cause business losses which wipe out the supposed saving, and leave the community actually poorer than before. This is why, if a situation arises in which the private owners of capital are not prepared to risk their savings by investment, it is imperative for the State to step in, in order both to provide employment, and to preserve a proportion of the capital of the community from being simply wiped out by the failure of demand. Ideas of public 'economy' which ignore this fundamental principle are radically false, and result, not in restoring sound financial conditions, but in impoverishing both the State and the private owners of capital.*

## II.—WHAT ECONOMY MEANS

**W**HEN a nation decides to cut down its public expenditure, the reductions may take any of the following forms:

- (a) A restriction of capital expenditure.
- (b) A restriction of public services paid for out of revenue.
- (c) A reduction in the cost of State services, without change in their character.
- (d) A reduction of the sums paid out in pensions, benefits, etc.
- (e) A reduction in the amount devoted to the repayment of debt.
- (f) A reduction in the fighting services.

When a Chancellor of the Exchequer finds himself in difficulties with his budget, or under strong pressure to 'economise', he naturally considers what can be done under each of these heads.

(a) State capital expenditure, apart from the sums spent on the development of actual public enterprises, such as the Post Office, consists in fact to-day mainly of grants made to Local Authorities in aid of capital works carried out under their auspices. The most important of these at present are grants for road construction, housing and slum clearance, and the building of new schools. Of secondary importance are other grants for relief works for the

unemployed, grants for agriculture and land drainage, and loans for Colonial development schemes.

(b) Expenditure on public services also consists largely of grants to local authorities, especially for education and for the general purposes of Local Government under the Act of 1929. Police grants, grants for the training of unemployed workers, grants to aid emigration, are other forms of expenditure belonging to this group.

(c) Most public services involve a considerable expenditure on wages or salaries, and the easiest way of reducing the cost of services is to reduce the wages and salaries paid. This applies to group (f) as well as group (c). It may of course be possible to achieve

TABLE A  
THE FIGURES OF NATIONAL EXPENDITURE

	Actual			Estimates	
	1913-14	1930-31	1931-32	1931-32 Revised*	1932-33
	£m	£m	£m	£m	£m
(a) National Debt Services	24.5	360	322	322	308.5
(b) Armaments .. ..	77.2	110.5	107.3	109.6	104.4
(c) Civil Services .. ..	53.9	307.4	331.9	352.3	330.2
(d) Customs and Inland Revenue .. ..	4.5	11.9			
(e) Other Expenditure (except (f) .. ..	12.8	9.3	9.4	9.4	10.3
(f) Self-balancing Expenditure .. ..	24.6	81.9	80.5	81.6	82.1
<b>TOTALS .. ..</b>	<u>197.5</u>	<u>881.0</u>	<u>851.1</u>	<u>886.8</u>	<u>848.1</u>
Receipts of Local Authorities from Rates .. ..	79	167	165	—	—

\* Before allowing for 'economies'.

economies in the cost of public services by other means as well; but rapid and spectacular economies are difficult to achieve except by cutting these items.

(d) Sums paid out as pensions and benefits include, besides ordinary civil and service pensions, the non-contributory Old Age Pensions, contributory pensions under the Widows, etc., Pensions Act of 1925, War Pensions, and benefits paid to the unemployed on both a contributory and a non-contributory basis.

(e) Before the financial crisis of 1931, the Sinking Fund on the National Debt was nominally a fixed amount; but it actually varied according as the year ended with a surplus or a deficit. Of the

Sinking Fund, part is contractual—that is to say, provision for it has to be made in accordance with the terms on which existing loans have to be repaid—and part is at the discretion of the State. But this distinction does not mean very much in practice.

(f) Expenditure on the fighting services includes considerable sums for 'non-effective services', including some pensions, as well as for the direct maintenance and equipment of the Navy, Army, and Air Force. Naval and aircraft construction and the size of the army personnel are the chief variable factors in determining total expenditure under this head, apart from rates of pay, already considered under (c).

#### PUBLIC EXPENDITURE AND THE PRICE-LEVEL.

At a time of falling prices, some reduction in the cost of public services can, of course, be expected to come about automatically as a result of the lowered prices of supplies. But so large a part of the total expenditure of public bodies consists either of fixed money payments, which can be altered if at all but slowly and in face of

TABLE B  
TOTAL EXPENDITURE ON THE SOCIAL SERVICES

	1930	1931
	£m	£m
Education .. .. .	104	103
Housing .. .. .	37	—
Pensions (Old Age and Widows') .. .. .	72	78
Pensions (War) .. .. .	49	49
Health Insurance .. .. .	39	37
Hospitals, Maternity, and Child Welfare .. .. .	12	—
Lunacy and Mental Deficiency .. .. .	5	—
Unemployment Benefits .. .. .	102	123
Poor Relief .. .. .	43	—
	<u>463</u>	<u>—</u>

The above figures include local as well as national expenditure, but do not include expenditure out of loans.

