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THE INVARIABLE STANDARD
AND MEASURE OF VALUE

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THE
INVARIABLE STANDARD
AND MEASURE OF VALUE

BY
J. TAYLOR PEDDIE

SECOND EDITION



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TO
MY FRIEND
FRANCIS FRANCIS

No gain of wealth and welfare is so certain as that which proceeds from self-reliance and the development of the resources we already have. For this we require freedom of trade by regulation, without the restrictions imposed by gold money. (p. xiv.)

PREFACE

I PURPOSELY omitted a study of the theory of value from my last book *The Flaw in the Economic System*, partly because it would have required more time and study than I could then afford to give to the subject, and partly because I was puzzled by some of the technical terms used by modern economists in connection with the science.

Such technical terms as Exchangeable Value, Law of Supply and Demand, Inflation, Déflation, etc., are effective in a gold standard science of political economy, but they are not effective in a science of political economy based on potential productive power. As the main theme develops, it will be seen that the technical terms employed in the one acquire a totally different meaning in the other. And I am certain that until the economists decide to classify and separate the principles involved, and begin to think in terms of productive power, they will be unable to find a solution for the present acute industrial depression.

In a science based on productive power, life is made up of service, and humanity obtains its

freedom. In a science based on gold, humanity is placed in bondage to the gold interests, who hold "that Labour has no value, that what is bought and sold is not the labour, but the product of the labour." The services of the human being have no exchangeable value, but the product of his labour may possess one. Therefore, my advice to producers and labour is that they should proceed to develop the true science that is based on productive power—to which end this work may be helpful. It is in this direction only that they will obtain salvation.

After developing my thesis I conducted a line of inquiry through the elder and modern economists to see if I could obtain support for my theories, and the aphorisms which I have extracted from the Works of Adam Smith, Ricardo, and Frederick List are the result. The advantages derived from the publication of the aphorisms in the condensed form in which I publish them are :—(1) that they afford extraordinary confirmation of "The Invariable Standard and Measure of Value," and (2) that they show clearly that the present Free Trade Gold Standard System has no solid basis in history, or in fact; and that in its present position, it is not only false, but untenable. I enlarge upon this in Chapters X, XI and XII. The quotations also show beyond dispute that Adam Smith, Ricardo, and J. B. Say were not free traders. I have

emphasized this fact as regards Adam Smith for many years past.

The aphorisms with which I agree are those that are related to a political economy based on productive power (the most important being indicated in italics); but I disagree with those that are related to a political economy based on gold *and silver*. The latter are easily distinguished.

It is to be observed that I oppose the new theories of a "Stable Price Level," and a "Fixed Purchasing Power," on the ground that Great Britain has to bear a burden of taxation which, per head of population, is greater than in any other country. Mr. Churchill in a Parliamentary paper quotes the following details of taxation per head of population in the following countries:—

	1913 or 1913-1914.	1925 or 1925-1926.
	£ s. d.	£ s. d.
United Kingdom .	3 11 4	15 2 8
France . . .	3 7 0	8 5 10
Germany . . .	1 10 8	5 6 5
Italy . . .	2 2 8	3 8 9
U.S.A. . . .	1 7 11	6 1 11
Canada . . .	3 8 3 ¹ / ₂	6 19 4
Australia . .	3 8 1	9 1 6
New Zealand .	6 3 0	14 0 9
South Africa .	6 15 4	11 17 2

The figures for South Africa are calculated on the basis of the population of European origin.

As a consequence, the basic industries of Great Britain have to include in all costs of production indirect charges that have no intimate relation to actual costs of production, and to suggest that we should fix the purchasing power of money in such circumstances is to suggest that we should permanently impair our competitive power in favour of other countries less heavily taxed. Furthermore, it would be necessary for the world to regularize the eight-hour day and standardize wages before the idea of "a fixed purchasing power," or a "stable price level," could come within the range of practical politics.

I am of the opinion that it would be unwise to accept any theory that may prevent the producers and labour from deciding the issue for themselves after a practical working experience of an invariable measure of value. For close upon a century producers and labour have been the slaves of economic laws and theories that have proved to be erroneous, and the basic industries should now energetically refuse to go beyond a simple reform of the monetary system until their competitive power has been restored to a profit-earning basis, even if it be only that of a penny in the pound.

What the basic industries of Great Britain require to-day is the right to adjust and overcome their economic difficulties through machine power, aided by a monetary system that is based on productive

power. In order that the burden of taxation per unit of goods produced may be minimized, an increase in the volume of production is essential, and it is in this direction only that the basic industries and labour will achieve their salvation. The whole burden of taxation has been applied in an unscientific and irregular way. A redistribution of its weight would produce some extraordinary results.

Another prerequisite condition is an era of cheap money and low interest rates on Government debt, so that a substantial reduction of the burden of taxation may be effected. This is one of the essential reforms. As I clearly indicate in *The Flaw in the Economic System*, page 211 :—

“ The only sound money is that which is created on wealth products, since it brings about an era of cheap money. Real capital savings come out of the profits earned in the development of production, and from no other source ; so that, in order to get cheap money, we must develop the nation's potential productive power, which alone creates it. We may continue to have a large quantity of credit based on gold, deposits and Government debt, but if our wealth productive power remains on a low scale, then, as we have said, the price of money must remain dear, since the demand for credit facilities from those who control our productive power must always be greater than the available supply.”*

* Always assuming that competitive power has been restored to the basic industries—subject to profit.

Mr. Edward A. Filene, a prominent business man of Boston, U.S.A., in a recent article * writes as follows :—

"A business is prosperous when it makes good profits. A consumer is prosperous when he can buy more than the usual amount of the things he would like to own. Obviously the prosperity of business depends upon the ability of the consumer to buy.

"Therefore, if we can find out how to make it possible for more consumers to buy more of the necessities and luxuries that they want, year in and year out, with no letup, we shall have greater, more general and more stable prosperity.

"Now, the ability of the consumer to buy increases when the amount of money he has to spend increases without a proportionate rise in prices, or when prices fall without a proportionate decrease in the amount of money he receives as wages or salary.

"To raise wages and salaries and at the same time reduce prices is doubly effective in promoting the prosperity of consumers. That at once points to the elimination of waste as one of the essential and most effective steps in promoting general prosperity.

"An industrial engineer has said that it is likely that in the next few years costs will be lowered and wages raised to such an extent that every farmer and wage earner will have the consuming power which to-day is enjoyed only by those with incomes of 10,000 dollars a year."

* *The Christian Science Monitor*, Boston, March 19, 1928.

The italics are mine. This quotation agrees with the economic concept I have developed, but how to make it effective, from a monetary point of view, is the problem. I invite my readers to study the general theme of this work minutely, as I think it provides the scientific solution.

Mr. Filene refers to the work of the "International Management Institute" at Geneva, whose objects I have examined, and among its considered opinions are the following :—

(b) p. 4. "Simplification of processes and types can, on the other hand, ensure considerable economies in production and international trade, not only by reducing waste of manufactured commodities, but also by making the mass production of such commodities possible, which, in turn, permits of lowering to an appreciable extent both the cost of producing those commodities and their sale price."

IV, p. 9. "One of the most important problems raised by the general application of rationalization is that of working out and applying an appropriate credit policy.

"It is therefore expedient that credit institutions should, with this object in view, carefully follow the evolution of modern methods of industrial organization. The fact that, in various countries, banks have set up industrial departments shows that bankers appreciate, apart from the purely financial guarantees afforded by an industrial undertaking, those guarantees which are provided by sound organization and cost accounting. It is the Insti-

tute's intention to encourage this development to the best of its ability."

The greatest form of co-partnership is that which is obtained by the community from a falling price level subject to profit, and from a purchasing power that is fixed in terms of wealth products and not in terms of gold. All other forms, except share ownership, are mere delusions. The danger to be guarded against from such propaganda is that the public mind may be diverted from the real flaw in the economic system. The great need of the moment is to create a common aim and a common purpose.

No gain of wealth and welfare is so certain as that which proceeds from self-reliance and the development of the resources we already have. For this we require freedom of trade by regulation, without the restrictions imposed by gold money.

In order to achieve and make effective the "dual system" of raising wages and lowering prices it will be necessary to stabilize money in costs of production. It certainly cannot be done by fixing the purchasing power of money and stabilizing the price level. The latter method would eventually lead to inefficiency and lack of enterprise, and to instability of credit.

The true principle has many times been clearly proved—that production and trade should control the currency, and that currency should not control

production and trade. The power of money to control prices and production should for all time be destroyed and the merit of any currency theory should be decided by this test. The only thing that producers and labour need concern themselves about in any new system of currency is that credit and money shall be automatically adjustable. Having enforced this principle, then let them retain their freedom and never part with it.

The power which the producers, chemists, scientists, and labour always have of creating cheap money and credit, through the lowering of costs of production and the maintenance of efficiency, should never be lightly abandoned. They alone should control the rate of interest, and not the Bankers. The latter should control the issue of credit, but not the price of it. The lowering of costs of production and of rates of interest are vital to the success of any new scheme of currency, and sufficient emphasis has not yet been laid on the need of this dual effect. I draw no limitation to the rewards or profits of enterprise, and it is here that the clear distinction between the uses of money and capital is to be seen.

By stabilization I mean the elimination of a currency system which expands credit before production and causes an unnatural rise of prices, and then, after the producers have expanded production to cope with the extra demand, causes

prices to fall because of the instability of credit. These tendencies are better known as "inflation" and "deflation," and in such a system the ultimate burden of loss falls on the producers and consumers.

What we need is a currency system that will reverse this procedure, namely, a currency that will expand pro rata with production (the processes) or later than production (on completion of contracts) and in no case to anticipate production. In such a system commodities would be made available for the consumers to buy, as and when they wanted them, at known predetermined prices, and would effectively check the unnatural rise and fall of prices. Such working conditions would therefore eliminate "inflation" and "deflation" and would give to producers the stabilization they ask for, that is, the right to develop a steady trade at a profit. In the new system proposed the working conditions would be stable because they would not operate inversely to the natural tendencies of production. The dual system of stability and falling prices would thus be achieved and made effective.

Can it be wrong then to ask for a currency system that will produce better and more scientific results than the present gold basis system, and so lower the burden of taxation which is the cause of the depression in all the basic industries? The Rating Bill will afford no real relief, since the burden of rates will merely be transferred from being a direct cause

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of industrial depression to being an indirect cause. The main portion of the burden of taxation, whether direct or indirect, must always be carried by productive industry, and this truth is not sufficiently appreciated.

This book should be read in conjunction with *The Flaw in the Economic System*, particularly Chapters XIII and XIV.

J. TAYLOR PEDDIE.

7th August, 1928,

LONDON, S.W.1.

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I

THE INVARIABLE STANDARD AND MEASURE OF VALUE

SUBJECT to an expenditure of labour, which includes management, science, and chemistry, nature could supply mankind with all the food and natural materials we require, and potential productive power could see to the production and distribution of utilities. All of which proves that labour is the real and ultimate standard of value.

The riches of nature are boundless, and likewise potential productive power, and although the needs of the people are great, nature and potential productive power can more than supply them. What, then, prevents an equitable distribution of those riches which both could place at the disposal of mankind? The preventive factor is gold, which has been made the standard and measure of value in opposition to labour; and the reason why it was thus chosen will be indicated later in the discussion.

It is certain that there are no artificial restrictions

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to be found within natural laws, or within potential productive power. In what way, then, can we remove the artificial restriction or limitation that prevents an equitable distribution of nature's products so as to allow potential productive power to develop and distribute them at the lowest possible cost? Of what use can these vast resources be if they are not to meet the needs of mankind and remove poverty and distress? An intelligent understanding of this problem is not possible without a discussion of the theories of value, of price and of the standard and measure of value.

It is but natural that a considerable amount of unsound reasoning should have been developed on the theories of value and of price, since none of the laws and theories that are based on the gold standard (and its concomitant, the "quantity theory of money") can be sound. If the base is false, all reasoning deduced therefrom must be faulty.

There are so many contradictory laws and theories within the present economic system that the average person has come to regard the science of economics as a "dismal" one. No logical process of reasoning has yet been evolved that can be followed by the average mind. But this is entirely due to the fact that there is one political economy based on gold, and another political economy based on productive power. There is, therefore, a confusion of principles,

and a perpetual conflict between each set for control. The task before us is to separate them so that they may be distinguished.

Our potential productive power has been built up with infinite care by previous generations, and by the present, and it is the result of an accumulated experience. Our engineers, inventors, chemists, and scientists have all aided in this development. Our potential productive power is therefore an inheritance. Yet within the last few years we have allowed this vast instrument of wealth production to be contracted because there has been an insufficiency of gold to finance it in combination with the great National Debt. The position is such that the work of generations in building up our national potential productive power is put to hazard, and may be destroyed in a night by the mistaken policy of those who favour the gold basis system of currency.

Relatively speaking Great Britain may be poor in terms of gold, but she is rich indeed in terms of potential productive power. And as Say has stated :—

“ The prosperity of a nation is not greater in the proportion in which it has amassed more wealth (i.e. in values of exchange) but in the proportion in which it has more developed its powers of production.”

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Frederick List has also declared that :—

“ The foreign trade of a nation must not be estimated in the way in which individual merchants judge it, solely and only according to the theory of values (*i.e.* by regarding merely the gain at any particular moment of some material advantage) ; the nation is bound to keep steadily in view all these conditions on which its present and future existence, prosperity, and power depend.”

Gold reserves cannot of themselves create wealth nor can they create profits. On the contrary, if there be an insufficiency of gold it can strangle the production of wealth and the prosperity of a nation. We have therefore to re-cast our theory of exchangeable values ; for it is clear that if the value of any commodity or utility is determined by what the owners of money are willing to pay for it under a gold basis system, the selling market is restricted, and from this arises the “law of supply and demand.” Productive power is service power. It can predetermine the price value of its productions, provided Labour (costs of production) is admitted to be the real and ultimate standard of value ; and provided also that the £ note itself is employed as the measure of value, *i.e.* the equivalent of the standard of value.

But the adherents of Free Trade and the Gold basis systems by their adhesion support the principle “ that labour has no value, that what is bought and

sold is not the labour but the commodities and services produced by the labour." The human being is denied the right of claiming that his services have an exchangeable value; or, in other words, that he has a right to live. The product of his labour may obtain an exchangeable value if there be a sufficiency of gold money; but even this value will be arbitrarily fixed and may have no relation to the worth of his services. Gold does not create wealth nor can it earn profits, but the gold merchants claim an arbitrary power and profit for the use of their metal. With potential productive power in full control of the monetary system the value of anything that is subject to quantity production can be predetermined; the more so if we agree that the function of money as a medium of exchange should be to facilitate a barter system, and in this way become the servant of mankind and not the master.

The gold reserves held by the Bank of England are clearly inadequate, in view of the functions they are called upon to perform; which are, to form the basis of the internal monetary system, and protect the external credit system. The internal system is called upon to finance both the great National Debt and potential productive power—a task that is far beyond it. The result is that either the holders of the National Debt or the productive industries of the country must go short of their requisite credit facilities; and when it comes to a choice of this kind

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the monied interests would sooner sacrifice the producers than they would the National Debt holders.

It is of course well understood that the "orthodox" economists largely influence the policy of the Treasury and the Bank of England. There seems to be a practical agreement among them that the prosperity of Great Britain depends upon its international trade, since they believe that exports must pay for imports. This is called the Equation of Exchange. If we refer to the orthodox text-books we shall find that the merchants of England may import goods into this country, but that if it pays them better to export gold instead of goods in payment for the imports then the gold will go out. It matters little to them if this gold forms the basis of the quantity of money and that the whole of the credit system based on this quantity, which has to finance potential productive power and the great National Debt in unison, will be contracted; and that in consequence of this potential productive power must suffer a loss of output. If productive industry has to carry the enormous burden of the War debt and the consequential National and Municipal taxation (which has to be included in all costs of production) its competitive power must obviously be impaired. In view of the higher cost of production thus imposed, it is clear that the merchants of England will always find it more profitable to ship gold than to ship British manufactures.

What then is the virtue of the theory that exports must necessarily pay for imports within a gold basis monetary system? May it not be regarded as an absurdity that the whole prosperity of Britain's potential productive power, and its capital value, should depend upon whether the merchants can accumulate a surplus of gold for the country in any one year? On the success of the merchant's operations in this respect depends the prosperity of the producers as a whole. This will be obvious when we realize that credit is expanded to ten times the gold basis, and if gold is exported credit will have to be contracted in a like ratio. We see no reason why the merchants and the monied interests should be given this arbitrary power, or why the public should continue to believe that the so-called Equation of Exchange is valid.

The orthodox point of view is clearly set forth in the following quotations which are taken from *The Times* of April 19th:—

"This country obviously cannot construct for itself a monetary system divorced from the general principle adopted as the basis of the monetary systems of the rest of the world.

"Being a great international trading country, Great Britain must necessarily remain on the gold standard.

"Being the only universally accepted medium of payment, gold acts as the equating factor in the stabilization of price-levels as between the different

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countries. If prices in one country are higher than in another, thus preventing it from selling customary goods in foreign markets, then it loses gold to the country which, owing to lower prices, is able to sell the goods instead. In that way credit in the high price country is contracted, bringing down prices and restoring its competitive power, while it is expanded in the low-price country, thereby helping to raise prices. Gold movements, therefore, play a very important part in preserving price equilibrium which is essential to maximum trade activity."

It is here clearly demonstrated that gold has been given an arbitrary power of interference and manipulation that it has no right to possess. By a transfer of residence it can effectively raise and lower prices in any country at will; on this point there is no dispute. The power of gold should extend no further than the settling of debts. We agree that gold should be retained for this purpose—but for no other purpose.

Frederick List's logic is more in accord with our immediate experience when he declares that:—

"The causes of wealth are something totally different from wealth itself. A person may possess wealth, *i.e.* exchangeable value; if, however, he does not possess the power of producing objects of more value than he consumes, he will become poorer. A person may be poor; if he, however, possesses the power of producing a larger amount of valuable articles than he consumes, he becomes rich.

"The power of producing wealth is therefore infinitely more important than wealth itself; it insures not only the possession and the increase of what has been gained, but also the replacement of what has been lost. This is still more the case with entire nations (who cannot live out of mere rentals) than with private individuals."

As the great National Debt of the country can be redeemed only out of the prosperity of our potential productive power, it is clearly incumbent on the nation to preserve its productive power intact; but in recent years we have allowed it to be contracted and impoverished in consequence of the defects of the monetary system. The producers in our basic industries, although rich in potential productive power, have been obliged to suffer grievous capital losses, or have been obliged to go bankrupt. Many producers have thus lost their reputations through no fault of their own. The result of this policy has been to drive the working classes out of employment and to force them on the dole and other social services; and the increase of these, in turn, adding to the heavy burden of taxation, has also added to the difficulties the producers have to contend with.

The question that now arises is, How can the defect in the monetary system be cured and the impoverishment of our National potential productive power be prevented? For it is clear that the

nation cannot live out of the interest paid on its national debt or out of the profits it receives on its foreign trade. This is proved by the fact that the present system has so far failed to bring about an effective reduction of debt or the heavy burden of taxation. On the contrary both of them seem to increase.

In his introduction to the *Wealth of Nations*, Adam Smith wrote as follows :—

“ Labour forms the fund from which every nation derives its wealth, and the increase of wealth depends first on the *productive power* of labour, namely, in the degree of skill, dexterity and judgment with which the skill of the nation is generally applied, and secondly, on the proportion between the number of those employed productively and the number of those not so employed.”

Frederick List, in commenting on this, observes :—

“ From this we see how clearly Adam Smith in general perceived that the condition of nations is principally dependent on the sum of their *productive powers*.”

Yet the Government and the Bank of England seem to be ignorant of this fundamental truth. Gold earns no part of the profits of industry, yet it is allowed to restrain or curtail its wealth productive power.

The great fundamental truths taught by Adam Smith and Frederick List have not been properly

interpreted by the orthodox economists, but this may be mainly due to Smith's erroneous theory of "exchangeable value," an indispensable part of which is that gold and silver (Bimetallism) shall be the measure of value. How he came to make this error, when he rightly held that "labour was the real and ultimate standard of value," is incomprehensible. As for Frederick List, he did not discuss the standard and measure of value at all; this was unfortunate, but he may have thought it wise to leave it alone.

List's vanity led him to say of Smith: "It does not, however, appear to be in the plan of nature that complete sciences should spring already perfected from the brain of individual thinkers." Be this as it may, Smith's great error was undoubtedly in accepting gold and silver as the measure of value when he correctly conceived that "labour was the real and ultimate standard of value." In trying to merge these two factors he was in reality endeavouring to merge two economic systems. He put the producers in pawn to the money leaders. It probably did not occur to him that gold alone would one day become an international currency and that the whole trade of the world would eventually be conducted on the basis of exchanging wealth products for gold, and not on the principle of the true barter system wherein exports would pay for imports.

Although Smith rightly conceived that labour was

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the "real and ultimate standard of value," he was evidently unable to evolve an invariable measure that could be made to approximate to the standard; and this was no doubt his reason for resorting to the precious metals. The science of banking was not, in his day, as far advanced as it is now, so that he is probably to be excused. The task before us, however, is to make good the deficiency.

II

THE QUANTITY THEORY OF MONEY

THE "Quantity Theory of Money" has established the fact that prices will vary in accordance with the amount of work a given volume of money and bank credit is called upon to perform, and it operates as follows :—

(1) If we assume that the supply of manufactures and produce remain the same, an increase in the quantity of money and bank credit will cause prices to rise. No increase in the quantity of money or in the volume of credit can occur without an importation of gold or an accumulation of foreign credits. Hence the reason why credit expands before production, and why (as the orthodox economists teach us) industrial prosperity is only possible in a period of rising prices. In other words, we have to allow an inflation of prices to occur before we can increase industrial activity. In a gold standard system this is unavoidable; and it is one of the defects of the system.

(2) If we assume that the supply of manufactures and produce remain the same, a decrease in the quantity of money and bank credit will cause prices to fall. And this fall may be brought about in two

ways: (a) from an exportation of gold—which will bring about a restriction of money and credit; and (b) from an inflation of prices, which, subsequently, will necessitate a deflation of prices. If prices are inflated it obviously impairs the power of the bankers to distribute credit equitably on a safe and secure basis throughout production; and, further, in a period of rising prices foreign producers will sell goods to us in exchange for gold and not for goods, so that, in the course of time, bankers will be forced to protect their cash position by raising the Bank Rate, and by so doing bring about a curtailment of credit and a deflation of prices.

But, as J. S. Mill has quite truly said, all prices do not rise equally at one and the same time. The speculators will always select the commodity that can be most easily manipulated, but when they have gone too far with their manipulation of prices the banker's position becomes a dangerous one; hence it is imperative for the bankers to diminish the quantity of credit in order to force a deflation of prices and so place their banking credits on a sound basis. But whilst deflation of credit can bring about a fall of prices, it cannot as promptly (without involving the producers in a loss) bring about a reduction in the costs of production. The gold standard system can force costs of production upwards against the producers, even although the volume of production has been increased; and,

likewise, it can force a reduction of the costs of production even although the volume of production has been decreased. These causes and effects are obviously contradictory, unscientific, and empirical. Potential productive power alone has the scientific right to lower or raise costs of production, and if it is freed from money control, it will produce the opposite effects to those produced by gold money. This is the main point to be borne in mind as our argument develops.

(3) On the other hand, if we assume the quantity of money and bank credit to remain the same, an increase in the supply of manufactures and produce will cause prices to fall ; but it should be noted that this fall of price would not be mainly due to the benefits derived from quantity production but to the fact that the total price-values of all the commodities produced must be reduced so as to conform to the quantity of money available. Accordingly, productive industry and labour derive no benefit. In other words, as the quantity of money is based on gold (which is limited), it follows that less of it will be given for each item produced in the mass. We may increase the quantity of production, but we are not allowed to increase the quantity of money necessary to facilitate its distribution. If we add to this the fact that free trade may cause (through imports) an additional increase in the supply of commodities, internal potential productive power

is further handicapped in regulating its output to conform to the quantity of money available. In consequence of these external interventions potential productive power is deprived of the full benefits to be derived from quantity production. Therefore, the gold standard and free trade are of no national advantage from the industrial and monetary points of view.

(4) Further, if we assume the quantity of money and bank credit to remain the same, a decrease in the supply of manufactures and produce will cause prices to rise. This would be brought about in two ways: (a) there would be more money to spend on a more limited production, and (b) there would be an increase in the costs of production in consequence of the smaller output. Thus we see that money based on gold still continues to compete with productive industry for the control of price-values; whereas the rise or fall of price-values should be determined solely by the volume of production. It is the producers' sole prerogative, and price should be used only as the indicator of the money's worth of their productions. Given quantity production, potential productive power can lower price-values profitably from week to week by invention, and through improvements in methods of production. If prices rise at all, it should be due to a rise in the costs of production occasioned by a reduction of the volume of production.

* * * * *

From the foregoing it will be observed—that the quantity of money remaining the same—an increase in the supply of manufactures and produce—whether from home production or free imports—will cause prices to fall, not in accordance with the costs of production, but in accordance with the quantity of money. Thus the fall of prices may be accelerated and so involve the producers in heavy losses. This system gives to money an arbitrary power which must operate to the detriment of the home manufacturers and of labour, for the reason that prices are not lowered profitably but unprofitably. Thus money becomes the master of production instead of its servant. And it must continue to be so as long as we are prepared to admit that the total possible output of gold as a commodity (which has its price fixed by law and from which the law of supply and demand has thereby been eliminated) shall control the potential output of all other natural materials and manufactures; and, in addition, expose them to a law of supply and demand. The logic of this proposition, if examined impartially, is absurd.

Also, when it is said that the value of money is in the inverse ratio to its quantity, such is not strictly correct. For instance, J. S. Mill asserts (*Principles of Political Economy*, Vol. 2, p. 13): "It is to be remarked that this ratio would be precisely that in which the quantity of money had

been increased. If the whole money in circulation was doubled, prices would be doubled. If it was only increased one fourth, prices would rise one fourth." An increase in the quantity of money will not cause prices to rise in the strict ratio as suggested by Mills; because manufacturers, merchants and retailers usually have a reserve of stocks in hand from which they can begin to meet any sudden increase of demand; and as stocks tend to diminish fresh orders are usually placed to make good the deficiency. There is also the second-hand market to be taken into consideration. Therefore the other rule begins to operate here, which says that as the supply of commodities increases prices fall. We can truly say that an increase in the quantity of money based on gold will cause prices to rise, yet not strictly in the inverse ratio to its quantity, for the reasons we have stated. There is always a time lag to be considered.

The implications of the Quantity Theory of Money are now clearly seen. We have shown that two opposite effects are created from an increase in the supply of money and commodities or from a decrease in the supply of both. But if money was really the counterpart of production this would not be possible; and for the sake of clarity we will summarize the movements again as follows:—

(a) If we increase production and the importation of foreign supplies—the quantity of money and

bank credit remaining the same—prices will fall, not because of the increase of production but irrespective of it. *We thus increase the supply before providing for the demand.*

(b) If we increase the supply of money and bank credit—the quantity of production and foreign supplies remaining the same—prices will rise. *We thus increase the demand before providing for the supply.*

Now, as an increase of money causes an increase of demand, and as an increase of demand causes an increase of production, and as an increase in production tends to decrease costs of production, why should prices rise? They rise because we have ourselves artificially created a law of supply and demand. Modern engineering practice clearly demonstrates that with every increase in the quantity of production costs of production will fall. There can be no dispute about this material fact,* which is confirmed in the economists' law of increasing returns.

* That very able economist Mr. R. G. Hawtrey in his book *Currency and Credit* writes as follows, page 43 :—" Now output cannot be increased without limit, and as the demand for fresh goods presses against the productive resources of the community prices rise. Retail prices rise because stocks are being depleted and cannot be quickly replenished ; wholesale prices rise because producers are besieged with orders that they cannot fulfil. As prices rise, the quantity of credit needed to finance a given consignment of goods increases in proportion, and the creation of credit is still further accelerated." This theory may have

Therefore, the kernel of our argument is this :— If money were really the counterpart of production—as it ought to be—these contrary movements would not be possible. With every increase in production money should expand in a corresponding ratio; and with every decrease in production money and bank credit should likewise decline—in order that the movements of money and credit may accord with modern engineering and chemical science which rules (1) that as the quantity of production increases prices will fall—because of the lower costs effected per unit of goods produced—and (2) that as the quantity of production diminishes prices will rise, because the cost of production per unit of goods

originated with the classical school but it would seem to be carried on by the modern one. It simply confirms our view that an increase in the quantity of money allows demand to increase before provision is made for a corresponding increase of supply (production). If prices rise against the producers' desire, it must be due to the reflex actions of monetary policy, such as speculation in natural materials and an increase in the costs of distribution; both of which, in turn, will increase the cost of living and set up a demand for an increase of wages. Thus is the vicious circle continued, of inflating credit before production, so that the demand for fresh goods will continue to press against the *unprepared* productive resources of the country.¹ But the truth must always remain that an increase in the quantity of production will, *per se*, decrease the cost per unit of goods produced. From this we can infer that if the producers were empowered to become their own distributors, the cost of distribution could be brought under control. The other question of speculation could be dealt with by legislation; so that the inherent difficulties we are now discussing are shown to be amenable to treatment.

produced will rise. Any reform of the Bank Charter Act should have due regard to these facts, and should be so designed as to give effect to the principles involved.

* * * * *

Let us now examine the theories of price and of value from the consumer's point of view ; that is, as it affects him through the operations of the Law of Supply and Demand. The definition of this Law is merely a restatement of the definition of the Quantity Theory of Money, hence our reason for saying that there is no natural Law of Supply and Demand.

If there be an increase in the quantity of money in circulation, it follows that there will be an increase of purchasing power in the hands of the people ; but with the return of prosperity and rising prices the purchasing power of the money in circulation diminishes. In other words, the £ note cannot buy as much as it would have bought in the period of depression. Prices have risen against the consumers because the speculators have raised prices in anticipation of the increase of demand. This operation is excused on the ground that it conforms to the Law of Supply and Demand !

