Economics - Income (Bulky) 10c

PUBLIC AFFAIRS PAMPHLETS

INCOME AND ECONOMIC PROGRESS

BY MAXWELL S. STEWART

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Why do we have unemployment in periods of prosperity?

Do high incomes retard or promote progress?

How can we restore consumer buying power?

PUBLIC AFFAIRS PAMPHLETS
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Income and Economic Progress†

NO EVENT in history, save possibly the World War, has caused mankind as a whole such physical and mental suffering as the economic crisis which swept over the world beginning in 1929. The number of deaths in the depression may have been insignificant compared to the millions who lost their lives on the battle fields of Europe, but the sense of personal frustration, the bewilderment and anxiety suffered by tens of millions of jobless men and women have been fully as agonizing as the physical hardships endured in the war. Faced by a disaster of this magnitude, it was only natural that men should question the efficiency of our economic system. Something seemed to be basically wrong when one man out of four in the world's richest country was denied the right to earn a living, when a sixth of the population of the United States was thrown on relief, and when the national income was reduced by fifty per cent in the course of three years.

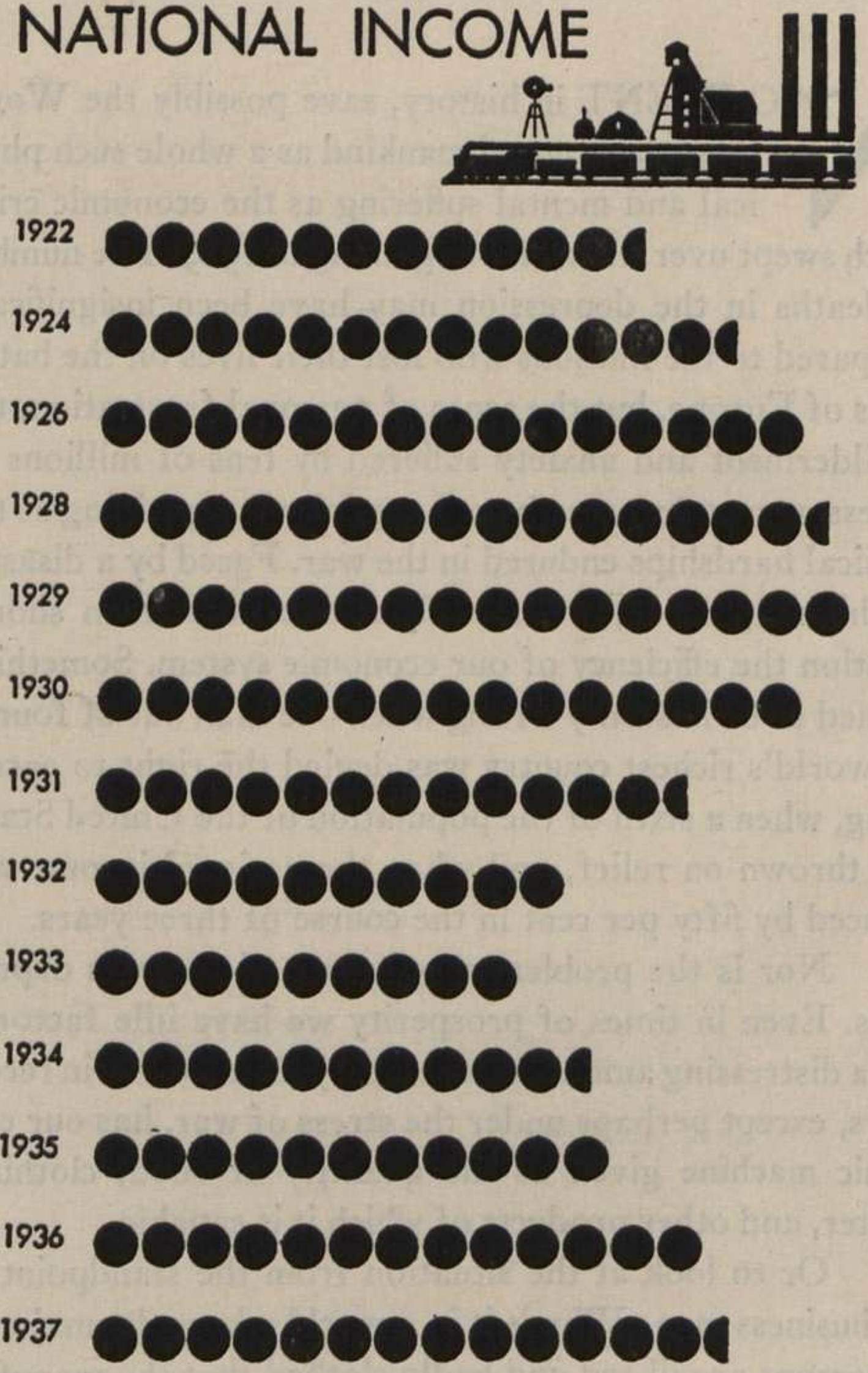
Nor is the problem simply one of periodic depressions. Even in times of prosperity we have idle factories and a distressing amount of unemployment. Never in recent years, except perhaps under the stress of war, has our economic machine given us the quantity of food, clothing, shelter, and other products of which it is capable.