considerable resistance, or of wages and salaries, to which the same conditions to some extent apply, that the immediate automatic savings from this source are not as a rule large. Thus, while the cost of new non-parlour houses, according to the average figures issued by the Ministry of Health, fell from £424 in June 1929 to £380 in June 1932, and to £369 in August 1932, this fall had no

immediate effect on the amount of the housing subsidy payable by the State. The fall in interest rates affected only the floating debt and that part of the long-term debt which was open to conversion without breach of contract; and it involved a definite breach of contract, authorised by Act of Parliament, to enforce the immediate reduction of 10 per cent. in teachers' salaries instituted in the autumn of 1931. Moreover, the same forces as were responsible for the fall in prices were causing certain items of public expenditure—on poor relief and unemployment benefits—automatically to increase. In face of the size of the National Debt and of the other contractual or semi-contractual items in public expenditure, it would be absurd to expect a contraction in it at all corresponding to the fall in either wholesale or retail prices. In the long run, certain parts of public expenditure do respond to a falling price-level; but the degree of the response depends mainly on two factors—the extent to which public wages and salaries are reduced, and the treatment of the problem of the rising real burden of the National Debt. Both these points are discussed on later pages of this pamphlet.

GROUP A.—'Economies' in this field must be looked for chiefly in the figures for road construction and housing.

*Roads.* When the May Economy Committee reported, the estimated expenditure for 1932-33 out of the Road Fund was £34,340,000, including £6,445,000 payable out of the Fund

TABLE C  
EXPENDITURE ON ROADS (GREAT BRITAIN), INCLUDING LOCAL  
EXPENDITURE

	Loans	Other	Total		Loans	Other	Total
	£m	£m	£m		£m	£m	£m
1913-14	3·4	18·4	21·8	1925-26	11·1	54·5	65·6
1919-20	1·4	28·5	29·9	1926-27	10·5	55·4	65·9
1920-21	4·1	42·0	46·1	1927-28	9·1	58·2	67·3
1921-22	7·0	45·3	52·3	1928-29	9·0*	57·5*	66·5*
1922-23	9·8	44·4	54·2	1929-30	10·5*	57·0*	67·5*
1923-24	9·3	46·1	55·4	1930-31	9·3*	66·4*	75·7*
1924-25	10·9	51·1	62·0				

\* Estimated.

towards the Exchequer contribution to Local Authorities under the Local Government Act of 1929. The May Committee proposed that the total should be reduced to £20,000,000, plus the contribu-

tion to the Exchequer Grant. Actually, the 'economies' made have exceeded this amount. Total Road Fund expenditure for 1932-33 is now estimated at under £26,000,000, a reduction of nearly £8,400,000. This includes reductions in expenditure on current maintenance and road improvements as well as on new construction.

These economies have been achieved only by a practically complete stoppage of all new construction, the suspension of most of the major road improvement schemes already started but not finished, and the postponement of much work on maintenance and minor improvements of existing roads. Nevertheless, the Ray Committee of 1932 recommends that further 'economies' of £2,000,000 should be made in the cost of maintenance for England and Wales alone, and that schemes of new construction still in progress should be reviewed in the hope of further possible cuts.

*Housing.* The estimates for housing, unlike those for roads, show for 1932-33 an actual increase—from £14,543,000 to £15,268,000 out of national funds. But this does not mean that housing has escaped the 'axe', but only that the greater part of the public expenditure upon it consists of annual payments in respect of houses built in past years, and that spending upon new construction takes longer to cut down than in the case of road schemes. Actually, housing subsidies for new building under the Chamberlain Act of 1923 have already been stopped altogether, and subsidies under the Wheatley Act of 1924 are to be completely ended by a Bill now before Parliament. This means that, apart from slum clearance, all subsidised new construction is to cease, as it has virtually ceased already except for schemes actually in progress. In respect of slum clearance, with which little progress has yet been made, a Bill is in prospect, and a reduction in the rates of subsidy is recommended by the Ray Committee. The unofficial Rentoul Committee of back-benchers went further, and proposed to abolish all grants in aid of new building even under slum clearance schemes, limiting State aid to a fixed maximum, to be used only in aid of the acquisition and clearing of sites. An idea of the retrenchments already in force can be got from the increase in the number of unemployed building trade workers from 76,000 in September 1929 and 132,000 in December 1929 to 265,000 in December 1932.