As the quantity of money diminishes prices and wages fall, and so we enter our long period of depression. But although prices fall, and although the purchasing power of money has thereby increased,

the consumers cannot take full advantage of the cheaper prices ruling because the quantity of money in circulation has been diminished. The bins at the factories are full, the consumers are willing to buy, but "never the twain shall meet." It is very much akin to the dangling of a "carrot in front of the donkey's nose." We tempt him but do not allow him to eat it. This operation is also excused on the ground that it conforms to the Law of Supply and Demand.

In a period of depression the people cannot fully satisfy their wants because the money is not there in sufficient quantity for them to take advantage of the cheap prices at which the goods are offered.

Likewise, with the advent of a period of prosperity, whilst it is true that the money in the hands of the public will have increased, prices will yet have been raised against them; so that (as in the case of the donkey) the full satisfaction of their wants must always be a postponed event. In depression or prosperity, the consumers are always exploited. For that reason we do not regard the Law of Supply and Demand as a just or natural law.

* * * * *

Now let us examine the operations of the Law from the producers' point of view. As we have shown elsewhere: when the bankers are obliged to restrict bank credit, they compel the producers to sell their merchandise in a market short of purchasing

power (the bankers call this a deflation of prices) so that the producers are obliged to accept, in terms of gold, such prices as an unwilling market may be induced to give. This clearly proves that a scarcity of money based on gold will destroy values and also diminish production and supply. In other words, a diminution in the quantity of money *available for production* can force a reduction of price-values at the expense of capital. Hence the reason for the heavy capital and trading losses in which producers have been involved since the recent process of deflation was set in motion. No monetary system has any right, in its own self-interests, to involve producers in heavy capital losses, by compelling a raising and lowering of costs of production, or by the forced sale of commodities in a market shortened of purchasing power.

It is for these reasons we contend that it is not the business of money to control production or to increase or decrease price-values at will. In acting thus it impoverishes the producers and consumers, to enrich the moneyed interests and speculators to the extent of millions per annum. The destruction of values should always be the sole prerogative of potential productive power; but in order that it may function normally, freely and without external restraint, it is imperative that money should be forced to revert to its original function of being the mere medium of exchange. Adam Smith has

truly remarked: "Money, therefore, the great wheel of circulation, the great instrument of commerce, like all other instruments of trade, though it makes a part and a very valuable part of the capital, makes no part of the revenue of the society to which it belongs; and though the metal pieces of which it is composed, in the course of their annual circulation,* distribute to every man the revenue which properly belongs to him, they make themselves no part of that revenue." † When Smith discusses "money" he means gold and silver money. The metal pieces make no part of the revenue, but they enable the holders to demand a substantial share of it.

When the medium of exchange is divorced from gold and silver the word "money" will acquire a new definition. In a proper economic system the medium of exchange should be the measure of value; therefore, it will not mean "money" in the sense in which it is understood to-day. ‡ The conception of stabilizing the purchasing power of money and the price level, which some economists are trying to bring to reality, is an erroneous one and will lead nowhere. If it be our intention—as it is—to prevent gold from influencing prices, it will be impossible to stabilize money

* *The Wealth of Nations* (Adam Smith), Vol. I, chap. II, p. 275.

† Smith ought to have inserted the word "should" before "distributes."

‡ The £ notes will pass as "Currency."

in relation to prices, or prices in relation to money. If it were the desire to achieve money stability in this way, it would mean the retention of gold, in whole or in part, as the basis of money. This is certainly not our objective. Our purpose is to restore productive power to its proper position, with "money" and "price" used as words or indicators only. From this it will be understood, that when (in the new sense) we use the word "money," we conceive it to indicate the invariable measure of value.

The real business of the £ note as a measure of value should be to facilitate effectively the exchange of goods on a price basis; and the paper £ note is the most effective instrument that could be devised for this purpose. The popular notion that goods are bartered for goods, is not strictly correct. Before any exchange can be effected the goods offered must first of all be converted into a price—a numerical expression—and this price should have no relation to any commodity such as gold, for all commodities are subject to a cost of production, and a permanent value cannot be given to any of them. Price should merely be an indicator, and numerically express the worth of a commodity offered for sale, and numerically express the worth of a commodity to be bought. The conversion of goods into a price is an intermediate stage that has to be followed in the process of distribution.

This procedure is necessary so as to give to the possessors of money the power of suspending their purchases to suit their convenience both as regards time and place. A barter economy does not mean an instantaneous change of goods for goods. The option of time and choice must always be given to the purchaser. Therefore, a paper £ note is all that is required for expressing the money's worth or price value of a commodity.

The paper £ can be divided into 240 pence without loss, or into smaller fractions, and its cost of production is negligible. Thus it is but logical to infer that a £ note representing the worth of labour (the standard of value) must always be the invariable measure of value, and that its convertibility should be guaranteed and secured on the mass of wealth products which are in the process of production and distribution. Argued in another way, the £ note should always be the counterpart of the bills of exchange, which, it is suggested, should form the basis of the quantity of money so as to ensure an automatic adjustment of credit and money. Consequently, as such bills would be secured on wealth products, the £ note would at all times effectively represent the worth of purchasing power.

The problem will become clearer if we conceive that each instrument used in the process of production and distribution (be it a piece of paper or a

machine tool) should be confined to its own sphere of utility, and that it should not be allowed to restrain or interrupt the smooth working of any other instrument. But this interference must always occur in the case of money if we regard it as representing the worth of gold—a variable measure of value—instead of regarding it, as it might easily be made to be, as representing the worth of wealth products. In other words, we suggest that price should merely be an indicator, and numerically express the money's worth of the commodities to be bought and sold. Money would thus become what it should always have been—an effective medium of exchange. The standard and measure of value should not both be incorporated in the £ unit, actually or theoretically. The measure of value, being a price measure, should stand by itself and its cost of production should be negligible. The paper £ fulfils this requirement admirably.

The present method of conducting industry and trade really amounts to this:—a seller of goods is obliged to convert his goods (theoretically) into a second commodity (gold), the price of which is fixed by law, before he can purchase any other commodity. If we reduce the problem to this plain statement of fact it at once becomes ludicrous and absurd; particularly if it be borne in mind that there is not a sufficiency of gold in the world to allow of the full range of transactions going

through that would be involved in a proper barter system of exchange.

Mr. Hawtrey has recapitulated the problem concisely in the conclusion to this book *Currency and Credit*, p. 414; as follows:—

“So long as the quantity of purchasing power is not unduly increased or decreased, prices are not disturbed, and the value of the monetary unit of account remains steady. But owing to the natural instability of credit this cannot be relied on. Therefore the expedient has been adopted of ‘fixing the price of one commodity.’ Gold is given its coinage price, and to make this price a reality, it is decreed that every debtor may be required, if his creditor so desires, to pay in gold at that price. The result is that the dealers in debts* have to keep a part of their assets in gold, in order to be in a position to comply with their legal obligations.”

We thus get a clear definition of price in the present accepted use of the word. We also like his description “dealers in debts.” Then again on page 420 he writes:—

“Criticism of any theory of currency leads up to the question: What is the real aim of a currency system? What qualities should we look for in our standard of value? In some sense the answer must be that we look for fixity of value. But fixity of value is a conception which itself calls for explanation. *Value is not a quality, but a relation, and*

* Bankers.

fixity of value must be fixity of value in terms of some other thing or things. No one commodity can supply a satisfactory measure and the economist has recourse to an index number for a test."

The italics are ours, and it will be seen that we disagree with this proposition.

Mr. Hawtrey continues as follows on page 421 :—

"When it comes to practical consequences, all that debtor and creditor ask is that they may know how they stand, that they may be secured against arbitrary or incalculable variations in the value of the monetary unit. If it approximates to a fixed amount of human effort, or to a fixed amount of wealth, or to something intermediate between the two, this is in all probability sufficiently accomplished. It is the inherent instability of credit that is perpetually involving the world in credit expansions, each of which would threaten the collapse of the gold standard if it were not succeeded by a contraction in time. The alteration of expansions and contractions would be comparatively harmless but for the dislocation and distress which accompany the contraction."

It is to be observed that Mr. Hawtrey's only proposal for overcoming the difficulty is to have recourse to "an index number for a test." But we fail to see what good this does beyond emphasizing the imperfections produced by the gold standard.

III

THE INVARIABLE STANDARD AND MEASURE OF VALUE

As we have said, productive power alone can permanently and profitably lower price-values, and if it were given the requisite freedom and opportunity it could offer wealth products, produced at the lowest possible basis of cost, as security for the stabilization of money. The stability of money can be secured on a scientifically secured deflated basis, and on one that would impoverish neither the producer nor consumer. Credits extended on such a basis need not be called in because of the instability of credit, which is the chief concern of all bankers to-day. Therefore, as money, through the medium of bills of exchange, would be secured on the mass of production at its lowest cost of production, the mass of production must offer a more stable security than gold—a single commodity—for the stabilization of the £ note as the invariable measure of value. It is in this way only that fixity of values can be given to the whole range of commodities in the process of production and distribution.

If productive power was allowed to reduce price-values effectively—and there can be no doubt about its capacity to do so—it would thereby dispose of the theory that the value of any one commodity was determined by its relation to every other commodity. The price-value of every commodity should be determined by its cost of production, that is, labour services. The price-value would thus be predetermined before an exchange for money was proposed. Thus it would not be literally true to say that goods were exchanged for goods. In the mass this would be true, but not in individual transactions. We would buy and sell goods for money's worth (price), such money being secured on the mass of production properly balanced as between manufactures and agriculture.

The £ note should measure the worth of purchasing power over the mass of production just in the same way as a yard stick will measure 36 inches of any kind of textile fabric, or as a 1 lb. weight will balance 16 ounces of any kind of material. If we removed the impressed graduations on the yard stick, we could not prove to anyone that the plain stick was a yard long merely by saying that it was. It would have to be proved against the standard measure. Therefore, the utility of the yard stick is to be found in its cheapness, in the fact that the accuracy of the measurement is to be found within itself, and in the fact that it can be carried conveni-

ently from place to place. The public trust in its usefulness and utility is implicit ; and this confidence could also, in equal degree, be extended to a paper £, since it can be made a secure and stable measure of value at a negligible cost of production. The measure of value should always be the instrument of exchange itself ; but it can never be invariable if it has to be measured in any commodity external to it, such as gold or wheat, for these commodities are subject to a cost of production that varies and approximates to the face value of the £ note. In thus attempting to stabilize the measure as the counterpart of a commodity the price of which is fixed by law, we are really attempting to stabilize two factors as one—which is an impossibility.

On the yard measure are impressed 36 inches ; all weights are impressed with their respective weights ; and all measures have their respective capacities engraved or impressed thereon. The measure of value is, therefore, contained within these particular instruments, and confirmation is not dependent on any outside factor. Nevertheless, a £ note has to be confirmed as a measure of value against a gold sovereign. But the price to be paid for the standard ounce of gold, or for pure gold, has to be provided for out of a sale of wealth products ; and the value of it has to be maintained by this means. In such circumstances it cannot reasonably be held that gold can be a satisfactory

standard and measure of value ; * particularly as by law established, the price for the purchase and sale of a standard ounce has been fixed at 77/9-77/10.

The price to be paid for the purchase and sale of gold as a standard of value was made invariable in the hope that the gold also, as a measure of value, could be made invariable. We have therefore discovered the truth that price can be made invariable but not the commodity ; and this aspect of the question was evidently not realized when the law was established. The law of Supply and Demand was eliminated from the purchase and sale of gold, but it was retained in the purchase and sale of the other commodities—hence the reason, perhaps, why the public look upon gold as being the least variable of all the commodities. Little do they know the price they are paying for this money illusion. It is a fraud and a sham.

In a monetary system such as we suggest—which would remove the present restraint placed upon the inventive genius of our engineers, chemists, and scientists—price-values would in fact be predetermined, so that an expansion of currency would cease to cause a rise of prices. Some of the large producers, even to-day, lower their price-values

* I have to admit that the economists have always held that gold was a variable measure of value and therefore was unsatisfactory. But they have not found anything else to put in its place ; instead they deify it in a most superstitious way. They speak of it " as a friend they know."

irrespective of monetary conditions. In this way, supply and consumption could be increased within the purchasing power of wages and income. Thus it would come about that the recipients of income and wages would benefit from all improvements in the arts of production—provided, and always provided, that wages were paid in terms of the worth of purchasing power, and not in terms of a mere subsistence allowance in the worth of gold.

The orthodox school talk airily about paying working men a gold subsistence wage, a difficult thing to provide all of them with to-day. They think that in paying them this wage they are doing a most wonderful thing. They hold that "what is bought and sold is not the labour but the product of the labour." The conception which lies behind this theory and that of "subsistence wage" is too dreadful for words. We must learn to pay wages in terms of the worth of purchasing power, and not in terms of a bare subsistence in "gold money"—which has no stability. Furthermore, the wages of all persons should be slightly in excess of the bare subsistence, and there should be a uniform and invariable minimum.

If there was a uniform and invariable minimum wage established in the worth of purchasing power, it would be possible for potential productive power (through the inventive genius of our engineers, chemists, and scientists) to increase the wage by lowering price-values. In this way supply and

consumption could be increased within the purchasing power of wages and income ; or wages could be increased for a like purpose. The wage earners, in such a system, would welcome and encourage all inventions instead of objecting to them as they do to-day. But within a gold standard system, if labour increases production with a view of lowering the cost per unit of goods produced, it increases the purchasing power of gold money to its own ultimate disadvantage. In the end it lowers its subsistence wage ; and this reacts on productive industry as a whole.

Should the internal price level in any industry fall below that of the external price level, it would be necessary for producers to increase wages so as to increase consumption and absorb supply. In a proper barter system, such as we advocate, producers would never wish to see the wages of their employees diminish ; since a lowering of wages diminishes purchasing power and consumption and begets unemployment. It is here that an index indicator will be useful—to check the relation between internal prices and world prices, so that these may be approximated.

The presence of unemployment in a true barter system, with gradually falling prices, may indicate a need for a shortening of the working week, or that there should be a general increase in the wage level. This could be proved if internal prices

remained below world prices for any length of time, or if the cost of distribution was rising in relation to the cost of production. In the latter case a fixed relation should be established. Therefore the ideal conception is not a stable price level, but some means of equitably increasing wages to their maximum point. It is the utmost we can expect to achieve pending a world regulation of hours and wages, but no other conception coincides so admirably with our standard of experience and moral ethics.*

Articles of utility have no value to the vast majority of people unless they can be offered at a price that comes conveniently within the purchasing power of their wages or income. For instance, a desire can be created for gramophones, pianos, typewriters and motor-cars on the hire-purchase system of credit, but without this assistance the utilities named would have no value to most potential buyers. Therefore, by lowering price-values potential productive power can tap the lower veins of purchasing power, which are ever present in varying degrees in any economic system; and, by so doing, it can create values which otherwise would not exist. Low costs of production bring within the range of possibility the manufacture of utilities and the construction of works that would be impossible otherwise; and nowhere is this doctrine more apparent than in the

* Even with a world regulation of wages inequalities will arise. The cost of living in the temperate zones must always be less than in the colder climates.

construction of ships, electrical machinery and locomotives.

Productive power is service power; and its true aim is to bring within the reach of mankind all those material things that can be made use of and therefore have value. Money based upon gold reverses this natural order of procedure; it limits desire and consumption, and consequently we hold that the orthodox school have wrongly interpreted the "Theory of Value."

We agree with Mill, however, that among rich men a difficulty of attainment will determine the price-value of rare works of art, such as ancient sculptures, pictures by old masters, rare books or coins, or other articles of antiquarian interest. The market price of these will be determined by the man who values his money the least. But this rule will always apply within any economic system.

We can well understand that unemployed persons, or others striving to make both ends meet, would, owing to the insufficiency of purchasing power, more greatly appreciate the necessities of life than those who possess an adequate income of money. But, if poor persons do show a greater appreciation of possession, it does not mean that they give a greater value to the necessities of life. In any event, a theory or law of value cannot be established on a defect of this kind, nor should the people concerned be kept in subjection in the belief that this law and

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the law of supply and demand are infallible, that God has so willed it ! Rather should they be taught that a cure can be found for any imperfections that may be found within the economic system ; and that, with patience and vigilance, our economic life may be made to accord, in due time, with nature itself.

* * * * *

We now come to the most important part of this thesis. If we hold that the value of one commodity has no relation to the value of any other, in what way do we establish relative values ? If we assumed for one moment that there was no agricultural produce from which we could feed the population, it would be obvious that no value could be attached to manufactured utilities or any kind of material wealth outside of food. Therefore, at starvation point all values disappear, and with them the theory of exchangeable values ; so that to give stability to all material values we must get as far away as we can from poverty and unemployment ; and this we can do only by developing and producing agricultural products to the fullest possible extent within the national economic system.

We may truly say, then, that the worth of the mass of industrial manufactures obtains its total relative value from the worth of the mass of agricultural produce. As Smith has said, the country supports the towns, and the towns support the country. We have to ensure that the divisions and

sub-divisions of labour as between industry and agriculture are balanced ; so that, for our purpose, balance and stability will be synonymous terms. If the logic of this proposition be admitted (and it must be if we comprehend that wages should always be paid in the worth of purchasing power and not in terms of a subsistence wage), due care would have to be exercised by bankers in ensuring that a proper balance was maintained between agricultural produce and manufactures, in the wealth products used as cover for the bills of exchange—which, it is recommended, should be used as the basis of the new monetary system. This view may explain the reason why many economists in the past have recommended wheat as a better measure of value than gold, and they were certainly near the truth.

Adam Smith, in discussing the measure of value, came remarkably near the truth, in the following quotations :—

“ But when barter ceases, and money has become the common instrument of commerce, every particular commodity is more frequently exchanged for money than for any other commodity. . . . Hence it comes to pass, that the exchangeable value of every commodity is more frequently estimated by the quantity of money than by the quantity either of labour or of any other commodity which can be had in exchange for it. . . . Labour alone, therefore, never varying in its own value, is alone the ultimate and real standard by which the value of

all commodities can at all times and places be estimated and compared. It is their real price ; money is their nominal price only." *

" As it is the nominal or money price of goods, therefore, which finally determines the prudence or imprudence of all purchases and sales, and thereby regulates almost the whole business of common life in which price is concerned, we cannot wonder that it should have been so much more attended to than the real price." †

It was at this point that Smith broke down. If he had persisted with his view that " the exchangeable value of every commodity should be estimated by the quantity of labour," the world would have been spared many of its economic and social difficulties.

Other economists have held that wheat, or the average price of wheat, as a commodity, was a better measure of value than gold. The conception that lies behind this theory, and Smith's, is good, but the inherent difficulty lies in the fact that as the quantity of production of manufactured utilities is increased prices will fall with greater acceleration than would be the case with agricultural produce. Therefore, if wheat were made the measure of value the farmers would be placed in the same position

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, chap. V, pp. 34-5.

† Extract from *The Wealth of Nations* (Adam Smith), Vol. I, chap. V, p. 40.

as the holders of gold are now happily placed. As the years progressed they would receive more manufactures in exchange for their wheat without in any way contributing to the result. In other words, they would obtain something for nothing at the expense of the manufacturing industries; so that the unemployment problem would remain just as acute as it is at the present time.

Humanity has no control over the climatic elements, and, beyond enriching the soil with the aid of manures, etc., the land is not capable of improvement in the same way as a machine tool might be. Furthermore, the price of labour should be somewhat constant, and this, no doubt, led Adam Smith to conclude that labour was the "ultimate and real standard."

It is here that we realize the truth that if the quantity of production is increased, the quantity of money (based on wheat or gold) remaining the same, prices will fall. This points to the fact that wages should be paid as a claim on the worth of the whole range of commodities (properly balanced as between manufactured utilities and agricultural produce), and not as a mere subsistence based on the average price of food.

It will be necessary for all nations to regulate their national working conditions in this way, so as to ensure an adequate supply of agricultural produce from its own soil with which it may feed its

population. The total quantity of essential foodstuffs required to maintain the population of any country (the provision of the annual wages payable in the mass) is easily ascertainable. If the quantity of food required to feed an individual be multiplied by the total population, the total national food requirements for the year can be ascertained with accuracy. If a nation cannot produce its own total requirements in foodstuffs it must import the balance required ; and exchange its own exportable surplus of manufactures in payment thereof. But the bankers would still have to ensure that, in the trade of importing and exporting, equitable proportions were maintained. In this way, also, the increase of purchasing power could be automatically regulated to conform to the requirements of an increasing population.

An expansion of stable currency on the lines above suggested must not be confused with what is known as an inflation of currency. Expansion and Inflation are two different terms. An expansion of stable currency such as we are suggesting, implies the issue of convertible legal tender money against bills of exchange ; such bills being secured on self-liquidating wealth products produced on a quantity basis, and thus produced at prices tending to fall and not to rise. Furthermore, as the bills would not be accepted against the full value of the wealth products—except under a contract for sale

—but only against a maximum of 80 per cent. of the producers' contract prices, the burden of maintaining the automatic adjustment of credit and money would be imposed on the producers. This would be just, for the monetary system in that event would be the servant of production and not its master.

The effect of the new system would be to make the total services of labour the real and ultimate standard of value, such as Adam Smith had in view though he did not develop the idea to a logical conclusion. In other words, if a line is drawn at a point not less than 20 per cent. below the producers' contract prices (wholesale prices being disregarded), it would constitute the invariable standard of value. This will appear logical if we bear in mind that approximately 80 per cent. of the value of all wealth products represents, on an average, the labour expended. Therefore, if bills of exchange are used as the basis of the quantity of money, this form of currency expansion, being definitely anchored, eliminates the risk of inflation, and ensures the fixity of values; and it is so designed as to be capable of easy adjustment and regulation by the Bank of England, acting as a Central Bank. This is further explained in Chapter XIII, of *The Flaw in the Economic System*.

On the other hand, an inflation of currency means an issue of notes, by a Central Bank or by a Government, that is not fully covered by gold or wealth

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products. In consequence of this, it is not possible to make the notes convertible, so that they must remain in circulation; and, if not controlled or managed, be subject to the usual violent fluctuations in their exchange rates. It was in order to protect the public, industry and trade against such violent fluctuations in the exchange value of the inconvertible currency notes that the orthodox economists and bankers conceived it to be necessary to tie our £5 Bank of England notes to gold; and, theoretically at all events, to make them convertible into gold on demand. But the £1 treasury notes are not so convertible, and when these notes and the Bank of England notes are merged into one they will be inconvertible, so that the last trace of the gold standard, or the theoretical gold standard, will have disappeared. We shall then have a managed currency. If, therefore, our present legal tender money becomes inconvertible, and if the new system proposed restores to the public the right of convertibility, can there be any virtue in retaining the gold standard system in theory? Is it not a spent force?

It should be noted that at no time has Great Britain ever had the privilege or experience of expanding its currency issues based on bills of exchange secured on wealth products. Wherever this system has been partially tried it has proved a success—as may be evidenced in the Federal Reserve Banking system employed in the United States.

In this system there is a ratio of bills of exchange to gold (60 per cent. of the former to 40 per cent. of the latter), and the result is the wonderful and continuous prosperity which the United States now enjoys, with a comparatively stable price level, accompanied with cheap money.* It is essential, therefore, that a clear distinction should be drawn between what is known as an expansion and inflation of currency; and that it be duly noted in all discussions of the subject. The public should not be frightened by the bogey of inflation (as occurred during the War), for it does not apply to the present discussion. Inflation and deflation are gold standard diseases and as soon as we get rid of the "gold standard" they will cease to trouble us.

We shall conclude this thesis with a few remarks made by Ricardo, which are rather apposite to the present discussion :—

"While a standard is used, we are subject to only such a variation in the value of money as the *standard* itself is subject to; but against such variation there is no possible remedy, and late events have proved that, during periods of war, when gold and silver are used for the payment of large armies distant from home, those variations are much more considerable than has been generally allowed. This admission only proves that gold and silver are not

* Notwithstanding all this progress they still have to contend with the problem of unemployment and speculation.

so good a standard as they have been hitherto supposed,—that they are themselves subject to greater variations than it is desirable a standard should be subject to. They are, however, the best with which we are acquainted. If any other commodity less variable could be found, it might very properly be adopted as the future standard of our money, provided it had all the other qualities which fitted it for that purpose ; but, while these metals are the standard, the currency should conform in value to them, and whenever it does not, and the market price of bullion is above the Mint price, the currency is depreciated. This proposition is unanswered and unanswerable." *

" A well-regulated paper currency is so great an improvement in commerce, that I should greatly regret if prejudice should induce us to return to a system of less utility. The introduction of the precious metals for the purposes of money may with truth be considered as one of the most important steps towards the improvement of commerce and the arts of civilized life ; but it is no less true that, with the advancement of knowledge and science, we discover that it would be another improvement to banish them again from the employment to which, during a less enlightened period, they had been so advantageously applied." †

* Extract from the *Works of David Ricardo*, Section III, p. 402. Ricardo is very sound when he insists that the measure of value should be stabilized in a standard of value. A similar but more effective provision should be made in any new system.

† *Ibid.*, Section IV, p. 404.

IV

THE INVARIABLE STANDARD AND MEASURE OF VALUE

THE outstanding virtues of the invariable standard and measure of value as we have conceived it are, firstly, that it introduces no new element into the science of production; and secondly, that it does not in any way disturb the producers' present conception of business management. The fundamental principles on which it rests are concisely stated as follows:—

(a) Contrary to the orthodox view we state that permanent prosperity is only possible in an era of gradually falling costs of production (subject to profit), the extra margin thus created being distributed through wages, or through a reduction of prices, or through both wages and prices. In the distribution of the margin the greatest care is needed to ensure that the volume of currency is not thereby diminished, since this should at all times correspond to costs of production.

(b) Given an increasing purchasing power and quantity production as in (a) and an expansion of currency corresponding to any further expansion of production, an increase of wages and a gradual fall in prices accords with the accepted principles that govern

production. On the other hand, in a gold standard system, an increase of currency and credit involves an increase of prices and a diminution of purchasing power, and this conflicts with the first principles of production and social justice.

(c) A stable price level is undesirable, even if it were possible. In any event it is the wrong conception. What is needed is a stable and uniform wages level, with wages fixed according to their worth in purchasing power and not on a mere subsistence scale payable in the worth of gold. The wages to be periodically regulated so as to approximate internal prices with world prices, but on a competitive basis. The main object in life is to increase supply within the purchasing power of wages and income, or to increase supply through an increase of wages, or through both methods. This is only possible in an era of gradually falling costs of production. Nature and potential productive power, in unison, can create and distribute an abundance ; but they can only do so under gradually falling costs and freedom from gold control.

(d) The real and ultimate standard of value is labour (costs of production), and if at starvation point all values disappear it must follow that all true values originate with food. Labour's first care, therefore, should be the development of agriculture. Other occupations and the utilities produced by them are of secondary importance. From this it

may be concluded that the mass of manufactured goods derive their relative values from the mass of agricultural products, and that the divisions and sub-divisions of production will require to be properly balanced. With this object, food supply should be used as the determining factor. The farmer can live without the factory labourer; the factory labourer cannot live without the farmer. The mutual services they render, therefore, must be co-ordinated. This co-ordination should not be beyond the capacity of a civilized community.

(e) It should be left to potential productive power to reach its own point of stability in each sphere of its activity. We cannot estimate the extent to which costs of production may be lowered; the potentialities of machine power and chemistry are not yet fully ascertained.

(f) Money will only become an effective purchasing power when it actually represents the worth of wealth products, and is stabilized in their costs of production.

(g) Thus what is required is that the £ note should be stabilized as the yard stick or invariable measure of value, and we should leave to potential productive power the business of increasing purchasing power by the dual system of increasing wages and lowering prices. If the present restraints on industry are removed, this will come about naturally from the development of productive

industry, always providing that money ceases to have any control over prices.

(h) When the medium of exchange is divorced from gold and silver, the word "money" will acquire a new definition. In a proper economic system the medium of exchange should be the measure of value; therefore, it will not mean "money" in the sense in which it is understood to-day.* The conception of "fixing the purchasing power of money," which some economists are trying to bring to reality, is an erroneous one and will lead nowhere. If it be our intention—as it is—to prevent gold money from influencing prices, it would be absurd to allow paper money to enter upon a control of the price level. If it were the desire to achieve money stability in this way, it could not be done without retaining gold as the standard of value. And this is certainly not our objective. Our purpose is to establish costs of production of a balanced production as the standard of value, with "price" used as an indicator only.† From this it will be understood, that when (in the new sense) we use the word "money," we conceive it to indicate the invariable measure of value as defined herein.

(i) Price should be a numerical expression only,

* The £ notes will pass as "Currency."

† If trade requirements are to control the volume of currency, it would be absurd to expect that the volume of currency should control trade prices. One must predetermine the other, and we cannot have it both ways.

and should merely indicate the worth in money (the measure of value) of a commodity to be bought or sold. Price should function as an indicator only, and should be determined by the standard of value (labour costs), and not by the limited quantity of gold available. In other words, producers should have the right to predetermine the price-values of their own productions; these should not be imposed by money.

(j) Subject to the foregoing qualifications, a line drawn at 20 per cent. below the producers' selling prices (wholesale prices being excluded) will be found to be the standard of value in labour, and this should constitute an invariable measure of value in money. As, on an average, 80 per cent. of the value of all wealth products in a gradually falling costs of production, subject to profit, consists of labour services and overhead charges, the Banks can safely extend credits up to this line of demarcation.* The Bills of Exchange accepted against such credits would then be available for discount at the Bank of England—acting as the Central Bank. Against these Bills legal tender currency would be issued. Currency thus based upon the purchasing power of wealth products that have

* Where bills of exchange have been drawn and accepted to cover the cost of goods that have been sold by manufacturers, the Banks should discount such bills at full-face value subject to the standing and credit of the signatories to the bills being satisfactory. In many cases this is, at the present time, a customary practice.

been accepted as security for credits would be the legitimate counterpart of wealth. At present, money is an arbitrary medium with a purely arbitrary foundation, which has no relation to true wealth, or to those products upon which man's actual existence depends. The expansion of currency should have a definite fixed relation to the costs of production of a balanced production, and should have no relation to prices.

