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Economic Intelligence Service

PROSPERITY  
AND  
DEPRESSION

*A Theoretical Analysis of Cyclical Movements*

BY

GOTTFRIED VON HABERLER

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## PREFACE

This book has its origin in a resolution adopted by the Assembly of the League of Nations in September 1930 by which it was decided that an attempt should be made to co-ordinate the analytical work then being done on the problem of the recurrence of periods of economic depression.

The literature concerning economic depressions and what is currently and somewhat loosely described as the trade cycle is abundant, and the publication of a further book on the theory of such cycles was not the primary object of the enquiry undertaken as a result of this resolution. This book is incidental to the first step in that enquiry.

It is apparent from the persistence with which depressions occur, from the gravity of their economic and social effects, and from the growing consciousness of that gravity, that—however abundant the literature on the subject, however elaborate and specious the theories—our knowledge of the causes of depressions has not yet reached a stage at which measures can be designed to avert them. This failure of society to control its own destinies may be due to one of three causes. It may be due to the fact that the causal relationship of events has not up to the present been ascertained; it may be due to the fact that, although the truth has been discovered and stated, it lies buried and obscured in a mass of false theory; finally, it may be due to the fact that, although the truth is known and recognised, depressions are as inevitable a phenomenon of our present economic structure as famines were of a more primitive economy which lacked means of transport and of storage.

The ultimate object of all enquiries into the occurrence of depressions must be to find ways and means to avert depressions or, if they are in fact inevitable, to render the structure of society

more apt to meet the shock which they cause. But, if practical measures to avert depressions, or to lessen their intensity or duration, or to adapt the economic structure to them can in the end be found, their discovery is likely to result from a slow and protracted process of research and their practical value is likely to result from a slow and painful process of trial and error.

With these considerations in mind, the enquiry undertaken by the League has been designed, not with a view to the elaboration of a new and complete theory of the cycle, but with the object of analysing and sifting (if necessary, supplementing) the theories which already exist and subjecting those theories to the test of fact.

The first stage in the League enquiry, therefore, has been to examine existing theories with a view to ascertaining what they had in common, the points at which differences of opinion arose and, in so far as possible, the causes of those differences.

In the second stage, which has now just been initiated, an endeavour will be made to confront these various theories with the historical facts—to subject them in so far as these facts can be quantitatively expressed to statistical analysis, in so far as they are not quantitatively expressed to the recounted records of the past.

This present volume is concerned with the first stage only. Professor Haberler, to whom the conduct of the enquiry in its initial stages was entrusted, has divided it into two parts. The first part contains a systematic analysis of existing theories; the second an attempt to weave from those theories a general synthesis.

A first draft of the systematic analysis was sent to the authors quoted for comments and criticisms. While this precaution was clearly necessary (and ready and most valuable help was afforded), it must not be interpreted as implying that the various authors have thus made themselves responsible for the summary of their reasoning contained in the following pages. A summary can never be a perfect reflection of what it summarises, and indeed one author—though only one—replied that his exposition would not remain recognisable if thus compressed.

In the course of this analysis of existing theories, it became apparent that many of the seeming differences of doctrine were due rather to the use of different terminologies than to any more fundamental causes.

The measure of agreement which appeared to exist between those who have devoted special attention to the problem of the trade cycle seemed to justify an attempt to make from their theories even at this early stage of the work the general synthesis which constitutes the second part of this volume. This synthesis, however, is more than a simple patching together of the theorems of others : it is an attempt to create a living and coherent, if incomplete, theory on the basis of the knowledge at present available. But it is confessedly tentative and preliminary : as Professor Haberler states in his Introduction, there are many points at which no definite solution can be proposed. At such points, various possibilities are suggested and these possibilities will be examined during the second stage of the enquiry. Indeed, the whole of this general synthesis will be subjected, together with the first part, to statistical control and test during the second stage of the enquiry. The intention is to confront the theories with the ascertainable facts—at first with those which can be expressed in terms of figures and later with those less tangible facts which the annals of the past record—with a view at once to testing the accuracy of the explanations or partial explanations of the cycle now current and to furnishing the basis of fact necessary for the further development of theory where theory is weak, views are discordant or doubt exists.

The publication of this work may, it is hoped, give rise to further discussion in a wider circle than could be approached by direct correspondence or by meetings.

A. LOVEDAY,

*Director of the Financial Section  
and Economic Intelligence Service.*

Geneva, September 1936.

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## INTRODUCTION

As has been explained in the Preface, this book  
*Purpose of the book.* is a first step in a more extended enquiry undertaken by the Economic Intelligence Service of the Secretariat of the League of Nations into the causes of the recurrence of periods of economic depression.

The present study confines itself to the task of analysing existing theories of the business cycle and deriving therefrom a synthetic account of the nature and possible causes of economic fluctuations. However, the next stage in this investigation—the application, as far as possible, of quantitative tests to the various causal hypotheses—has largely influenced the manner in which the preliminary problem has been approached in the following pages. The reader is invited to keep in mind, while studying the present report, the fact that it is planned as but a part of a greater whole.