Yet it is impossible to suggest that we have solved the housing problem, or that private enterprise, even with the support of the Building Societies, is likely to solve it, if the subsidies are withdrawn. The truth is that we have not yet even begun to face the realities of the housing question. We have built a great number of houses

since the war; but the vast majority of them have been sold at prices, or let at rents, which only the middle classes and the best-paid sections of the working classes have been able to afford. The poorer workers have not merely continued to live in second-hand houses, often in very bad repair; they have been more and more crowded together in these inferior dwellings, while those better off have got almost the entire benefit of the large sums paid out in State and municipal housing subsidies. Let us by all means change our policies, and concentrate our attention in the immediate future on building new houses and blocks of flats—on the Viennese model—in which the poorer workers can afford to live. But that is an argument for changing the conditions of the housing subsidy, not for abolishing it. It is, indeed, obvious that the Government's latest proposals, for building houses at economic rents with the aid of capital supplied by the Building Societies, will aggravate the very mistake we have been making hitherto; for the one type of house that certainly will not be built under the new scheme is the house—or flat—available for letting at a rent which the worse-paid workman can afford to pay. The new plan may get some houses built; but even less than earlier plans will it provide dwellings for those who need them most. If such dwellings are to be provided, a subsidy must be given; and the Government has in effect admitted this by deciding to prolong the control of rents for five years more in the case of the smaller houses. For the reason why it is necessary to go on controlling rents is that there is still an acute shortage of the cheaper type of housing accommodation. If there were not a shortage, the danger of rents rising would not exist.

In short, the new scheme will not give us the houses we need; and, as there is already, in face of falling wages and employment, a slackening of demand for the types of houses that can be built to let or sell at an economic price, the result is likely to be a sharp further fall in the total amount of house-building, and a further rise in the number of unemployed workers in the building trades.

*School Building.* In 1929, as an integral part of the plan for reorganising elementary education, especially for the older children, in accordance with the Report of the Hadow Committee, a special school building grant of 50 per cent. was established. This has now been altogether cancelled, except for expenditure already subject to contract. The effect has been practically to suspend over the country as a whole the plans for carrying through the long-overdue reorganisation of the elementary schools. Apart from this, normal expenditure on school building and repairs has been

everywhere slowed down; and the Board of Education is refusing to sanction such expenditure for grant aid wherever it can possibly be postponed. Local Authorities are prevented from raising loans for school building; and the same policy is being followed in respect of secondary and other special types of schools as well as elementary schools. The building of new secondary schools has practically ceased.

*Other Public Building.* The estimates for works, buildings, and establishment charges in the budget for 1932-33 were cut down from £5,564,000 to £5,094,000, mostly at the expense of building work. On a far larger scale, Local Authorities have everywhere suspended their programmes of new construction, some going so far as to put an absolute embargo on capital expenditure for a period of years. 'Economy' by the State has been the signal for an exaggerated policy of 'economy' by local governing bodies, so that large arrears of necessary work are already beginning to accumulate.

GROUP B.—The most important services in this group are education and public health—apart from the constructional work in those services included in Group A.

*Education.* In 1931-32 national expenditure on education amounted to £56,767,000. The budget of 1932 cut this down to £50,516,000—a cut of over £6,250,000. A very large part of this sum is due to the reduction of 10 per cent. in teachers' salaries. But in addition the State has abolished the provision under which it agreed to meet half the cost of elementary education, thus saving not far short of £2,000,000, and setting the Local Authorities to work to devise drastic local schemes of educational economy, because under the revised conditions a larger proportion of whatever they spend will fall upon the rates. The London County Council, for example, has cut down its educational budget since last year by £1,500,000; but in spite of this the educational expenditure payable out of rates has risen by £422,000. An important fraction of the State's savings thus consists, not of real retrenchments, but of transfers of burdens from taxes to rates. But this is bound to intensify the campaign for further 'economies' in education to be effected locally.

Apart from general economies in the ordinary schools, the Board of Education has refused to sanction any additional Nursery Schools; plans for school clinics have been abandoned, school medical services cut down, the provision of school meals restricted, and plans for the provision of playing-fields given up. Teaching staffs

have been reduced; at the cost of increasing the size of classes, and provision for equipment and repairs has been curtailed.

Moreover, additional heavy 'economies' are now threatened in Secondary Education. Under a circular issued by the Board of Education, the facilities for poorer children in the secondary schools are to be drastically curtailed by the general institution of a 'means test'. Free secondary schools, such as exist in some areas, are to be wholly abolished; and the existing system of 'free places' is to be altered to one of 'special places', under which parents whose incomes are above a very low figure are to be compelled to pay fees. The precise working out of the new scheme is to be left to the Local Authorities, subject to the veto of the Board; but the effect is bound to be the placing of far heavier burdens on poor parents who desire to give their children a good education as a start in life. For, in addition to the restriction of free places, secondary school fees are to be raised; and the new 'means test' implies a considerable cutting down of the maintenance allowances hitherto granted by the Local Authorities. The Ray Committee of 1932 even contemplates the reimposition of school fees in the higher types of elementary school, thus going back on the principle of free elementary education conceded as long ago as 1890.

Education is thus the chief of all the victims of the present 'economy' campaign; and the cuts already foreshadowed for the future go considerably beyond the drastic reductions allowed for in the budget for the current year. The unofficial Rentoul Committee went so far as to demand a further curtailment of £14,000,000 in public educational expenditure.