(k) Gradually falling costs of production are necessary in order to enable the productive industries to export their manufactures on a price basis that is equal to, or more attractive than, gold. In a period of rising prices the foreign buyer will always prefer gold to manufactures, and, at the present time, owing to the heavy burden of taxation, it is found to be more profitable for them to take gold than to take manufactures. In a system that permits of gradually falling costs of production the nation will acquire the power to balance its imports with its exports, and thus avoid the necessity of maintaining substantial gold reserves. Although the Bank of England has increased its gold reserves by many millions over a year ago, it has neutralized them to a large extent by a sale of securities. The Bank is afraid to expand credit freely because it is afraid of the rise in prices which must follow, and the resultant loss of competitive power. Thus are the British people held in bondage.

(i) Credit can always be safely extended in an era of gradually falling costs, provided that the gradual fall is brought about by productive power, and provided also that the system employed ensures an automatic adjustment of credit and money. In this way the currency in circulation would always be convertible ; and the notes issued against the worth of the gold reserves, being also convertible, could be used for the purposes of external trade, or to meet the legitimate claims of the Bills of Exchange on London. The gold reserves would thus become effective as reserves against the quantity of currency. But the gold reserves should not be allowed to increase beyond £200,000,000, and the guaranteed price of 77s. 9d. to 77s. 10d. per troy ounce of standard gold which the Bank of England is now compelled to maintain should be abolished. Should the gold reserves fall below the limit indicated, then the Bank would be obliged (in order to maintain the working proportion which experience will dictate) to purchase gold in the open market at the current rate of the day. This will effectively divorce the control of Britain's industrial and agricultural prosperity from gold, since it will effectively deprive it of any influence in the expansion or contraction of credit, and from having any influence on prices. Thus the world will have a barter system of economy ; and imports will pay for exports, which certainly is not the case to-day. Great Britain

will then be able to carry the burden of her War Debts with ease. The Bank of England would, of course, have to be guaranteed against any loss that may arise in the carrying of the gold reserves.

(*m*) In the system suggested, it would be necessary for the Bank of England to classify the credits issued by the Clearing Banks as credits A, B and C, etc. Credits issued against wealth products would be classified under A; the more speculative credits under B and C. Credits A should never be curtailed; but the extent of the credits issued to B and C should have a fixed ratio to A. If for any reason the price level is disturbed by those interests covered by credits B and C, these credits, in rotation, should be contracted. This system would not disturb the genuine producer, and would be much more effective as a corrective than the use of the discount rate—a method which harms producers who conduct their business legitimately. Recourse to the discount rate as a corrective cuts at the very roots of steady trade, employment, and national enterprise. The additional annual interest charges that are imposed on productive industry and commerce by an increase of the discount rate exceed, by many millions, the gold reserves which a rise in the discount rate seeks to protect. It thus becomes an absurdity. Furthermore, recent American experience has shown that the employment of the discount

rate, as a means for curbing speculation, is quite ineffective. A less costly and more direct method is required.

* * * * *

At the present time the balance sheets of most of the producers connected with the basic industries are not in a healthy condition; consequently it is possible that the limit of 80 per cent. up to which it is suggested the Banks should extend credit on wealth products may be too high. Above all other considerations the Banks must have unquestionable security, without which no scheme of monetary reform is possible; and as I have suggested in Chapter XIII, *The Flaw in the Economic System*, the working capital, assets, and goodwill of a Company must be the marginal security on which the Banks may fall back if the Bills of Exchange accepted as the basis of credit are not met at the due dates. But, given the requisite opportunity, the basic industries would soon take steps to adjust their financial position to the new conditions.

In any event the basic industries have declined slowly and heavily, and a violent recovery is not to be expected. The process of recovery and adjustment will be equally heavy and slow; but the assurance that a certain recovery was in progress—and would continue—would act as a tonic generally. The reflex actions would be considerable.

The use of the Bill of Exchange as the basis of

credit has been proved a sound and workable scheme by the Federal Reserve Board. There is really no violent change suggested if we merely ask the Clearing Banks to insist upon all overdrafts being covered by a Bill of Exchange so that they may be rediscounted and classified at the Central Bank. The changed condition is that which calls for the quality of the assets behind the bills to be of a self-liquidating character, *i.e.* wealth products.

Finally, if a bank considers a customer good enough for a bank loan, his bill should be good enough to use as a basis for the quantity of money. The distinction is merely a subtle one. If we bear in mind that a bank loan forms part of the credit structure, there can be no added risk in using the bill, which will correspond to the bank loan, as part of the basis of that structure. On the contrary, owing to the improved security called for, the risks involved in using the bill as the basis of credit must be considerably lessened.

The main criticism that may be directed against costs of production as a standard of value is that costs in different factories will vary. But the banks will only extend credit up to 80 per cent. of the average of producers' selling prices (wholesale prices excluded), and if costs of production exceed this limit then the loss will be covered by the producers' profit; failing which, by his capital. If costs of production are found to be below the 80 per cent. limit, then the pro-

ducers must declare this fact to their bankers, who will lend accordingly. The banks must never lend beyond costs of production, subject to the limit of 80 per cent. of producers' selling prices. It will thus be seen that the whole system ensures automatic stabilization, makes for the maintenance of efficiency, and the elimination of waste and obsolete methods.

NOTES ON CHAPTER IV

(1) In this Chapter we are dealing with normal monetary systems. In cases where there are substantial fiduciary issues, as in Great Britain, it may perhaps be necessary to employ the gold reserves together with bills of exchange as the basis of the quantity of money, but *without a fixed ratio of gold to wealth products, and without a fixed price for the purchase and sale of gold.*

In other words, the gold reserves should be treated like other wealth products, and used as part cover for the fiduciary issue, and for the adjustment of adverse balances of trade as and when they occur. The gold reserves will thus fluctuate in quantity, but the limits of this can be determined by experience. The Fiduciary issue ought to be retired gradually by the Treasury (this being an obligation of the State) with such assistance as the Bank may be able to afford from time to time from its profits.

The object of the foregoing arrangement is, as before, to maintain the principle of preventing any foreign nation from interfering with our internal prices and production by sending us gold, or withdrawing it. Thus will Great Britain achieve her independence, and so will all other Nations who may adopt the same system.

(2) When a manufacturer borrows a £10,000 gold credit from

his bank it is not the gold he requires to enable him to develop his production, but the labour, natural materials, and merchandise which the credit will enable him to buy. Profit is the reward of successful enterprise and effort, but this is not obtainable from the development of natural materials and merchandise without the co-operation of Labour. The manufacturer is, therefore, willing to pay interest on the credit that is necessary to enable him to obtain the labour services, materials, and merchandise he requires; but he could not afford to pay interest for the use of the gold only, for it cannot be used in the actual processes of production.

But as wages constitute the greatest portion of costs of production, it follows that the bulk of the credits the manufacturers obtain will have to be paid to their workers. The manufacturers, therefore, in giving new forms to the natural materials extracted from the earth, and in increasing the value of them by stages until the finished products are ready for marketing, are only able to do so in consequence of the food consumed by Labour during the stages of development. Thus the theory is confirmed that all true wealth comes from the soil, and profits from the development of it.

The augmentation of the gold reserves, therefore, do not of themselves increase the lendable capital or credit of the country. On the contrary, it is the wealth products that are available for circulation in the immediate present. If this be so—Why should we not use the wealth products themselves to extend the basis of credit? And why should gold be paid for a service which it does not really perform?

As J. B. Say asserts with truth:—

"The voluminous head of perishable products consumed within the year, nay, often at the very moment of production, as in the case of all immaterial products, is nevertheless an item of national revenue. For what are they but so many values produced and consumed in the satisfaction of human wants, which are the sole characteristics of revenue?"

"Thus, although the greater part of revenue, that is to say, of value produced, is momentarily resolved into money, the money, the quantity of silver coin itself, is not what constitutes revenue.

"No value, whether received in the shape of money or otherwise, can form a portion of annual revenue, unless it be the product, or the price of a product, created within the year. All else is capital—is property passing from one hand to another, either in exchange, as a gift, or by inheritance. For an item of capital, or one of revenue, may be transferred or paid anyhow, whether in the shape of personal or real, or movable or immovable property, or of money. But, no matter what shape it assume, revenue differs from capital essentially in this: that it is the result or product of a pre-existing source, whether land, capital, or industry."

Likewise, it may be said that when there is an abundance of wealth products available for circulation—and provided they be put into circulation on the lines we have suggested—bank interest rates will fall because the volume of money will sink them to their nominal level. But those who control gold money are averse to this scientific competition against what they now regard as their exclusive perquisite. But as Adam Smith truly said :—"Money, therefore, the great wheel of circulation, the great instrument of commerce, like all other instruments of trade, though it makes a part and a very valuable part of the capital, makes no part of the revenue of the society to which it belongs."

(3) A bill of exchange is defined by J. B. Say as follows :—

"A bill of exchange, a promissory note or cheque, and a letter of credit, are written obligations to pay, or cause to be paid, a sum of money, either at a future time, or at a different place.

"The right conveyed by the assignment of these engagements, though not capable of being enforced immediately, or elsewhere than at the stipulated place, yet gives them an actual value, greater or less according to circumstances.

"These engagements may be used as money in all transactions of purchase, as soon as they are invested with actual present value, by the prospect of their future value; indeed, most of the greater operations of commerce are effected through the medium of these securities.

"Sometimes, the circumstance of a bill of exchange being payable at another place will increase, instead of diminishing,

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its value; but this depends upon the state of commerce for the time being."

We may add to the above by saying that Foreign Banks prefer to invest their liquid funds in Bills of Exchange on London. These bills are bought and sold in the money markets and on being offered for sale it is the custom for the last seller to endorse the bills. If the bills are not paid at date of maturity, that is, in three or six months, the last endorser of the bill is first liable, and so the liability goes backward until the endorsers reach the acceptor and drawer of the bill. Failure to meet the bill at date of maturity is of rare occurrence, as the acceptors are usually the Clearing Banks or Merchant Bankers of very high standing; hence it comes about that Foreign Banks prefer to keep their liquid cash in such bills of exchange (even in preference to British Treasury Bills), and are frequently prepared to pay a finer price for them. It is more than a psychological question with the Foreign Banks; they prefer bills of exchange because they are really backed by wealth products; thus it leads them to conclude that in a time of crisis the bills may have a greater liquidity than the I.O.U. of the British Treasury.

V

THE LAW OF PREDETERMINATION ; AND A COMPARISON OF THE TWO SYSTEMS OF STABILIZATION

BEFORE discussing the merits of the two systems of stabilization, it will be necessary to refer again to the Law of Supply and Demand. We have repeatedly attacked this Law, and have shown how it originates with the expansion and contraction of credit based on gold, and how the speculators take advantage of it in their manipulations of prices. On the other hand, if the new monetary system herein outlined were to become effective, it should be possible to eliminate the present defects of the law, and make it function in a more normal and rational way. But this result could only be achieved if producers were allowed to predetermine prices. We have frequently discussed this idea in broad outline, and to facilitate discussion we shall call it the "Law of Predetermination," which will operate as follows :—

In order to ensure an automatic adjustment of credit and money (stabilization) it would be a prerequisite condition that producers should predetermine the prices at which all agricultural pro-

duce and manufactures should be sold. But this idea could only be made effective if an expansion of currency did not precede an expansion of production.

In a gold basis system currency and credit are expanded before production, and this originates a demand for commodities that do not exist—hence the rise of prices, the Law of Supply and Demand, Inflation and Deflation. Therefore, if producers were allowed to predetermine prices it would follow that all produce and merchandise would be listed for sale, and thus the public would know in advance what they would have to pay for what they may wish to buy. In this way the implications of the Law of Supply and Demand—as we now understand them—would be neutralized and made innocuous.

In the early days of civilization, and before money was invented, the producers always had to bring their goods to market before they could effect a barter exchange, or obtain a credit receipt for goods delivered but not sold. It did not necessarily follow that the goods brought to market had to be bartered immediately. An arrangement was no doubt made by which debits and credits offset each other and any balances remaining being adjusted at a future market. In the adjustment of such debits and credits, however, the producers would find their own standard of value, which might have been wheat, gold, cows or pigs. But in view of the

great progress since made in monetary science, £ notes can now be used as the measure of value, provided they are secured on the commodities against which they may be called upon to act as the medium of exchange.

The characteristic feature of a barter system of economy is, therefore, that commodities are first brought to market and prices are predetermined before the currency is called upon to act as the medium of exchange. In other words, their marketability and liquidity are ascertained. Thus, in any new monetary system proposed, full provision should be made for the principles of a barter economy as defined in the Law of Predetermination, without which automatic stabilization is not possible.

Even if prices were predetermined, however, it would not necessarily follow that all commodities produced would have value, or be entitled to credit. Whilst it is true that the price-value of any wealth product must be based on its cost of production, yet its realizable value (marketability and liquidity) will be determined by its utility, and the potential demand that can be attracted to it. Bankers, therefore, cannot be expected to extend credit on wealth products without these essential qualifications, which are an essential part of the security that will be required under Credits "A." Costs of production plus the qualifications mentioned will, in fact, constitute the standard of value.

For instance, a banker may be disposed to lend money on stock exchange securities if they have a marketable value; but he would obviously not dream of lending against securities that are unmarketable. Therefore, a similar distinction is certain to arise in the case of all wealth products that may be produced for marketing in a barter system. As we have indicated on more than one occasion, profits are the reward of successful enterprise and loss is the penalty of failure. All enterprise cannot succeed, but all effort is commendable since it is in this way alone that progress is achieved.

* * * * *

It will have been observed that in the monetary system herein advocated, the system of stabilization developed is based on stabilizing money in costs of production, with a balance maintained between agriculture and manufactures. Thus an automatic adjustment of credit and money is ensured, which will provide steady trade and employment; and, as costs of production fall, subject to profit, there will be an increase of wages and a lowering of prices—discretionary power remaining at all times with the producers. This form of stabilization we define as the "dual system."

The "dual system" is opposed to the other form of stabilization which calls for "a fixed purchasing power" and "a stable price level." From the pro-

ducer's point of view there are many grave objections to this latter system ; and for the sake of clarity we will recapitulate the points at issue as follows :—

(1) If the fall in the price of a commodity, which is subject to a potential demand, is met by a proportional increase of consumption only, stability will be maintained since the amount to be spent on the commodity will remain the same. In this case a fall in price will have no direct effect on the prices of other commodities, and therefore no adjustment will be needed. Thus stability will be maintained in other commodities. Hence we obtain the " dual system."

(2) If the fall in the price of a commodity, subject to a potential demand, is met by a more than proportional increase of consumption, there will be a transfer of purchasing power usually spent on other commodities to that one. This however will be balanced by the increase of labour services employed in satisfying the increased market requirements in this one commodity, which in turn will be balanced by an automatic and more than proportional increase of currency. Both these operations will automatically prevent a fall in the price of all the other commodities which might have occurred owing to the transfer of spending power. Thus the same amount of purchasing power will remain to be spent on the other commodities, and again the " dual system " of stability will be effectively maintained.

(3) If the demand for a commodity is a limited one, a fall in its price causes a less than proportional increase in the demand for it. In this case less is spent on it, so that the balance of purchasing power is available for the purchase of other commodities. As this will increase the quantity of production of other commodities their costs of production will fall; it would not be possible for their prices to rise. But, in any event, as all prices would be predetermined, it would be impossible for this diversion of spending power to cause a rise in prices of all other commodities. The cause and effect would be too limited in scope to be noticed.

(4) A fall in the price of a commodity, subject to profit, will tend generally to lower costs of production in all manufactures, but as costs of production fall it brings within the scope of enterprise the building of constructional work which previously had been considered impossible owing to excessive cost. Thus there will be a continuous demand for labour to complete work, and not, as at present, a continuous demand by labour for work. This conception has to be considered in order to make way for the progressive development of the arts, design, and architecture.

(5) A fall in the price of a commodity, subject to profit, gives to the nation the power of exporting its productions on a price basis that is at least equal to competitive world prices, and thus will enable

it to command foreign credits. In other words, it tends to keep industrial competitive power on an efficient basis. Thus the nation can with facility balance its imports with its exports, and the need for holding substantial gold reserves to protect the external trade is rendered unnecessary.*

(6) If it be admitted that Great Britain cannot produce all the foodstuffs she requires to feed her population, then it is essential for her to acquire the ability to pay for her imports on a price basis that is equal to, or more attractive than, gold. If we fixed the purchasing power of money, this would not be possible, and there would be a constant pressure on our gold reserves.

(7) Even if the purchasing power of the £ was fixed by an international arrangement (thus creating a stable price level), there would be no guarantee that the price of commodities in all countries could be regulated to scale. A violent movement of prices could occur within "a fixed purchasing power," and thus certain commodities may be made dearer in one country than in another.† To allow prices to find their own natural level, subject to profit, is the most certain way of eliminating irregularities

* Frederick List aptly describes this law as "The Power of Disposition" (see p. 139).

† If, for instance, prices of agricultural produce were forced to rise, this would increase costs of production generally, and unsettle the balance of trade as between agricultural production and manufactures.

of this kind. Furthermore, and as we have indicated elsewhere, world stability could best be promoted if nations were to study each other's wants—and so balance, and exchange, their exportable surpluses. Nations should study more closely the principles governing the division and subdivision of labour, so that they may create the exportable surpluses that are likely to be required, either in agriculture or manufactures.

(8) A fall in the price of a commodity, subject to profit, offers to the banker an improved and more liquid security as a basis of credit. It thus ensures an automatic adjustment of credit and money and eliminates "inflation" and "deflation."

(9) As the burden of taxation has to be included in the price-values of all productions offered for sale, it impairs competitive power; and in the event of a forced sale of the manufactures, it induces instability of credit and capital. A lowering of costs of production is desirable in order that the extra margin created may partly absorb the burden of taxation and thus assist in restoring competitive power at a profit.

(10) As the burden of taxation is mainly carried by productive industry, and as its overweight is due to the imperfections of the monetary system and high interest rates, a revision of the principles that govern monetary science is necessary.

* * * * *

The aim of a monetary system should be to distribute economic justice to all sections of the community—producers, consumers, and labour. This is best achieved when it promotes steady trade and employment at a steady profit, and when it maintains a balance between agriculture and manufacturing industry. Within the present system these ideals are not possible, owing to the inevitable inflation and deflation of currency and prices; and it is because of these latter evils that some economists have conceived the idea of stabilizing the purchasing power of money and thus ensuring a stable price level. But this conception, we submit, is wrongly conceived, since "a fixed purchasing power" could not ensure stable prices. What would really happen is that money would be given an arbitrary power of fixing artificial values.

If the purchasing power of money were fixed, and our engineers, chemists and scientists should then lower costs of production and distribute the margin through wages and prices, it would be necessary—in order to ensure the fixing of purchasing power—to increase the volume of the currency so as to curtail the fall in the price of those commodities whose prices could be lowered, and to bring about a rise in the price of all other commodities in general, in order to maintain the balance. But there could be no economic justice in such an arrangement. Productive power is service power, and should a

group of producers render a service to the community by lowering prices, they should not suffer the penalty of paying more for other commodities in general, and so provide increased profits for other producers.

A rise of prices even within a fixed purchasing power is a form of inflation, and to make the system effective money must still retain its control over prices, but we see no reason why it should continue to retain this arbitrary power. Furthermore, it could not reasonably be held that money lent to-day would be worth the same in ten years' time to the lender and borrower. Its value would depend entirely on the prices of the commodities in which they were each interested. Then again, there is a danger that in fixing the purchasing power of money there would be a loss of effort and enterprise due to the foregoing disabilities.

An argument put forward against the dual system of stabilization by those who favour "a fixed purchasing power" is that a lowering of prices will benefit debt holders to the disadvantage of the producers, since the latter must sell more of their manufactures to pay their debts. Within a gold standard system this argument holds good, but within a monetary system based on productive power it cannot be sustained. A lender should be able to obtain all the economic advantages he could have obtained if he had not lent his money. But he should not receive back less than he lent.

Producers will be able to repay their debts if they are earning profits, and it must be emphasized that the volume of goods they are able to deliver is immaterial. Everything will be measured by effort, and profit-earning capacity is all that will matter. Furthermore, interest rates on all prior lien industrial securities in the new system will be on a lower scale than they are to-day, but the holders of ordinary shares should be able to obtain a larger and more steady yield than at present—which, of course, would be simple justice. It should also be borne in mind that interest rates on Government debt and mortgages would also be on a much lower scale without impairing capital values. Therefore, so long as profits are being earned, all debts—other than gold debts—can be repaid or renewed without disadvantage to the borrower or lender.

The greatest care must be exercised in observing that in the new monetary system proposed current technical terms assume entirely new meanings. Also that productive industry should be given the opportunity of extricating itself from the meshes in which it is now entangled, and of gradually liquidating and discharging existing burdens. For these purposes economic freedom is necessary; and this should not be ignored whatever the difficulties may appear to be.

By fixing the purchasing power of money another injustice would be imposed on producers, namely,

the present burden of the National Debt would be fixed at its present weight, and so would all other debts. At present the burden of taxation is so onerous that the producers must be given an opportunity of dealing with it scientifically, and on the lowest basis of cost.

It is clear, therefore, that the benefits arising out of improvements in the arts of production should be passed on to all sections of the community without restriction ; that the arbitrary restrictive power now possessed by money in preventing an equitable distribution should be destroyed ; and that all power of interference should be withdrawn from it in any new scientific monetary system. Producers and labour will raise no objection to the new scheme of things so long as they can be assured of steady trade and employment at a profit, and of an adequate monetary system acting as their servant and not as their master. Producers and labour will receive their profits in the way of dividends and in the form of increasing wages and falling prices. It is the finest natural scheme of general co-partnership yet devised.

There is a further consideration of the problem of stabilization that must not be overlooked, and that is the " speculation " that is carried on in natural materials and cereals. It is the greatest disturbing factor in the present monetary system, and will be in any other system unless controlled or prohibited. We cannot develop a monetary science

unless all the known factors that make for stability are brought under control.

It would be unwise to attempt to regulate speculation by an expansion or contraction of currency, since this procedure would impose an unjust penalty on all those producers who conduct their business in a legitimate manner. The only positive method is to prohibit speculation altogether, and to insist on the producers of natural materials conducting their business in the same way as manufacturers have to do, that is, by becoming their own distributors; or, at least, to prohibit any person from buying or selling a commodity for the express purpose of gaining a difference in the market rate. The produce and metal markets should be confined to the actual producers and actual buyers, but the safest course would be to close the markets altogether. Given this latter assurance, the monetary system outlined herein would automatically provide scientific stability, leaving every man free to conduct his own business in his own way.

NOTES ON CHAPTER V

I invited an economist friend of mine to submit an opinion of my thesis, and his defence of it, as follows, may be of general interest :—

"For the purpose of facilitating our argument, let us call the commodity whose price has fallen commodity x ; in this way it may be distinguished from other commodities in general. Under the dual system the benefit of the fall in price of the commodity x accrues *In Toto* to the consumers of that commodity while the prices of all other commodities remain unchanged. It may be argued, however, that the purchasing power of the monetary unit has changed, and that that must lead to injustice. This is not so, however. All those who hold property may sell their property at the same price as before. Again, with the money which they receive for this property they may buy as much as before of all commodities, except commodity x , and of this commodity they may buy more than before . . . the advantage only therefore accruing to the consumers of the commodity, and not at the expense of anyone else. This idea is entirely in accordance with the conception of economic justice.

"Under 'a fixed purchasing power' there are two differences in the price movements which arise from the reduction in costs of commodity x . Firstly, the price of commodity x does not fall to the same extent as it does under the 'dual system,' therefore the consumers do not derive such a great advantage as in the other case. Secondly, there is a rise in the price of all other commodities. This latter movement means a gain to producers, in the form of profits, as it is not likely to be distributed as wages for some time. In so far as the producers obtain this extra profit, it is not indicative of an absolute gain except in so far as they spend their extra increment on the commodity x , but, on the other hand, their expenditure on other commodities is preserved at a level at which they can obtain as much as they did before of these commodities. Then again there is the individual who is not a consumer of commodity x , and to him all prices rise. Thus, he is sacrificed to the advantage

of the producers. As far as justice to property holders is concerned, there is no difference in the working of this system and the 'dual system.' All who hold property can sell at increased prices, but the money which they receive will only buy more of the commodity x than it bought before. Thus the position of property holders is the same under either system. As to those who hold money, however, the purchasing power of this money is reduced in respect of all commodities other than x , and hence all those who are not consumers of x suffer.

"From the above arguments, then, it seems that there is a great deal to be said for concentrating a fall in the price of one commodity to that commodity, and for preventing such a fall to influence the price level of other commodities at all. Thus, on this consideration as well, the 'dual system' seems the more desirable.

"The last argument which may be adduced against the 'dual system' as above described is that it would be impossible to work it. There is some doubt, however, even as to the soundness of this argument. For example, since by a method of index numbers changes in the general level of prices may be approximately calculated, and since too it is possible to calculate movements in the prices of individual commodities measured in terms of commodities in general, then it is possible to calculate how great a fall in the price level is due to a fall in the price of any given commodity. So long as the fall in the price level can be co-ordinated with a movement of this nature in the price of any one commodity, then the movement is desirable . . . but when a fall in the price level is unaccompanied by any movement in the price of one or more commodities relative to the rest, it is a sign that deflation is taking place. Thus, it seems that in practice it would be equally possible to allow the price level to fall as costs of production were reduced in individual industries as to stabilize the price level at any one position."

In connection with the foregoing observations I would like to mention that under the monetary system I propose it would be impossible to bring about a deflationary movement. There might be an indication of an insufficiency of employment in the manufacturing industries owing to a disturbance of the

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balance of trade. This would suggest that the balance between industrial and agricultural credits (internally and externally) was not being equitably maintained by the Central Bank authorities, but the requisite adjustment could be made by them without difficulty. Suitable charts and index numbers could be devised for this purpose.—J. T. P.

VI

A COMMERCIAL SYSTEM OF PRICES FOR AGRICULTURE

WE now arrive at the most acute problem of all, namely, the need for establishing a system of commercial prices, based on costs of production, in the agricultural industry. It will be obvious that before a policy of stabilization can be made generally effective, a standard and uniform system of calculating commercial prices for all commodities must prevail throughout the whole of the productive industries.

Apart from the adverse reflex actions of monetary policy, the most important difficulty the farmers have to contend with is their inability to conduct their business, like the manufacturers, on a commercial basis. The farmers are not allowed to determine the commercial prices at which their productions should be sold—the speculative markets and the dealers do this for them.

By commercial prices we mean prices that are based on costs of production below which it is not possible to sell any commodity without effecting a

loss. The sale of commodities at commercial prices enables the producers to maintain themselves in a high state of efficiency and to pay satisfactory wages to their employees, effect improvements in the arts of production, and thus lower costs of production. With such an economic organization the farmers generally would be encouraged to embark on extensive cultivation, to apply measures of rationalization to their industry, and to eliminate the greater part of the waste involved in their methods of distribution.

Market prices (as distinguished from commercial prices) are prices dictated by speculators and dealers in anticipating the supplies the farmers may have for marketing. If the farmers produce an abundance, and if they lack the requisite credit facilities, the speculators and dealers invariably anticipate the farmers' time for marketing by selling short in advance. It thus frequently happens that the farmers are obliged to sell at the bottom of the market and at prices which do not cover their costs of production. On the other hand, if there is likely to be a shortage the speculators raise their prices in advance against the consumers; from this rise in prices the farmers are compensated, and it frequently happens that they obtain more for a small crop than they do for a large one.

The operations of the speculators and dealers are excused on the ground that they conform to the Law

of Supply and Demand. It is for this reason we suggest that all agricultural prices should be based on costs of production. It is necessary that this should be so in order that the farmers may be given an opportunity of organizing their production on a business-like basis, and thus in their turn help to provide a sound basis for the new monetary system.

A manufacturer of engineering utilities does not hope to market the total output of his factory in the autumn of the year or in the spring of the year ; on the contrary, distribution is a gradual process. Production is released day by day to satisfy public demand, and this adequate production and continuous release eliminates all interference by speculators.

If then the farmer is given the same economic organization, there is no reason why he should not be able to introduce the quantity theory of production in the agricultural industry. The greater the production, the lower the cost, and it seems to us that nowhere is this principle more applicable than in agriculture.

If the services of distribution carry a larger personnel than is really necessary to do the work, or if they overrule or dominate the services of production, then the producers must accept a lower price for their output, and the wages of labour will be correspondingly reduced ; likewise, the consumers must pay more for what they consume. In a sound

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economic system the services of production should at all times dominate the services of distribution.

The quantity theory of production presupposes the existence of a mass of consumers and the direct distribution of the utilities or commodities produced to the consumers through retailers. The existence of middlemen is not necessary, since we can always produce and distribute more cheaply than we can buy and distribute. Middlemen are, of course, necessary in the trade of importing since they take the place of the manufacturers.

All things that exist were born in conception, so that the creation of a supply of utilities or commodities at reduced prices must precede the demand for them; and this is the basis of all enterprise. Supply and demand are not simultaneous in action and reaction; therefore if the community desires to have its wants satisfied, such wants must be studied and catered for, and it is but natural that those engaged in this work should have the right of selling what they may produce without interference by the speculators, dealers or merchants.

Given that the foregoing principles are accepted, all that remains is the formation of an economic organization that will directly connect the farmers as producers with the public as consumers. A simple scheme will have to be formulated that will enable the farmers to get their produce to the consumers with a minimum cost of distribution. In

this way only may the farmers obtain a larger price for their produce and the consumers pay less.

The agricultural problem presents no difficulty that is incapable of solution, provided it is dealt with on a strictly commercial basis. Take for example the case of wheat! What would be more natural than that the farmers economic organization should conclude a commercial agreement with the flour-millers, as an organized body, whereby the latter would undertake to purchase all the wheat produced in Great Britain at an agreed price of, say, 60s. per quarter? Such an arrangement would obviously eliminate all the speculators and dealers who at present intervene between the actual producers, *i.e.*, farmers and millers. The flour-millers would, of course, require that the Government should prohibit the importation of flour from abroad, so that the agreed commercial prices established by them with the farmers for the purchase of their wheat, and with the public for the sale of flour, were not disturbed. In return for this consideration, however, the flour-millers would have to agree to prohibit the exportation of grain offals except under license. This would ensure to the farmers plenty of cheap food for cattle breeding. Therefore, it is clear that the advantages to be derived from the commercial stabilization of agricultural prices are considerable.

