AN INTERNATIONAL MONETARY AGREEMENT.

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INTRODUCTION.

During the last few years, and particularly since 1929, proposals for monetary reconstruction have appeared thick and fast in almost every country. While embarrassing in their number and occasionally not too clear in their provisions, these "plans" are nevertheless altogether to be welcomed. Few of them but contain some useful side-light on the question at issue, while the best furnish analyses of monetary processes unexampled in economic literature. At the same time, the movement is not without its drawbacks. A plethora of panaceas is all too liable to become a source of confusion rather than enlightenment. What would seem most required at present is some means of distilling from this multiplicity of plans a unified scheme of practical action. The progressive breakdown in the currencies of the various countries, and the opportunity for joint discussion presented by the Monetary and Economic Conference, emphasise the need for working out some far-reaching measure adapting the monetary system to the conditions of the present-day world.

In attempting to do this, it is necessary at the outset to be clear that, as matters stand, it is definitely impossible to please all parties. Between those whose idea of what is appropriate goes no further than a simple return to the gold standard, and those who are persuaded that nothing can be done so long as the present price system exists, a compromise is not likely to be found. This is unfortunate, but it cannot be helped. The most necessary thing at the present time is not so much to attempt to reconcile divergent opinions as to distinguish the basic facts of the situation and the types of action suitable for meeting them. If this can be done at all adequately, sufficient unanimity of opinion will follow as the facts in question make themselves felt.

The outstanding feature of the present financial-economic situation is the much-cited "paradox" of poverty in plenty—the fact that men, machines, management, materials and money are all available in excess but for some reason cannot be brought together to meet human needs. The broad outlines of this phenomenon are too distressingly familiar to call for reiteration here. But it may not be out of place to consider, very briefly, the essential reason why such a situation tends to come about.

In order to produce goods on a commercial scale, it is necessary to lay out money in advance—for materials, for labour, for the use of machinery, and so forth. To make production worth while, the costs thus incurred must be covered in the selling price of the product. Owing to a variety of factors, which need not be gone into here,* the total volume of purchasing power being used to buy goods is sometimes sufficient and more than sufficient to enable the total volume of goods for sale to find a market at remunerative prices; but at other times it is definitely insufficient, with the consequence that goods are either left unsold or must be disposed of at a loss.

Under conditions such as obtained during the nineteenth century, a general superabundance or a general deficiency of purchasing power of this type was met by an adjustment of prices and costs. If the volume of purchasing power used to buy goods was unduly large in relation to the volume of goods for sale, active buying led to a general rise in prices. This made for larger profits, which in turn led to an influx of new producers and a consequent increase in output tending eventually to improve both the standard of living and the economic situation generally. If, on the other hand, the volume of purchasing power used to buy goods was small in relation to the volume of goods for sale, the resultant inadequate buying led to a general fall in prices. The immediate effect of this was to make production unprofitable; but the increase in unemployment and destitution so brought about tended to force down wage rates, with the consequence that, in a comparatively short time, costs could be reduced to such a point that production over a large part of industry once again became remunerative. Those producers who, for one reason or another, failed to meet the new circumstances were automatically eliminated.

Such a system, while very far from ideal, nevertheless had in it sufficient elements of stability to work without any really catastrophic breakdown. It has not been successful, however, in adapting itself to modern conditions. For a variety of reasons, too numerous to mention here, this process of automatic or semi-automatic adjustment no longer takes place. The large-scale organisation of industry prevents the rapid influx of new producers and the rapid elimination of the less efficient. Owing to monopolistic or semi-monopolistic conditions, the prices of many important commodities do not respond readily either upwards or downwards. Above all, costs, particularly wage rates and still more overhead charges, are no longer speedily adjusted when a general fall in prices occurs.†

* For an analysis of these factors, see: P. W. Martin, *The Problem of Maintaining Purchasing Power*, P. S. King. Chapters IV—IX.

† *Cf. e.g.* data from the Census of Manufacturers for the United States showing changes in selling prices and production costs:

Year.	*Average selling price.*	*Average cost of material.*	*Average labour cost.*	*Average overhead costs plus profits.*
1927	100	100	100	100
1929	98	95	93	108
1931	78	72	80	95

The extreme flexibility that made the system possible in the nineteenth century is thus definitely a thing of the past. As a consequence, when for any reason the volume of purchasing power being used to buy goods proves inadequate, industry does not tend to find a new adjustment at a lower price and cost level, as once was the case. Instead, it is involved in a vicious downward spiral of declining production and declining demand. The fact that goods cannot be sold at remunerative prices leads to a restriction of output; this, by affecting both earnings and confidence, makes for reduced demand; reduced demand, in turn, leads to further restriction of output, and so on more or less indefinitely. It would seem that, if the world is to achieve anything in the way of sustained prosperity, a new and consciously directed system must be devised in which the price and cost system is no longer counted upon to make the adjustments necessitated by a general superabundance or a general deficiency of purchasing power.

Precisely what form this new system will take, it is of course impossible to predict; but there are two things about it which may reasonably be anticipated. The first is that revolutionary changes in monetary methods are on the whole unlikely. A large proportion of the ingenious "plans" now being put forward involve a total break with the past. Such a break is not impossible. But if history is any guide it is hardly probable. Gradual modification of existing methods, unsatisfactory as it may be to more ardent spirits, is to be expected—unless, indeed, catastrophe intervenes, in which case anything may occur. But so long as all else proceeds on the evolutionary plane, it is hardly conceivable that monetary technique will be revolutionised.