*Local Government Grants.* Under the Local Government Act of 1929, which transferred the old Poor Law services to the Local Authorities, de-rated agricultural and to a great extent industrial property, and made many other changes in Local Government, many of the old grants in aid of local expenditure were swept away, and replaced by a new consolidated grant which took account of the loss to local revenues as a result of de-rating. The amounts payable under the Act of 1929 cannot for the most part be cut down, as they rest on an agreed settlement with the Local Authorities; and accordingly national expenditure for 1932-33 shows under this head only a small fall—from £46,250,000 to £45,750,000. But other grants to local bodies have been heavily cut. Grants for agricultural services, including land settlement, forestry, and agricultural subsidies were brought down from £5,653,000 to £5,027,000, and smaller grants have also suffered. Moreover, the curtailment of State spending

on unemployment has necessarily added to local burdens in the distressed areas, and so strengthened the cry for local economies in other spheres.

*Other National Services.* The last budget cut the estimate for training and transfer services for the unemployed from £563,000 to £374,000—a monstrous ‘economy’ in face of the increase in unemployment. It reduced the grants for Empire Marketing and Colonial Development from £1,417,000 to £1,020,000, and grants for scientific research from £1,263,000 to £1,175,000. Overseas settlement grants fell from £265,000 to £91,000—a more excusable reduction in face of the collapse of emigration schemes; and miscellaneous services showed a fall of £1,740,000.

GROUP C.—It is naturally impossible to disentangle the ‘economies’ achieved by reducing wages and salaries of public servants from those due to the restriction of services and the cutting down of personnel. But, as we have seen, a substantial fraction of the educational savings was secured by a 10 per cent. cut in teachers’ salaries; and there have been in addition similar cuts in the pay of civil servants, policemen, and the fighting services. Even the Rentoul Committee admitted that Civil Service salaries were not too high, and refrained from proposing further direct cuts, though it demanded a drastic overhauling of municipal wages and salaries, and desired a further attack to be launched upon the salaries of the teachers. The May Committee of 1931 wanted teachers’ and other salaries to be cut by 20 per cent., and the Ray Committee of 1932 wants Local Government wages and salaries to be reduced. Moreover, both the Ray and the Rentoul Committees want to make indirect reductions by slowing down the rate of increment under salary scales; and the Rentoul Committee proposes to increase Civil Servants’ hours, and to make indirect salary reductions by putting the pensions of new entrants on a contributory basis.

Of course, any action taken by the State and the Local Authorities in reducing wages and salaries is bound to react on the wages and salaries paid by private employers; for a wage-cutting campaign initiated by the State is certain to carry great weight in the minds of employers, and pressure to reduce contract prices for public works will also act as an inducement to bring wages down.

GROUP D.—This group includes the whole range of pensions and insurance payments, and also the sums paid to unemployed workers

outside the scope of the insurance scheme. It has been the sphere of the most dramatic 'economies' enforced during the past year.

*Old Age and Widows' Pensions.* The expenditure of the State under these heads has increased in the current year; for the number of old age pensioners necessarily continues to grow, and the State contribution under the contributory Widows', etc., Pensions Act was fixed on a rapidly rising scale. Not even the present Government has ventured to cut down these services; and accordingly the charge for Old Age Pensions is up on last year's charge from £38,200,000 to £39,745,000, and that for contributory pensions from £10,000,000 to £11,000,000. On the other hand, War Pensions are a steadily falling charge, down from £50,400,000 to £47,600,000, so that, on balance, this whole group of pensions shows a fall in cost of £250,000.

*Unemployment Benefits.* The May Committee built up its sensational forecast of a budget deficit of £120,000,000 largely on the basis of including the entire borrowing of the Unemployment Insurance Fund as a debt. For years past, this fund had been financed in part by borrowing—which involved an addition to the floating debt, but not any charge appearing in the budget accounts. This method of accountancy was misleading and unsound; and it was certainly the right policy to insist that the entire current cost of maintaining the unemployed, as far as it was not met out of employers' and workers' contributions, should be charged upon the budget. On this basis, unemployment payments as paid before the crisis would have involved for 1932-33 an estimated charge of over £143,000,000, whereas the budget made provision for a total expenditure of only £105,000,000, including nearly £6,000,000 for interest on the accumulated debt. Of this sum, under £66,000,000 was chargeable to the Exchequer, the remainder being met out of the increased contributions to be levied on employers and employed. Actually, this estimate of cost, based on an over-optimistic forecast of the state of trade, has proved to be too low, and a supplementary estimate has had to be approved. The 'economies' at the expense of the unemployed remain, however, by far the most drastic among the measures of retrenchment made during the crisis.