As an important contribution to the subject under

discussion, we would like to direct attention to a circular letter of the Chamber of Shipping of the United Kingdom dated 14th July, 1928, in which it is said that the International Shipping Conference, London, 1928, had before them the reports of the World Economic Conference, Geneva, 1927. In a Resolution passed by the Shipping Conference, it is emphasized that increased attention should be given to the following recommendations of the Economic Conference :—

(a) "Agriculture is the occupation of the majority of workers throughout the world ; its various products represent in value the greater part of human labour, and the exchange of its products against industrial products forms indeed the basis of world trade."

(b) "In those States in which Customs protection is maintained, it should be reduced, both for industry and agriculture, to the lowest possible point indispensable to production ; care should be taken to assist in the maintenance of an equitable balance between industry and agriculture and not to stifle one to the advantage of the other."

If we had drafted clause (a) we should have done so as follows :—

"Agriculture is the occupation of the majority of workers throughout the world ; its various products represent in value the greater part of human labour, and the exchange of its products against industrial

products forms indeed the basis of 'National wealth and prosperity.' "

The Shipping Conference believes that "upon the maintenance of this 'equitable balance' the restoration of prosperity largely depends, and they are of the opinion that unless steps can be taken to reduce tariff barriers and other obstacles to trade which already exist and to prevent introduction of new tariffs where none exist to-day, a situation must develop in which primary production will diminish. A reduction in primary production can only result in a diminution of manufacture which depends entirely upon raw materials, with the result that exports will still further decline and all parties will automatically be the poorer."

The Secretary of the Chamber of Shipping then continues to write as follows :—

"I have therefore to ask that you will give further consideration to this question in order to prevent the detriment first to British Agriculture and secondly to British Manufacturing and Exporting Interests which must arise from a continuance or increase of trade barriers."

Although the Chamber of Shipping does not appear to appreciate the full significance of the resolutions passed by the World Economic Conference, yet it does admit the principle that a balance should be maintained between agricultural production and manufactures. It is to be noted, however,

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that the British Economists and the Shipowners blame the tariff barriers for the present lack of balance, *i.e.*, the world-wide depression. We dispute this assumption and say that the lack of balance throughout the world is due to the "money barriers." Scientific stability can only be definitely regulated at the basis of the monetary systems of each country, and it certainly is not possible at the "tariff barriers." But certain bankers, economists and shipowners must draw a red herring somewhere, in order to divert public attention from the real defect.

If it is necessary to maintain a balance between agriculture and manufactures in international trade, it is surely of fundamental importance that we should begin to effect a balance within the home trade. But without a revised monetary system the development of a prosperous national trade is not possible. It would be a mistake to assume that either safeguarding or protection would find a cure, and those who plead this reform alone do more harm than good to the cause. As part of a larger scheme of reform it would be effective, and it is to this end that reformers must direct their attention.

If "agriculture is the occupation of the majority of workers throughout the world, and its various products represent in value the greater part of human labour," it must surely be of fundamental importance from a national point of view. It is difficult

to see why this great question should be dealt with as a primary consideration from an international point of view, unless perhaps the merchants, ship-owners, and bankers are fearing the loss of their international markets. But in the position in which Great Britain is placed to-day, and in view of the burden of taxation which the producers in all the basic industries have to carry, it is of fundamental importance that the country should accept the recommendations of the Geneva Conference and apply them, with energy, at the earliest possible moment. The merchants and bankers are taxed only on the profits of their international trade, and in so far as the goods they import do not bear their due proportion of British Taxation, just so far are they "tax dodgers." In quoting prices they are always able to undersell British producers. We can well appreciate their motive in wishing to see a breakdown of "tariff barriers"—it would widen their privileges.

The eminent economists that assembled at the World Economic Conference, Geneva, made a frank admission of scientific fact when they asserted that the real cause of industrial depression was due to a lack of balance between the production of agricultural produce and manufactures. In other words, that world prosperity is based on the production of wealth products and not upon gold. But if the principles they enunciate are true (about which

there can be no question), surely a solid beginning can be made by developing prosperous national trades. If these theories are right from the point of view of international trade, they must be ideal from the point of view of national production.

The fact remains, however, that the British Gold Standard System could not finance the great volume of trade that would result from a balancing of British agriculture with British manufactures. And so long as it implies a transfer of the bulk of the import trade from the merchants to the producers, just as long will the Bank of England refuse to consider a change in the currency system. The merchants are in control of the Bank of England, and for this reason we strongly urge that there should be a larger industrial representation on the Court of the Bank, in order that its policy may be influenced more in favour of the national interests than in those of the international merchants and financiers. We can now see clearly the distinguishing features between a political economy based on gold and one that is based on productive power.

NOTES ON CHAPTER VI

The Chamber of Shipping did not quote the essential paragraphs from the recommendations of the World Economic Conference, Geneva, 1927, and it has, to our way of thinking, assumed too much. As its manner of presentation is likely to create an erroneous impression, we quote the essential resolutions as given in the Agriculture section of the final report, p. 43 :—

I. INTRODUCTION

" Agriculture is the occupation of the majority of workers throughout the world ; its varied products represent in value the greater part of human labour, and the exchange of its products against industrial products forms, indeed, the basis of world trade.

" The agricultural population remains for humanity a reservoir of energy capable of preserving the nations from the rapid human wastage which may result from any excessive growth of industry.

" The quantity of foodstuffs and raw materials produced by agriculture is one of the factors which determine the maximum limit of industrial development.

" The interdependence existing between nations

is no less close between the main classes of occupations—agriculture, industry, and commerce—and it would be vain to hope that one class could enjoy lasting prosperity independently of the others.

"Agriculture is at present hampered in the complete fulfilment of the economic rôle assigned to it by a general depression varying in degree but affecting a large number of countries on which the world depends for its supply of foodstuffs and raw materials.

"The economic depression in agriculture is characterized by the disequilibrium which has arisen between the prices of agricultural products and those of manufactured products; as a result, agriculturists in a great number of countries no longer receive a sufficient return for their labour and on their capital. This depression is aggravated in many countries by the difficulty of obtaining credit on normal terms and by the great increase in fiscal charges; while it has led to a decrease in the purchasing power of agriculturists, consumers have not, in all cases, benefited by a fall in the price of foodstuffs.

"The diminution in the purchasing power of the agricultural population has reacted upon industrial production, and is consequently one of the causes of unemployment, which in its turn reduces the outlets for agricultural products.

"Unless practical measures are taken to restore the price equilibrium, it is feared that sooner or later there will be a diminution in agricultural production detrimental to the welfare of mankind.

"Technical means exist, however, for a consider-

able development of agricultural production. They must therefore be put into operation. Their general adoption would have the most beneficial consequences for the prosperity and economic peace of the world."

II. GENERAL RESOLUTIONS

1. "The Conference regards as a vital economic question the increase of agricultural production, and, with this in view, the placing of agriculture on an equal footing with industry by enabling all those engaged in agriculture to obtain a satisfactory standard of living and a normal return for their labour and on their capital.

"It is important that this necessity should be brought home to public opinion, which does not always realize the true situation of agriculture and too often regards it as an industry of secondary importance.

2. "The improvement of agriculture must in the first place be the work of the agriculturists themselves. The general adoption of technical improvements, the scientific organization of production and stock-breeding, of the campaign against the diseases and the enemies of plants and animals, of marketing, of the standardization of agricultural products in the interests both of the producers and consumers, of the search for outlets, and of credits and insurance, will permit agriculturists to reduce their costs of production in their own interests and to the benefit of consumers.

"Owing to the considerable number of small and medium-sized agricultural undertakings—the tendency towards concentration displayed in industry

being absent—the organization of agriculturists should be continued along the lines of association and co-operation which have already been tested in many countries ; it may with advantage be supplemented by agreements between agricultural and consumers' co-operative societies.

" It is to the interests of Governments to encourage agriculture and the agricultural associations which have as their object the improvement of the situation of the agricultural population. In particular, the creation and development of mutual credit would be greatly facilitated by Government assistance.

" The Conference draws the attention of the Governments to the fact that high rates of interest and heavy taxation hamper production.

3. " Other measures to be contemplated depend chiefly on legislative action. In particular, the Conference is of opinion that social laws ensuring the welfare and security of workers should benefit agriculturists no less than industrial workers and employees, it being understood that such laws must be adapted to the special requirements of agriculture and to the special living and working conditions of rural populations. It is also of the opinion that agricultural instruction at all stages and the technical training of agriculturists should receive the attention of the different Governments as well as of agricultural associations.

4. " It is desirable that all hindrances to the free circulation of and trade in agricultural products should be removed, *in so far as their removal does not endanger the vital interests of the different countries and their workers.*

"In those States in which Customs protection is maintained, it should be reduced, both for industry and agriculture, to the lowest possible point indispensable to production; *care should be taken to assist in the maintenance of an equitable balance between industry and agriculture and not to stifle one to the advantage of the other.*

"The system of export prohibitions and export duties (*with the exception of taxes levied for the benefit of the industry concerned*) and frequent changes in Customs tariffs, which long experience has shown to be ineffectual and dangerous, should be definitely abandoned.

5. "The agriculturist should find his just remuneration not through speculation but in the regularity of prices, permitting him to reckon on a legitimate return equivalent to that accorded to other producers.

6. "Since, finally, the policy pursued in industrial or commercial questions reacts on the economic situation of agriculture, and vice versa, the Conference requests the League of Nations to ensure that in all its organizations already existing or to be formed which are or may be entrusted with economic questions, a place be always reserved for agriculture proportionate to its importance as a social and economic factor."

We do not dissent from any of the principles so ably set forth by the World Economic Conference, but they certainly do not support the free trade point of view. On the contrary, the resolutions indicate all too clearly the instability and adverse

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effects produced by gold monetary systems and the policy of *laissez-faire*. It seems strange that free traders should now take such a keen interest in the welfare of agriculture. Are they beginning to realize that all true wealth comes from the soil and production, and not from gold or from the science of exchange ?

VII

THE EFFECT OF DIRECT AND INDIRECT TAXATION ON COSTS OF PRODUCTION AND WAGES

IN the Preface (p. ix) it will be seen that the burden of taxation per head of population is greater in this country than in any other, and, as a consequence of this, we estimate that the competitive power of Britain's basic industries has been impaired by 12-18 per cent.—and this estimate has been arrived at after a most careful inquiry. From the argument which follows, it will be seen that we attribute this handicap to the reflex actions of the Free Trade Gold Standard System.

The Government is somewhat conscious of the adverse effects produced by the burden of taxation and has introduced a "Rating Relief Bill," but this measure will afford no real relief to the basic industries, however much Mr. Baldwin and Mr. Churchill may plead to the contrary. It may be regarded as a new "red herring." In reality the Rating Relief Bill will add to the burdens of an already over-burdened population, and it merely confirms our view that the whole method of applying

taxation in Great Britain in unscientific. Cause and effect are not sufficiently considered.

All direct and indirect taxation must be borne by productive industry and commerce, and mainly by industry. In other words, it is borne by the total wealth productive power of the country, that is, by the fixed and circulating capital. Under the Free Trade system the bulk of indirect taxation is obtained from the taxation of produce that cannot be produced within the country, and from the taxation of such articles as sugar, beer and whisky. But all taxation upon articles consumed by labour—and we use this term in its broadest sense—must be paid for at the expense of the purchasing power of wages, and ultimately at the expense of profits. Therefore, with every increase of indirect taxation, under the present system, wages and costs of production will rise, or, as in the present period of deflation, producers will find it next to impossible to reduce wages in order to increase their competitive power, because the purchasing power of wages will have been impaired to the extent of the burden of taxation.* Thus costs of production are permanently increased, and competitive power and purchasing power are both impaired.†

* See *Flux in the Economic System*, Chapter IX, p. 113.

† We are here discussing the combined effect of taxation and the quantity theory of money.

A reflex action of all this will be that the profit-earning capacity of the basic industries will fall. Some of the industries will earn no profits (they may trade at the margin) and most will trade at a loss. In such circumstances the volume of profit that is subject to income tax will be diminished, and thus a further increase of direct and indirect taxation must take place to compensate the Treasury. And this, in turn, will cause a still further increase in costs of production.

Taking all the facts into consideration, therefore, there can be no logical reason for taxing the imports of produce that cannot be produced at home, and for not taxing the imports of manufactures which can be produced at home. We tax the imported produce which comes within the spending power of the workers' wages, and thus diminish their consumption of food generally, but we do not tax those imports the manufacture of which are necessary to their employment at home. They are thus hit both ways. We here depart from doctrine laid down by the Physiocrats, Adam Smith, Ricardo, J. B. Say and Frederick List, and many other eminent economists since their time. If, therefore, we were to reverse the method of applying taxation, we should increase the consumption of both food and manufactures.

If we conceive that the wages of labour should be paid in terms of the "worth of purchasing power,"

the imposition of direct and indirect taxation will really mean that labour is deprived of a given quantity of food. But this conception is lost sight of at the present time because all taxation is paid in terms of gold. Furthermore, in a free trade gold standard system low wages must be the rule, as it cannot afford to pay wages beyond the "bare necessity." It expects costs of production to be brought down to a level which will enable home industries to compete with foreign imports which do not have to contribute to the burden of taxation.

The volume of gold money, which is limited, has to finance the greatest possible volume of work. In other words, gold money aims at cheapness; therefore, it is the mother of low wages and starvation. Its cardinal principle is that "labour has no value, that what is bought and sold is not the labour, but the commodities and services produced by the labour."

It may be accepted as a definite rule that savings, capital, and production, cannot accrue or increase without the payment of the highest possible wages, and any system of taxation which prevents this result from being achieved should be reformed.

The payment of high wages will only be possible in an economic system that is based on productive power, and whilst it is true that a lower profit per unit of goods produced will undoubtedly prevail, yet, owing to the total quantity of production

having been increased thereby, the total aggregate of profits will be larger. There cannot, however, be any conflict of interest between the manufacturers and the wage earners on this economic principle, since high wages promote an increase of consumption (and therefore supply) and brings nearer the approximation of potential consumption to potential production.

It is again necessary to issue a warning to those who advocate "safeguarding" as a cure for the evils we are now discussing. If such an increase in the volume of business was to occur as they expect and have every reason to hope for, the price level would fall away—for the simple reason that the present monetary system could not provide the requisite credit facilities and currency. Under the "quantity theory of money" prices will vary in accordance with the amount of work a given volume of money is called upon to perform. Therefore, what is first needed is a reform of the monetary system and then a redistribution of the weight of the "burden of taxation." If this were achieved, we could hope for the employment within two years of at least 1,000,000 more men than there are employed to-day, and the creation of a Budget surplus of at least £150,000,000 per annum, with a corresponding reduction of municipal taxation.

Some economists are at present claiming that the productive power of the basic industries is

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greater than is required, but such is not the case. The present total volume of trade is sufficient, if properly regulated, to absorb the bulk of the unemployed, and to restore the competitive power of the basic industries. But they do, however, speak truly as regards cause and effect within the present Free Trade Gold Standard System. The reason why they are right is that the bulk of the national credit resources is employed in financing the National Debt, and a limited amount only is available for production. The banks and the money market have sufficient credit resources to finance the import trade which does not have to carry any portion of the burden of taxation, but they cannot provide the full facilities required by industry which has to carry the bulk of it. This is not the fault of the Clearing Banks, however, but is the fault of those who support the present system.

VIII

APHORISMS FROM THE WORKS OF ADAM SMITH

"The annual labour of every nation is the fund which originally supplies it with all the necessaries and conveniences of life which it annually consumes, and which consist always either in the immediate produce of that labour, or in what is purchased with that produce from other nations.

"According, therefore, as this produce, or what is purchased with it, bears a greater or smaller proportion to the number of those who are to consume it, the nation will be better or worse supplied with all the necessaries and conveniences for which it has occasion.

"But this proportion must in every nation be regulated by two different circumstances: first, by the skill, dexterity, and judgment with which its labour is generally applied; and, secondly, by the proportion between the number of those who are employed in useful labour, and that of those who are not so employed. Whatever be the soil, climate, or extent of territory of any particular nation, the abundance or scantiness of its annual supply must, in that parti-

cular situation, depend upon those two circumstances." *

"This division of labour, from which so many advantages are derived, is not originally the effect of any human wisdom which foresees and intends that general opulence to which it gives occasion. It is the necessary, though very slow and gradual, consequence of a certain propensity in human nature which has in view no such extensive utility: the propensity to truck, barter, and exchange one thing for another." †

"When the division of labour has been once thoroughly established, it is but a very small part of a man's wants which the produce of his own labour can supply. He supplies the far greater part of them by exchanging that surplus part of the produce of his own labour, which is over and above his own consumption, for such parts of other men's labour as he has occasion for. Every man thus lives by exchanging, or becomes in some measure a merchant, and the society itself grows to be what is properly a commercial society." ‡

"Every man is rich or poor according to the degree in which he can afford to enjoy the necessities, con-

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Introduction, p. 1.

† Ibid., Chapter II, p. 15.

‡ Ibid., Chapter IV, p. 24.

veniences, and amusements of human life. But after the division of labour has once thoroughly taken place, it is but a very small part of these with which a man's own labour can supply him. The far greater part of them he must derive from the labour of other people, and he must be rich or poor according to the quantity of that labour which he can command, or which he can afford to purchase. The value of any commodity, therefore, to the person who possesses it, and who means not to use or consume it himself, but to exchange it for other commodities, is equal to the quantity of labour which it enables him to purchase or command. Labour, therefore, is the real measure of the exchangeable value of all commodities.

"The real price of every thing, what every thing really costs to the man who wants to acquire it, is the toil and trouble of acquiring it. What every thing is really worth to the man who has acquired it, and who wants to dispose of it or exchange it for something else, is the toil and trouble which it can save to himself, and which it can impose upon other people. What is bought with money or with goods is purchased by labour, as much as what we acquire by the toil of our own body. That money or those goods indeed save us this toil. They contain the value of a certain quantity of labour which we exchange for what is supposed at the time to contain the value of an equal quantity. Labour was the first price,

the original purchase-money that was paid for all things. It was not by gold or by silver, but by labour, that all the wealth of the world was originally purchased; and its value, to those who possess it, and who want to exchange it for some new productions, is precisely equal to the quantity of labour which it can enable them to purchase or command." *

"But when barter ceases, and money has become the common instrument of commerce, every particular commodity is more frequently exchanged for money than for any other commodity. . . . Hence it comes to pass, that the exchangeable value of every commodity is more frequently estimated by the quantity of money than by the quantity either of labour or of any other commodity which can be had in exchange for it. . . . Labour alone, therefore, never varying in its own value, is alone the ultimate and real standard by which the value of all commodities can at all times and places be estimated and compared. It is their real price; money is their nominal price only." †

"As it is the nominal or money price of goods, therefore, which finally determines the prudence or imprudence of all purchases and sales, and thereby regulates almost the whole business of common life in which price is concerned, we cannot wonder that it

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Chapter V, p. 32.

† *Ibid.*, pp. 34-5.

should have been so much more attended to than the real price." *

"When in any country the demand for those who live by wages—labourers, journeymen, servants of every kind—is continually increasing; when every year furnishes employment for a greater number than had been employed the year before, the workmen have no occasion to combine in order to raise their wages. The scarcity of hands occasions a competition among masters, who bid against one another, in order to get workmen, and thus voluntarily break through the natural combination of masters not to raise wages." †

"The liberal reward of labour, therefore, as it is the effect of increasing wealth, so it is the cause of increasing population. To complain of it is to lament over the necessary effect and cause of the greatest public prosperity." ‡

"Great labour, either of mind or body, continued for several days together, is in most men naturally followed by a great desire of relaxation, which, if not restrained by force or by some strong necessity, is almost irresistible. It is the call of nature, which

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Chapter V, p. 40.

† *Ibid.*, Chapter VIII, p. 70.

‡ *Ibid.*, p. 82.

requires to be relieved by some indulgence sometimes of ease only, but sometimes too of dissipation and diversion. If it is not complied with, the consequences are often dangerous, and sometimes fatal, and such as almost always, sooner or later, bring on the peculiar infirmity of the trade. If masters would always listen to the dictates of reason and humanity, they have frequently occasion rather to moderate than to animate the application of many of their workmen. It will be found, I believe, in every sort of trade, that the man who works so moderately as to be able to work constantly, not only preserves his health the longest, but, in the course of the year, executes the greatest quantity of work." *

"In countries which are fast advancing to riches, the low rate of profit may, in the price of many commodities, compensate the high wages of labour, and enable those countries to sell as cheap as their less thriving neighbours, among whom the wages of labour may be lower.

"In reality high profits tend much more to raise the price of work than high wages."†

"The establishment of any new manufacture, of any new branch of commerce, or of any new practice

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Chapter VIII, p. 84.

† *Ibid.*, p. 99.

in agriculture, is always a speculation, from which the projector promises himself extraordinary profits. These profits sometimes are very great, and sometimes, more frequently, perhaps, they are quite otherwise; but in general they bear no regular proportion to those of other old trades in the neighbourhood. If the project succeeds, they are commonly at first very high. When the trade or practice becomes thoroughly established and well known, the competition reduces them to the level of other trades." *

" Money, therefore, the great wheel of circulation, the great instrument of commerce, like all other instruments of trade, though it makes a part and a very valuable part of the capital, makes no part of the revenue of the society to which it belongs; and though the metal pieces of which it is composed, in the course of their annual circulation, distribute to every man the revenue which properly belongs to him, they make themselves no part of that revenue."†

" When the people of any particular country have such confidence in the fortune, probity, and prudence of a particular banker as to believe that he is always ready to pay upon demand such of his promissory

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Part I, p. 116.

† Book II, Chapter II, p. 275.

notes as are likely to be at any time presented to him, those notes come to have the same currency as gold and silver money, from the confidence that such money can at any time be had for them." *

"When we compute the quantity of industry which the circulating capital of any society can employ, we must always have regard to those parts of it only which consist in provisions, materials, and finished work; the other, which consists in money, and which serves only to circulate those three, must always be deducted. *In order to put industry into motion, three things are requisite: materials to work upon, tools to work with, and the wages or recompense for the sake of which the work is done. Money is neither a material to work upon, nor a tool to work with; and though the wages of the workman are commonly paid to him in money, his real revenue, like that of all other men, consists, not in the metal pieces, but in what can be got for them. . . .* The quantity of industry which any capital can employ must, evidently, be equal to the number of workmen whom it can supply with materials, tools, and a maintenance suitable to the nature of the work. Money may be requisite for purchasing the materials and tools of the work as well as the maintenance of the workmen. But the

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter II, p. 276.

quantity of industry which the whole capital can employ is certainly not equal both to the money which purchases, and to the materials, tools, and maintenance which are purchased with it, but only to one or other of those two values, and to the latter more properly than to the former."*

"When a bank discounts to a merchant a real bill of exchange drawn by a real creditor upon a real debtor, and which, as soon as it becomes due, is really paid by that debtor, it only advances to him a part of the value which he would otherwise be obliged to keep by him unemployed and in ready money for answering occasional demands. The payment of the bill, when it becomes due, replaces to the bank the value of what it had advanced, together with the interest. The coffers of the bank, as far as its dealings are confined to such customers, resemble a water pond, from which, though a stream is continually running out, yet another is continually running in, fully equal to that which runs out; so that, without any further care or attention, the pond keeps always equally, or very near equally full. Little or no expense can ever be necessary for replenishing the coffers of such a bank."†

"It is not by augmenting the capital of the country, but by rendering a greater part of that

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter II, pp. 278-9.

† *Ibid.*, p. 287.

*capital active and productive than would otherwise be so, that the judicious operations of banking can increase the industry of the country. That part of his capital which a dealer is obliged to keep by him unemployed, and in ready money for answering occasional demands, is so much dead stock, which, so long as it remains in this situation, produces nothing either to him or to his country. The judicious operations of banking enable him to convert this dead stock into active and productive stock; into materials to work upon, into tools to work with, and into provisions and subsistence to work for; into stock which produces something both to himself and to his country. The gold and silver money which circulates in any country, and by means of which the produce of its land and labour is annually circulated and distributed to the proper consumers, is, in the same manner as the ready money of the dealer, all dead stock. It is a very valuable part of the capital of the country, which produces nothing to the country. The judicious operations of banking, by substituting paper in the room of a great part of this gold and silver, enables the country to convert a great part of this dead stock into active and productive stock; into stock which produces something to the country." **

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter II, pp. 303-4.

*"A paper money consisting in bank notes, issued by people of undoubted credit, payable upon demand without any condition, and in fact always readily paid as soon as presented, is, in every respect, equal in value to gold and silver money, since gold and silver money can at any time be had for it. Whatever is either bought or sold for such paper must necessarily be bought or sold as cheap as it could have been for gold and silver." **

"It would be otherwise, indeed, with a paper money consisting in promissory notes, of which the immediate payment depended, in any respect, either upon the good will of those who issued them, or upon a condition which the holder of the notes might not always have it in his power to fulfil, or of which the payment was not exigible till after a certain number of years, and which in the meantime bore no interest. Such a paper money would, no doubt, fall more or less below the value of gold and silver, according as the difficulty or uncertainty of obtaining immediate payment was supposed to be greater or less, or according to the greater or less distance of time at which payment was exigible." †

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter II, p. 307.

† *Ibid.*, p. 308.

*"The same quantity of money, besides, cannot long remain in any country in which the value of the annual produce diminishes. The sole use of money is to circulate consumable goods. By means of it, provisions, materials, and finished work are bought and sold, and distributed to their proper consumers. The quantity of money, therefore, which can be annually employed in any country must be determined by the value of the consumable goods annually circulated within it." **

"Great nations are never impoverished by private, though they sometimes are by public prodigality and misconduct. The whole, or almost the whole public revenue, is in most countries employed in maintaining unproductive hands." †

"The quantity of money, on the contrary, must in every country naturally increase as the value of the annual produce increases. The value of the consumable goods annually circulated within the society being greater, will require a greater quantity of money to circulate them. A part of the increased produce, therefore, will naturally be employed in purchasing, wherever it is to be had, the additional quantity of gold and silver necessary for circulating

* Extract from *The Wealth of Nations* (Adam Smith). Vol. I. Book II, Chapter III, p. 322.

† *Ibid.*, p. 324.

the rest. The increase of those metals will in this case be the effect, not the cause, of the public prosperity." *

"The progress is frequently so gradual that, at near periods, the improvement is not only not sensible, but from the declension either of certain branches of industry, or of certain districts of the country, things which sometimes happen though the country in general be in great prosperity, there frequently arises a suspicion, that the riches and industry of the whole are decaying." †

"In the course of the four French wars, the nation has contracted more than a hundred and forty-five millions of debt, over and above all the other extraordinary annual expense which they occasioned, so that the whole cannot be computed at less than two hundred millions. So great a share of the annual produce of the land and labour of the country has, since the revolution, been employed upon different occasions in maintaining an extraordinary number of unproductive hands. But had not those wars given this particular direction to so large a capital, the greater part of it would naturally have been employed in maintaining productive

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Chapter III, pp. 322-3.

† *Ibid.*, p. 326.

hands, whose labour would have replaced, with a profit, the whole value of their consumption." *

"The stock which is lent at interest is always considered as a capital by the lender. He expects that in due time it is to be restored to him, and that in the meantime the borrower is to pay him a certain annual rent for the use of it. The borrower may use it either as a capital, or as a stock reserved for immediate consumption." †

"Almost all loans at interest are made in money, either of paper, or of gold and silver. But what the borrower really wants, and what the lender really supplies him with, is not the money, but the money's worth, or the goods which it can purchase. If he wants it as a stock for immediate consumption, it is those goods only which he can place in that stock. If he wants it as a capital for employing industry, it is from those goods only that the industrious can be furnished with the tools, materials, and maintenance necessary for carrying on their work. By means of the loan, the lender, as it were, assigns to the borrower his right to a certain portion of the annual produce of the land and labour of the country, to be employed as the borrower pleases."

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter III, p. 327.

† Ibid., Chapter IV., p. 332.

"The quantity of stock, therefore, or, as it is commonly expressed, of money which can be lent at interest in any country, is not regulated by the value of the money, whether paper or coin, which serves as the instrument of the different loans made in that country, but by the value of that part of the annual produce which, as soon as it comes either from the ground, or from the hands of the productive labourers, is destined not only from replacing a capital, but such a capital as the owner does not care to be at the trouble of employing himself." *

"A capital lent at interest may, in this manner, be considered as an assignment from the lender to the borrower of a certain considerable portion of the annual produce; upon condition that the borrower in return shall, during the continuance of the loan, annually assign to the lender a smaller portion, called the interest; and at the end of it, a portion equally considerable with that which had originally been assigned to him, called the repayment. Though money, either coin or paper, serves generally as the deed of assignment both to the smaller, and to the more considerable portion, it is itself altogether different from what is assigned by it.

"In proportion as that share of the annual produce which, as soon as it comes either from the

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter IV, p. 333.

ground, or from the hands of the productive labourers, is destined for replacing a capital, increases in any country, what is called the monied interest naturally increases with it. The increase of those particular capitals from which the owners wish to derive a revenue, without being at the trouble of employing them themselves, naturally accompanies the general increase of capitals ; or, in other words, as stock increases, the quantity of stock to be lent at interest grows gradually greater and greater.*

“ As the quantity of stock to be lent at interest increases, the interest, or the price which must be paid for the use of that stock, necessarily diminishes, not only from those general causes which make the market price of things commonly diminish as their quantity increases, but from other causes which are peculiar to this particular case. As capitals increase in any country, the profits which can be made by employing them necessarily diminish. It becomes gradually more and more difficult to find within the country a profitable method of employing any new capital. There arises in consequence a competition between different capitals, the owner of one endeavouring to get possession of that employment which is occupied by another. But upon most

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter IV, p. 334.

occasions he can hope to jostle that other out of this employment, by no other means but by dealing upon more reasonable terms. He must not only sell what he deals in somewhat cheaper, but in order to get it to sell, he must sometimes too buy it dearer. The demand for productive labour, by the increase of the funds which are destined for maintaining it, grows every day greater and greater. Labourers easily find employment, but the owners of capitals find it difficult to get labourers to employ. Their competition raises the wages of labour, and sinks the profits of stock. But when the profits which can be made by the use of a capital are in this manner diminished, as it were, at both ends, the price which can be paid for the use of it, that is, the rate of interest, must necessarily be diminished with them.