Or to look at the situation from the standpoint of the business man: Why is it in a world where the majority of persons are ill-fed and badly clothed that the manufacturer and merchant encounter such difficulties in disposing

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† This pamphlet was prepared by Maxwell S. Stewart on the basis of a four-volume study by the Brookings Institution into the effect of income distribution on economic progress.

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of their wares? They would like to expand their businesses, put new men at work and create new wealth through increased production. This is the way in which economic

progress has been promoted for hundreds of years. But they dare not borrow money for expansion when they find such difficulty in selling their present output. The people who want their goods, in most instances, have not the money with which to buy them.

In the last few years we have heard a great deal about the lack of consumer purchasing power. Cranks and political charlatans have seized upon this obvious but superficial flaw in our economic mechanism as an argument for their pet nostrums. Every raid on the government treasury has been defended as adding to the buying power of some particular group. Actually, of course, the solution is not as simple as these persons would make it appear. The economic well-being of any country depends on two factors: (1) the amount of real wealth—such as food, clothing, houses, and recreational facilities—which is produced and available for consumption; and (2) the manner in which this total product is divided among the various classes which make up the population. If we seek to discover the source of our economic difficulties, it is necessary to examine both of these factors.

DIAGNOSIS

Can We Produce Enough?

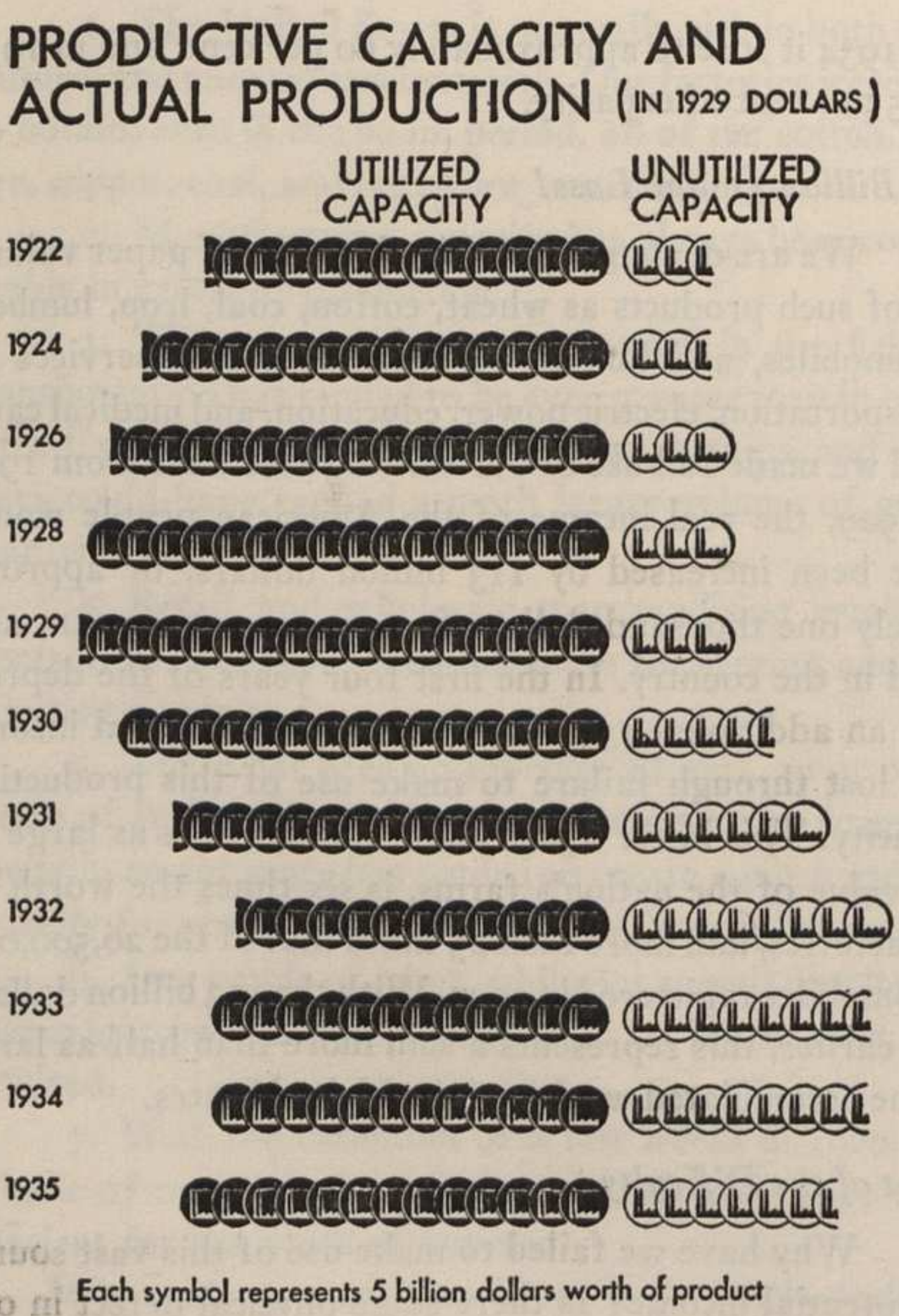
OUR first task is to investigate the productive capacity of the United States to see whether it is adequate to our demands upon it. Such a survey was the first of four studies undertaken by the Brookings Institution, and the results are incorporated in their publication, **America's Capacity to Produce.** This study does not attempt to predict what increase in production could be brought about