Basic to this "evolutionary" type of development is the general principle that progress, to be sound, must be by experiment. It is easy to be dogmatic on questions of monetary theory; but if one thing is more certain than another, it is that dogmatism in this sphere is out of place. There is nothing simpler than to make sweeping proposals for monetary reorganisation; and at a time such as the present, when there is some reason to feel that almost any change would be for the better, such proposals necessarily gain many adherents. But it is well to remember that few more terrible disasters can befall a people than the complete disorganisation of its monetary affairs; and some at least of the suggestions now being put forward would almost certainly have this effect if once they were applied. The fact has to be faced that it is impossible to foresee with certainty the outcome of any given change in monetary technique. The only reasonable course is to act as wisely as possible, in the light of known facts; to observe the results; and from time to time make such modifications as these results may indicate.

Any practical attempt to deal with the present situation has therefore these three guiding considerations to take into account. First, that a new monetary system must be devised to replace the old automatic system which no longer operates. Next, that so long as other changes remain evolutionary, the changes in the monetary system are likely to remain evolutionary also. Lastly, such changes as may be made should be scientific and experimental in character, giving the maximum attention to facts and taking the least account possible of dogma.

If these premises are accepted, there must be a considerable narrowing in the types of action which can be looked upon as practicable at the present time. On the one hand, such half-hearted measures as a mere return to gold cannot be expected to work, since they fail to take account of the fact that the old system of automatic adjustment is now out of commission. At the other extreme, the exceedingly attractive proposals for root and branch reorganisation of the monetary system, sound though they may be, stand little chance of adoption under present circumstances; and in any case rest too much on dogma and too little on experiment to be acceptable. What is required is first of all a clear understanding of the problems to be solved, and after that a selection and subsequent integration of those solutions which, while effective, depart as little as possible from present practice. Such a programme is not heroic. But what is needed in the monetary field at present is not so much heroism as informed common sense.

THE PROBLEMS TO BE SOLVED.

There is on the whole fairly general agreement as to the main problems that a thorough-going monetary settlement must tackle. In the order in which they are generally stated (though not necessarily the order of relative importance) they are: (1) the restoration of an effective international monetary standard; (2) the approximate stabilisation of the value of money in terms of commodities; and (3) the maintenance of a sufficient volume of buying to keep industry reasonably fully employed.

Various schools attach varying degrees of importance to these three aims. Conservative thought, with a backward glance at the pre-war experience of the gold standard, is absorbed in the problem of restoring an effective international monetary standard, *i.e.* of re-establishing approximate exchange stability between the currencies of the different countries. Monetary reformers, on the other hand, tend to concentrate on a stable standard of value;

that is to say, they would use their chief endeavours to keep the fluctuations of the price level within bounds. Finally, an increasing number of monetary students, while admitting the desirability of exchange stability and price stability, look upon the maintenance of active purchasing power as the major objective. In their view what is necessary above everything else is that the volume of buying of goods in general should be so sustained as to enable industry at all times to find a ready market for its products.

In addition to these differences of approach, opinions vary as to the precise meaning to be attached to certain of the proposals; as to the methods which may best be employed in order to secure the required results; as to the possibility of combining any one of these aims with the remaining two; and as to the extent to which these objects may be achieved by monetary measures. It is accordingly necessary to examine in rather more detail the respective claims of exchange stability, price stability and the maintenance of purchasing power; and the means by which they might conceivably be brought about.

Exchange Stability.

There has been a tendency in recent years to question the importance of exchange stability. This to some extent is natural and even justifiable, inasmuch as in the past the tendency was (and in some quarters still is) to exaggerate its benefits and to sacrifice anything and everything in order to retain it. But while it is possible to pay too high a price for exchange stability, the fact remains that exchange stability is exceedingly important—not so much for itself, perhaps, but by reason of the consequences that follow from exchange *instability*.

As recent events have shown, these consequences are formidable. Unstable exchanges are a standing temptation to countries to depreciate their currency unduly so as to secure a competitive advantage on world markets; and even if they resist this temptation, it is more than likely that events themselves may bring about some such movement. When this occurs, trade is filched from other States and sooner or later these States endeavour to protect themselves by trade barriers; with the result that between the exchange fluctuations themselves and the restrictions of trade thus occasioned, industry and commerce are everywhere disorganised. Markets are lost, thriving and efficient industries are destroyed, while elsewhere uneconomic industries are artificially encouraged.

The social consequences of such a situation are necessarily serious. The uneconomic reorientation of industries involves an inevitable loss in productive efficiency and reduces standards of living throughout the world. The restriction of trade to national markets leads to widespread unemployment and business losses in industries organised to meet a world demand. The continual changes in the currents of international trade, brought about by shifting exchange rates and multiplying tariff barriers, imply chronic insecurity for every worker and every employer who in any way depends on products bought from or sold to other countries. Whatever the relative merits of exchange stability may be—as compared with price stability, for instance—there can be no question that it is of the very greatest practical significance to the generation now living. For the present edifice of production and trade has been built upon the foundation of exchange stability and to rupture that foundation permanently would be likely to entail years of economic chaos and social regression.