“ Mr. Locke, Mr. Law, and Mr. Montesquieu, as well as many other writers, seem to have imagined that the increase of the quantity of gold and silver, in consequence of the discovery of the Spanish West Indies, was the real cause of the lowering of the rate of interest through the greater part of Europe. Those metals, they say, having become of less value themselves, the use of any particular portion of them necessarily became of less value too, and consequently the price which could be paid for it. This notion, which at first sight seems so plausible, has been so fully exposed by Mr. Hume, that it is,

perhaps, unnecessary to say anything more about it." *

" No equal capital puts into motion a greater quantity of productive labour than that of the farmer. Not only his labouring servants, but his labouring cattle, are productive labourers. In agriculture too nature labours along with man ; and though her labour costs no expense, its produce has its value, as well as that of the most expensive workmen." †

" The capital employed in agriculture, therefore, not only puts into motion a greater quantity of productive labour than any equal capital employed in manufactures, but in proportion too to the quantity of productive labour which it employs, it adds a much greater value to the annual produce of the land and labour of the country, to the real wealth and revenue of its inhabitants. Of all the ways in which a capital can be employed, it is by far the most advantageous to the society." ‡

" When the capital of any country is not sufficient for all those three purposes, in proportion as a greater share of it is employed in agriculture, the greater will be the quantity of productive labour which it puts into motion within the country ; as will like-

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter IV, p. 335.

† *Ibid.*, Chapter V, p. 343.

‡ *Ibid.*, p. 344.

wise be the value which its employment adds to the annual produce of the land and labour of the society. After agriculture, the capital employed in manufactures puts into motion the greatest quantity of productive labour, and adds the greatest value to the annual produce. That which is employed in the trade of exportation has the least effect of any of the three." *

"The capital, therefore, employed in the home-trade of any country will generally give encouragement and support to a greater quantity of productive labour in that country, and increase the value of its annual produce more than an equal capital employed in the foreign trade of consumption; and the capital employed in this latter trade has in both these respects a still greater advantage over an equal capital employed in the carrying trade. The riches, and so far as power depends upon riches, the power of every country must always be in proportion to the value of its annual produce, the fund from which all taxes must ultimately be paid. But the great object of the political economy of every country is to increase the riches and power of that country. It ought, therefore, to give no preference nor superior encouragement to the foreign trade of consumption above the home-trade, nor to the carrying trade above either of the other two. It

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chapter V, p. 346.

ought neither to force nor to allure into either of these two channels a greater share of the capital of the country than what would naturally flow into them of its own accord.

"Each of those different branches of trade, however, is not only advantageous but necessary and unavoidable, when the course of things, without any constraint or violence, naturally introduces it.

"When the produce of any particular branch of industry exceeds what the demand of the country requires, the surplus must be sent abroad and exchanged for something for which there is a demand at home." *

"The great commerce of every civilized society is that carried on between the inhabitants of the town and those of the country. It consists in the exchange of rude for manufactured produce, either immediately, or by the intervention of money, or of some sort of paper which represents money. The country supplies the town with the means of subsistence and the materials of manufacture. The town repays this supply by sending back a part of the manufactured produce to the inhabitants of the country. The town in which there neither is nor can be any reproduction of substances, may very properly be said to gain its whole wealth and

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I. Book II, Chapter V, pp. 351-2.

subsistence from the country. We must not, however, upon this account, imagine that the gain of the town is the loss of the country. The gains of both are mutual and reciprocal, and the division of labour is in this, as in all other cases, advantageous to all the different persons employed in the various occupations into which it is subdivided. The inhabitants of the country purchase of the town a greater quantity of manufactured goods, with the produce of a much smaller quantity of their own labour, than they must have employed had they attempted to prepare them themselves. The town affords a market for the surplus produce of the country, or what is over and above the maintenance of the cultivators, and it is there that the inhabitants of the country exchange it for something else which is in demand among them." *

"As subsistence is, in the nature of things, prior to conveniency and luxury, so the industry which procures the former must necessarily be prior to that which ministers to the latter. The cultivation and improvement of the country, therefore, which affords subsistence must, necessarily, be prior to the increase of the town, which furnishes only the means of conveniency and luxury. It is the surplus produce of the country only, or what is over and

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book III, Chapter I, pp. 355-6.

above the maintenance of the cultivators, that constitutes the subsistence of the town, which can therefore increase only with the increase of this surplus produce. The town, indeed, may not always derive its whole subsistence from the country in its neighbourhood, or even from the territory to which it belongs, but from very distant countries; and this, though it forms no exception from the general rule, has occasioned considerable variations in the progress of opulence in different ages and nations." *

"In seeking for employment to a capital, manufactures are, upon equal or nearly equal profits, naturally preferred to foreign commerce, for the same reason that agriculture is naturally preferred to manufactures. As the capital of the landlord or farmer is more secure than that of the manufacturer, so the capital of the manufacturer, being at all times more within his view and command, is more secure than that of the foreign merchant." †

"If, notwithstanding all this, gold and silver should at any time fall short in a country which has wherewithal to purchase them, there are more expedients for supplying their place than that of almost any other commodity. If the materials of manufacture are wanted, industry must stop. If

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book III, Chapter I, p. 356.

† *Ibid.*, p. 358.

provisions are wanted, the people must starve. But if money is wanted, barter will supply its place, though with a good deal of inconveniency. Buying and selling upon credit, and the different dealers compensating their credits with one another, once a month or once a year, will supply it with less inconveniency. A well-regulated paper money will supply it, not only without any inconveniency, but, in some cases, with some advantages. Upon every account, therefore, the attention of government never was so unnecessarily employed as when directed to watch over the preservation or increase of the quantity of money in any country." *

"It would be too ridiculous to go about seriously to prove that wealth does not consist in money, or in gold and silver, but in what money purchases, and is valuable only for purchasing. Money, no doubt, makes always a part of the national capital; but it has already been shown that it generally makes but a small part, and always the most unprofitable part, of it." †

"What is prudence in the conduct of every private family can scarce be folly in that of a great kingdom. If a foreign country can supply us with a commodity

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I. Book IV, Chapter I, p. 402.

† *Ibid.*, p. 404.

cheaper than we ourselves can make it, *better buy it of them with some part of the produce of our own industry, employed in a way in which we have some advantage.* The general industry of the country, being always in proportion to the capital which employs it, it will not thereby be diminished, no more than that of the above-mentioned artificers ; but only left to find out the way in which it can be employed with the greatest advantage. It is certainly not employed to the greatest advantage when it is thus directed towards an object which it can buy cheaper than it can make."*

" But if foreigners, *either by prohibitions or high duties*, are hindered from coming to sell, they cannot always afford to come to buy ; because coming without a cargo, they must lose the freight from their own country to Great Britain. By diminishing the number of sellers, therefore, we necessarily diminish that of buyers, and are thus likely not only to buy foreign goods dearer, but to sell our own cheaper than if there was a more perfect freedom of trade. As defence, however, is of much more importance than opulence, the act of navigation is, perhaps, the wisest of all the commercial regulations of England.

" The second case, in which it will generally be

* Extract from *The Wealth of Nations* (Adam Smith). Vol. I. Book IV, Chapter I, p. 422.

advantageous to lay some burden upon foreign for the encouragement of domestic industry, is, when some tax is imposed at home upon the produce of the latter. In this case, it seems reasonable that an equal tax should be imposed upon the like produce of the former. This would not give the monopoly of the home market to domestic industry, nor turn towards a particular employment a greater share of the stock and labour of the country than what would naturally go to it. It would only hinder any part of what would naturally go to it from being turned away by the tax into a less natural direction, and would leave the competition between foreign and domestic industry, after the tax, as nearly as possible upon the same footing as before it."*

"Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer. The maxim is so perfectly self-evident, that it would be absurd to attempt to prove it."†

"Artificers, manufacturers and merchants can augment the revenue and wealth of their society by parsimony only; or, as it is expressed in this system, by privation, that is, by depriving them-

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book IV, Chapter I, p. 429. † Ibid., Chapter VIII, p. 159.

selves of a part of the funds destined for their own subsistence. They annually reproduce nothing but those funds. Unless, therefore, they annually save some part of them, unless they annually deprive themselves of the enjoyment of some part of them, the revenue and wealth of their society can never be in the smallest degree augmented by means of their industry. Farmers and country labourers, on the contrary, may enjoy completely the whole funds destined for their own subsistence, and yet augment at the same time the revenue and wealth of their society. Over and above what is destined for their own subsistence, their industry annually affords a neat produce, of which the augmentation necessarily augments the revenue and wealth of their society. Nations, therefore, which, like France or England, consist in a great measure of proprietors and cultivators can be enriched by industry and enjoyment. Nations, on the contrary, which, like Holland and Hamburgh, are composed chiefly of merchants, artificers and manufacturers, can grow rich only through parsimony and privation. As the interest of nations so differently circumstanced is very different, so is likewise the common character of the people. In those of the former kind, liberality, frankness, and good fellowship naturally make a part of that common character. In the latter, narrowness, meanness, and a selfish disposition, averse to all social pleasure and enjoyment.

"The unproductive class, that of merchants, artificers and manufacturers, is maintained and employed altogether at the expense of the two other classes, of that of proprietors, and of that of cultivators. They furnish it both with the materials of its work and with the fund of its subsistence, with the corn and cattle which it consumes while it is employed about that work.

"The unproductive class, however, is not only useful, but greatly useful to the other two classes. By means of the industry of merchants, artificers and manufacturers, the proprietors and cultivators can purchase both the foreign goods and the manufactured produce of their own country which they have occasion for, with the produce of a much smaller quantity of their own labour than what they would be obliged to employ if they were to attempt, in an awkward and unskilful manner, either to import the one, or to make the other for their own use." *

"It can never be the interest of the proprietors and cultivators to restrain or to discourage in any respect the industry of merchants, artificers and manufacturers. The greater the liberty which this unproductive class enjoys, the greater will be the competition in all the different trades which compose it, and the cheaper will the other two classes be

* Extract from *The Wealth of Nations* (Adam Smith), Vol. II, Book IV, Chapter VIII, pp. 166-7.

supplied, both with foreign goods and with the manufactured produce of their own country.

"It can never be the interest of the unproductive class to oppress the other two classes. It is the surplus produce of the land, or what remains after deducting the maintenance, first, of the cultivators, and afterwards, of the proprietors, that maintains and employs the unproductive class. The greater this surplus, the greater must likewise be the maintenance and employment of that class. The establishment of perfect justice, of perfect liberty, and of perfect equality, is the very simple secret which most effectually secures the highest degree of prosperity to all the three classes. . . .

"It can never be the interest of those landed nations, if I may call them so, to discourage or distress the industry of such mercantile states, by imposing high duties upon their trade, or upon the commodities which they furnish. Such duties, by rendering those commodities dearer, could serve only to sink the real value of the surplus produce of their own land, with which, or, what comes to the same thing, with the price of which, those commodities are purchased. Such duties could serve only to discourage the increase of that surplus produce, and consequently the improvement and cultivation of their own land. The most effectual expedient, on the contrary, for raising the value of that surplus produce, for encouraging its increase, and conse-

quently the improvement and cultivation of their own land, would be to allow the most perfect freedom to the trade of all such mercantile nations.

"This perfect freedom of trade would even be the most effectual expedient for supplying them, in due time, with all the artificers, manufacturers and merchants, whom they wanted at home, and for filling up in the properest and most advantageous manner that very important void which they felt there." *

"By a union with Great Britain, Ireland would gain, besides the freedom of trade, other advantages much more important, and which would much more than compensate any increase of taxes that might accompany that union. By the union with England, the middling and inferior ranks of people in Scotland gained a complete deliverance from the power of aristocracy which had always before oppressed them. By a union with Great Britain, the greater part of the people of all ranks in Ireland would gain an equally complete deliverance from a much more oppressive aristocracy: an aristocracy not founded like that of Scotland, in the natural and respectable distinctions of birth and fortune; but in the most odious of all distinctions, those of religious and political prejudices; distinctions which, more than any other, animate both the insolence

* Extract from *The Wealth of Nations* (Adam Smith), Vol. II, Book IV, Chapter VIII, pp. 168-9.

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of the oppressors and the hatred and indignation of the oppressed, and which commonly render the inhabitants of the same country more hostile to one another than those of different countries ever are. Without a union with Great Britain, the inhabitants of Ireland are not likely for many ages to consider themselves as one people." *

* Extract from *The Wealth of Nations* (Adam Smith), Vol. II, Book V, Chapter III, p. 430.

NOTE ON CHAPTER VIII

In Lectures, p. 192, Adam Smith is quoted as follows :—" All commerce that is carried on betwixt any two countries must necessarily be advantageous to both. The very intention of commerce is to exchange *your own commodities for others which you think will be more convenient for you.*" Therefore, it is what *you in your discretion may think*, and not what the foreigner thinks.

IX

APHORISMS FROM THE "WORKS OF DAVID RICARDO"

*"If we had then an invariable standard, by which we could measure the variation in other commodities, we should find that the utmost limit to which they could permanently rise, if produced under the circumstances supposed, was proportioned to the additional quantity of labour required for their production; and thus unless more labour were required for their production, they could not rise in any degree whatever. A rise of wages would not raise them in money value, nor relatively to any other commodities, the production of which required no additional quantity of labour, which employed the same proportion of fixed and circulating capital, and fixed capital of the same durability. If more or less labour were required in the production of the other commodity, we have already stated that this will immediately occasion an alteration in its relative value, but such alteration is owing to the altered quantity of requisite labour, and not to the rise of wages."**

"When commodities varied in relative value, it would be desirable to have the means of ascertaining

* Extract from *Works of David Ricardo*, Chapter I, Section III, p. 20.

which of them fell and which rose in real value, and this could be effected only by comparing them one after another with some invariable standard measure of value, *which should itself be subject to none of the fluctuations to which other commodities are exposed*. Of such a measure it is impossible to be possessed, because there is no commodity which is not itself exposed to the same variations as the things the value of which is to be ascertained; that is, there is none which is not subject to require more or less labour for its production. But if this cause of variation in the value of a medium could be removed—if it were possible that in the production of our money, for instance, the same quantity of labour should at all times be required, still it would not be a perfect standard or invariable measure of value, because, as I have already endeavoured to explain, it would be subject to relative variations from a rise or fall of wages, on account of the different proportions of fixed capital which might be necessary to produce it, and to produce those other commodities whose alteration of value we wished to ascertain. It might be subject to variations, too, from the same cause, on account of the different degrees of durability of the fixed capital employed on it, and the commodities to be compared with it—or the time necessary to bring the one to market, might be longer or shorter than the time necessary to bring the other commodities to market, the variations of

which were to be determined ; all which circumstances disqualify any commodity that can be thought of from being a perfectly accurate measure of value.

" If, for example, we were to fix on gold as a standard, it is evident that it is but a commodity obtained under the same contingencies as every other commodity, and requiring labour and fixed capital to produce it. Like every other commodity, improvements in the saving of labour might be applied to its production, and consequently it might fall in relative value to other things merely on account of the greater facility of producing it.

" If we suppose this cause of variation to be removed, and the same quantity of labour to be always required to obtain the same quantity of gold, still gold would not be a perfect measure of value, by which we could accurately ascertain the variations in all other things, because it would not be produced with precisely the same combinations of fixed and circulating capital as all other things ; nor with fixed capital of the same durability ; nor would it require precisely the same length of time before it could be brought to market. It would be a perfect measure of value for all things produced under the same circumstances precisely as itself, but for no others." *

* Extract from *Works of David Ricardo*, Chapter I, Section VI, pp. 28-9.

"If, then, I may suppose myself to be possessed of a standard so nearly approaching to an invariable one, the advantage is, that I shall be enabled to speak of the variations of other things, without embarrassing myself on every occasion with the consideration of the possible alteration in the value of the medium in which price and value are estimated.

"To facilitate, then, the object of this enquiring, although I fully allow that money made of gold is subject to most of the variations of other things, I shall suppose it to be invariable, and therefore all alterations in price to be occasioned by some alteration in the value of the commodity of which I may be speaking.

"Before I quit this subject, it may be proper to observe that Adam Smith, and all the writers who have followed him, have, without one exception that I know of, maintained that a rise in the price of labour would be uniformly followed by a rise in the price of all commodities. I hope I have succeeded in showing that there are no grounds for such an opinion, and that only those commodities would rise which had less fixed capital employed upon them than the medium in which price was estimated, and that all those which had more would positively fall in price when wages rose. On the contrary, if wages fell, those commodities only would fall which had a less proportion of fixed capital employed on them than the

medium in which price was estimated; all those which had more would positively rise in price." *

"Money being a variable commodity, the rise of money-wages will be frequently occasioned by a fall in the value of money. A rise of wages from this cause will, indeed, be invariably accompanied by a rise in the price of commodities; but in such cases it will be found that labour and all commodities have not varied in regard to each other, and that the variation has been confined to money." †

"Experience, however, shows that neither a State nor a Bank ever have had the unrestricted power of issuing paper money without abusing that power: in all States, therefore, the issue of paper money ought to be under some check and control; and none seems so proper for that purpose as that of subjecting the issuers of paper money to the obligation of paying their notes either in gold coin or bullion." ‡

"It is the cost of production which must ultimately regulate the price of commodities, and not, as has been often said, the proportion between the supply and demand: the proportion between supply and demand may, indeed, for a time, affect the market value of a commodity, until it is supplied in greater or less abundance,

* Extract from *Works of David Ricardo*, Chapter I, Section VI, pp. 29-30.

† *Ibid.*, Section VII, p. 31.

‡ *Ibid.*, Chapter XXVII, p. 215.

according as the demand may have increased or diminished ; but this effect will be only of temporary duration.

"Diminish the cost of production of hats, and their price will ultimately fall to their new natural price, although the demand should be doubled, trebled, or quadrupled. Diminish the cost of subsistence of men, by diminishing the natural price of the food and clothing by which life is sustained, and wages will ultimately fall, notwithstanding that the demand for labourers may very greatly increase.

*"The opinion that the price of commodities depends solely on the proportion of supply to demand, or demand to supply, has become almost an axiom in political economy, and has been the source of much error in that science."**

"We have seen," says M. Say, "that the cost of production determines the lowest price to which things can fall : the price below which they cannot remain for any length of time, because production would then be either entirely stopped or diminished."†

"The same opinion is expressed by the Earl of Lauderdale" as follows:—

'With respect to the variations in value, of which every thing valuable is susceptible, if we could for a moment suppose that any substance possessed

* Extract from *Works of David Ricardo*, Chapter XXX, p. 232.

† Cost of production is therefore the invariable standard of value.

intrinsic and fixed value, so as to render an assumed quantity of it constantly, under all circumstances, of an equal value, then the degree of value of all things, ascertained by such a fixed standard, would vary according to the proportion *betwixt the quantity of them* and the demand for them, and every commodity would, of course, be subject to a variation in its value, from four different circumstances :

1. ' It would be subject to an increase of its value, from a diminution of its quantity. .
2. ' To a diminution of its value, from an augmentation of its quantity.
3. ' It might suffer an augmentation in its value, from the circumstance of an increased demand.
4. ' Its value might be diminished by a failure of demand.

' As it will, however, clearly appear that no commodity can possess fixed and intrinsic value, so as to qualify it for a measure of the value of other commodities, mankind are induced to select, as a practical measure of value, that which appears the least liable to any of these four sources of variations, *which are the sole causes of alteration of value.*'

' When, in common language, therefore, we express the *value* of any commodity, it may vary at one period from what it is at another, in consequence of eight different contingencies :—

1. ' From the four circumstances above stated,

in relation to the commodity of which we mean to express the value.' . . .

*"Commodities which are monopolized either by an individual or by a company vary according to the law which Lord Lauderdale has laid down ; they fall in proportion as the sellers augment their quantity, and rise in proportion to the eagerness of the buyers to purchase them ; their price has no necessary connexion with their natural value : but the prices of commodities which are subject to competition and whose quantity may be increased in any moderate degree, will ultimately depend, not on the state of demand and supply, but on the increased or diminished cost of their production." **

"Strictly speaking, there can be no permanent measure of value. A measure of value should itself be invariable ; but this is not the case with either gold or silver, they being subject to fluctuations as well as other commodities. Experience has indeed taught us that though the variations in the value of gold or silver may be considerable, on a comparison of distant periods, yet, for short spaces of time, their value is tolerably fixed. It is this property, among other excellences, which fits them better than any other commodity for the uses of money. Either gold or silver may, therefore, in the point of view in

* Extract from *Works of David Ricardo*, Chapter XXX, p. 234.

which we are considering them, be called a measure of value." *

"There are two ways in which a country may be benefited by trade—one by the increase of the general rate of profits, which, according to my opinion, can never take place but in consequence of cheap food, which is beneficial only to those who derive a revenue from the employment of their capital, either as farmers, manufacturers, merchants, or capitalists, lending their money at interest—the other by the abundance of commodities, and by a fall in their exchangeable value, in which the whole community participates. In the first case, the revenue of the country is augmented; in the second the same revenue becomes efficient in procuring a greater amount of the necessities and luxuries of life. †

"It is in this latter mode only (excepting when the extension of commerce enables us to obtain food at really cheaper prices) that nations are benefited by

* Extract from *Works of David Ricardo*, Chapter XXX, p. 270.

† It should be noted that Dr. Marshall supports this view of Ricardo's. In "An Introduction to the Study of Prices," page 106, Mr. Walter T. Layton states that Dr. Marshall made the following observation to him:—"Under an ideal system of currency prices should fall at such a rate that receivers of fixed incomes (such as annuitants, civil servants, etc.) should secure a fair proportion of man's increasing hold over his material environment, i.e., the purchasing power of a given income should increase with every improvement in the arts of production, transport, etc."

the extension of commerce, by the division of labour in manufactures, and by the discovery of machinery—they all augment the amount of commodities and contribute very much to the ease and happiness of mankind; but they have no effect on the rate of profits, because they do not augment the produce compared with the cost of production on the land, and it is impossible that all other profits should rise whilst the profits on land are either stationary or retrograde.

" Profits, then, depend on the price, or rather on the value, of food. Everything which gives facility to the production of food, however scarce, or however abundant commodities may become, will raise the rate of profits; whilst on the contrary, everything which shall augment the cost of production without augmenting the quantity of food, will, under every circumstance, lower the general rate of profits. The facilities of obtaining food are beneficial in two ways to the owners of capital: it at the same time raises profits and increases the amount of consumable commodities. The facilities in obtaining all other things only increase the amount of commodities.

" If, then, the power of purchasing cheap food be of such great importance, and if the importation of corn will tend to reduce its price, arguments almost unanswerable respecting the danger of dependence on foreign countries for a portion of our food—for in no other view will the question bear an argument—ought to be brought forward to induce us to restrict

importation, and thereby forcibly to detain capital in an employment which it would otherwise leave for one much more advantageous.

" If the legislature were at once to adopt a decisive policy with regard to the trade in corn—if it were to allow a permanently free trade, and did not, with every variation of price, alternately restrict and encourage importation, we should undoubtedly be a regularly importing country. We should be so in consequence of the superiority of our wealth and population, compared to the fertility of our soil over our neighbours. It is only when a country is comparatively wealthy, when all its fertile land is in a state of high cultivation, that it is obliged to have recourse to its inferior lands to obtain the food necessary for its population ; or when it is originally without the advantages of a fertile soil, that it can become profitable to import corn." *

" All writers on the subject of money have agreed that uniformity in the value of the circulating medium is an object greatly to be desired. Every improvement, therefore, which can promote an approximation to that object, by diminishing the causes of variation, should be adopted. No plan can possibly be devised which will maintain money at an absolutely uniform value, because it will always be subject to those variations to which the

* Extract from *Works of David Ricardo*, pp. 380-2.

commodity itself is subject, which has been fixed upon as the standard." *

"This idea of a currency without a specific standard, was, I believe, first advanced by Sir James Steuart, but no one has yet been able to offer any test by which we could ascertain the uniformity in the value of a money so constituted. Those who supported this opinion did not see that such a currency, instead of being invariable, was subject to the greatest variations—that the only use of a standard is to regulate the quantity, and by the quantity the value of the currency—and that without a standard it would be exposed to all the fluctuations to which the ignorance or the interests of the issuers might subject it.

"It has indeed been said that we might judge of its value by its relation, not to one, but to the mass of commodities. If it should be conceded, which it cannot be, that the issuers of paper money would be willing to regulate the amount of their circulation by such a test, they would have no means of so doing; for when we consider that commodities are continually varying in value, as compared with each other; and that when such variation takes place, it is impossible to ascertain which commodity has increased, which diminished in value, it must be

* Extract from *Works of David Ricardo*, Section I, p. 398.

allowed that such a test would be of no use whatever." *

" Nothing is so easy to ascertain as a variation of price, nothing so difficult as a variation of value ; indeed, without an invariable measure of value, and none such exists, it is impossible to ascertain it with any certainty or precision." †

" While a standard is used, we are subject to only such a variation in the value of money as the *standard* itself is subject to ; but against such variation there is no possible remedy, and late events have proved that, during periods of war, when gold and silver are used for the payment of large armies distant from home, those variations are much more considerable than has been generally allowed. This admission only proves that gold and silver are not so good a standard as they have been hitherto supposed—that they are themselves subject to greater variations than it is desirable a standard should be subject to. They are, however, the best with which we are acquainted. If any other commodity less variable could be found, it might very properly be adopted as the future standard of our money, provided it had all the other qualities which fitted it for that purpose ; but, while these metals are the standard, the currency

* Extract from *Works of David Ricardo*, Section II, p. 400.

† *Ibid.*, p. 401.

should conform in value to them, and whenever it does not, and the market price of bullion is above the Mint price, the currency is depreciated. This proposition is unanswered, and is unanswerable." *

"A well-regulated paper currency is so great an improvement in commerce, that I should greatly regret if prejudice should induce us to return to a system of less utility. The introduction of the precious metals for the purposes of money may with truth be considered as one of the most important steps towards the improvement of commerce and the arts of civilized life; but it is no less true that, with the advancement of knowledge and science, we discover that it would be another improvement to banish them again from the employment to which, during a less enlightened period, they had been so advantageously applied." †

* Extract from *Works of David Ricardo*, Section III, p. 402.

† *Ibid.*, Section IV, p. 404.

X

APHORISMS FROM THE WORK OF FREDERICK LIST

"The causes of wealth are something totally different from wealth itself. A person may possess wealth, i.e. exchangeable value; if, however, he does not possess the power of producing objects of more value than he consumes, he will become poorer. A person may be poor; if he, however, possesses the power of producing a larger amount of valuable articles than he consumes, he becomes rich.

*"The power of producing wealth is therefore infinitely more important than wealth itself; it insures not only the possession and the increase of what has been gained, but also the replacement of what has been lost. This is still more the case with entire nations (who cannot live out of mere rentals) than with private individuals." **

"It was impossible that so clear an intellect as Adam Smith possessed could altogether ignore the difference between wealth and its causes and the overwhelming influence of these causes on the con-

* *The National System of Political Economy*, p. 108.

dition of nations. In the introduction to his work, he says in clear words in effect : ' Labour forms the fund from which every nation derives its wealth, and the increase of wealth depends first on the *productive power* of labour, namely, on the degree of skill, dexterity, and judgment with which the labour of the nation is generally applied, and secondly, on the proportion between the number of those employed productively and the number of those who are not so employed.' From this we see how clearly Smith in general perceived that the condition of nations is principally dependent on the sum of their *productive powers*.

" It does not, however, appear to be the plan of nature that complete sciences should spring already perfected from the brain of individual thinkers. It is evident that Smith was too exclusively possessed by the cosmopolitical idea of the physiocrats, ' universal freedom of trade,' and by his own great discovery, ' the division of labour,' to follow up the idea of the importance to a nation of its *powers of production*. However much science may be indebted to him in respect of the remaining parts of his work, the idea ' division of labour ' seemed to him his most brilliant thought. It was calculated to secure for his book a name, and for himself posthumous fame." *

* *The National System of Political Economy*, p. 109.

" However, we on our part believe ourselves able to prove that just this zeal to put the important discovery '*division of labour*' in an advantageous light, has hindered Adam Smith from following up the idea '*productive power*' (which has been expressed by him in the introduction, and also frequently afterwards, although merely incidentally) and from exhibiting his doctrines in a much more perfect form. By the great value which he attached to his idea '*division of labour*' he has evidently been misled into representing labour itself as the 'fund' of all the wealth of nations, although he himself clearly perceives and also states that the productiveness of labour principally depends on the degree of skill and judgment with which the labour is performed.

" It cannot be doubted that all wealth is obtained by means of mental and bodily exertions (labour), but yet from that circumstance no reason is indicated from which useful conclusions may be drawn; for history teaches that whole nations have, in spite of the exertions and of the thrift of their citizens, fallen into poverty and misery.

" Whoever desires to know and investigate how one nation from a state of poverty and barbarism has attained to one of wealth and prosperity, and how another has fallen from a condition of wealth and well-being into one of poverty and misery, has always, after receiving the information that labour is the cause of wealth and idleness the cause of

poverty (a remark which King Solomon made long before Adam Smith), to put the further question, what are the causes of labour, and what the causes of idleness? " *

" If Adam Smith had followed up the idea 'productive power,' without allowing his mind to be dominated by the idea of 'value,' 'exchangeable value,' he would have been led to perceive that an independent theory of the 'productive power' must be considered by the side of a 'theory of values' in order to explain the economical phenomena. But he thus fell into the mistake of explaining mental forces from material circumstances and conditions, and thereby laid the foundation for all the absurdities and contradictions from which his school (as we propose to prove) suffers up to the present day, and to which alone it must be attributed that the doctrines of political economy are those which are the least accessible to the most intelligent minds. That Smith's school teaches nothing else than the theory of values, is not only seen from the fact that it bases its doctrine everywhere on the conception of 'value of exchange,' but also from the definition which it gives of its doctrine. It is (says J. B. Say) that science which teaches how riches, or exchangeable values, are produced, distributed, and consumed. This is undoubtedly not the science which teaches how

* *The National System of Political Economy*, p. 110.

the productive powers are awakened and developed, and how they become depressed and destroyed. McCulloch calls it explicitly 'the science of values,' and recent English writers 'the science of exchange.' " *

" If we consider merely bodily labour as the cause of wealth, how can we then explain why modern nations are incomparably richer, more populous, more powerful, and prosperous than the nations of ancient times? The ancient nations employed (in proportion to the whole population) infinitely more hands, the work was much harder, each individual possessed much more land, and yet the masses were much worse fed and clothed than is the case in modern nations. In order to explain these phenomena, we must refer to the progress which has been made in the course of the last thousand years in sciences and arts, domestic and public regulations, cultivation of the mind and capabilities of production. The present state of the nations is the result of the accumulation of all discoveries, inventions, improvements, perfections, and exertions of all generations which have lived before us; they form the *mental capital of the present human race*, and every separate nation is productive only in the proportion in which it has known how to appropriate these attainments of former generations and to increase them by its own acquirements, in which

* *The National System of Political Economy*, pp. 111-12.