by reform or reorganization of our economic system. Nor does it seek to forecast the effect of future scientific discoveries. It merely endeavors to find out what portion of our industrial and agricultural capacity was allowed to stand idle at the height of American prosperity.

20 Per Cent Unused Capacity

It shows, for instance, when business activity was at its peak in 1929 the total output of America's farms, mines, factories, and service industries was only about 80 per cent as large as it might have been had all our physical and human capacities been utilized. In individual industries the amount of idle plant varied from 15 to 30 per cent, with 20 per cent a very conservative estimate for our economic machine as a whole. For the five-year period 1925-1929, the amount of slack was approximately 22 per cent. A similar survey was made of the war years, when every effort was being made to speed up the nation's industrial machine, and it was found that under this stimulus production actually expanded 15 per cent without the addition of new plant. This seemed to confirm the accuracy of the 1929 estimate.

Until the beginning of the depression in 1929 there was no tendency for this unused capacity to increase. The problem was a chronic one, but there was no indication of a growing overproduction of industrial plant such as was alleged to have existed. During the depression, however, the amount of unused equipment became much greater, as can be seen from the chart on the following page. This chart is adjusted for changes in the price level, and therefore accurately reflects year to year changes in physical production. At the depth of the depression in



1932 the total amount of goods and services produced in the United States was approximately 31 per cent less than in 1929. Assuming that productive capacity had remained stationary since 1929, it will be seen that the actual output was only 55 per cent of the possible production. In 1933

and 1934 it rose to approximately 60 per cent, and in 1935 to 65 per cent of capacity.

248 Billion Dollar Loss!

We are dealing here with a loss, not of paper values, but of such products as wheat, cotton, coal, iron, lumber, automobiles, and homes, together with such services as transportation, electric power, education, and medical care. Had we made full use of our existing resources from 1922 to 1929, the real income of the American people would have been increased by 113 billion dollars, or approximately one thousand dollars for every man, woman, and child in the country. In the first four years of the depression an additional 135 billion dollars of potential income was lost through failure to make use of this productive capacity. This latter figure alone is four times as large as the value of the nation's farms, is six times the worth of its factories, and more than 25 times that of the 26,500,000 automobiles registered in 1929. With the 113 billion dollars lost earlier, this represents a sum more than half as large as the accumulated wealth of the United States.

Root of the Difficulty

Why have we failed to make use of this vast source of potential income? Is there some physical defect in our economic mechanism that prevents us from taking advantage of our surplus plant capacity? The complex process of production includes a whole series of operations. It is conceivable that a weakness in any one of these processes could seriously handicap production as a whole. We find, however, on examining each of these steps, the following to be the situation:

1. The United States is unusually rich in both agricultural and mineral raw materials. Our factories were able to obtain, even in the boom period, all of the cotton, iron ore, copper, coal, and other raw materials required.