Of the possible methods by which approximate exchange stability might be obtained, two are outstanding. The first is based upon the general adoption of some international monetary medium such as gold, this gold being free to move from country to country. So long as every country losing gold takes steps to restrict consumption and force down prices, while every country gaining gold increases consumption and lets its prices rise, a flexible balance between exports and imports (of capital as well as of commodities) can be maintained and constant conversion of the national currency into the international medium thereby secured.

The difficulties inherent in such a method are many. One only need be mentioned here. The obligation to make the national economy subservient to the movement of gold must either take the form of a specific international agreement or be left as a loose obligation upon the various States. If it takes the form of a specific international agreement, it is not easy to imagine how it would be possible to decide whether or not the agreement was being kept. The countries losing gold would be likely to complain that the countries gaining gold were not inflating sufficiently rapidly, and the countries gaining gold would reproach the countries losing gold for their ineffective efforts to deflate. The prospect of international chicanery and recrimination thus opened up bodes ill for the success of any such measure. If, on the other hand, the agreement is left in a looser form, it is difficult to believe that the countries would carry out the obligation when it did not suit them to do so. And with the modern inflexibility of prices and costs such a situation would not be by any means rare.

The alternative method of preventing exchange instability is for the various countries to agree to hold their commodity price levels approximately stable. In such a case, since the unit of currency in different countries would have a constant buying power over commodities, the exchange values of these currencies would tend to remain stable in terms of one another.* This proposal has considerable advantages, inasmuch as it fits in with the proposal for price stability considered in the ensuing section. Furthermore, it avoids the cardinal difficulty likely to arise in applying the method previously examined. A stable price level, carefully defined, is at least a fairly objective criterion, while an undertaking, implicit or explicit, to make gold movements have their full effect upon the price and cost situation is susceptible of many interpretations. On the other hand, exchange stability based upon an international agreement to keep the price level approximately stable is by no means free from objections. Quite apart from seasonal or merely random influences, circumstances would almost certainly arise from time to time tending to upset the exchange stability so attained. Tariff changes; changes in the direction and volume of foreign investments; unequal rates of increase of productivity in undertakings catering for the home market and for the foreign market respectively; major changes in the currents of international trade; these and yet other factors would undoubtedly tend to have this effect, calling for exceptional measures of adjustment on the part of the countries affected.

So far as exchange stability is concerned, therefore, we have these general conclusions. In the first place, exchange stability in itself is not of such vital importance; what is necessary, rather, is to avoid the consequences of exchange instability. For the rest, neither of the chief methods available for stabilising the exchanges can be looked upon as wholly satisfactory. Each has points in its favour and points against it and a decision between them is best left for the moment until the other requirements of a satisfactory monetary system have been examined.

Price Stability.

There is, these days, a considerable amount of agreement on the general principle that a widely fluctuating commodity price level is, as far as possible, to be avoided. The experience of the last twenty years has supplied cogent arguments in favour of such a view. Rapidly rising prices destroy the value of savings and discourage thrift; automatically reduce real wages; and lead to great social and industrial unrest. A rapidly falling price

* Supplementary financial measures would of course be necessary to prevent seasonal or random movements from exercising undue influence upon exchange rates.

level increases the burden of debt, handicaps all enterprise and forces countries and business undertakings into suspension of payments, bankruptcy and default. Workers lose by unemployment much more than they gain by falling costs of living, and constant pressure for wage reductions leads to the losses and waste of industrial strife and social unrest. Even if the purely economic considerations were against a larger measure of price stability—if it could be shown that the production of material wealth would be greater under a fluctuating price level than under an approximately stable price level—the social considerations would be likely to outweigh them. But in point of fact economic considerations and social considerations here point in the same direction. A price level liable to move inconsequently upwards or downwards destroys confidence, fosters errors of optimism and pessimism and makes intelligent planning in large part impossible. Given approximate price stability there are grounds for anticipating not only a larger measure of security and social justice but, with the removal of one of the major causes of uncertainty and economic disorganisation, an improvement in industrial efficiency also.

On the other hand, while there is substantial agreement on the undesirability of a widely fluctuating price level, the exact meaning to be given to the expression "price stability" is a matter of dispute.

Price stability is variously interpreted to mean stability of the price level of commodities at wholesale; stability of the price level of commodities at retail (in particular, those entering into the cost of living of the working classes); stability of the price of labour; and stability of prices of all commodities, services, titles, etc., on which money is spent. These various conceptions of price stability differ greatly one from the other. Thus, a stable cost of living index would permit of wide fluctuations in the price level of commodities at wholesale. Stabilisation of the price of labour would entail a *falling* commodity price level as and when output per man-hour increased. Stability of the "general" price index (including all purchases of whatever sort) would mean widely different things in different countries—particularly as between a country with a highly developed business organisation and a country engaged mainly in small-scale agriculture.

On the whole, the price index best adapted for the purpose of stabilisation would appear to be that of commodity prices at wholesale. This index is more sensitive than any of the others. It already exists in some form in all the chief commercial countries. So long as it is held stable, large fluctuations in the cost of living index are not likely to occur. Most important of all, the price index of commodities at wholesale is particularly appropriate from the international point of view.*

Given that the commodity price level at wholesale is taken as the most appropriate index, the question arises by what method price stability is to be secured. For this purpose two things are obviously necessary: the power to check and reverse a rise in the price level; and the power to check and reverse a decline.