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the natural capabilities of its territory, its extent and geographical position, its population and political power, have been able to develop as completely and symmetrically as possible all sources of wealth within its boundaries, and to extend its moral, intellectual, commercial, and political influence over less advanced nations and especially over the affairs of the world." *

"We now see into what extraordinary mistakes and contradictions the popular school has fallen in making material wealth or value of exchange the sole object of its investigations, and by regarding mere bodily labour as the sole productive power." †

"The errors and contradictions of the prevailing school to which we have drawn attention, can be easily corrected from the standpoint of the theory of the productive powers. Certainly those who fatten pigs or prepare pills are productive, but the instructors of youths and of adults, virtuosos, musicians, physicians, judges, and administrators, are productive in a much higher degree. The former produce values of exchange, and the latter productive powers, some by enabling the future generation to become producers, others by furthering the morality and religious character of the present generation, a

* *The National System of Political Economy*, pp. 113-14.

† *Ibid.*, p. 115.

third by ennobling and raising the powers of the human mind, a fourth by preserving the productive powers of his patients, a fifth by rendering human rights and justice secure, a sixth by constituting and protecting public security, a seventh by his art and by the enjoyment which it occasions fitting men the better to produce values of exchange. In the doctrine of mere values, these *producers of the productive powers* can of course only be taken into consideration so far as their services are rewarded by values of exchange; and this manner of regarding their services may in some instances have its practical use, as e.g. in the doctrine of public taxes, inasmuch as these have to be satisfied by values of exchange. But whenever our consideration is given to the nation (as a whole and in its international relations) it is utterly insufficient, and leads to a series of narrow-minded and false views." *

"The prosperity of a nation is not, as Say believes, greater in the proportion in which it has amassed more wealth (i.e. values of exchange), but in the proportion in which it has more developed its powers of production. Although laws and public institutions do not produce immediate values, they nevertheless produce productive powers, and Say is mistaken if he maintains that nations have been enabled to become wealthy under all forms of government, and

* *The National System of Political Economy*, pp. 116-17.

that by means of laws no wealth can be created. *The foreign trade of a nation must not be estimated in the way in which individual merchants judge it, solely and only according to the theory of values (i.e. by regarding merely the gain at any particular moment of some material advantage); the nation is bound to keep steadily in view all these conditions on which its present and future existence, prosperity and power depend.*" *

" Since the school of physiocrats did not recognize the difference between productive power and mere values of exchange, and did not investigate the former independently of the latter, but subordinated it to the theory of values of exchange, it was impossible for that school to arrive at the perception how greatly the nature of the agricultural productive power differs from the nature of the manufacturing productive power. It does not discern that through the development of a manufacturing industry in an agricultural nation a mass of mental and bodily powers, of natural powers and natural resources, and of instrumental powers too (which latter the prevailing school terms 'capital'), is brought to bear, and brought into use, which had not previously been active, and would never have come into activity but for the formation and development of an internal manufacturing power; it imagines that by the estab-

* *The National System of Political Economy*, p. 117.

lishment of manufacturing industry these forces must be taken away from agriculture, and transferred to manufacture, whereas the latter to a great extent is a perfectly new and additional power, which, very far indeed from increasing at the expense of the agricultural interest, is often the means of helping that interest to attain a higher degree of prosperity and development." *

" The essential character of the natural law from which the popular school explains such important phenomena in social economy, is evidently not merely *a division of labour*, but *a division of different commercial operations between several individuals*, and at the same time *a confederation or union of various energies, intelligences, and powers on behalf of a common production*. The cause of the productiveness of these operations is not merely that *division*, but essentially this *union*. Adam Smith well perceives this himself when he states, ' The necessities of life of the lowest members of society are a product of *joint labour* and of the co-operation of a number of individuals.' What a pity that he did not follow out this idea (which he so clearly expresses) of *united labour*." †

" The popular school, because it has regarded the division of operation alone as the essence of this

* *The National System of Political Economy*, p. 120.

† *Ibid.*, pp. 121-22.

natural law, has committed the error of applying it merely to the separate manufactory or farm ; it has not perceived that the same law extends its action especially over the *whole manufacturing and agricultural power, over the whole economy of the nation.*"*

" Smith affirms that the division of labour is less applicable to agriculture than to manufactures. Smith had in view only the separate manufactory and the separate farm. He has, however, neglected to extend his principle over whole districts and provinces. Nowhere has the division of commercial operations and the confederation of the productive powers greater influence than where every district and every province is in a position to devote itself exclusively, or at least chiefly, to those branches of agricultural production for which they are mostly fitted by nature." †

" This division of commercial operations, this confederation of the productive forces occupied in agriculture, can only take place in a country which has attained the greatest development of all branches of manufacturing industry ; for in such a country only can a great demand for the greatest variety of products exist, or the demand for the surplus of agricultural productions be so certain and considerable that the

* *The National System of Political Economy*, p. 122.

† *Ibid.*, p. 123.

producer can feel certain of disposing of any quantity of his surplus produce during this or at least during next year at suitable prices." *

"We may notice how the augmentation of the powers of production in consequence of the separation of occupations and the co-operation of the powers of individuals begins in the separate manufactory and extends to the united nation. The manufactory prospers so much the more in proportion as the commercial operations are divided, the more closely the workmen are united, and the more the co-operation of each person is insured for the whole. The productive powers of every separate manufactory are also increased in proportion as the whole manufacturing power of the country is developed in all its branches, and the more intimately it is united with all other branches of industry." †

"That nation will therefore possess most productive power, and will consequently be the richest, which has cultivated manufacturing industry in all branches within its territory to the highest perfection, and whose territory and agricultural production is large enough to supply its manufacturing population with the largest part of the necessaries of life and raw materials which they require." ‡

* *The National System of Political Economy*, p. 123.

† *Ibid.*, p. 124.

‡ *Ibid.*, p. 124.

*"If this state of things sets in at the proper time, agricultural and industrial productive power will increase reciprocally, and indeed ad infinitum. The demand for agricultural products on the part of the industrial population will be so great, that no greater number of labourers will be diverted to agriculture, nor any greater division of the existing land be made, than is necessary to obtain the greatest possible surplus produce from it. In proportion to this surplus produce the population occupied in agriculture will be enabled to consume the products of the workmen employed in manufacturing." **

"The whole social state of a nation will be chiefly determined by the principle of the variety and division of occupations and the co-operation of its productive powers. What the pin is in the pin manufactory, that the national well-being is to the large society which we term 'the nation.' The most important division of occupations in the nation is that between the mental and material ones. Both are mutually dependent on one another. The more the mental producers succeed in promoting morality, religion, enlightenment, increase of knowledge, extension of liberty and of perfection of political institutions—security of persons and property within the State, and the independence and power of the nation externally—so much greater will be the production

* *The National System of Political Economy*, p. 126.

of material wealth. On the other hand, the more goods that the material producers produce, the more will *mental production be capable of being promoted.*" *

" *The most important division of occupations, and the most important co-operation of productive powers in material production, is that of agriculture and manufacture. Both depend mutually upon one another, as we have shown.*" †

" *A nation which only carries on agriculture, is an individual who in his material production lacks one arm. Commerce is merely the medium of exchange between the agricultural and the manufacturing power, and between their separate branches. A nation which exchanges agricultural products for foreign manufactured goods is an individual with one arm, which is supported by a foreign arm. This support may be useful to it, but not so useful as if it possessed two arms itself, and this because its activity is dependent on the caprice of the foreigner. In possession of a manufacturing power of its own, it can produce as much provisions and raw materials as the home manufacturers can consume; but if dependent upon foreign manufactures, it can merely produce as much surplus as foreign nations do not*

* *The National System of Political Economy*, p. 129.

† *Ibid.*, p. 129.

care to produce for themselves, and which they are obliged to buy from another country." *

" Both *international and national division of labour* are chiefly determined by climate and by Nature herself. We cannot produce in every country tea as in China, spices as in Java, cotton as in Louisiana, or corn, wool, fruit, and manufactured goods as in the countries of the temperate zone. It would be folly for a nation to attempt to supply itself by means of national division of labour (*i.e.* by home production) with articles for the production of which it is not favoured by nature, and which it can procure better and cheaper by means of international division of labour (*i.e.* through foreign commerce). And just as much does it betoken a want of national intelligence or national industry if a nation does not employ all the natural powers which it possesses in order to satisfy its own internal wants, and then by means of the surplus of its own productions to purchase those necessary articles which nature has forbidden it to produce on its own territory." †

"The school cannot deny that the internal market of a nation is ten times more important to it than its external one, even where the latter is in the most flourishing condition; but it has omitted to draw from

* *The National System of Political Economy*, p. 130.

† *Ibid.*, p. 131.

this the conclusion, which is very obvious, that it is ten times more important to cultivate and secure the home market, than to seek for wealth abroad, and that only in those nations which have developed their internal industry to a high degree can foreign commerce attain importance." *

"Manufactures are at once the offspring, and at the same time the supporters and the nurses, of science and the arts. We may observe how little the condition of raw agriculture puts sciences and arts into requisition, how little of either is necessary to prepare the rude implements which it employs. It is true that agriculture at first had, by yielding rents of land, made it possible for men to devote themselves to science and art ; but without manufactures they have always remained private treasures, and have only extended their beneficial effects in a very slight degree to the masses. In the manufacturing State the industry of the masses is enlightened by science, and the sciences and arts are supported by the industry of the masses. There scarcely exists a manufacturing business which has not relations to physics, mechanics, chemistry, mathematics, or to the art of design, etc. No progress, no new discoveries and inventions, can be made in these sciences by which a hundred industries and processes could not be improved or altered. In

* *The National System of Political Economy*, p. 150.

the manufacturing State, therefore, sciences and arts must necessarily become popular. The necessity for education and instruction, through writings and lectures by a number of persons who have to bring into practice the results of scientific investigations, induces men of special talents to devote themselves to instruction and authorship. The competition of such talents, owing to the large demand for their efforts, creates both a division and co-operation of scientific activity, which has a most beneficial influence not merely on the further progress of science itself, but also on the further perfection of the arts and of industries. The effects of these improvements are soon afterwards extended even to agriculture. Nowhere can more perfect agricultural machines and implements be found, nowhere is agriculture carried on with so much intelligence, as in countries where industry flourishes. Under the influence of manufactures, agriculture itself is raised to a skilled industry, an art, a science." *

"The commercial conditions between England and North America which we have above explained, therefore teach :

(5) "That the fluctuations in the money market under all circumstances act on the economy of the nations in a highly disadvantageous manner, especi-

* *The National System of Political Economy*, pp. 161-62.

ally in countries where an extensive bank and paper-money system is based on the possession of certain quantities of the precious metals.

(6) "That the fluctuations in the money market and the crises which result therefrom can only be prevented, and that a solid banking system can only be founded and maintained, if the imports of the country are placed on a footing of equality to the exports.

(7) "*That this equality can less easily be maintained in proportion as foreign manufactured goods can successfully compete in the home manufacturing markets, and in proportion as the exportation of native agricultural products is limited by foreign commercial restrictions; finally, that this equality can less easily be disturbed in proportion as the nation is independent of foreign nations for its supply of manufactured goods, and for the disposal of its own produce.*" *

"A nation obtains the power of disposition of the amount of ready money which is always required for its internal trade, mainly through the possession or the production of those goods and values whose facility of exchange approaches most nearly to that of the precious metals." † ‡

"The diversity of this property of the facility of

* *The National System of Political Economy*, pp. 223-26.

† *Ibid.*, p. 228.

‡ See reference p. 67.

exchange in respect to the various articles of commerce and of property, has been as little taken into consideration by the popular school of economists in judging of international commerce, as the power of disposition of the precious metals.

“How is it that a decidedly and continuously disadvantageous balance of trade has always and without exception been accompanied in those countries to whose detriment it existed (with the exception of colonies) by internal commercial crises, revolutions in prices, financial difficulties, and general bankruptcies, both in the public institutions of credit, and among the individual merchants, manufacturers, and agriculturists?”

“How is it that in those nations which possessed a balance of trade decidedly in their favour, the opposite appearances have always been observed, and that commercial crises in the countries with which such nations were connected commercially, have only affected such nations detrimentally for periods which passed away very quickly?”*

On the theory of exchangeable values Frederick List comments as follows:—

“The mistake has been simply, that this system at bottom is nothing else than a system of the *private economy of all the individual persons in a country, or of the individuals of the whole human race, as that*

* *The National System of Political Economy*, p. 234.

economy would develop and shape itself, under a state of things in which there were no distinct nations, nationalities, or national interests—no distinctive political constitutions or degrees of civilization—no wars or national animosities ; that it is nothing more than a theory of values ; a mere shopkeeper's or individual merchant's theory—not a scientific doctrine, showing how the productive powers of an entire nation can be called into existence, increased, maintained, and preserved—for the special benefit of its civilization, welfare, might, continuance, and independence." *

" This system regards everything from the shopkeeper's point of view. The value of anything is wealth, according to it, so its sole object is to gain values. The establishment of powers of production, it leaves to chance, to nature, or to the providence of God (whichever you please), only the State must have nothing at all to do with it, nor must politics venture to meddle with the business of accumulating exchangeable values. It is resolved to buy wherever it can find the cheapest articles—that the home manufactories are ruined by their importation, matters not to it. If foreign nations give a bounty on the export of their manufactured goods, so much the better ; it can buy them so much the cheaper. In its view no class is productive save

* *The National System of Political Economy*, p. 279.

those who actually produce things valuable in exchange. It well recognizes how the division of labour promotes the success of a business in detail, but it has no perception of the effect of the division of labour as affecting a whole nation. It knows that only by individual economy can it increase its capital, and that only in proportion to the increase in its capital can it extend its individual trades ; but it sets no value on the increase of the productive power, which results from the establishment of native manufactories, or on the foreign trade and national power which arise out of that increase. What may become of the entire nation in the future, is to it a matter of perfect indifference, so long as private individuals can gain wealth. It takes notice merely of the rent yielded by land, but pays no regard to the value of landed property ; it does not perceive that the greatest part of the wealth of a nation consists in the value of its land and its fixed property." *

" At present the Theory of Exchangeable Values has so completely lost its influence, that it is almost exclusively occupied with inquiries into the nature of Rent, and that Ricardo in his *Principles of Political Economy* could write, 'The chief object of political economy is to determine the laws by which the produce of the soil ought to be shared between

* *The National System of Political Economy*, pp. 279-80.

the landowner, the farmer, and the labourer.' While some persons are firmly convinced that this science is complete and that nothing essential can further be added to it, those, on the other hand, who read these writings with philosophical or practical insight, maintain, that as yet there is no political economy at all, that that science has yet to be constructed ; that until it is so, what goes by its name is merely an astrology, but that it is both possible and desirable out of it to produce an astronomy." *

* *The National System of Political Economy*, p. 288.

XI

THE FINAL CASE AGAINST THE FREE TRADE GOLD STANDARD SYSTEM

It has been said of Ricardo by orthodox economists that he was "in no high sense an educated man" and that "he was the most incorrect writer who ever attained social eminence." But however that may be, he was a man of practical common sense. Those who criticize him most say that our present industrial troubles may very well be left to the "orthodox economists" to solve; but they have said this for generations past, and notwithstanding all the majestic and pontifical phraseology which they have introduced into the science they have not brought the world nearer to a solution. Ordinary business men must therefore be excused if they take a hand at solving the problem. And we venture to suggest that the world owes more to such practical men of affairs as Ricardo, List, and Say, than it does to their critics.

Eloquence may seek to cover a lack of intelligence or original thought—but is no substitute

for them. Adam Smith expresses our view admirably in the following :—

“ Man . . . must not expose himself to the charge which Avidius Cassius is said to have brought, perhaps, unjustly, that while he employed himself in philosophical speculations, and contemplated the prosperity of the Universe, he neglected that of the Roman Empire.”

We may retort by asking the orthodox school :— What is free trade ? Who founded it, or where did it originate ? Has it merely happened, or did some great brain think it out ?

We shall endeavour to prove that the whole Free Trade Gold Standard system is an empirical one and that it has no scientific basis : that it has been allowed to drift into position without design on the authority of merchants and bankers, owing to the orthodox school having wrongly interpreted the philosophies of Adam Smith and his successors.

In the aphorisms quoted, there is a clear indication that the greatest economists of the past gave no support to the free trade theories as they exist to-day. On the contrary, it will be found that the Free Trade Gold Standard System originated through a misconception of the term that “ exports shall pay for imports,” and because it suited the merchants.

The fight against the precious metals as the master

of production has continued for close upon two centuries. It began with the Physiocratic School and Adam Smith, and since then many economists have written books, essays, and tracts on the subject. In several countries Money Reform Associations have now been formed, but Great Britain has the most difficult task of all to deal with, for it is here that the "Free Trade Gold Standard System" first originated, and reformers will have a heavy and difficult task in trying to get rid of this dual system.

The underlying principles of the Free Trade Gold Standard System are as follows :—

(1) It is held that an expansion of credit can only take place if there be an increase in the Gold Reserves.

(2) That an increase of National wealth and prosperity depends on our success in accumulating gold. That gold is in fact the basis of all wealth. (Free traders may attempt to dispute this fact, but they cannot logically do so.)

(3) That an accumulation of the precious metal is best obtained through an exchange of commodities for gold—hence the origin of the theory of exchangeable value. If it is more profitable for a merchant to import gold instead of commodities, he will do so. If it is more profitable for him to export gold instead of manufactures, he will do so.

(4) Locke aptly epitomizes the free trade gold standard view in the following :—" In a country not furnished with mines, there are but two ways of growing rich, either conquest or commerce." He was also of the opinion that it was only from an increase in the quantity of gold and silver that interest rates could be lowered. (The modern interpretation of this view is to be found in *The Times* quotation on page 7 herein.)

(5) That as the gold reserves increase, credit expands, and prices rise; hence inflation and deflation.

It has been held by the orthodox school that Adam Smith was the founder of free trade, but, as we have on more than one occasion stated, this is an erroneous assumption. The expression "free trade" is not to be found within any of the works of Adam Smith. We do find that he advocated "freedom of trade" and that his main objective was to reform the "mercantile system," which embodied the vicious principles of prohibitions and monopolies in favour of certain trading guilds. These prohibitions and monopolies did not operate for the good of the people as a whole, but were generally designed in the interests of a privileged class. Here again free traders, who are not masters of finance, have drawn false inferences. They object to any prohibitive regulation that may be designed to improve

industry and promote the greatest amount of employment because they fear a return to "mercantilism." Some infer that the physiocratic school may have founded the "free trade" theory because one of its early members, Jean V. Gournay, originated the phrase "*Laissez-faire, laissez-passer*." The intent of this phrase, however, has not been properly understood, for this school held that national wealth did not consist in gold and silver, but in useful things (wealth products), foremost among which were the products of agriculture. For instance, Bois Guillebert speaks of gold and silver as being the "*Argent criminel*" which from being the slaves of trade had become its tyrants. This is probably the origin of the modern phrase "money is the master of production and not its servant."

The physiocratic school laid special emphasis on the claims of agriculture. Vauban held that labour was the foundation of all wealth, and that agriculture was the most important species of labour; that the most essential condition of successful industry was freedom; and that all unnecessary or excessive restrictions on manufactures and commerce should be swept away. He protested in particular against the inequalities of taxation, and the exemptions and privileges enjoyed in his day in France by the higher ranks. But no regulations can be conceived which would impose greater restrictions on production, than those which gold imposes.

Sir Thomas Munn, Hutcheson, and the Physiocratic School seem to have been the sources from which Adam Smith drew his inspiration. But if they teach us anything it is this: that they were all advocating a sound healthy national system of trade, free from private monopoly and privilege. Every man was to be free to trade in his own way *subject* to the good of the greatest number. But the greatest freedom is that enjoyed under regulation free from gold restrictions.

Montesquieu aptly sums up the position in the following :—

“ It is in free countries that men of trade encounter innumerable obstacles ; they are never less hampered than in countries not free,” since a “ nation in a state of servitude labours rather to preserve than to acquire.”

There were many germs of truth in the theories developed by the physiocratic school and by earlier and subsequent writers. They held that the wealth of the community consisted in the excess of the mass of agricultural products (with metals) over their cost of production, and that “ Commerce did nothing more than transfer the wealth already existing from one hand to another ; *what the trading classes gained thereby was acquired at the cost of the nation, and it was desirable that the amount should be as small as possible.*” And how true this is of free

trade to-day! But the mistake the Physiocrats made was in assuming that the manufacturers and merchants were both parasites, and that they fed on the surplus created by the agriculturist. The manufacturers are no doubt fed on the surplus, but the merchants live on it. For it is obvious that no value can be given to any commodity unless it can be exchanged for something useful, and if they had conceived that the maintenance of a balance as between industry and agriculture was indispensable, their school would have prospered. But this they failed to see, and also that if all true wealth came from the soil the maintenance of a gold and silver coinage was illogical; for if gold and silver were not wealth, they must, as mediums of exchange, limit the distribution of all true wealth.

Adam Smith correctly interpreted the economic position (his work in our view is the greatest of all, notwithstanding criticism to the contrary), but even he, although condemning gold and silver, had to continue to use them as a measure of value. But as we have said previously, the science of banking was not in his time so far advanced as it is to-day and therefore he could not design measures such as would now be possible. Furthermore, in his days gold and silver were National Legal Tender Money, and the currency was really a form of Bi-metalism, if not actually so. There was no such thing as a gold standard, as we understand it to-day. Due

regard should be given to this aspect of the question when studying his writings. For instance, in discussing the quantity theory of money, he writes as follows :—" Any increase in the quantity of silver, while that of the commodities circulated by means of it remained the same, could have no other effect than to diminish the value of that metal." As we show later, it was not until 1874 that the continental nations of Europe, and the United States, began to demonetize silver and monetize gold. So that if one of the main props is withdrawn upon which Smith constructed all his theory, the interpretations given to the principles enunciated by him and by his successors should be conformed to this fact. In the next chapter we shall discuss the general effect produced by the demonetization of silver in 1871-5.

It should also be noted that even although gold and silver (Bi-metalism) were the basis of European monetary systems, J. B. Say,—who bases his theories mainly on silver * and its available supplies, and not on gold,—was compelled to issue the following warning :—

" Thus the necessity, and consequently the demand, for metal money never advances in equal ratio with the progressive multiplication of other

* Say writes, Vol. II, p. 65: " By this expedient, the use of metal money, and, consequently, that of *silver* for the purposes of money, is considerably diminished."

products ; and it may be truly said, that the richer a nation is, the smaller is the amount of its coin, in comparison with other nations.

" If the nations of the world go on increasing their wealth, as most of them certainly have done for the last three centuries, their want of the precious metals will progressively advance, as well in consequence of the gradual wear, which will be greater in proportion to their increasing use, as of the multiplication and increased aggregate value of other commodities, which will create a larger demand for the purposes of transfer and circulation. If the produce of the mines do not keep pace with the increasing demand, the precious metals will rise in value, and less of them be given in exchange for other products in general."

Two essential facts must also be borne in mind when discussing the theories of Adam Smith: (1) that it was not until after the introduction of the Bank Charter Act in 1844 that the cheque system was developed as a substitute for money transfers ; and (2) that it was not until 1875 that the London money market became a free gold market. The latter factor alone changed the whole character of the science of foreign exchange. It should be realized that merchants now import for gold, and settle their balances in gold and not, as commonly believed, by an export of merchandise. If exports balance imports at all, it is a mere fortuitous circumstance.

This now leads us to the kernel of Adam Smith's conception which is contained in the following quotations :—

" Though a great number of people should, by thus restoring the freedom of trade, be thrown out of their ordinary employment . . . it would by no means follow that they would thereby be deprived of employment. The stock which employed them in a particular manufacture before will still remain in the country to employ an equal number of people in some other way. The capital of the country remaining the same, the demand for labour will be the same, though it may be exerted in different places and for different occupations."

" When the produce of any particular branch of industry exceeds what the demand of the country requires, the surplus must be sent abroad, and exchanged for something for which there is a demand at home. Without such exportation, a part of the productive power of the country must cease, and the value of its annual produce diminish. The land and labour of Great Britain produce generally more corn, woollens, and hard ware, than the demand of the home-market requires. The surplus part of them, therefore, must be sent abroad, and exchanged for something for which there is a demand at home. *It is only by means of such exportation, that this surplus can acquire a value sufficient to compensate the labour and expense of producing it. The neighbourhood of the sea coast, and the banks of all navigable rivers are advantageous situations for industry, only*

because they facilitate the exportation and exchange of such surplus produce for something else which is more in demand there.

"When the foreign goods which are thus produced with the surplus produce of domestic industry, exceed the demand of the home-market, the surplus part of them must be sent abroad again, and exchanged for something more in demand at home."*

"When the capital stock of any country is increased to such a degree, that it cannot be all employed in supplying the consumption, and supporting the productive labour of that particular country, the surplus part of it naturally disgorge itself into the carrying trade, and is employed in performing the same offices to other countries. *The carrying trade is the natural effect and symptom of great national wealth; but it does not seem to be the natural cause of it. Those statesmen who have been disposed to favour it with particular encouragements, seem to have mistaken the effect and symptom for the cause.*"

"The extent of the home-trade and of the capital which can be employed in it, is necessarily limited by the value of the surplus produce of all those distant places within the country which have occasion to exchange their respective productions with one another. That of the foreign trade of consumption, by the value of the surplus produce of the whole country, and of what can be purchased with it. That of the carrying trade, by the value of the surplus produce of all the different countries in the

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chap. V, p. 352.

world. Its possible extent, therefore, is in a manner infinite in comparison of that of the other two, and is capable of absorbing the greatest capitals." *

"That the mercantile system has not been very favourable to the revenue of the great body of the people, to the annual produce of the land and labour of country, I have endeavoured to show in the fourth book of this inquiry. . . . In consequence of that system, the importation of several sorts of goods has been prohibited altogether. . . . *In both cases it has entirely annihilated the revenue of customs which might have been levied upon such importation.*" †

In these aphorisms Smith clearly indicates that after the balance has been maintained as between home agricultural products and manufactures "the surplus must be exported and exchanged for something for which there is a demand at home"; and he clearly meant "and which cannot be produced at home at a profit." This confirms our theory that nations should study each other's wants more closely and concentrate upon balancing their "exportable surpluses," in which alone freedom of trade should be conducted. Only in this way will the diversity of employments be brought about, and the present excessive competition in identical products cease. It was never intended by Smith

* Extract from *The Wealth of Nations* (Adam Smith), Vol. I, Book II, Chap. V, p. 353.

† *Ibid.*, Vol. II, Book V, Chap. II, p. 365.

that the total productions of a nation should be subject to interference by imports, and that its industry and workers should be impoverished thereby.

If we interpret Adam Smith correctly, what he really meant to indicate was, that we should concentrate on the manufacture of those commodities which our potential productive power was best suited to produce ; and that we should leave to other countries the production of those commodities which their potential productive power could best produce. But the implication which lies underneath this principle is that our full potential productive power should in any event be kept fully employed in balancing, as far as possible, the production of agricultural produce with such manufactures as could be produced at a profit ; and that should our production of agricultural produce fall short of what may be required, it should be left to manufacturing industry to create an exportable surplus in those manufactures in which it could create an excess, which surplus could be exported to pay for the imports we should most require to balance our trade. From this it will follow that he intended a system of freedom of trade in exportable surpluses, that is,—if one Nation was best qualified to produce manufactures then it should concentrate on those particular ones in which an exportable surplus could be created with the greatest facility and profit ;

and that the imports accepted by way of exchange should, in any event, bear their fair proportion of the taxation of the country in which they were to be consumed.

Then again, it would be found that certain countries could more profitably employ their productive power in the production of agricultural products, and that they should concentrate on creating an exportable surplus in these, accepting in exchange imports of manufactures, which should likewise bear their proportion of the burden of taxation of the country in which they were to be consumed. Such an international arrangement would be ideal, since it would promote the division of employment,—that is, the division and sub-division of labour as conceived by Adam Smith—and prevent the present intensification of identity of employments, which tend to promote ill-feeling between nations (and as past experience has shown) frequently leads to war.

Such a conception does not prevent each Nation adopting the greatest diversity of employment within its own potential productive power, in order to maintain a balance between its own agricultural and manufacturing industries. If we have thus correctly interpreted Adam Smith's conception, then it should tend to promote a solution of the economic difficulties now facing the Nations. This interpretation agrees with that

part of the Resolutions of the World Economic Conference, Geneva, 1927, which says:—"Care should be taken to assist in the maintenance of an equitable balance between industry and agriculture, and not to stifle one to the advantage of the other."

Smith clearly perceived that the total capital of the nation (this we take to mean "potential productive power") should above all be fully employed in providing work for labour. Imports were on no account to displace the nation's capital and labour. But the mercantile restrictions and regulations were to be removed so that our surplus of manufactures could be freely exported in order to bring home all other forms of wealth and luxury which the home industry was incapable of producing at a profit. In so far as Great Britain is concerned, true "freedom of trade" is thus best promoted by facilitating the export of surplus manufactures to pay for the essential imports of natural materials and food. In this way the principle would be maintained of "exports paying for imports." And so long as foreign imports did not interfere with the internal balance of trade, Adam Smith (and even the modern "safeguarders") would not object to this "freedom of trade." But Smith did not anticipate (nor did the Manchester school) that the world would to-day be trading for gold margins instead of maintaining the salutary principle of

trading "exports for imports" with a currency system constructed on a wider basis than gold.

What views then may we correctly attribute to Ricardo as regards free trade? If we take a line through Jean Baptiste Say we may arrive at a conclusion. Of this author Ricardo wrote as follows :—

"He was the first, or among the first, of Continental writers who justly appreciated and applied the principles of Smith, and has done more than all other Continental writers taken together to recommend that enlightened and beneficial system to the nations of Europe."