Curtailement began with the Anomalies Act of the late Labour Government, estimated to save about £3,000,000 a year. But this was as nothing compared with what was to come. The National Government cut rates of benefit by 10 per cent., curtailed the rights of contributors to draw benefits at the standard rate, and instituted

for all claimants who exhausted their reduced statutory claims a 'means test', under which hundreds of thousands were struck out of benefit altogether, and hundreds of thousands more had their payments drastically reduced. This was done, not on any uniform scale for the whole country, but according to the particular attitude of each of the local Public Assistance Committees to which was entrusted the administration of the new test. This gave rise to so many fresh anomalies that an amending Act, laying down certain general conditions to be observed by the local Committees, had to be passed in the autumn of 1932. But this Act touched only the fringe of the problem; and over most of the country the administration of the 'means test' continued to be a source of widespread dissatisfaction and unrest. Moreover, the Report of the Royal Commission on Unemployment Insurance, published in the autumn of 1932, foreshadows further reduction of benefits, and further curtailment of the period of benefit for the workers under insurance, with the effect of making a still larger section of the unemployed subject to the hated 'means test'.

*Health Insurance.* Retrenchments and reductions have also been made in the health insurance services, partly at the expense of the approved societies, with the result that the estimated State expenditure on health insurance remains the same as last year, but shows a substantial fall as compared with 1930-31.

**GROUP E.**—There is obviously no advantage in repaying existing debt with one hand and borrowing at the same time with the other, unless the new borrowing can be secured at a lower rate of interest. Nor is a time when the State is undergoing serious financial embarrassments a suitable time to provide for large repayments of debt. Accordingly, it is natural for a Government seeking means of balancing its budget to consider total or partial suspension of Sinking Fund payments.

*Debt Interest.* Owing to the lack of profitable uses for money, and the consequent fall in interest rates, the charge for interest on the National Debt has fallen considerably. Over £2,000,000,000 of long-term debt has been converted, broadly, from a 5 per cent. to a 3½ per cent. rate of interest; and there has been an even sharper reduction in the rates for short-term borrowing on Treasury Bills and other temporary advances. The Treasury Bill rate has fallen in some weeks to under ½ per cent., and has seldom been much above 1 per cent. This has saved the State a great deal of money;

and the total charge for debt interest and management, which was £289,400,000 in 1931-32, and was estimated at £276,000,000 for 1932-33, has in fact fallen far below that sum. On the other hand, no provision was made in the budget for the payment of interest (or part repayment of principal) on the debt to the United States, whereas in fact the December instalment of £29,000,000 on this account has been paid (over two-thirds for interest and under one-third for principal). This will more than offset the saving in debt interest, even apart from the principal repaid, and thus help to create a deficit on the year's accounts.

*Sinking Fund.* For 1930-31 the nominal Sinking Fund stood at nearly £67,000,000; but a deficit of over £23,250,000 brought the real repayment of debt down to £43,500,000, leaving out of account accrued interest on Savings Certificates (£3,500,000) and the borrowings of the Unemployment Insurance Fund, which came to £36,500,000, leaving a final real balance of £3,500,000 for debt reduction. For 1931-32 the nominal Sinking Fund was reduced to £32,500,000. There was a small budget surplus, which brought this up to nearly £33,000,000. But the Unemployment Fund borrowed over £39,600,000, and the Savings Certificates item accounted for nearly £8,500,000, while £8,750,000 was withdrawn from the Dollar Reserve Fund to help the accounts to balance. Instead of a debt repayment, there was in reality in that year a net increase in debt of nearly £24,000,000.

For 1932-33 the Sinking Fund was maintained on paper at £32,500,000, and the budget made to balance in prospect, including this item, despite the stopping of fresh borrowing by the Unemployment Fund. This result was to be achieved partly by economies in expenditure, as described above, partly by increases in taxation, and partly by the 'dodge' of making the income-taxpayer pay three-quarters of his tax, instead of half, in January, and so bringing forward a substantial amount of revenue from the following financial year. If the sum provided for in the reduced Sinking Fund were to be actually applied to debt reduction during the current year, without being offset by new borrowing, the net effect would be a larger repayment of debt than has really been made in any year since 1928-29.

GROUP F.—The fighting services ought, it might be supposed, to offer the most profitable of all fields for economy in national expenditure. But proposals to reduce them always meet with fierce opposition in high quarters, and especially from the Ministries

concerned. Some 'economies' have been made in these services during the crisis; but it will be seen that they are relatively small. It should, however, be borne in mind that, in spite of talks and conferences about Disarmament, world expenditure on armaments has been growing steadily and rapidly in recent years; and British expenditure, high as it is, has at least fallen slightly while the expenditure of France and other countries has been rising sharply. According to the estimate made by the League of Nations, world expenditure on armaments rose each year from 1925, when it amounted to 3,500,000,000 dollars, to 1930, when it reached nearly 4,130,000,000. Meanwhile, British expenditure fell slightly, from £115,000,000 to £110,500,000. But, all the same, what a sum to waste, for no useful purpose of human welfare!