In view of the scope of the investigation as a  
*Analysis of theories.* whole, the purpose of the first part of this report—*i.e.*, of the Systematic Analysis of the Theories of the Business Cycle—is not to present a history of the development of economic thought on this subject (although every attempt has been made to interpret as accurately as possible the meaning of the various writers whose theories are discussed), nor to give anything like an exhaustive bibliography of business-cycle theory. The purpose is rather to gather together various hypotheses of explanation, to test their logical consistency and their compatibility with one another and with accepted economic principles. It is intended to give a rounded picture of the possible explanations of economic fluctuations and it is hoped that, by theoretical reasoning, the number of these possibilities can be considerably reduced.



The second part of the present report—the “*Synthetic Exposition relating to the Nature and Causes of Business Cycles*”—contains the comprehensive explanation which emerges from the analysis of theories in the first part. As has been said, it does not claim to be an entirely new theory, but a synthesis and development of existing theories, so far as they can be synthesised. What is presented there is furthermore not a closed and rigid system, but a flexible and open one: there are many points where no definite solution can be proposed, but where the existence of a number of possibilities will be indicated. The choice between these can then be made only on the basis of empirical investigations. In many cases, theoretical reasoning supported only by such broad facts as one happens to know without special statistical or historical investigations can put intelligent questions, but cannot definitely answer them.

That by analysing various theories it should be possible to give an explanation of the business cycle which, while leaving some questions open or offering in other cases alternative answers, nevertheless clarifies a number of problems presupposes that the difference between the theories analysed is not so radical as is sometimes believed. In fact, the assumption is that the real differences in opinion have been frequently exaggerated, and that, for certain important questions, a much greater harmony between writers of different schools can be established than the superficial observer would believe or even than these same writers would be willing to admit. It is a natural thing that most writers are inclined rather to dwell on the controversial issues than to stress the points of general agreement. Here the opposite principle will be followed and, in the following sections, it will be shown how theories which seem *prima facie* to contradict one another can sometimes be reconciled.

\* \* \*

The manuscript of Part I of this book was substantially completed by December 1935; that of Part II, by May 1936. An attempt has, however, been made to refer at least in footnotes to some of the important publications which have appeared after the completion of the relevant parts of the manuscript.

## Appendix I.

DESCRIPTION OF THE INDICES ILLUSTRATING CYCLICAL  
MOVEMENT IN VARIOUS COUNTRIES<sup>1</sup>

The "reference cycle curve" gives for each country for the years 1880 or 1890 to 1931 a diagrammatic picture of the general fluctuations in business activity as described by W. L. THORP in the volume "Business Annals" (1926, National Bureau of Economic Research; continued in the *National Bureau News Bulletin*, No. 43, September 1932). This verbal account has been expressed in visual terms by assigning a numerical value to the main characteristics cited for each year, as follows :

Exceptional prosperity . . . . .	+ 3
Prosperity . . . . .	+ 2
Mild prosperity . . . . .	+ 1
Mild depression . . . . .	— 1
Depression . . . . .	— 2
Deep depression . . . . .	— 3
Revival (Recession)	preceding level + (—) 1

Each year is indicated on the curve by a point, the level of which is intended to represent the average activity during the year. In cases where a reversal of the situation occurred during the first half of the year, the level is determined by the situation prevailing after the turning-point. If the reversal occurred during the second half of the year, the situation before the turning-point has been held decisive. The other indices are described below, country by country :

## UNITED STATES OF AMERICA.

*Industrial Production.*

1880-1920 : Index of the volume of mining output. E. E. DAY,  
*Review of Economic Statistics.*

1899-1920 : Index of the volume of manufacturing output.  
E. E. DAY, *ibid.*

1920-1935 : Federal Reserve Board indices of industrial production : general index and group index for mining.

<sup>1</sup> See pages 170 and 171.

*Employment in Manufacturing Industries.*

1899-1923 : Professor P. H. DOUGLAS' index, "The Theory of Wages".

1919-1935 : Bureau of Labor Statistics index.

## UNITED KINGDOM.

*Industrial Production.*

1880-1931 : HOFFMANN'S index. *Weltwirtschaftliches Archiv*, September 1934.

1927-1935 : Board of Trade index.

*Employment.*

1880-1925 : Percentage of employment (= 100 — the percentage of unemployment) among trade-unionists. Abstract of Labour Statistics.

1926-1935 : *Idem*, among compulsorily insured workers. Abstract of Labour Statistics.

*General Business Activity.*

1880-1913 : Miss D. S. THOMAS' index. *Journal of the American Statistical Association*, March 1926.

1924-1935 : *The Economist* index (*The Economist*, July 25th, 1936), deviations from trend.

## GERMANY.

*Industrial Production.*

1880-1913, 1925-1935 : Index of the "Institut für Konjunkturforschung", *Vierteljahreshfte zur Konjunkturforschung*, Sonderheft Nr. 31, 1933. *Konjunkturstatistisches Handbuch*, 1936.