And of Ricardo, J. B. Say wrote as follows :—

"Ricardo, whom I look upon as the individual in Europe the best acquainted with the subject of money, both in theory and in practice, has shown, in his *Proposals for an economical and secure Currency*, that, when the good government of the state may be safely reckoned upon, paper may be substituted for the whole of a metallic money; and a material possessed of no intrinsic value, by skilful management, be made to supplant a dear and cumbrous one, whose metallic properties are never called into play by the functions of money."

The following principles as enunciated by Say will be of intense interest at the present time as they are remarkably prophetic. They certainly

throw a great deal of light on the purpose and intent of the philosophies of Adam Smith and his school, to which Ricardo subscribed :—

*“The internal commerce of a country, though, from its minute ramification, it is less obvious and striking, besides being the most considerable, is likewise the most advantageous. For both the remittances and returns of this commerce are necessarily home products. It sets in motion a double production, and the profits of it are not participated with foreigners. For this reason, roads, canals, bridges, the abolition of internal duties, tolls, duties on transit, which are in effect tolls, every measure, in short, which promotes internal circulation, is favourable to national wealth.”**

“Commerce in general, and maritime commerce in particular, facilitates the interchange of products, even with the most remote countries, and thus renders it practicable to import articles of subsistence, in return for several other kinds of produce ; but too great a dependence on this resource, leaves the nation at the mercy of every natural or political occurrence, which may happen to intercept or derange the intercourse with foreign countries. This intercourse must then be preserved at all events, no matter whether by force or fraud ; competition must be got rid of by every means, however unjustifiable ; a separate province, or weak ally, perhaps, is obliged to purchase the national products, under restrictions equally galling, as the exaction of actual tribute ;

* *A Treatise on Political Economy*, Vol. I, pp. 96, 97.

and a commercial monopoly enforced, even at the hazard of a war ; all which evils make the state of the nation extremely precarious indeed.

" The produce of England, in articles of human subsistence, had undoubtedly increased largely towards the end of the eighteenth century ; but its produce in articles of apparel and household furniture had probably increased still more rapidly. The consequence has been, that immensity of production, which enables her to multiply her population beyond what the produce of her soil can support, and to bear up under the pressure of public burthens, to which there is no parallel nor even approximation.

" But England has suffered severely, whenever foreign markets have been shut against her produce ; and she has sometimes been obliged to resort to violent means to preserve her external intercourse. She would act wisely, perhaps, in discontinuing those encouragements, that impel fresh capital into the channels of manufacture and external commerce, and directing it rather towards that of agricultural industry. It is probable that, in that case, several districts, which have not yet received the utmost cultivation of which they are susceptible, particularly many parts of Scotland and Ireland, would raise agricultural produce enough to purchase most part, if not the whole, of the surplus product of her manufactures and commerce beyond her present consumption.

" Great Britain would therefore create for herself a domestic consumption which is always the surest and the most advantageous. . . . But, after all, if her manufactured should still be disproportioned

to her agricultural produce, what is there to prevent her from adopting a system of judicious colonization, and thus creating for herself fresh markets, for the produce of her domestic industry in every part of the globe, whence she might derive, in return, a supply of food for her superfluous population? " *

" National population is uniformly proportionate to the quantum of National production."

" Strictly speaking there is no act of government but what has some influence upon production. . . . The grand mischiefs of authoritative interference proceed, not from occasional exceptions to established maxims, but the false maxims built upon them. It is then that mischief is done by wholesale, and evil pursued upon system ; for it is well to be aware, that no set of men are more bigoted to system, than those who boast they go upon none." †

" I can hardly suppose any Government will be bold enough to object, that it is indifferent about the profit which might be derived from a more advantageous production, because it would fall to the lot of individuals." ‡

" Indeed, it is impossible to find any reasonable ground for exempting the production of values by the channel of external commerce from the same pressure of taxation, that weighs upon the production effected in those of agriculture and manufacture. Taxation is, doubtless, an evil, and one which should be reduced to the lowest possible

* *A Treatise on Political Economy* (J. B. Say), Vol. II, pp. 206-8.

† *Ibid.*, Vol. I, pp. 188-9.

‡ *Ibid.*, Vol. I, p. 194.

degree ; but, when once a given amount of taxation is admitted to be necessary, it is but common justice to lay it equally on all three branches of industry.* The error I wish to expose to reprobation is, the notion, that taxes of this kind are favourable to the public welfare, except by the good use that is made of its proceeds." †

It will thus be seen that the misconceptions that have arisen with regard to the principles enunciated by Smith, Ricardo, and Say, are, in the main, due to a lack of intimate knowledge as to the restrictive influence of gold money and credit on production, and as to the preference which they concede in favour of commerce and the science of exchangeable values. From the plural "precious metals," we have fallen to the singular "precious metal," and it is thus evident that we cannot begin to interpret Smith, Ricardo and Say, as they intended we should do, until the basis of money has been extended to a wider one than that of gold. The warnings issued by these economists with regard to placing too much reliance on commerce would also seem to have been ignored. We have not felt justified in reviewing the works of the later economists for this reason, and for further reasons that will appear in the next and final chapter.

* i.e., Agriculture, Industry and Commerce.

† *A Treatise on Political Economy*, Vol. I, p. 241.

XII

ON TARIFF BARRIERS AND THE FREE GOLD MARKET

To those who assert that tariff barriers are the cause of Britain's industrial depression, we would direct their attention to the "Memoranda, Statistical Tables, and Charts," prepared by the Board of Trade in 1903 for the purpose of the fiscal inquiry instituted in the early years of Mr. Joseph Chamberlain's campaign for "Tariff Reform." It is there pointed out that the increase in protective tariffs did not begin until 1879-84, in which period Germany, Victoria, Canada, Russia, and France raised their duties on imports, followed by further increases during 1885-9 and 1890-4 on the part of Germany, Russia, Italy, the United States, France, Spain and Portugal. But it will also be observed that in the period 1871-5 Germany and the Latin Union demonetized silver and monetized gold, and that beginning with the year 1874 British exports fell off considerably although imports continued to increase. A direct connection would thus seem to be established between these two latter events. In view of this, how can it be possible for free traders

to assert that foreign protective tariffs—which began in 1879—caused the Free Trade Fall* which began in 1874? The decline in British exports began five years before the foreign protective tariffs were imposed in the countries mentioned, and it was clearly due to the demonetization of silver and not to the imposition of tariffs.

Although partial free trade was introduced in 1853, it was not until 1861 that the United Kingdom was placed on a complete free trade basis. But in the period 1853-73, owing to the discoveries of gold in Australia and California, the imports of gold from these countries were of a substantial character. For the period 1858-71 (no information earlier than 1858 is obtainable) the amount of gold retained in this country, after deducting the exports, amounted to £67,773,471. For the period 1872-86 (in the latter year gold was discovered in South Africa) the amount of gold retained in the country, after deducting exports, only amounted to £9,565,328.

As the accumulation of gold during the period 1858-71 was of a substantial character, it was certain to extend the basis of credit, so that this would account for the great increase of prosperity that occurred prior to 1874, which has mistakenly been attributed to the policy of free trade.

* Mr. Francis Francis is the originator of this expression.

It is a very open question whether the country would not have been more prosperous in the period 1853-73 without free trade. During this time, it is highly probable that if the National system advocated by Adam Smith had been in force the country's prosperity would have been much greater.

When we come to study the period after 1874 (the year when London really became a free gold market) we find that imports of merchandise suddenly increased and exports suddenly declined.* This was no doubt due to the fact that Germany and the Latin Union sold us their merchandise for gold without any obligation on their part to import our manufactures. These countries—having monetized gold—desired to increase their gold reserves; and, as the United Kingdom was a free trade market as well as a free gold market, the acquisition of the requisite gold was facilitated by an export of goods to this country; and by such means the essential credits with which to pay for the gold were placed at their disposal. For instance, in the period 1860-70 Germany's net imports of gold from this country amounted to the value of £1,534,659, but, in the period 1871-81, her net imports of gold from this country amounted to the value of £44,239,950. It is, of course, quite true that in the period 1872-86

* See statistical table of imports and exports 1854 to 1898 on pp. 214-15.

Great Britain gained on balance a sum of 9,565,328 in gold, but this probably disappeared through the manufacturing industries, together with a larger sum through continental tourist travel (see table on p. 216). Gold sovereigns exported abroad in this latter way would not be accounted for in the exports, and, in all probability, they were for the most part melted down. But there can also be no doubt that in consequence of the demonetization of silver the whole basis of credit throughout Europe and America was contracted, and thus the purchasing power of the people in each country was curtailed. This is rather proven by the fact that the Argentine and India avoided the general depression which ensued, because they had not monetized gold.

To explain away the anomaly that arose as regards the increase of imports and the decline of exports in 1873-5, the free trade economists would no doubt begin to suggest about this period that it was due to invisible exports. But the widening margin since 1875 should have induced the deepest concern in the majority of them, particularly when in 1898 the adverse balance was really greater than the actual exports of manufactured goods from this country. To emphasize this point in another way, it is only necessary to say that, per head of population, the annual average excess of net imports over exports in the period 1855-9 was only £1 1s. 3d., and in the period 1870-4 it was

£1 15s. 1d., but in the period 1895-9 it rose to £3 17s. 0d. At the present time it amounts to £15 16s. 0d.

In view of these facts it is essential that we should now begin to make some attempt to increase the real exports of the country at the expense of the invisible exports, and this can certainly be achieved without pleading with foreign nations for a lowering of their protective barriers. If free trade has to depend for its success on the goodwill of other nations, can it possibly justify itself as a National Economic System? Furthermore, if the virtues of free trade were at their best between the years 1844-74, would it be unreasonable to suggest that the above present ratio of £15 16s. 0d. should be reduced to the highest level attained at the height of the so-called free trade boom, namely £1 15s. 1d. in 1870-4; or at any rate to a level not exceeding £5 per head of the population?

The economic problem to be solved is largely a monetary one, and, when it is solved, foreign countries may be inclined to lower their tariffs to the average of their taxation as recommended by Smith.

If we study the course of wheat prices (see chart on p. 210) between 1874-1900, we shall also find that there was a gradual decline in these with occasional rises due to bad crops, world shortage,

or corners created by Chicago speculators. In the period 1876-9 there was a shortage in the world's crops of wheat which caused a temporary rise in prices. The rise in the price of wheat in the year 1891 was due to the Russian rye famine which caused an increased demand for wheat, and, as the export of wheat from Russia was stopped, it caused a rise of wheat prices in this year. In the years 1897-8 there was a shortage in the world's crops of wheat which resulted in the Leiter corner in the Chicago wheat market. These exceptional occurrences, however, did not prevent the gradual fall in the price of wheat between 1874 and 1900.

On pages 210-11 we publish two charts showing the value of the imports and exports of merchandise, and this is followed by a statistical table on pages 212-13 showing the actual value of the imports and exports, which table has been supplied by *The Economist*.

Following this, on pages 214-15, there is a table showing the value of the exports and imports of gold of the United Kingdom in the years 1858-98.

On pages 216-17 there is also a table showing the Coin and Bullion Reserves held by the Bank of England in the years 1858-1927 inclusive. The table does not distinguish between gold and silver, but, as the proportion of silver has always been extremely small, it will not materially affect the figures, which will be useful for comparative purposes.

Further corroborative evidence is to be found in a very interesting paper read by Mr. C. Dampier-Whetham, before the Farmers' Club, and as he is a "free trade economist" his views should carry considerable weight. Although we agree as to causes we do not agree with his solution. Mr. Dampier-Whetham's solution of the difficulty he outlines is "a more economical use of gold." But if gold is the cause of the "great depression," a more economical use of it will merely minimize the depression and will not cure it. However this may be, it does not affect his argument which, in part, is as follows:

"The broad tidal movements in prices are not confined to agricultural produce. Other commodities show similar and simultaneous changes. Since 1873 the Ministry of Agriculture has issued an index number, showing the average prices of agricultural produce with the different products weighted according to their relative importance in British farming. Since 1871 the Board of Trade has issued index numbers giving the average prices of all wholesale commodities. Two of the lines in Diagram 1 are plotted from the yearly averages of these two sets of index numbers, the values in the year being taken as 100. The diagram shows the general concordance which exists between agricultural and other prices.

"Such a close agreement indicates that the cause or causes of the variations in price cannot

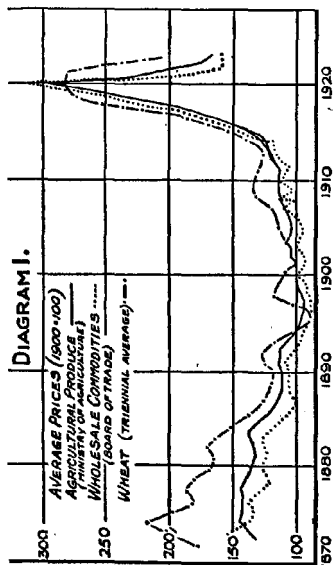


DIAGRAM REFERRED TO BY MR. C. DAMPIER-WRETHAM IN HIS PAPER.

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be confined to agriculture; we must search for factors which affect all industries and not farming alone.

"Between the Napoleonic Wars and the German War of our own day, there have been two long periods when the general level of prices was falling, and two when it was rising. Mr. W. T. Layton, in his book 'An Introduction to the Study of Prices,' gives the following figures for the index numbers, averaged over five years at each turning point in the price curve:

Average Index Number.			Percentage Change in each Period.	
1821-25	..	154	..	- 25
1846-50	..	116	..	+ 20
1871-75	..	138	..	- 40
1894-98	..	82	..	+ 25
1906-10	..	102		

"Each period of rising prices saw farming prosperous, each period of falling prices marked an agricultural depression.

"Layton's book, or any similar work on prices, explains these changes. At any given time, special causes may usually be detected. Perhaps some things are cheapened by technical improvements in methods of production or distribution; perhaps costs are raised by a scarcity of raw material or an increase in the rate of wages. But there is one essential factor always at work fixing the general level of prices. Price is the amount of currency or credit an article will fetch. If currency and credit are plentiful and circulate fast, money becomes less valuable relatively to other

things; more of it must be given to buy them and prices rise. On the other hand, if business grows faster than currency and credit can be supplied, money becomes scarce and dear relatively to goods and services, and prices fall.

"Many people seem to find it hard to realize that money, which we use as a *standard* of value, can *change* in value. A gold sovereign, it is true, always contains the same weight of gold. But it will buy different amounts of clothes or wheat or labour at different times. These things represent approximately constant amounts of human effort, and it is these things which constitute wealth. We do not eat gold, nor make coats out of Treasury notes. Money is not wealth; it is only a measure of wealth, and its possession is but an order to deliver goods or services. The difficulty arises from the fact that, while a change in the value of money is going on, it produces its effect by altering prices, and, to the onlooker, accustomed to think of a pound as a constant unit, it is the value of other things which seems to change. So, to pre-Copernican man, accustomed to regard the earth as fixed in space, the sun appeared to move.

"Between the two great Wars, British currency was based on a gold standard, and, for the security of the banks, currency and credit were only allowed to expand in rough proportion to the gold held in reserve. Thus, if our view be correct, we ought to be able to explain the variation in the price-level in the nineteenth century by changes in the world's supply of and demand for gold.

"During the first of the periods considered above,

from about 1823 to 1848, business was expanding rapidly ; but gold was running short, many South American mines being closed down. Prices accordingly fell. The Bank Charter Act of 1844, restricting the issue of Bank Notes, would have intensified the effect much more had not the system of cheques been developed and thus a new form of currency introduced.

" The Corn Laws were repealed in 1846 amid prophecies of disaster. But free trade in corn was more than counterbalanced by a new factor—the discovery of gold mines in Australia and California. Gradually the new supplies increased the world's stock of gold ; credit expanded, prices continually rose, and British farming entered on its period of greatest prosperity and renown.

" It should be observed that all this time transport was getting cheaper and new wheat lands were being opened up. Yet, as long as gold was coming in fast, neither cheapening transport nor importing foreign wheat prevented prices from rising and our farmers from flourishing. Even wheat rose by 6 per cent. and other agricultural products much more. Why did the tide turn in 1873 ? There was no sudden increase in foreign competition, yet from 1873 onward the great depression began.

" The chief cause again appears to be monetary. The supply of gold from the Australian and Californian mines began to shrink, while the demand increased rapidly. In 1871, after the Franco-Prussian War, Germany adopted a gold standard, and she was followed by the United States in 1873, and the Latin Union in 1874. Thus, besides

the natural growth of business, a demand arose for gold reserves, while supplies were getting less abundant. These changes exactly coincided with the turn from prosperity to adversity in agriculture. Moreover, the depression was not confined to England. The farmers of nearly all other nations were in like case, even in heavily protected countries like France and Germany, and in new lands whose wheat we were importing. The only significant exceptions were India and Argentina, where agriculture flourished and the value of land rose. Now Indian currency was based on silver, and that of Argentine on nothing—save the credit of Government paper. Neither of these countries was tied to gold.

"In Diagram 1 a third line is added to show the triennial averages of wheat prices from 1873 onwards. Between the extremes, wheat fell about twice as much as other commodities. Thus perhaps, as a rough approximation, we may say that, increasing foreign competition was responsible for about half the fall in wheat prices, while the fall in the prices of other agricultural produce was chiefly due to monetary causes.

"The severity of the depression in England is still within living memory. A Royal Commission was appointed to investigate its causes and to consider possible remedies. In his evidence before that Commission in 1894, Sir Robert Giffen prophesied its speedy end owing to the discovery of the South African mines in 1886 and the increasing output of gold therefrom. Giffen proved to be right. Prices touched their lowest point in 1896-7 ;

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from 1900 to 1914 they rose by about 20 per cent., and agriculture enjoyed a modest prosperity.

"It may be seen, therefore, that the varying relations between the supply of and the demand for gold is enough to account for the general changes in the average price level from 1820 to 1914."

We have given this short review of the historical free trade periods 1853-74 and 1874-98 in order that they may be compared with the events of the present time; and because we are of the opinion that history is repeating itself. The Financial Editor of *The Times* has recently declared that "the theory that trade can be properly and safely stimulated by inflation dies hard." We agree with this view, but no sound money reformer desires inflation. But if certain theories die hard, it is harder still to kill the false inferences which those who support the gold standard will persist in dragging into the discussion. They make no attempt to suggest where improvements could be made in the monetary system so that production may be encouraged and developed. On the contrary they seek to destroy all schemes of reform designed for this purpose by suggesting that they are inflationary in character. In this way they employ the tricks of the politician who sometimes is able to kill opposition by ridicule. But when the facts of the case are fully appreciated by the

public there will not be so many gold standard cynics about.

We may retort to the Financial Editor of *The Times* by suggesting that the theory that industry can be properly and safely stimulated in the free trade gold standard system dies hard. But if he will carefully study the historical facts disclosed in this chapter and the preceding one it may help him to reform his views as regards the system he so ably defends.

It is a well-known fact that there is not a sufficiency of gold to enable all foreign nations to adopt a gold standard basis. Therefore, the expedient has been resorted to in most countries of adopting a gold exchange basis system. The countries who adopt this latter system find it a more profitable one to operate than a purely gold basis system, inasmuch as they need hold only a small part of the cover for their note issues in gold, and the balance can be held in Bills of Exchange on London. In this way the Bank of England can increase its gold reserves—the cost of maintaining which has to be paid by the Bank and indirectly by the British Public—but the foreign Central Banks, who hold Bills of Exchange on London in lieu of gold as cover for their notes, obtain the profits through the discount rate earned on the Bills of Exchange which are payable in gold in London. In consequence of this excellent arrangement in favour of

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the foreign Banks, the foreign deposits held by the London money market are estimated to be not less than £200,000,000—which is the disturbing element in the present economic position. In other words, the presence of this fund enables the Bank of England to increase its gold reserves, which thus compels it to pursue a foreign policy.

It may be asked, "How is it possible for foreign Banks, most of which are poorer than the Bank of England, to accumulate this vast amount of reserve cash in the London money market, which gives them an equivalent call on the gold reserves held by the Bank of England?" The explanation is very simple. As the Bank of England and other Central Banks have gradually increased their gold reserves, the depression in the basic industries has gradually become more acute, and this is somewhat akin to the course of events that followed the monetization of gold in 1874 by Germany and the Latin Union. In order to increase their gold exchange reserves (either by importing gold or holding cash balances in the London money market) foreign nations are obliged to increase their exports of merchandise to England as the free gold market; and, instead of importing our manufactures to pay for these, they allow the credits thus created to remain in the London money market for the credit of their account. In the event of a crisis, therefore, these foreign Central

Banks have the right to convert their cash credits into gold bullion on demand, and, as this gold forms the basis of our whole monetary system, it will be seen that it might cause a violent contraction of credit, unless, perchance, the Bank is able to offset the demand by its own control of foreign credits—which is unlikely. In order to induce the foreign banks not to convert their cash credits into gold at the present time, the Bank of England keeps its discount rate at a high level. In pursuing a policy of this kind the Bank of England is really borrowing short term foreign deposits at usurious rates of interest, in order to make its weekly statements look more healthy than they really are: and thus it indirectly increases the burden of taxation on Britain's basic industries.

But how does this affect Great Britain's productive industries in the long run? It affects them in this way: that so long as the Bank of England maintains a gold standard system, and London as a free gold market, just so long will there be an acute depression in the basic industries. The reason is that foreign nations must place themselves in funds in the market in which they desire to purchase the gold they require, and this, as will be obvious, is only possible by an export of merchandise from their respective countries to Great Britain. It may happen, of course, that they could do so by a transfer of credits from other

countries, but this is not likely to have much effect so long as a free trade market is available to which manufactures can be sent for realization. And so long as foreign nations are hungry for gold this process will continue; and thus Great Britain's industries are hit in two ways: (a) by an increase in costs of production due to the reflex actions of monetary policy, and (b) by the free gold market.

Furthermore, in the period 1844-74, gold was the national legal tender money of this country, and was not legal tender money in any other. Therefore, the gold-producing countries had to send their gold to Great Britain, and to accept manufactures in exchange; it was the only country in which they could spend their money. Since 1874, however, the position has been entirely changed. Gold can be shipped to this country, but the credits obtained in exchange can be spent abroad. And as the selling prices of British manufactures have been increased by 12%-18%, in consequence of our monetary policy, this will tend to force the gold-producing countries to spend their credits out of the country. Broadly speaking, therefore, the advantages of a free gold market—in a gold standard free trade system—do not cover the disadvantages by at least one-third.

Also, as Locke has said on p. 167: "In a country not furnished with mines there are but two ways of growing rich, either conquest or commerce." In

a free trade gold standard system merchants will always buy and sell for gold margins. If it is more profitable for them to import gold instead of commodities, they will do so. If it is more profitable for them to export gold instead of manufactures, they will do so. Therefore, in such a system a prosperous home market, and a successful export policy, will largely depend on factors which industry and agriculture do not control, but which they ought to control.

The Bank of England is now fully aware that, by its monetary policy, it has materially assisted in increasing costs of production in the basic industries, and that, if it allowed credit to expand prices would rise and also costs of production. It realizes that if any attempt were made at the present time to increase prosperity by expanding credit, it would only result in bringing disaster to the gold standard system; consequently, the Bank has neutralized its considerably increased lending power. The Productive Industries are striving to lower their costs of production, but the monetary policy pursued by the Bank of England increases these. There is now a definite line of demarcation between the Bank of England and the Productive Industries beyond which either side cannot pass, and this will continue indefinitely so long as the present monetary system is continued.

When the authorities at the Bank of England and the Treasury decided on a return to the gold standard, they were of the opinion that they could deflate prices by contracting the credit resources available for production ; but they have been hoist with their own petard. They overlooked the excess burden of taxation, and the fact that the bulk of the national credit resources would be used in financing the National Debt, both of which have increased factory selling prices by at least 12%-18%, and which cannot be deflated because all taxation imposed is payable in terms of gold. They forgot that they could not deflate costs of production as effectively as they could deflate prices ; and this defect will always be present in any monetary system that attempts to control prices. Money can never be an effective medium of exchange until it ceases to control production and prices. When it does these things it controls the policies and enterprise of all the producers, and likewise the wealth and prosperity of all industry, agriculture, and labour ; which, of course, is hopelessly wrong.

To sum up. An import of gold is presumed to be paid for by an export of British Manufactures. This may not be so. But if it is, the value of the gold imported is, in any event, sterilized. On the other hand, exports of gold are paid for by imports of foreign manufactures ; and it will be found, on close examination, that our imports of gold are, for

the most part, really paid for by the foreign credit balances held in the London Market; which, as we have said, are created by imports of foreign manufactures.

Therefore, a large portion of the gold reserves held by the Bank of England are really held under call at the option of foreign central banks. The profits of the system are earned by the latter, and the loss is paid for by the Bank of England, which recovers it from the British public. But, in consequence of the high discount rate which the Bank of England has to maintain in order to make the whole system effective, an additional burden of at least £191,000,000 per annum is imposed upon the British Public, Industry, and Commerce through the increase of the interest charges which they are obliged to pay on their bank overdrafts, mortgages, and prior lien securities, and through the increase of social services caused by the increase of unemployment; all of which, as we have indicated, are regulated by the Bank Rate. Thus we observe the adverse effects produced by the Free Trade Gold Standard System and a Free Gold Market.

NOTES ON CHAPTER XII

Mr. H. Parker Willis, the well-known American economist and monetary authority, has an article on the stabilization of the French franc in the September issue of the *Banker*, and the following extracts from this article, received as we go to press, will be of general interest, since they somewhat confirm the views expressed in this Chapter.

" The definite announcement of the stabilization of the French franc is in line with the expectations that have been entertained by American bankers and financial authorities for a long time past. The management of the Bank of France have taken special pains to have it well understood in the United States exactly what they were trying to do. It is well recognized that the management of the bank has desired to maintain a thoroughly friendly relationship both with the Government at Washington and with the Federal Reserve System, so far as this was at all within the bounds of possibility. It is also well recognized that what the bank has attempted, and the policy it has pursued in providing itself with gold in the United States, have by no means been pleasing either in Washington or in New York. The Bank of France gradually developed a large balance in New York amounting, it is estimated, at one time to as much as \$150,000,000 in earmarked gold and \$200,000,000 in exchange subject to order; and then, as it had occasion, it has withdrawn gold without asking permission or, so far as the community is informed, feeling obliged to resort to any 'credits.' In all, it is believed to have withdrawn about \$325,000,000 up to the end of June, building up its earmarked balance as shipments took place, and it has still due, in earmarked account, gold to the amount of \$50,000,000, whose immediate exportation has however been postponed. That it could withdraw from its balances with banks here without engaging in any further elaborate exchange operations \$250,000,000 additional, if not more than that amount, is the prevailing opinion. The Bank of France,

and French resumption in general, is thus one of the chief, if not the chief cause of the gold 'drain' upon the United States of which so much has been said. Not many months ago, when Federal Reserve authorities were constantly issuing statements to the effect that they could, and would, 'offset' the effects of a leakage of gold out of the country by furnishing a 'cushion of credit,' in the form of an additional expansion of Reserve bank loans, they spoke undoubtedly with the private conviction that the Bank of France could, and would, be prevailed upon to discontinue its gold accumulation policy. This conviction turned out to be unfounded, and the interviews which have taken place between Federal Reserve officials and Bank of France representatives are generally described as 'unsatisfactory.' "

" This is the background upon which French stabilization is now to work itself out, so far as the New York market is concerned. The first question of substantial interest now clearly is whether France itself will be able to draw more gold from the United States, or will be obliged, as some have predicted, to suffer a minor return flow of gold to the United States, as was the case with Great Britain when that country undertook stabilization. As to this point opinions differ. The following figures, designed to show the situation as to the balance of trade, throw light upon the merchandise aspect of the case :

TRADE BETWEEN U.S. AND FRANCE, 1927-8 ⁶

	Imports France to U.S. <i>Dollars.</i>	Exports U.S. France. <i>Dollars.</i>
December, 1927 . . .	13,202,704	23,127,248
January, 1928 . . .	12,107,095	21,289,708
February, 1928 . . .	13,913,950	15,701,309
March, 1928 . . .	12,292,499	18,693,049
April, 1928 . . .	10,433,049	13,130,992
May, 1928 . . .	11,159,184	18,337,593
Total (6 months)	<u>\$73,108,481</u>	<u>\$110,479,899</u>

" In all, France has taken from the United States in the past few months (say twelve) about \$305,000,000 and during the

latter half of that period she has had an 'adverse' balance of trade (reckoning up to the end of May, 1928) of about \$37,000,000 on merchandise account. She has therefore been able, by sale of securities and by exchange operations, to deplete, or fund, the whole of the merchandise claims held by the United States and, in the form of gold bullion or coin, to supply herself with the specie needed by the Bank of France. From this the immediate future may be inferred, always provided that no new factor intervenes to change the character of the situation, such as those which have been suggested in a foregoing paragraph.

"Accordingly, considerable interest is felt in the financial relations which are believed likely to develop between France and the United States. Some time ago France was apparently anxious to get access to the American capital market, and a little less than a year ago she had a plan to re-finance a part of her public debt which had previously been borrowed here at a very high rate. At that time the Government of the United States was still worrying over the debt-funding treaty and took a long time to reach any conclusion about the treatment of the refunding plan which France had proposed. The final result was that consent was rather grudgingly and unofficially given; but in the meantime the arrangement with the International Match Co., whereby the latter financed the transaction on the basis of an issue of its own bonds in exchange for valuable match privileges in France, had been planned and carried through. The result was that the French Government did not have to appear in the New York market directly at all. Finally, the Washington authorities determined to authorize the admission of French industrial securities into the American market, and a rush of these was predicted. No such rush has occurred, and so far as can be learned none is likely to occur."