In 1931-32 British estimated expenditure on armaments came to £109,600,000; and the budget for 1932-33 provided for our spending £104,360,000. As compared with 1931-32, Navy estimates were cut by over £1,000,000, Army estimates by nearly £3,500,000, and Air Force estimates by £700,000. But the real reduction was less than this; for the actual sum spent in 1931-32 was not £109,600,000, but £107,300,000, giving an estimated reduction of £3,000,000 only for the current year. This can be compared with an estimated cut of over £6,000,000 on education (not including the cut in local educational expenditure), and a fall of nearly £40,000,000 in the annual cost of provision for the unemployed in relation to the cost which would have accrued if the system had remained unchanged. Nor must it be forgotten that a part of this meagre reduction in expenditure on armaments has been achieved by cutting service pay.

### III.—THE ECONOMICS OF 'ECONOMY'

**P**ART II has given the facts about 'economy', as far as they are at present available. The total result has been to reduce estimated expenditure from £772,600,000 in the original budget of 1931-32, and from £750,600,000 in the revised budget of September 1931 to £733,500,000. These figures do not include either the Sinking Fund or the self-balancing expenditure of the Post Office and the Road Fund. Total 'economies' thus apparently amount to under £40,000,000. But account must also be taken of the cessation of borrowing by the Unemployment Insurance Fund, which reached nearly £40,000,000 in 1931-32, and would have been much higher but for the changes made in the system in 1931.

These reductions do not, of course, represent the whole of the retrenchment in public spending. The fall in national expenditure has been paralleled by a sharp fall in that of local authorities; and the reductions in current charges on national and local budgets represent in many cases a far greater fall in the actual sums paid out, for the former often show only interest and sinking fund charges, which depend far more on past than on present expenditure, whereas the latter include the capital sums issued by way of loan. The total fall in the current paying out of money by public bodies in consequence of the demands for 'economy' certainly runs into hundreds of millions of pounds.

Now, it is natural enough for taxpayers and ratepayers, especially when they find their own incomes reduced by the trade depression, to clamour for reductions in public expenditure, in order to lighten the burden of taxation. On the basis of a continuance of the present economic system, such claims seem thoroughly reasonable; for if the individual has to reduce his expenditure, why, he asks, should not the State do the same? The case for 'economy' seems to be self-evident; and yet somehow when 'economy' is put into force, it does not appear to produce the desired results. The taxpayer mysteriously finds himself not with more money to spend, but with less; and the money released by the fall in State spending, so far from flowing into private industry and bringing about a revival of trade, seems totally to disappear, as if it had simply turned to dry leaves when the Chancellor of the Exchequer renounced his claim to its use.

How does this happen? In the first place, if hundreds of millions of pounds are withdrawn from spending by public bodies, what are the immediate results? All those who receive less pay, wages or salaries, or less in benefits or allowances of any sort, have less money to spend. Most of this lost money would have been spent on consumable goods and services, and the effect of withdrawing it is that the demand for these things falls off. This compels the sellers of them to reduce their prices, so that those whose incomes have fallen but little can perhaps soon buy as much as before. But this does not apply to those who are harder hit—the unemployed under the 'means test', for example; and there is, even at the reduced prices, some fall in demand from this source. Moreover, the reduced prices mean smaller profits, and cause employers to discharge some of their workers; and this involves a further fall in demand. Similar conditions apply when the wage-reduction movement spreads to private industry. Prices, already unprofitable to many producers,

fall still further; and further cancellations of income and demand follow.

Secondly, the reduction of public capital expenditure means that less contracts are given out for roads, houses, schools, town halls, and many other types of public work. This reduces contractors' profits, and causes them to discharge workers on a large scale. The present unemployment in the building industry is, as we have seen, the chief outward and visible sign of this effect.

But, it may be urged, all the money thus liberated by the State and the local authorities at once becomes available for spending by someone else. If taxes and rates are reduced (as in fact they have not been) the taxpayers and ratepayers have more money to spend. But have they? Only if, in face of the contraction of public demand, they can still make as large incomes as before. This, in fact, many of them cannot do; so that, even if the result of reduced public expenditure had been lower rates and taxes, it does not follow that private persons would have had more money to spend. As matters actually stand, the taxpayers have had their taxes increased far more than the ratepayers have had their rates reduced. There is not even the tenuous hope of a net increase in private spending power from this source.

But, at any rate, if the State and the local authorities stop borrowing, or reduce their loans, the sums of money which they would have absorbed become available for other forms of investment. There is more truth in this; and the reduction in public borrowing is *one* reason for the sharp fall in interest rates. But another, and far more important, reason is that private people and business firms do not want, under present conditions, to extend their borrowing; for they cannot see their way to make profitable use of the borrowed money. Accordingly, the funds which public bodies 'liberate' by reducing their capital expenditure or their short-term borrowing are not used at all, and do nothing to help the revival of industry. For what industry wants to-day is not more money, but more demand at better prices for its products. But the effect of reduced public spending is not to increase, but to diminish, total demand.