In a country working on accepted financial principles, the power to check and reverse an upward movement of prices rests, actually and potentially, with the central bank. The main instruments available or that might be made available are: (*a*) the central bank rate of discount; (*b*) open market operations on the part of the central bank; and (*c*) the rationing of credit, including possibly the ability to change the legal reserve ratios of the commercial banks. Provided the central bank raises its discount rate sufficiently, thereby discouraging the extension of loans; and/or sells securities in sufficient volume in the open market, thereby withdrawing currency and credit from circulation; and/or rations credit to whatever extent may be required, as, for instance, by limiting the lending capacity of the commercial banks by raising the legal reserve ratio they must hold against their deposits; there is every reason to believe that an undesirable rise in the price level can be effectively checked and reversed. It is not essential that a central bank should have all these instruments at its disposal. In certain countries, indeed, this would not be possible at present from a purely technical point of view. But there is little question that in any country working on sound financial principles sufficient powers can be given to the central bank in one form or another to enable it to exercise an effective restraint upon the volume of currency and credit, and hence upon any upward movement of prices.

On the other hand, the central bank by itself is not in such a strong position when it is a question of checking and reversing a fall in the price level. It may reduce its discount rate; but a low discount rate cannot invariably be relied upon to bring about a recovery in prices. In particular, if business is sinking into or

* *Cf.* Report of the Gold Delegation of the Financial Committee of the League of Nations, para. 96:—

"... An index of wholesale prices measures those fluctuations of the purchasing power of money which, when there is a reasonable degree of freedom of trade, are common to all countries and have a direct international influence. This influence is, in such conditions, exerted by the fact that all countries participate in international trade, and the prices of the commodities which enter international trade not only form a significant part of the domestic price-structures, but, through their effect upon the foreign exchange rates, exert a profound influence upon the volume of credit and therefore upon the level of domestic prices. The only index which measures the price-fluctuations of the commodities which enter into international trade is an index of commodity prices at wholesale."

is already deep in depression, a low discount rate will have little effect, since borrowing, even at the lowest rate conceivable, would still be unprofitable. On occasions, moreover, the general monetary position of a country may make reductions in the discount rate impracticable, owing to their effect upon international capital movements.

The other major recourse, available to some of the central banks, is to engage in open market operations; that is to say, to buy securities in the open market, thereby placing more currency and credit in circulation. But here also, as recent experience has shown, there is no guarantee that such measures will be immediately effective. The currency and credit may pass out of effective circulation as rapidly as it comes in, being repaid to the central bank, exported, going into hoards or being kept as surplus bank reserves. Furthermore, such operations, if persisted in, are inherently more likely to create a security market boom than to act directly upon the commodity market.

Thus, while the central bank, given suitable powers, is fully capable of checking and reversing a rise in the price level, it is not always capable of checking and reversing a decline. The essential difficulty lies in the fact that there is no guarantee that the additional currency and credit that may be made available will find its way on to the buying side of the commodity market. This is not to say that purely monetary measures are altogether ineffective in this respect. At certain times and in certain countries they may well prove sufficient. But under less favourable circumstances, for the effect to be felt upon the commodity market without unreasonable delay, additional measures would appear to be required.

So far as price stability is concerned, therefore, the arguments in its favour are overwhelmingly great; but there is some dissension as to which index is most appropriate; and while the central banks in the various countries have or could be given the means of checking and reversing a rise in the price level, it is much to be doubted whether they would be equally capable of counteracting a fall.

Maintenance of Purchasing Power.

By the maintenance of purchasing power is meant conscious measures for sustaining the volume of buying of goods in general (producers' goods and consumers' goods alike) to such an extent as to keep industry reasonably fully employed.

As matters stand the volume of buying is liable to be inadequate on two separate counts. Except at rare intervals (during periods of intense prosperity) effective demand is not sufficient to provide a market at remunerative prices for the total volume of goods industry is *capable* of producing, with the consequence that men thrown out of work by technological advance or similar causes tend to remain out of work. In addition to this, from time to time (during periods of industrial recession), the volume of buying is not sufficient to enable the volume of goods *actually being offered for sale* to be disposed of as rapidly as they are coming upon the market; with the consequence that production is restricted, men are unemployed and industry falls into the vicious downward spiral of declining output and declining demand.

As already noted, under the "automatic" system that operated in the past, these two factors were present but were met more or less rapidly by the flexible adjustment of prices and costs. Men thrown out of work by technological changes were driven by semi-starvation to compete with their fellows for such jobs as were available. In this way wage rates were forced down (or prevented from rising) and sooner or later the unemployed men were re-absorbed. When the volume of goods for sale outran the volume of buying a similar process ensued. Prices at once declined, costs were forced down and sooner or later activity was resumed at the lower price and cost level thus reached. Modern industrial and social conditions effectively prevent rapid price and cost adjustment along these lines, with the result that the situation does not tend to right itself. The tendency, rather, is for a new "equilibrium" to be struck, not at a lower price and cost level, but at a low level of output, and with a large proportion of the working force involuntarily idle. This being so, what is now required is some means of adjusting effective demand. Instead of leaving the volume of buying to fluctuate widely, relying upon price and cost adjustments to take the whole of the strain thus imposed, the volume of buying requires to be reinforced or restricted as the case may be so as, on all occasions, to enable goods in general to be marketed in sufficient quantities and at sufficiently remunerative prices to keep industry reasonably fully employed.