2. Manufacturing capacity has always been considerably in excess of production.

3. The amount of excess capacity in the field of transportation has tended to be even greater than in other lines. Except during the war, our railways, ships, and highways could have carried a much larger volume of goods than was actually produced.

4. Retail and wholesale merchandising establishments have been more than adequate for storing and distributing goods to the consumer.

5. There has been no shortage of coal, oil or other forms of fuel. In fact, the development of new forms of power in recent years has tended to create a much greater capacity for power production than is likely to be needed.

6. Our supply of labor, while not as well distributed as it might be, has always tended to be larger than was required.

7. With the exception of a few weeks in 1920, the volume of money and credit has always been more than sufficient for the needs of business.

It is evident, then, that there is no bottle neck on which we can blame our failure to make use of our full productive possibilities. Every part of our productive machine would be able to carry a much heavier load than is normally placed upon it. The question then arises whether our inability to create this potential wealth is not due to the inevitable friction associated with economic growth. Does not the very process of technological advance, with

its continuous scrapping of out-of-date machinery, necessarily involve lost motion?

Lack of Markets

These factors are undoubtedly important, but they were taken fully into consideration in the estimate of productive capacity. We are forced to conclude, therefore, that the failure to operate at full capacity is not due to any discernible weakness in our productive machine as such. The plant, the raw materials, the transportation and distribution facilities, and the labor supply are adequate for a much larger output than we have been obtaining. No technical flaws exist either in the productive process or in the financial system which prevents us from enjoying a much higher standard of living. Moreover, business men would like nothing better than to expand their production, but they encounter extreme difficulty in disposing of their present output. The vast amount of money which is spent on advertising, the growth of high-pressure salesmanship, the emphasis on installment buying, and the energy which is consumed in the search for new markets, all indicate that the problem of American business is not how to increase output but how to sell that which has been produced.

Division of the Output

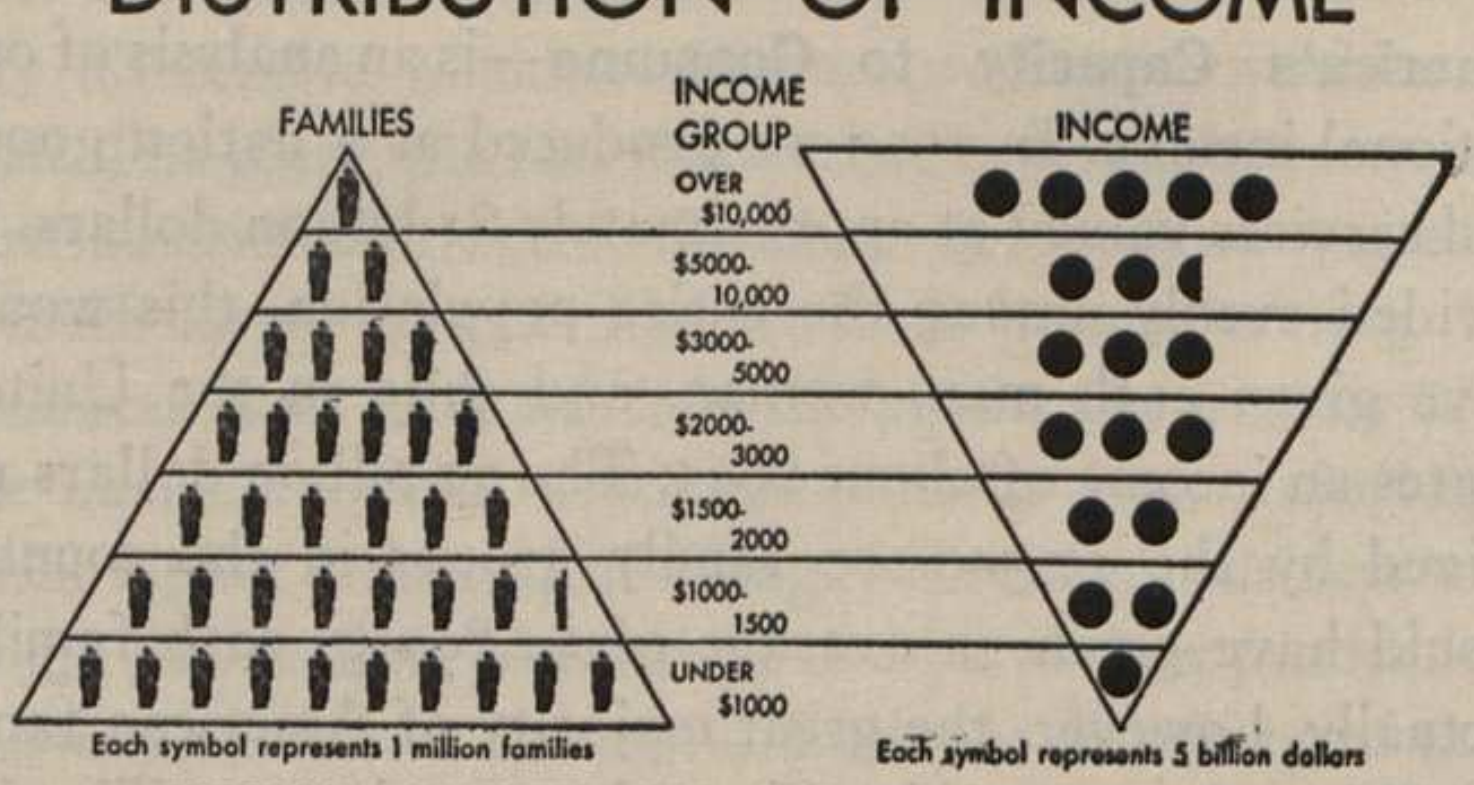
We have not gone so far as to state that America's farms and factories can produce enough to satisfy all of the needs of our population, but we have indicated that they are capable of turning out far more than they have in the past sixteen years. It would be useless, therefore, for us to turn to an engineer for a solution of our problem. Our job is to find some way of bringing into operation