There is indeed one class of income-receivers whose power to demand goods and services has greatly increased; and additional demand from this source does do something to counterbalance the fall elsewhere. This is the 'class' of *rentiers*—those who get their incomes from fixed interest-bearing claims. In terms of wholesale prices, the National Debt is 'worth' three times as much as it

was in 1920, and in terms of retail prices twice as much. This enormously adds to the real burden of the Debt on the nation, and to that of all other debts, public or private, that cannot be converted to a lower rate of interest corresponding to the fall in prices. In spite of the success of Conversion Schemes, the real burden of interest on the National Debt has very greatly increased; and this implies an increase in the power of those who get this interest to buy goods. But the *rentiers* are only in part a separate class. In fact, a large part of the debt is held by big companies, and being used to meet current business losses. Another part is held by persons who depend also on profits, or salaries, for their incomes; and this part is helping these persons to contract their private spending less than they otherwise would. The pure *rentiers* are quite a small class; and some of them are finding that, while the British Government continues to pay them full interest on their holdings, defaults by Governments abroad are reducing their incomes so as to offset the gain which they have reaped from the fall in prices.

While, however, the increased purchasing value of fixed interest payments does do something to maintain demand, it does this only at the cost of creating an intolerable situation for the borrowers and for the community as a whole; for interest payments fixed in the past are so high, in relation to present prices, as to make industry in many cases unprofitable (e.g. the railways) and to cause urgent demands for wage reductions and the discharge of workers, and also as to confront the State with an impossible budgetary burden. For most of the public debt bears an interest fixed for a long period of years, and is not open to early conversion without a breach of existing contracts.

Moreover, on the whole, *rentiers* are more likely than other people to wish to 'save' rather than 'spend' a large part of their incomes. But under present conditions there are few good openings for the investment of their savings. Accordingly, as we have seen, they tend to leave a substantial part of their savings idle in the banks, and to use them to buy neither consumable goods and services nor capital goods. This withholding of money inevitably causes a deficiency of demand, and so reacts to force down prices yet further, and to make industry still less profitable. It brings about more unemployment, and fresh business losses which, from the standpoint of the community as a whole, wipe out completely the nominal 'savings' of the *rentiers*.

The importance of the State and other public bodies in creating a demand for capital goods, and thus stimulating employment and

production especially in the constructional trades, can be seen clearly from the figures of the new capital market. In 1928 the new issues of capital in Great Britain on the capital market amounted

TABLE D  
OUTSTANDING DEBT (WHICH IS LARGELY CAPITAL) OF LOCAL AUTHORITIES  
IN ENGLAND AND WALES IN 1930

	Total Outstanding £m	Capital Expenditure in 1930 £m
Debt (or Loan Capital) of Trading Services	423	27
Debt (or Loan Capital) of Housing Services	438	39
Debt (or Loan Capital) of Other Services ..	297	36
TOTAL .. .. .	<u>1,158</u>	<u>102</u>

to over £360,000,000, and in 1929 to over £250,000,000. But in 1931 the total was under £90,000,000. These figures include overseas issues; for home issues alone the corresponding totals were, roughly, £220,000,000, £160,000,000, and £43,000,000. For 1932 the total is about £110,000,000, or, excluding foreign issues, rather over £80,000,000. Now compare with these amounts the capital

TABLE E  
CAPITAL EXPENDITURE OF LOCAL AUTHORITIES, 1920-30, ENGLAND  
AND WALES

	Housing £m	Total £m		Housing £m	Total £m
1920	5	24	1926	47	105
1921	52	96	1927	65	121
1922	82	131	1928	68	127
1923	30	74	1929	39	97
1924	11	53	1930	39	102
1925	24	74	1931	—	—

expenditure of public bodies. In 1928 capital expenditure out of loans on housing alone was £68,000,000, not including Scotland, and the total loan expenditure of Local Authorities in England and Wales came to £127,000,000. Even in 1930 the total loan figure was over £100,000,000, apart from an expenditure out of revenue on road maintenance and construction in Great Britain averaging over £60,000,000 a year. Obviously, if a sharp contraction in the volume of business issues on the capital market is accompanied by a restriction of capital expenditure by public bodies, the combined

effects on employment and demand in the constructional industries are bound to be overwhelming.

But, it will be urged, even if the reduction of public spending brings about these disastrous consequences, what else is the State to do? Can it be right for the State either to live beyond its income by borrowing, or to exact additional taxes when people can ill afford to pay those which already exist? The orthodox answer is that it cannot, and that accordingly it must retrench, however unfortunate the immediate consequences may be. But is this unhappy conclusion really unavoidable?