How this can best be done is a much disputed question. But given that in all likelihood the evolutionary method is the one most likely to be adopted in practice, and given that there are the other two considerations of exchange stability and price stability to be borne in mind, the most promising line at least for the present would appear to consist of the direct reinforcement of the volume of purchasing power coming into the hands of those needing to buy goods, such reinforcement to be carried to the utmost extent possible short of giving rise to an upward movement of the commodity price level.

Taking first the question of the reinforcement of purchasing power actually used to buy goods, it is evident that this can be brought about in either or both of two ways: by taking purchasing power otherwise remaining idle and placing it in the hands of potential buyers; or by increasing the total quantity of currency and credit in circulation and ensuring that it is used to buy goods. In other words, dependent upon the circumstances of the particular situation, idle or new money must be put into active use upon the buying side of the commodity market.

The means most readily available of doing this in the great majority of countries is almost certainly that of public works. If purchasing power is lying idle in large quantities a Government loan would be raised to finance public works. By this means purchasing power, otherwise inactive, would be brought to some extent into the hands of the public works contractors (who would use it to buy materials, equipment and producers' goods generally) and to some extent into the hands of the men employed by these contractors (who would use it in the main to buy consumers' goods). There would thus be a direct reinforcement of the volume of buying. Where no such idle funds were available, but an increase in the volume of buying was nevertheless called for, it would be necessary for the Government, in co-operation with the banking system, to finance such works out of new money. In either case the result is essentially the same—there is a direct increase in the volume of buying; and since the arterial roads, parks, public buildings, etc., thus produced would not for the most part be put upon the market for sale, this increase in the volume of buying is *net* in the sense that it would not be automatically balanced by additional goods seeking purchasers. Its immediate influence would therefore be in the direction of working off the surplus stocks hanging over the market, of bringing unused productive capacity into operation, of checking and arresting a fall in the commodity price level, and, if carried beyond that point, of bringing about an upturn in prices.

It should, perhaps, be emphasised that public works thus financed are totally different from public works financed out of taxation in the normal course. Such a process results in little more than a transference of purchasing power from one set of buyers to another. It is widely different also from the old-fashioned idea of using public works as a means of affording relief to a certain number of the unemployed. The object of a public works programme along the lines sketched out here is not to "make employment" but to reinforce effective demand to the extent necessary to enable industry to produce at something approaching full capacity. The fact that the public works themselves will be useful and that men otherwise unemployed will be given work upon them are points of altogether secondary importance. The essential feature is the injection of purchasing power upon the buying side of the market in such a way as to bring about the absolute increase in effective demand that a resumption of business activity requires.*

There remains the question, to what extent purchasing power may appropriately be reinforced. On this point again opinions differ. But as already pointed out, if the claims of exchange stability and of price stability are to be given due weight, such reinforcement must normally stop short at the point where the price level begins to show an upward tendency. The maintenance of purchasing power would thus consist of the conscious use of public works to keep up the volume of buying, and hence the volume of employment, but always within the limit laid down by the condition that (once the system has been initiated) the price level must not be allowed to rise. It is not intended, of course, that the price level should be the determinant of what action is appropriate at any particular moment. Far more sensitive indexes are available for this purpose and it is these indexes that would be used. The rôle played by the price level is that of a boundary beyond which further reinforcement of purchasing power would be undesirable, since if the reinforcement were carried beyond this point price stability, and with it the essential basis of exchange stability, would be upset.

In sum, therefore, the maintenance of purchasing power must be reckoned of vital importance in view of the fact that the old automatic adjustment tending to keep industry reasonably fully employed now no longer operates. On the whole, it would seem that such reinforcement of purchasing power as may be necessary can most practically be effected by the appropriate financing of public works. Finally, in order to reconcile the maintenance of purchasing power with the other essential features of a satisfactory monetary system, this reinforcement should not be carried beyond the point where it begins to give rise to an upward movement of commodity prices.

From this necessarily brief and rather general analysis a line of action making for approximate exchange stability, approximate price stability and the maintenance of purchasing power would appear on the whole to be feasible—the more so since the measures required to achieve these aims are to a certain extent complementary. In particular, the public works programme and the price stabilisa-

* Incidentally it may be noted that public works measures along these lines are not calculated to increase the burden of taxation, but rather the reverse. Quite apart from the probable saving on relief schemes, there is the all-important point that, with business activity restored, rates of taxation can be lowered and still yield a far larger total return than before.

tion policy lend one another mutual support. Thus, the public works programme makes it possible to reinforce the volume of buying to whatever extent may be necessary to promote and sustain business activity. The price stabilisation policy ensures that this reinforcement shall not go too far. On the other hand, the price stabilisation policy, while fully capable of checking and reversing a rise in prices, may not be so successful in checking and reversing a fall. But here the public works programme, by ensuring that the purchasing power thus put into circulation shall come upon the buying side of the commodity market, renders the price stabilisation policy effective against a fall as well as against a rise in price.

So much for the interaction between the maintenance of purchasing power and the approximate stabilisation of the commodity price level. There remains the exceedingly important question of the scope of application, with its special reference to the problem of exchange stability.