*Employment.*

1904-1932 : Percentage of employment (= 100 — the percentage of unemployment) among organised workers. *Statistisches Jahrbuch für das Deutsche Reich*.

1931-1935 : *Idem*, based on the percentage of registered unemployed to workers under Health Insurance. International Labour Office.

## FRANCE.

*Industrial Production.*

1898-1913, 1919-1935 : Index of the "Statistique générale de la France". *Annuaire statistique de la France*.

## SWEDEN.

*Industrial Production.*

1913-1935 : Index of the "Kommerskollegium". *Kommerciella Meddelanden*.

*Employment.*

1911-1935 : Percentage of employment (= 100 — the percentage of unemployment) among trade-unionists. *Statistisk Årsbok.*

## CANADA.

*Industrial Production.*

1919-1935 : Index of the Dominion Bureau of Statistics. *Monthly Review of Business Statistics.*

*Employment.*

1915-1935 : Percentage of employment (= 100 — the percentage of unemployment) among trade-unionists. *The Canada Yearbook.*

## AUSTRALIA.

*Employment.*

1906-1935 : Percentage of employment (= 100 — the percentage of unemployment) among trade-unionists. *Official Yearbook of the Commonwealth of Australia.*

*General Business Activity.*

1880-1922 : Yearly index of Roland WILSON. *The Economic Record, 1930.*

*Note.*—With the exception of the United States, all employment indices are corrected for trend : the currently available labour supply is taken as equal to 100 and the fluctuations shown are relative thereto. In the case of the United States, the fluctuations in employment are related to the employment (not the available labour supply) of a given base period, 1923-1925.

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## Appendix II

### DESCRIPTION OF CURVES ON PRODUCTION AND EMPLOYMENT BY GROUPS OF INDUSTRIES <sup>1</sup>

#### UNITED STATES OF AMERICA.

##### *Industrial Production.*

Indices of production in investment goods industries and in consumers' goods industries.

1880-1918 : Economic Intelligence Service of the League of Nations.

1919-1935 : Federal Reserve Board.

##### *Employment.*

A. Indices of employment in producers' goods and in consumers' goods industries.

1899-1918 : From Professor P. H. DOUGLAS, "The Theory of Wages".

1919-1935 : From the Bureau of Labor Statistics.

B. Actual number of workpeople employed in producers' goods and in consumers' goods industries according to the Censuses of Manufactures.

1919-1933 : Census years.

#### UNITED KINGDOM.

##### *Industrial Production.*

Index of production of producers' goods and of consumers' goods.

1880-1928 : HOFFMANN. *Weltwirtschaftliches Archiv*, September 1934.

1929-1935 : from the Board of Trade.

##### *Employment.*

A. Percentage of workpeople wholly employed (= 100 — the percentage of unemployment) in producers' goods and in consumers' goods industries.

1880-1923, among trade-unionists (for consumers' goods up to 1914 only) : Abstract of Labour Statistics.

1924-1935, among compulsorily insured workers : Abstract of Labour Statistics.

<sup>1</sup> See pages 182 and 183.

- B. Number of workpeople wholly employed among compulsorily insured workers in producers' goods and in consumers' goods industries.

1924-1935 : Abstract of Labour Statistics.

#### GERMANY.

##### *Industrial Production.*

Indices of production of producers' goods and of consumers' goods of the "Institut für Konjunkturforschung".

1880-1913 : *Vierteljahreshefte zur Konjunkturforschung*, Sonderheft Nr. 31, 1933.

1925-1935 : *Konjunkturstatistisches Handbuch*, 1936.

##### *Employment.*

- A. Percentage of workpeople wholly or partially employed among organised workers in producers' goods and in consumers' goods industries.

1924-1932 : *Statistisches Jahrbuch für das Deutsche Reich*.

- B. 1888-1912, 1923-1934 : Number of persons insured against accident in German industrial unions, in capital-producing and in other industries. *Statistisches Jahrbuch für das Deutsche Reich*. (Figures for 1888-1909 have been reproduced from G. CASSEL, "The Theory of Social Economy", Vol. II, and his classification has been adopted for the rest of the period.)

#### SWEDEN.

##### *Industrial Production.*

Indices of production of investment goods and of consumers' goods.

1880-1912 (Consumers' goods, 1909-1912) : Economic Intelligence Service of the League of Nations.

1913-1935 : from the index of the "Kommerskollegium".

##### *Employment.*

- A. Percentage of employment among trade-unionists in producers' goods and in consumers' goods industries. *Statistisk Årsbok*.

1920-1935 : producers' goods industries.

1921-1935 : consumers' goods industries.

- B. Number of workers engaged in producers' goods and in consumers' goods industries.

1913-1934 : *Industri*, Annual Report of the Kommerskollegium.

**AUSTRALIA.*****Employment.***

- A. Percentage of employment among trade-unionists in producers' goods and in consumers' goods industries.**

1912-1935 : *Official Yearbook of the Commonwealth of Australia.*

- B. Number of workers employed in producers' goods and in consumers' goods industries.**

1904-1935 : *Production Statistics.* Annual report of the Commonwealth Bureau of Census and Statistics.

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