The answer is that a great deal depends, not on how much, but on how, the State spends. People were quite right when they urged that it was clearly uneconomic, and indeed sheer insanity, for the State to be spending at the rate of over £140,000,000 a year on the relief of unemployment without having anything at all to show for the money, except the keeping alive of three million unemployed, for whom provision would have to be made next year. What most of the critics did not see was that the remedy lay, not in giving the unemployed less to live on, and thus restricting still further the demand for goods and services, but in getting for the money spent upon them a sound productive return. What most of the critics understood even less was that, if it was madness to spend at this rate on maintaining the unemployed in idleness, it was far worse insanity to spend more than twice as much a year in equally unproductive interest payments on the National Debt. It was grossly unfair to cut down the 'doles' of the unemployed without touching the 'doles' of the bondholders; but it was insane as well as unfair to attempt to work a system of State finance which involved paying out by far the greater part of the public revenue in totally unproductive ways. To be sure, it was better that these sums should be distributed as 'doles' than not distributed at all. But it would have been far better still so to distribute them as to secure in addition a direct productive return.

To find work for the unemployed is, however, a costlier business, in direct and immediate outlay, than to keep them in idleness; for they would have to be paid more if they were to do efficient work, and there would be the additional cost of materials for them to work upon. But on this principle it is always costlier to produce anything than not to produce it; for the calculation totally ignores the value of the product. The assumption is that finding employment is the task of private industry, and that the State must do nothing that might compete with it, and so make its task harder.

But what is to happen if, in spite of the State's abstinence, private industry fails in this task? The State is necessarily called upon to maintain the unemployed; but the fact that they are unemployed means that private industry is producing less than it could, and that its real taxable capacity is reduced. The State, however, if it is to maintain the unemployed, must either levy additional taxes or borrow the necessary funds. Further taxation is likely to depress industry yet more: borrowing for current expenditure means an unbalanced budget. There remains only the alternative of borrowing on capital account; but this can be sound finance only if real assets are created with the borrowed money. Real assets can be created only by using the unemployed to produce useful things. To borrow for this purpose is sound, whether the State then uses the money directly in providing employment or indirectly in passing on orders for goods to private industry.

It is the more sound—the only sound course—because (a) at times of depression the money can be borrowed at very cheap rates, and (b) State borrowing brings idle funds into use, and offsets the contraction of private investment.

On what, then, should the State spend the borrowed money? First, and most obviously, on directly reproductive works of construction—above all, housing, land drainage, agricultural improvements. Secondly, on indirectly reproductive works, such as roads. Thirdly, on works designed to raise the social standards of the nation, and so improve its productive as well as its cultural capacity, e.g. schools, slum clearance, playing-fields, and open spaces. Fourthly, on large schemes for the reconstruction of industries at present privately owned, such as railway electrification, and the reorganisation of productive power in coal-mining, the cotton industry, iron and steel manufacture, and other derelict or distressed trades and services. There is no dearth of objects on which the money can be spent, if once the case for spending is admitted. Into this question I need not enter further in this pamphlet. I have argued it at length elsewhere, and so have many other writers.

Finally, it is unjustifiable and disastrous, in times of depression, to interrupt the normal development of the social services. The budgetary equilibrium so achieved is purchased at too high a social cost, and involves in addition most unfortunate economic results. It defeats even its own immediate ends by exaggerating depression over the whole industrial field. Far better incur a budgetary deficit during the emergency than make the budget balance at this cost. Or, if this seems too dreadful a prospect, far better an enforced

reduction of interest on the Debt than a default in respect of the health and education of the community.

The policy of 'economy' is wrong in principle and practice. The sole case for it—the need to avert a 'run on the pound'—disappeared as soon as Great Britain went off the gold standard, that is, before most of the recent 'economies' had been introduced. For to-day we have no need to fear a run on gold; and, if the effect of State spending were to bring about some rise in prices and interest rates, most sensible people would regard that as a blessing and not a curse. Our existing troubles are not due to lack of either money or productive resources; for we have a great deal of both lying idle. They are due to a failure to use our money and our resources—a failure greatly aggravated by the public 'economy' to which we have so rashly resorted. Let us by no means go back to the condition of spending vast sums on the maintenance of idle workers. That would be folly. But let us, instead of making abstinence a god, courageously use the public credit both directly to provide work and indirectly to stimulate demand over the whole field of industry. For in that way, and in that alone, can we hope to rebuild our shattered prosperity.

## MONEY AND THE PRICE LEVEL

By F. M. HUNTINGDON-WILSON. Can the burden of private and public debts be relieved except by bankruptcy? How can normal trade be restored without resort to currency inflation? Here is a plan of interest to every investor, banker and business man, which if put into early operation would seem to offer an immediate way out of deflation. 7/6

## ENGLISH PUBLIC FINANCE 1558-1641

By FREDERICK C. DIETZ, Ph.D. An interesting examination of the general fiscal problem of an earlier time worthy of special attention. The book analyses the special revenues and outstanding expenditures, throwing light on the standards of living in the sixteenth and seventeenth centuries. 21/-

## DISTRIBUTED LEISURE

By L. G. WALKER. An approach to the problem of over-production and unemployment. The principles set forth in this book have been successfully tried out in the author's own extensive organization. 10/6

**D. APPLETON & CO., 34 BEDFORD STREET, LONDON**