The measures examined here for maintaining purchasing power and for stabilising the commodity price level call for national rather than world action. Conceivably they might be applied by a single country acting alone, irrespective of what is being done by other countries. But, while individual national action is possible, some measure of international co-ordination is necessary for completely successful working. If the maintenance of purchasing power is to be effective upon the external as well as upon the home market, co-ordinated effort among the chief commercial nations is required; for there can be no assurance of sustained buying from abroad if purchasing power is not being consciously maintained outside as well as inside a country's borders. In like manner, if approximate exchange stability is to be achieved, international agreement to keep commodity price levels stable is imperative; for so long as some countries are stabilising their price levels while others permit their price levels to fluctuate widely, the prospect of exchange stability is remote. This is not to say that an undertaking on the part of the various nations to hold their respective price levels relatively stable would be sufficient in itself to guarantee unvarying exchange stability; but it would provide a certain basis for exchange stability and there can be little question that, unless the commodity price levels of the different countries are held in some such relation to one another, unstable exchanges are practically inevitable.

Eventually, therefore, an international monetary agreement on the widest possible scale is essential. But it is to be noted that this does not preclude individual action in the meanwhile; indeed the reverse. The international co-ordination required does not involve any far-reaching scheme of world control requiring something like unanimity before it can be put into effect. What it calls for is action of a national character, to be gradually extended first of all from one or two nations to a group, and later from a group to the commercial world generally, as the need for some such measures as these is progressively driven home by the unremitting argument of economic facts.

THE POSSIBILITY OF PRACTICAL ACTION.

When we turn from theory to the possibility of practical action the prospect is less re-assuring. To put these general precepts into practice it would be necessary for a number of the principal industrial, commercial and financial countries to enter into an agreement: first of all to take active measures to reinforce purchasing power on a scale sufficient to restore business activity; after that to bring about an approximate stabilisation of their respective price-levels; and finally, on the basis of this price stabilisation, to arrive at a sufficiently high degree of exchange stability to permit of a return to an international monetary standard.

Such a programme calls for active measures on the part of each individual country and some amount of international co-operation. The difficulties involved are admittedly great, though not necessarily prohibitive. In most cases the central bank must acquire both a new outlook and new powers if it is to be successful in adjusting the total quantity of currency and credit in circulation. The Treasuries and Finance Ministries must be prepared to frame their budgets on sounder and more flexible principles than are at present observed, principles that bear in mind that a country's budget is not merely a balancing of the Government accounts but a powerful instrument of adjustment (or maladjustment) in the whole national and international economy. The public works programme must be enlarged in scope, centralised, and kept up to date. Means must be found by which simultaneous action can be taken in a number of countries, on approximately the same scale. It would be unduly optimistic to suppose that certain of the more important countries are prepared to take such steps; and still more so to imagine that the necessary international co-operation will be readily forthcoming. In some countries, notably Great Britain, and the United States, public opinion is perhaps not far removed from the point where measures along these general lines will be politically practicable. In others, notably France, public opinion is as yet almost entirely unprepared.

On the whole, therefore, it is probably vain to imagine that an international monetary agreement of this type is to be looked for in the near future on anything like a world scale. At the same time the outlook is not one of unrelieved blackness. Decision on this whole range of questions rests at present with the World Monetary and Economic Conference. What course this Conference will take when it meets it is impossible to predict. But two important international statements dealing with world monetary and economic reconstruction—the Economic Resolution of the International Labour Conference and the Draft Annotated Agenda submitted by the Preparatory Commission for the Monetary and Economic Conference—are not without their significance as showing the direction in which world opinion is moving.

The Economic Resolution of the International Labour Conference.

On 30th April, 1932, the International Labour Conference, comprising official representatives of Governments, employers and workers from some 50 countries, adopted a Resolution of which the following are the essential clauses :—

> That Government delegates duly authorised to that effect should as soon as possible be given instructions to draw up a list of big international works for economic equipment and for national works on a large scale calculated to encourage the general development of the economic situation of the countries concerned, to make the necessary financial arrangements therefor and to have them put in hand without delay;
>
> That States should take joint action to settle the general problems of currency and credit and to lay the foundations for an international monetary system possessing the necessary qualities of stability;
>
> That the problems of production and international trade should be examined by Governments in collaboration with delegates from the most representative organisations of employers and workers in each country, for the purpose of concluding, in a severely practical spirit, such international Conventions as will ensure the resumption of economic activity, on the basis of broad concerted plans, taking into consideration the gradual and systematic increase in the consumption of the masses and the co-ordinated extension of international trade.

These clauses were adopted after protracted debate, both in Committee and in full Conference, by the overwhelming majority of 80 votes to 1. They obtained the approval of the official Government representatives of 30 countries,* of three of the 31 representatives of the employers present and of 26 of the 31 representatives of the workers. One employers' representative voted against the clauses in question.

As will be seen, the general line of action advocated is substantially similar to that emerging from the analysis made above. This is in some ways remarkable, since the Resolution as it stands is the product of many hands, many minds and many different points of view. Remembering the heterogeneous constitution of the International Labour Conference it is not easy on the face of it to account for the logical cohesion and completeness of these proposals. But some consideration of the position in which the International Labour Conference was placed may perhaps furnish a clue.