Our congratulations are due to M. Poincaré for the very able manner in which he has managed the stabilization of the franc, particularly as it was predicted by those who support the gold standard that he could not achieve his object without securing the aid of foreign gold credits. He has

achieved success with a bill of exchange basis, and starting from a depreciated paper franc. But he would not have been so successful if he had not had a free trade market in England, and a free gold market in London, to play with. Proof of this is to be found in the balances of merchandise trade in recent years as between France, Belgium, Germany, and Great Britain, which are as follows :

	Imports from £	Exports to £	Excess of Exports. £	Excess of Imports. £
FRANCE :				
1921 .	53,013,656	44,259,945	—	8,753,711
1922 .	48,537,887	48,538,111	224	—
1923 .	58,462,433	49,258,145	—	9,204,288
1924 .	66,578,211	41,714,860	—	24,863,351
1925 .	65,042,372	31,026,406	—	34,015,966
1926 .	59,176,536	20,384,170	—	38,792,366
1927 .	65,846,898	24,889,586	—	40,957,312
GERMANY :				
1921 .	20,513,801	17,861,350	—	2,652,451
1922 .	26,523,377	32,110,750	5,587,373	—
1923 .	39,994,041	42,624,167	2,630,126	—
1924 .	36,888,265	42,586,928	5,698,663	—
1925 .	48,403,494	44,226,072	—	4,177,422
1926 .	72,609,965	26,351,802	—	46,258,163
1927 .	62,066,798	44,035,421	—	18,031,377
BELGIUM :				
1921 .	32,861,836	19,629,388	—	13,232,448
1922 .	23,618,752	25,031,582	1,412,830	—
1923 .	27,476,497	25,234,088	—	2,242,409
1924 .	36,386,576	22,667,817	—	13,718,759
1925 .	35,556,819	18,667,080	—	16,889,739
1926 .	44,853,301	14,266,224	—	30,587,077
1927 .	47,617,057	17,373,073	—	30,243,984

The above figures clearly indicate the reason why France, Belgium, and Germany, at the present time, have a command over gold in the London and New York gold markets.

In addition to her exports, Germany has been borrowing to such an extent in the New York and London Money Markets that she has been able to meet her reparation payments under the Dawes Plan solely from borrowed money (which directly and indirectly benefits France), and, from the surplus credits remaining, to draw gold away from the New York and London Money Markets. Between September 1st, 1924, and May 31st, 1926, the total payments made by Germany on reparations account amount to £243·7 millions. In the same period Germany has borrowed between £350 to £443 millions. Thus she has not really begun to make effective reparation payments, and what the effect will be on British Industry when she begins to do so must be left to the imagination. The whole economic position is artificial and dangerous.

According to the Midland Bank's Monthly Review (Sept.-Oct.), during the past three months Germany has bought £9 millions of gold in London, and since the middle of March the Reichbanks' stock of gold has increased by £22 millions to £115 millions. But all this seems to be a case of history repeating itself, *vide* the demonetization of silver in 1874. We take Germany's exports, and lend her money, in order that she (and indirectly France) may take away the gold we need to expand our own basis of credit. It is very much open to question whether our financial authorities should be allowed

to continue to commit the country to such a policy.

Mr. D. M. Mason, Chairman of the Sound Currency Association, is very anxious that the Liberal Party should not be called the Soft-Money Party owing to the energetic and courageous campaign pursued by Mr. J. M. Keynes, who has joined the Liberal party. But Mr. D. M. Mason and his friends can certainly be called the Soft-Money Party. In view of the facts disclosed we can think of no term that so aptly describes their outlook on monetary policy.

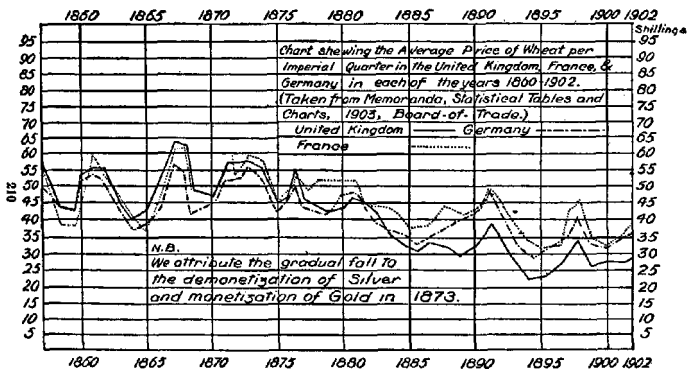
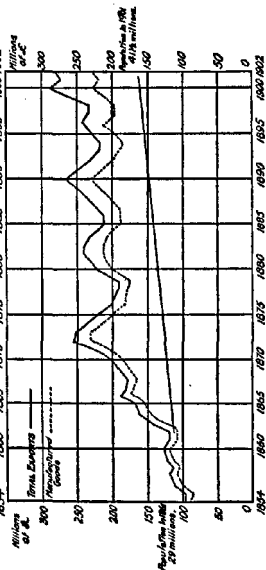


CHART SHOWING FOR THE UNITED KINGDOM THE TOTAL VALUE OF THE EXPORTS OF BRITISH PRODUCE AND THE VALUE OF THE EXPORTS OF MANUFACTURED AND PARTLY MANUFACTURED GOODS FOR A SERIES OF YEARS.

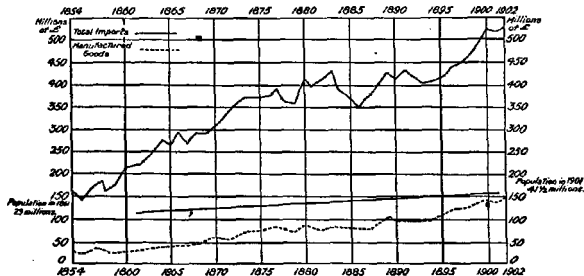
(Taken from Memoranda, Statistical Tables and Charts, 1903, Board of Trade.)



The beginning of the Free Trade Fall in 1874 should be noted.

CHART SHOWING FOR THE UNITED KINGDOM THE TOTAL VALUE OF THE IMPORTS (INCLUDING RE-EXPORTS) AND THE VALUE OF THE IMPORTS OF MANUFACTURED AND PARTLY MANUFACTURED GOODS FOR A SERIES OF YEARS.

(Taken from Memoranda, Statistical Tables and Charts, 1903, Board of Trade.)



N.B.—The Population Line is drawn to a scale four times that of the imports and exports.

BANK OF ENGLAND

TOTAL OF GOLD AND SILVER COIN AND BULLION HELD IN BOTH DEPARTMENTS

1858-1927
(End of Year)

	£		£
1858	18,967,100	1893	24,488,512
1859	16,810,054	1894	32,547,478
1860	12,298,119	1895	43,631,321
1861	15,961,439	1896	34,158,899
1862	14,956,421	1897	30,453,493
1863	14,362,605	1898	29,337,841
1864	14,100,974	1899	29,342,367
1865	13,403,102	1900	28,541,163
1866	19,247,859	1901	32,064,544
1867	21,941,047	1902	29,776,817
1868	18,445,858	1903	28,911,813
1869	19,196,622	1904	29,927,272
1870	22,703,536	1905	28,530,251
1871	29,914,822	1906	29,064,478
1872	23,666,857	1907	30,745,846
1873	22,618,685	1908	30,732,402
1874	21,492,793	1909	32,628,075
1875	21,703,879	1910	31,355,545
1876	28,365,434	1911	32,438,162
1877	24,032,070	1912	30,328,567
1878	27,453,075	1913	34,983,149
1879	27,601,562	1914	69,493,610
1880	24,268,616	1915	51,476,497
1881	20,316,994	1916	54,304,915
1882	20,395,245	1917	58,337,469
1883	21,566,273	1918	79,110,764
1884	20,695,406	1919	91,342,155
1885	20,112,228	1920	128,267,670
1886	18,820,089	1921	128,434,359
1887	19,918,881	1922	127,443,007
1888	19,288,866	1923	128,019,382
1889	17,805,190	1924	128,560,002
1890	23,465,834	1925	144,556,367
1891	22,295,403	1926	151,218,648
1892	24,397,928	1927	152,408,849

There are no means of ascertaining the volume of gold coins that was in circulation in the country, not recorded in the Bank of England reports, between the years 1858-1913; but according to the Cunliffe Committee Report, the total of gold coins in circulation in 1913 was estimated at £123,000,000. Since 1914 all gold coins have been withdrawn from circulation. But there is no doubt that, in the period mentioned, the Bank of England could withdraw gold from circulation for export, and likewise contract credit, by a sale of securities.

VALUE OF THE EXPORTS AND IMPORTS OF MERCHANDISE OF THE UNITED KINGDOM, 1854-98, 1921-27.

	Exports.	Imports.	Excess of Imports including re-exports.
1854	97,184,726	152,389,053	55,204,327
1855	95,688,085	143,542,850	47,854,765
1856	115,826,948	172,544,154	56,717,206
1857	122,066,107	187,844,441	65,778,334
1858	116,608,756	164,583,832	47,975,076
1859	130,411,529	179,182,355	48,770,826
1860	135,891,229	210,530,873	74,639,644
1861	125,102,814	217,485,024	92,382,210
1862	123,992,264	225,716,976	101,724,712
1863	146,602,342	248,919,020	102,316,678
1864	160,449,053	274,952,172	114,503,119
1865	165,835,725	271,072,285	105,236,560
1866	188,917,536	295,290,274	106,372,738
1867	180,961,923	275,183,137	94,221,214
1868	179,677,812	294,693,608	115,015,796
1869	189,953,957	295,460,214	105,506,257
1870	199,586,322	303,257,493	103,671,171
1871	223,066,162	331,015,480	107,949,318
1872	256,257,347	354,693,624	98,436,277
1873	255,164,603	371,287,372	116,122,769
1874	239,558,121	370,082,701	130,524,580
1875	223,465,963	373,939,577	150,473,614
1876	200,639,204	375,154,703	174,515,499
1877	198,893,065	394,419,682	195,526,617

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1878	.	.	.	.	.	.	.	192,848,914	368,770,742	175,921,828
1879	.	.	.	.	.	.	.	191,531,758	362,991,875	171,460,117
1880	.	.	.	.	.	.	.	223,060,446	411,229,565	188,169,119
1881	.	.	.	.	.	.	.	234,022,678	397,022,489	162,999,811
1882	.	.	.	.	.	.	.	241,467,162	413,019,608	171,552,446
1883	.	.	.	.	.	.	.	239,799,473	426,891,579	187,092,106
1884	.	.	.	.	.	.	.	233,025,242	390,018,569	156,993,327
1885	.	.	.	.	.	.	.	213,044,500	370,967,935	157,923,455
1886	.	.	.	.	.	.	.	212,725,200	349,863,472	137,138,272
1887	.	.	.	.	.	.	.	221,913,910	362,227,564	140,313,654
1888	.	.	.	.	.	.	.	234,534,912	387,635,743	153,100,831
1889	.	.	.	.	.	.	.	248,935,195	427,637,595	178,702,400
1890	.	.	.	.	.	.	.	263,530,585	420,691,997	157,161,412
1891	.	.	.	.	.	.	.	247,235,150	435,441,264	188,206,114
1892	.	.	.	.	.	.	.	227,077,053	423,793,882	196,716,829
1893	.	.	.	.	.	.	.	218,094,865	404,688,178	186,593,313
1894	.	.	.	.	.	.	.	215,824,335	408,344,810	192,520,475
1895	.	.	.	.	.	.	.	225,890,016	416,689,658	190,799,642
1896	.	.	.	.	.	.	.	240,145,551	441,808,904	201,663,353
1897	.	.	.	.	.	.	.	234,219,708	451,028,960	216,809,252
1898	.	.	.	.	.	.	.	233,359,240	470,544,702	237,185,462
1921	.	.	.	.	.	.	.	703,399,702	1,085,500,061	382,100,359
1922	.	.	.	.	.	.	.	719,507,410	1,003,098,899	283,591,489
1923	.	.	.	.	.	.	.	769,257,771	1,096,226,214	326,968,443
1924	.	.	.	.	.	.	.	800,966,837	1,277,439,144	476,472,307
1925	.	.	.	.	.	.	.	773,380,702	1,320,715,190	547,334,488
1926	.	.	.	.	.	.	.	653,046,909	1,241,361,277	588,314,368
1927	.	.	.	.	.	.	.	709,105,402	1,219,387,424	510,282,022

VALUE OF THE EXPORTS AND IMPORTS OF GOLD OF THE UNITED KINGDOM, 1858-98.

	Exports.	Imports.	Excess of Exports.	Excess of Imports.
1858	12,567,040	22,793,126	—	10,226,086
1859	18,081,130	22,297,698	—	4,216,568
1860	15,641,578	12,584,684	3,056,894	—
1861	11,238,372	12,163,937	—	925,565
1862	16,011,963	19,903,704	—	3,891,741
1863	15,303,279	19,142,665	—	3,839,386
1864	13,279,739	16,900,951	—	3,621,212
1865	8,493,332	14,485,590	—	5,992,258
1866	12,742,059	23,509,641	—	10,767,582
1867	7,889,030	15,800,159	—	7,911,129
1868	12,708,308	17,136,177	—	4,427,869
1869	8,473,699	13,770,812	—	5,297,113
1870	10,013,521	18,806,728	—	8,793,207
1871	20,698,275	21,618,924	—	920,649
1872	19,748,916	18,469,442	1,279,474	—
1873	19,071,220	20,611,165	—	1,539,945
1874	10,641,636	18,081,019	—	7,439,383
1875	18,648,296	23,140,834	—	4,492,538
1876	16,515,748	23,475,975	—	6,960,227

1877	20,373,886	15,441,985	4,931,901	—
1878	14,968,507	20,871,410	—	5,902,903
1879	17,578,818	13,368,675	4,210,143	—
1880	11,828,822	9,454,861	2,373,961	—
1881	15,498,837	9,963,006	5,535,831	—
1882	12,023,804	14,376,559	—	2,352,755
1883	7,091,365	7,755,800	—	664,435
1884	12,012,839	10,744,408	1,268,431	—
1885	11,930,818	12,576,561	—	645,743
1886	13,783,706	12,950,846	832,860	—
1887	9,323,614	9,955,326	—	631,712
1888	14,944,143	15,787,588	—	843,445
1889	14,453,318	17,914,039	—	3,458,721
1890	14,306,628	23,568,049	—	9,261,421
1891	24,167,925	30,275,620	—	6,107,695
1892	14,832,122	21,583,232	—	6,751,110
1893	19,502,273	24,834,727	—	5,332,454
1894	15,647,551	27,572,347	—	11,924,796
1895	21,369,323	36,009,329	—	14,640,006
1896	30,123,925	24,468,580	5,655,345	—
1897	30,808,571	30,808,858	—	287
1898	36,590,050	43,722,960	—	7,132,910

CONCLUSION

It will be seen from the constructive proposals outlined that the monetary system evolved accords with the Federal Reserve System. I did not start out with this idea in view, but it has just happened that way. This will be a point in favour of the scheme, since the Federal Reserve System has been tested and proved; and, whilst it is admitted that certain modifications of that system are necessary, yet, on the whole, a large measure of success has been obtained. I would also like to emphasize that the new system proposed is one that could be adopted in this country forthwith—without waiting for international co-operation—and that through its operations the foreign exchanges could be brought under more effective control than is possible under our present gold bullion standard.

The Federal Reserve Board, and other banking authorities in the United States, admit that the Federal Reserve System could be improved. This will be evident from the fact that the Board is not able to control the speculative credits which are tending to put the whole financial system in the United States out of its control. It is only held

within bounds with the utmost difficulty, and although a high discount rate has been employed it has proved ineffective. Nevertheless, the employment of a high discount rate has thrown an unnecessary burden on the productive industries in the United States, since it has forced them to pay increased interest charges for the credit facilities they carry from day to day, although they are in no way responsible for the breakdown of the system. An injustice has thus been imposed on the productive industries.

The speculative fever has risen to such heights in the United States that the shares of the chain stores, mail-order houses, motor companies, and soft-drink firms, are selling at prices where their interest yield is only half that obtainable on United States Government securities. Industrial shares are also selling at prices twice as high as the high records reached in the most excited boom markets of the past.

Mr. Leonard Ayres, Vice-President of the Cleveland Trust Company, in a recent speech, has stated:

"that it was safe to say that the next few years would be very different from those just behind the country. Transition to soberer days would not be easy, but the next decade would probably belong to the plodders and not to the plotters, to the calculators and not to the speculators."

Then, again, Mr. Louis T. McFadden (Chairman of the House of Representatives Committee on Banking and Currency) in an address delivered before the clearing-house section of the American Bankers' Association at its recent Convention in Philadelphia, said :

"The Federal Reserve System faces a grave responsibility in dealing with inflation of the stock market and in real estate transactions. The risk of producing a business 'slump' without intending to do so would have been obviated six months ago if the Reserve System had been more drastic in dealing with stock speculation. *Brokers' loans at present made up a greater total than the credit extended to agriculture, to foreign trade, and to the automobile industry.*

"There was ample credit in the United States for all normal and legitimate use, but there seemed to be no standard of practice in the proper use of credit, and no instrumentality which had the power in an emergency to force those who deal in credit to employ sound principles. Wise statesmanship would establish a standard and preserve a proper balance so that capital needs and the needs of industry and commerce should not suffer."

The huge volume of credit that is being used to finance all of these speculative transactions, including real estate, is causing unfavourable comment in responsible quarters not only throughout the United States but throughout the world. It is generally agreed that the inordinate demands for credit for

speculation have raised the cost of interest charges which industry and trade have to pay in the United States for their day-to-day credits. And that if the excessive speculation is not curbed it will bring about a check in industrial expansion, if it does not bring about acute depression.

The main difficulty would appear to be that the Federal Reserve Authorities are not able to control the private deposits of individuals and industrial companies which are being lent in the speculative markets. But it is clear that these private deposits must be commodity money and not gold money, or else it would be impossible for any private individual or corporation to defy the Federal Reserve Authorities. It should also be noted that the excessive speculation in the stock markets has not raised the wholesale price level to any extent. The prices of manufactured goods still tend downwards. Such a state of affairs would not be possible in England. It would be absurd to expect it, for the simple reason that private individuals and those business men and agriculturists who control our basic industries are so heavily taxed under the gold standard system, that those who have been fortunate enough to escape bankruptcy are fully engaged in doing their utmost to keep away from the bankruptcy courts. But how they must envy those rich individuals and business men who are now dominating the New York financial markets !

Mr. Charles E. Mitchell, President of the National City Bank of New York, in a recent speech at a luncheon given by the American Chamber of Commerce in London, said :

" On the stock market there has been a marked advance in prices. Stock Exchange figures produced on September 1st showed that brokers' loans at that date were 5,051 million dollars. That meant that the ratio of loans to the total share values of the listed securities at that date was 8.80 per cent. That percentage was the lowest which they had had during the year 1928, and he thought it was not excessive. In March, 1926, when, as they would remember, there was a stock market break and prices fell by their own weight, the ratio of loans to share values was 10.23 per cent. There was no doubt some point above the level of to-day when they might get on dangerous ground, but the borrowing on shares and securities was not excessive to-day.*

" Looking at the matter from the bankers' standpoint, they would find that the figures issued by the New York clearing bankers differed from those of the Stock Exchange. The bankers' figures showed loans of 4,524 million dollars. Something like 50 per cent. of the lending was done by individuals and corporations.

" If he were asked to point out a danger in the situation, it would be in the fact that *so large a percentage of loans on stock collateral was being made by a class of lenders who were not responsible, and did*

* It is if values are twice what they were.—J. T. P.

not feel any responsibility for the maintenance of sound money conditions.

"That meant a strain on the banks who were directly responsible for good money conditions, and they had curtailed their own lendings in order that they might be in a position to deal with the situation which might arise if this great body of lenders not responsible for sound money conditions were to want their money from the market.

"There were people who even went to the point of expressing the view that the necessary inflation coming from their gold base in America would result in America being eliminated for a time from the export fields. *If inflation had come into prices and into wages, that conclusion would have been undoubtedly sound*, but during that time they had a development of stock speculation, and the increased credit showed entirely in that new outlet—the carriage of stocks. That was distinctly an advantage to their country, and it went on as an advantage up to the spring and summer of last year.*

"About that time their Federal Reserve Bank, in order to help the English market and enabling gold reserves to be built up in the central banks of Europe, reduced its rediscount rates. Gold stocks coming in—whether it would have stopped in any case he could not say—and so these heavy demands to which he had referred on the credit structure had to be carried on a smaller gold base. *Therefore they*

* If inflation has not entered into prices in the United States, it is due to the sound practice of the Federal Reserve Board in accepting Bills of Exchange with gold as the basis of credit.—J. T. P.

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had increased rates to-day, and those high rates were bound to continue until industry needed less, until crops needs had been satisfied, and until there was some decrease in the requirements of the carriers of stock."

Yes! "Until industry, agriculture, and the carriers of stock needed less." But why should industry ever need less credit, or be invited to accept less of it, because the Federal Reserve Authorities are not able to control the speculative position? And why should the high discount rate in the United States (increased with a view of curbing speculation) be permitted to increase the price of credit in all other countries who are not sharing in the speculation?

Thus far we have seen that as a wealth creative machine the Federal Reserve System is excellent. But that certain modifications of the system are necessary in order to enable the Federal Reserve Board effectively to control and classify all speculative credits. My readers will now see (by reason of the defects shown in the Federal Reserve System) that the monetary system I have evolved is confirmed as a practicable and effective scheme. And that the opinions I have expressed in the past to the effect that the speculative markets would throw any financial system out of control have proved to be sound. The Federal Reserve Authorities now confirm the validity of these opinions.

For the sake of clarity I will now recapitulate the

main points of the monetary system I recommend in this book (and in my last one) as follows :

(1) There should be no fixed ratio of gold to Bills of Exchange when they are used as the basis of the quantity of money.

(2) There should be no fixed price for the purchase and sale of gold.

(3) Gold should be treated as a simple commodity, the market price of which should be determined in the same way as any other wealth product.

(4) Bills of Exchange, together with the Gold Reserves, should constitute the basis of the quantity of money.*

(5) The gold reserves should not exceed a limit of £200,000,000.

(6) No loans should be granted by a Banker, or a Merchant Banker, without accepting Bills of Exchange therefor, and such bills should immediately be rediscounted by them with the

* The notes at the end of Chapter IV should be studied here, also Chapters XIII and XIV in "The Flaw in the Economic System." It should be observed that in the latter I mention that "gold in whole or in part" should not form the basis of the quantity of money. By "in part" I meant that gold should not be employed in a ratio system, with a fixed price maintained for the purchase and sale of gold. Subject to this proviso, and in view of the existence of the fiduciary issues, the Gold Reserves could be used more conveniently with bills of exchange as the basis of the quantity of money than as reserves against the quantity of money.

Bank of England. The latter to issue legal tender money against all Bills of Exchange rediscounted which money the Joint Stock Banks should hold at the disposal of their customers.

(7) No Stockbroker, Produce Merchant, or Dealer to be allowed to accept loans for the carrying of stocks, shares, or produce for speculative purposes, except these are obtained through the Joint Stock Banks. The same rule to apply to real estate agents and property.

(8) The Bank of England would then classify all Bills of Exchange into grades A, B, C and D, etc., and it should be a rule that the more speculative credits should not exceed a fixed ratio to Class A, which would be the producers' credits secured on wealth products.

Under the new system proposed we ensure that all currency in circulation would be convertible which is not possible under the present system. As all the new currency issues required, in excess of that fiduciary issues and the gold reserves, will have to be issued by the Bank of England against Bills of Exchange, it follows that all such issues of currency will have to be repaid to redeem the Bills as they fall due for payment. There is thus an effective automatic adjustment of credit and currency. In other words, the currency in circulation will be the measure of value of the Bills of Exchange, which, in turn, will be the measure of the standard of value.

The Bills are issued against wealth products on a fixed standard, and the responsibility for their redemption at face value rests with the borrowers and endorsers of the Bills. From this it is to be inferred that the sole use of currency is to facilitate the distribution of purchasing power in the smallest possible units at a negligible cost.

Owing to free imports and the heavy burden of taxation the competitive power of the basic industries is impaired. Selling prices are, on an average, 15 per cent. higher than prevails on the Continent, and, in consequence of this, the basic industries are not able to use the increased credit facilities which the Bank of England could now place at their disposal. The Bank has neutralized this credit by selling securities, and it has certainly acted wisely. But in making this admission it does not excuse the monetary policy pursued by the Bank since 1919, as it is the reflex actions of this policy that has placed the basic industries in their present precarious position.

What it really comes to is this: No material expansion of credit can take place under the gold standard system without causing inflation, an increase of prices, and an increase in costs of production. And rather than have the gold standard accused of such tendencies the Bank of England prefers to neutralize credit and pursue a deflationary policy. Hence the reason why I have said that the

gold standard system is the mother of high taxation, unemployment, low wages, and trading losses. But it is for the country now to decide whether this system shall continue. .

In any event the increased credit facilities which the Bank of England is now able to place at the disposal of the productive industries of the country are totally insufficient to meet their full requirements ; and it is because of this that I have said that safeguarding alone will not satisfy the full needs of the case. In fact, owing to the limited quantity of money available for production, if safeguarders were to obtain all the business they have every reason to expect from the policy of safeguarding, prices and wages must fall. If this were to happen then the policy of safeguarding would be prejudiced, since it would be blamed for the inevitable increase of unemployment that must follow the fall of prices and the lowering of wages.

It is true that certain industries have derived considerable benefit from the policy of safeguarding, yet it cannot be said that the unemployment figures have shown any reduction. On the contrary, there has been an increase of about 275,000 unemployed persons in the last year. Thus it is conclusively proved that the industries that have benefited from protection, or from the creation of trusts, have done so at the expense of other industries not so protected, *i.e.* there has been a transfer of the limited

purchasing power available from one industry to another. (See Chapter V.) *

The nation's productive power has to carry a total national debt of about £7,500,000,000, and, although upwards of £800,000,000 has been paid in cash since 1919 to redeem part of the debt, the nominal debt is greater to-day than it was in 1919. The interest charges on the debt are still approximately the same, so that the vast sum of money paid towards the redemption of debt has, to all intents and purposes, been lost.

Therefore, if any real impression is to be made on the National Debt, a greater productive effort will be required than has hitherto been possible. But before this can be brought within the realm of probability, I estimate that the increased credit facilities required by the Joint Stock Banks will ultimately be not less than £1,500 millions, and it will be hopeless to expect this result from a gold standard system. As I have said at the beginning of Chapter I, nature and machine power can both place an abundance at the disposal of mankind, but the orthodox merchants and bankers would seem to be more afraid of an abundance than of a shortage. May it not be due to the fact that without recurring shortages

* There has also been an increase of taxation in the current year of approximately £30,000,000 which Mr. Churchill is collecting for his Rating Relief Bill. This has also caused unemployment since it has absorbed purchasing power. The case for safeguarding has thus been prejudiced.

their businesses could not prosper. The law of supply and demand is to them an extremely profitable law to operate in the alternating shortages and abundances which are bound to occur periodically within a gold standard system.

A monetary system which compels us to give to producers a larger price for short supplies, than we have to do for abundant supplies, must surely be an imperfect one. I have known of cases where farmers have received a debit note in exchange for the produce they have sent to market, the freight charges on which exceeded the price realized for the produce, though the retail selling price was more than sufficient to cover all costs of distribution and leave to the farmer some return for his services. It may be held, of course, that this defect is due to the methods employed in distribution ; on the contrary, it is due to the monetary system which inevitably brings about and maintains the existing working conditions.

One of the main objects to be achieved under items 6, 7 and 8 (pp. 225-8) is to prevent merchants, speculators, and dealers making a business of earning marginal profits (commonly called "differences") that are obtainable between cheap money and dividends, income and revenue ; or between cheap imports, which do not carry their fair share of the national burden of taxation, and home manufactures. These classes of business prosper because

they are able to monopolize the volume of liquid credit.

The productive industries create cheap money through the development and marketing of wealth products ; but the manipulations of the merchants, speculators, and dealers are the cause of dear money. If we examine the working conditions in the United States we shall find that the reason why there is an abundance of lendable capital in the New York financial markets is because the manufacturing industries in the United States have had a long period of prosperous industrial activity ; and the surplus profits thus earned are finding their way to New York, to be lent at the highest possible rate of interest.

The only way that merchants, speculators, and dealers can obtain profits is through their ability to buy in the cheapest market and to sell in the dearest. But, to be successful in their business, it is essential for them to obtain free access to liquid credit, and, as the loans required are usually for short periods, they seldom encounter any difficulty in obtaining what they want.

Therefore, unless their activities are brought under the control of the Central Banks, it will be impossible for any Central Bank effectively to administer and control the credit system. There can be no objection to individuals, corporations, speculators, merchants, or dealers using their own money to buy

stocks, shares, real property, or produce ; but when, for speculative purposes, they are allowed to borrow money to purchase more than they could from their own resources they create an artificial demand in excess of effective demand ; hence the reason for the inflation of prices now occurring in stocks, shares, real property, and natural materials.

Unless the restrictive methods herein suggested are made effective the only alternative is the destruction of Capitalism, and that would be fatal ; for thus Capitalism and Speculation would be destroyed together. We can all grow more prosperous by allowing potential productive power to control the creation of wealth. The American engineer spoke truly when he said " that it is likely that in the next few years costs will be lowered and wages raised to such an extent that every farmer and wage-earner will have the consuming power which to-day is enjoyed only by those with incomes of 10,000 dollars a year." We had all much better agree to allow our economic welfare to be improved in this way than court revolution. It will be more scientific, and therefore more permanent and enduring.

There cannot be more than one economic system. There is only one true science, and it remains for us to make up our minds to accept it. The Bolsheviks, Communists, Socialists, Fascists, Liberals, Conservatives, Democrats, and Republicans all believe they can produce a cure for our economic ills, and,

acting in this belief, they seek to impose their will and purpose on the community. They forget all about the existence of the natural laws, the wonderful regularity of time and nature, and that the economic system should co-operate with nature and not against it.

The true economic system will give to the Bolsheviks, Communists, and Socialists, far more than they ever dreamt of in their wildest moments. But no progress is possible so long as they each attempt to impose their own will and purpose. There can be no progress without change, but similarly there can be no progress without a large measure of agreement and goodwill.

"He only gains his freedom and existence
Who daily conquers them anew."

We shall gain our economic freedom only through mutual goodwill, and a united endeavour to do what is best for the good of the greatest number.

Throughout the development of the general theme, I have followed closely the inductive process of reasoning, and I have not attempted to formulate any new law or theory that is not based on experience or existing tendencies. To my mind the sole use of economic philosophy is to gather up and record world tendencies in concepts—which is only possible after a lapse of time—so that they may be at the command of those who, in the present and future, may wish to study them. But when

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politicians and revolutionaries forget this, and attempt to lay down laws and theories for the guidance of humanity that are based merely upon assumption (deductive process), they are rendering the greatest dis-service to the cause which they seek to promote.

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