what the engineer has already created. Since the flaw is not to be found in the process of production, let us examine the way in which the goods and services that have been produced are divided up among the population. It is possible that we shall find here not only the cause for the distress of certain groups, but also the key to the problem of unused capacity.

The second of the Brookings Institution's studies—**America's Capacity to Consume**—is an analysis of our national income. In 1929 we produced as a nation goods and services valued at approximately 81 billion dollars. If divided evenly among the entire population, this would have given each man, woman, and child in the United States an income of about $625. The 77 billion dollars received by the 27,500,000 family groups in the country would have given an average of $2,800 to each family. Actually, however, the great majority of American families did not have anything like so large an income. The distribution for families and unattached individuals is shown in the chart on page 10. Of the families only, 6 million —or 21.5 per cent—received less than $1,000 in 1929; 12 million had incomes under $1,500; over 16 million had less than $2,000; and more than 19 million, or 71 per cent of the total, were below $2,500. Only about one family out of twelve received as much as $5,000. At the other end of the income scale we find that 220,000 families, approximately eight-tenths of one per cent of the entire population, got over 20 per cent of the total national income. The 36,000 families at the extreme pinnacle of the income pyramid received in the aggregate an amount equal to that obtained by the 12 million families with incomes less than $1,500—or over 300 times as much per family.

At 1925 prices, a family income of $2,000 was sufficient to furnish only the basic necessities of life, and yet we find that 60 per cent of the total number of families were below this level. If we accept the model diets worked out by the Bureau of Home Economics of the Department of Agriculture as standards, we find that 74 per cent of

DISTRIBUTION OF INCOME



PICTORIAL STATISTICS, INC., FOR PUBLIC AFFAIRS COMMITTEE, INC.

America's urban and village families lacked sufficient income in 1929 to provide an adequate diet at moderate cost. Only one family out of ten could enjoy a liberal diet without denying itself the comforts which are normally associated with this standard of living.

From this we may conclude that the basic wants of the American people were by no means satisfied even during the period of greatest prosperity. The failure of our economic system to operate at full capacity was not due to the fact that people did not want to buy goods, but was the result of their inability to obtain enough money to purchase the things which they desired. If the incomes of the 19 million families receiving less than $2,500 in 1929 had been raised to the $2,500 level, the United States would