In the eyes of the Conference the outstanding problem was that of unemployment and the general low state of business activity. Accordingly, its first concern was how to promote employment and increase effective demand. From various points of view the public works programme appealed to the different elements in the Conference—partly because it meant an immediate return to employment of at least some small proportion of those out of work, but primarily because (as it was commonly expressed) it tended to act as a "self-starter" to the economic machine. In more precise terms, it was calculated to inject additional purchasing power on to the buying side of the market, without which the process of production and consumption cannot go forward.

The second clause—calling for monetary stability—followed naturally on the first. For one thing it was evident to all that the state of monetary disorder must be straightened out if the effects of the public works "self-starter" were to be anything more than temporary. Furthermore, the need for a stable price-level had long been one of the main tenets of prominent members of the Conference, particularly those most concerned with unemployment. Above all it was recognised, consciously or unconsciously, that the reinforcement of purchasing power must not be allowed to run to excess, thereby undoing in the monetary sphere the good done in the sphere of industry. For all these reasons, therefore, the monetary clause was obviously essential.

The third main provision of the Resolution enters into the field

* The countries in question were: Austria, Belgium, Brazil, Bulgaria, Chile, China, Cuba, Czechoslovakia, Denmark, Estonia, Finland, France, Germany, Greece, Guatemala, Hungary, Irish Free State, Italy, Latvia, Lithuania, Luxemburg, Mexico, Norway, Netherlands, Poland, Spain, Sweden, Switzerland, Uruguay and Yugoslavia. A number of Government representatives, including that of Great Britain, while not feeling competent to vote upon the question, nevertheless expressed their personal approval of its tenor.

where monetary questions impinge upon the whole broad concept of economic planning. To attempt to follow it here would carry the argument beyond the scope of the present discussion. It may however be worth while to emphasise that in this field also the Conference felt that the essential point to be borne in mind was the "gradual and systematic increase in the consumption of the masses" and that permanent measures having this end in view were fundamental to world prosperity.

Finally, the International Labour Conference, as an international body, tended to see the question not from a purely national but to some extent from a world aspect. It realised that the recovery of any one nation depended in large part upon the recovery of the world as a whole—in the industrial and in the monetary spheres alike. As a consequence it called for international agreement and co-ordination as regards both the programme of public works and that of monetary stabilisation; and in so doing provided the essential foundations for approximate exchange stability.

On the other hand, while the Resolution of the International Labour Conference is of outstanding importance both from the point of view of the proposals it puts forward and from the point of view of the different elements which went to its making, it has to be remembered that it is no more than a resolution. Effective power to take measures along these lines does not lie with employers, workers and Ministries of Labour, but with Treasuries and Central Banks. Those sections of the Draft Annotated Agenda for the Monetary and Economic Conference that deal with monetary reconstruction are accordingly of very special interest, since the expert committee which drew them up consisted in the main of representatives of these two bodies.

The Draft Annotated Agenda of the Monetary and Economic Conference.

The monetary sections of the Annotated Agenda laid down by the Preparatory Commission of Experts deal essentially with the same three questions as those analysed above:—

> "In the field of monetary and credit policy, the objective must be the restoration of an effective international monetary standard to which the countries which have abandoned the gold standard can wisely adhere."
>
> . . . . .
>
> "The question has to be considered whether measures can be taken, with the co-operation of Central Banks on the lines of the recommendations suggested in the report of the Gold Delegation of the League of Nations, to ensure a greater stability of price-levels in the future."
>
> . . . . .

"Some increase in the level of world prices is highly desirable and would be the first sign of world recovery. The Conference will no doubt wish to explore all possibilities of counteracting this fall in prices. One of the methods that should be considered is the continuation and development, where monetary conditions permit, of a general policy of easy money designed to promote a healthy expansion of business."*

As these extracts from the "General Programme of the Conference" show, the central preoccupation of the Preparatory Commission was with exchange stability, price stability and what amounts, in effect, to the reinforcement of purchasing power. On the other hand, when it comes to the question of what practical action might appropriately be taken no clear lead is given. In particular, a deep gulf separates those countries which, however hesitatingly, look forward to a new system and those countries which have not yet realised that the old system has ceased to work.

The countries which recognise to some extent that automatic adjustment of prices and costs is a thing of the past, are intent on securing an initial recovery in world prices (which postulates some reinforcement of purchasing power, whether deliberately brought about or otherwise) and a larger measure of price stability.† Unfortunately they are not as yet prepared to take positive measures to bring about the necessary reinforcement of purchasing power, their hope being that cheap money and a declared intention to raise prices may have the wished-for effect. They do not ignore, of course, the possible use of public works as a means of reinforcing purchasing power, but as is natural with representatives of Treasuries and Central Banks, they are inclined to give monetary questions precedence over industrial questions. The following passage is highly significant in this respect:—

"The suggestion is often made that Governments and other authorities should actively increase the purchasing power in the hands of the public by extensive schemes for public expenditure, financed by borrowings from the market. If such a policy were not kept within reasonable limits, and if it were to result in deteriorating Government credit, debt conversions might be interfered with and the lowering of long-term interest rates delayed."‡

In such a statement the hand of the Treasury is manifest.

* League of Nations: Monetary and Economic Conference, Draft Annotated Agenda, p. 8.

† *Cf.* Draft Annotated Agenda, pp. 17–20.

‡ Draft Annotated Agenda, p. 20.

The main task of a country's Treasury is to balance the budget and, incidentally, to reduce the interest on the national debt to the lowest figure possible. There is a consequent tendency to look upon any measure having this effect as exceedingly desirable. But important as debt conversions and the lowering of long-term interest rates undoubtedly are, they require to be seen in some perspective. Low long-term interest rates may be a valuable long-term factor in business recovery; but at the present time short-term factors—the direct reinforcement of purchasing power—are of more immediate concern. Debt conversions are likewise valuable, but action which will prevent the necessity of £20,000,000, say, being taken from the community annually in taxation (to be returned to it as interest on war loan) hardly compares with action leading to some £500,000,000 worth of more goods being made and consumed in the country each year. It is greatly to be hoped that the delegates to the Monetary and Economic Conference itself, while giving every attention to the special preoccupations of the Treasuries and Central Banks, will be able to see this question from the point of view of the community as a whole.

While the proposals put forward in the Annotated Agenda thus leave a good deal to be desired, the fact nevertheless remains that there are already certain countries which, consciously or unconsciously, are feeling their way towards a new monetary system. Unfortunately there are others—in particular the European countries still on the gold standard—whose representatives have not yet realised the need for a new system. From the point of view of these countries there is only one course of action open to reasonable people; an immediate return to the gold standard. In this they are of course perfectly logical—provided the system of price and cost adjustment could still be relied upon to work. As it happens two of these countries—the Netherlands and Switzerland—were not directly involved in the World War, while the other two—France and Belgium—have been working until recently with the not inconsiderable advantage of a greatly depreciated exchange. As a consequence, the mechanism of price and cost adjustment in these countries has not as yet had an excessively severe strain put upon it for any long period. Furthermore, it is possible that in certain countries where business organisation is not yet fully developed, where trade unions are relatively weak and where there is no comprehensive system of unemployment insurance, the system still has a certain resiliency remaining. In which case, the need for any fundamental change is naturally less apparent than elsewhere. But however this may be, the essential fact to be taken into account is that a number of countries at the present time are not prepared to take part in the setting up of a new monetary system and as yet are hardly in a position to realise that such action is necessary.

CONCLUSION.

If the above analysis and review may be taken as presenting a substantially accurate view of the broad facts of the situation, certain positive lines of action would appear to be indicated.

There can be little question that the need for measures to maintain purchasing power and to stabilise the price level and the foreign exchanges will eventually make itself felt in all countries and all sections of the community. How long this process will require depends entirely upon circumstances which, in the nature of things, are wholly unpredictable. Conceivably a few months may suffice; possibly many years. The only certainty is that until conscious action is taken in this direction one or other of these problems—at times all three together—will clamour for solution. In the meanwhile it is for those countries and those sections of the community that have already appreciated this necessity to take the lead in seeing that it is met.

So far as national action is concerned the way is plain. Those countries which are in a position to realise that conscious control and deliberate international co-operation are now imperative in this sphere, must constitute the first nucleus around which the new world monetary system may eventually form. To wait hopefully for simultaneous action on the part of all the chief industrial and trading countries is time wasted and worse. Such a policy condemns those countries which have made the greatest advance in political freedom, industrial organisation and the provision of social guarantees to long drawn-out depression; while those countries where dictatorships, lack of organisation or absence of social guarantees render it still possible for drastic price and cost adjustments to be made are, in comparison, favourably placed. The immediate requirement is for a group of countries to take the first steps towards control and co-operation in the monetary field: specifically, to agree together to reinforce purchasing power to the extent necessary to revive business activity within their frontiers; to follow this up by the stabilisation of their respective commodity price levels at wholesale; and on this basis to set up an international monetary standard. As and when other countries come to appreciate the need for such measures, the group may be enlarged to receive them.

So much for national action. Within each nation are certain sections which, by reason of their peculiar position, are likely to be the first to recognise the need for active measures. There is little question which sections these are in the majority of countries.

The chief immediate victim of a financial-economic system where the volume of active purchasing power is deficient, and where the price and cost system has lost its automatic resiliency, is industry. The producer who cannot obtain a remunerative price for his product and the worker who finds his employment gone are so placed as to realise the facts of the situation long before the banking system, the professional classes, or the civil servants and politicians have fully grasped its implications. Eventually, of course, these other sections of the community will be made to apprehend the position by the logic of events, but only at the cost of great disorganisation, injustice and distress. It is incumbent upon those engaged in industry, employers and workers alike, to use their utmost influence and power to shorten the period of transition between the two monetary systems. In doing this they will be acting not only in their own interests but in the interests of the community at large. The central and unescapable fact of the modern industrial world is that a monetary system which does not take the necessary measures, national and international, to sustain a volume of buying which shall be adequate but not excessive, is a subversive and anti-social element which must not be permitted to continue.

In conclusion, it should perhaps be specifically said that monetary measures are not the be-all and end-all of the reorganisation necessary to meet the needs of the modern world. They are no more than a beginning; but, as a beginning, immensely important. Money is the medium by which the innumerable units making up the economic world are enabled to co-operate one with another. Failure on the part of this medium means disintegration—economic, social and political. It does not in the least follow that successful working of the monetary system will solve the many problems, material and moral, with which the world is at present faced. But it can be said with some confidence that so long as the monetary system fails to work little real progress towards solving these other problems is likely to be made.

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