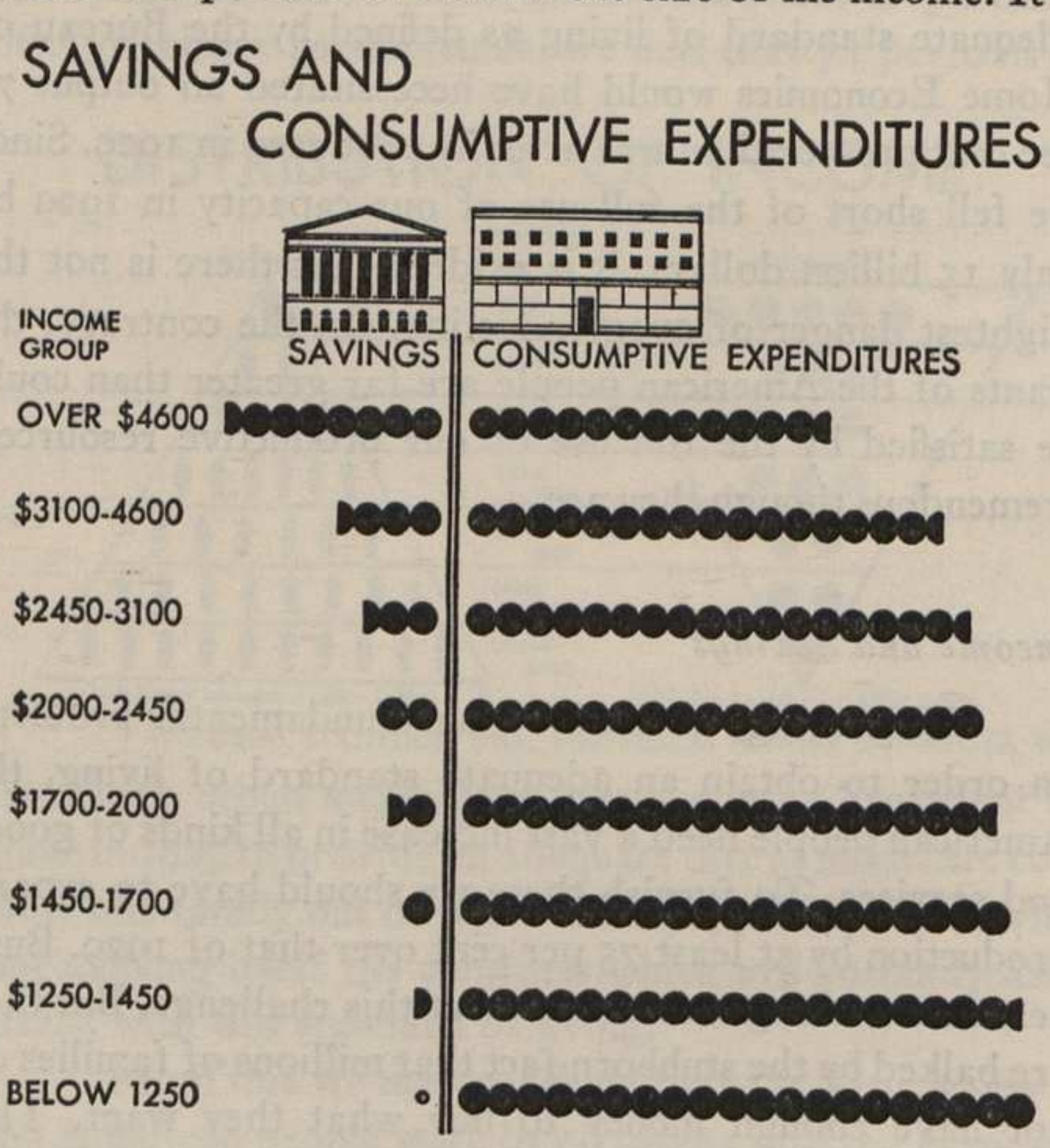
have had to increase its total production by 16 billion dollars in order to meet the new demands of these families. An increase of $1,000 in the income of every family receiving less than $5,000 would have required an expansion in output of over 25 billion dollars. To give all families an adequate standard of living as defined by the Bureau of Home Economics would have necessitated an output 75 per cent greater than was actually produced in 1929. Since we fell short of the full use of our capacity in 1929 by only 15 billion dollars, it is evident that there is not the slightest danger of overproduction. On the contrary, the wants of the American people are far greater than could be satisfied by the full use of our productive resources, tremendous though they are.

Income and Savings

This brings us back to our fundamental problem. In order to obtain an adequate standard of living, the American people need a vast increase in all kinds of goods and services. To furnish these we should have to expand production by at least 75 per cent over that of 1929. Business men are eager to try to meet this challenge. But they are balked by the stubborn fact that millions of families do not have enough money to buy what they want. This lack of purchasing power should not be taken to indicate, as some writers contend, that the market price of commodities exceeds the amount of money distributed in the process of production. This is impossible, since every dollar which is spent for an article goes to someone—whether as wages, rent, interest, or profits—and may be re-spent by him. If consumers do not buy all the goods on the market,

it can mean only one thing: someone does not wish to spend his money, preferring to lay it aside for a "rainy day."

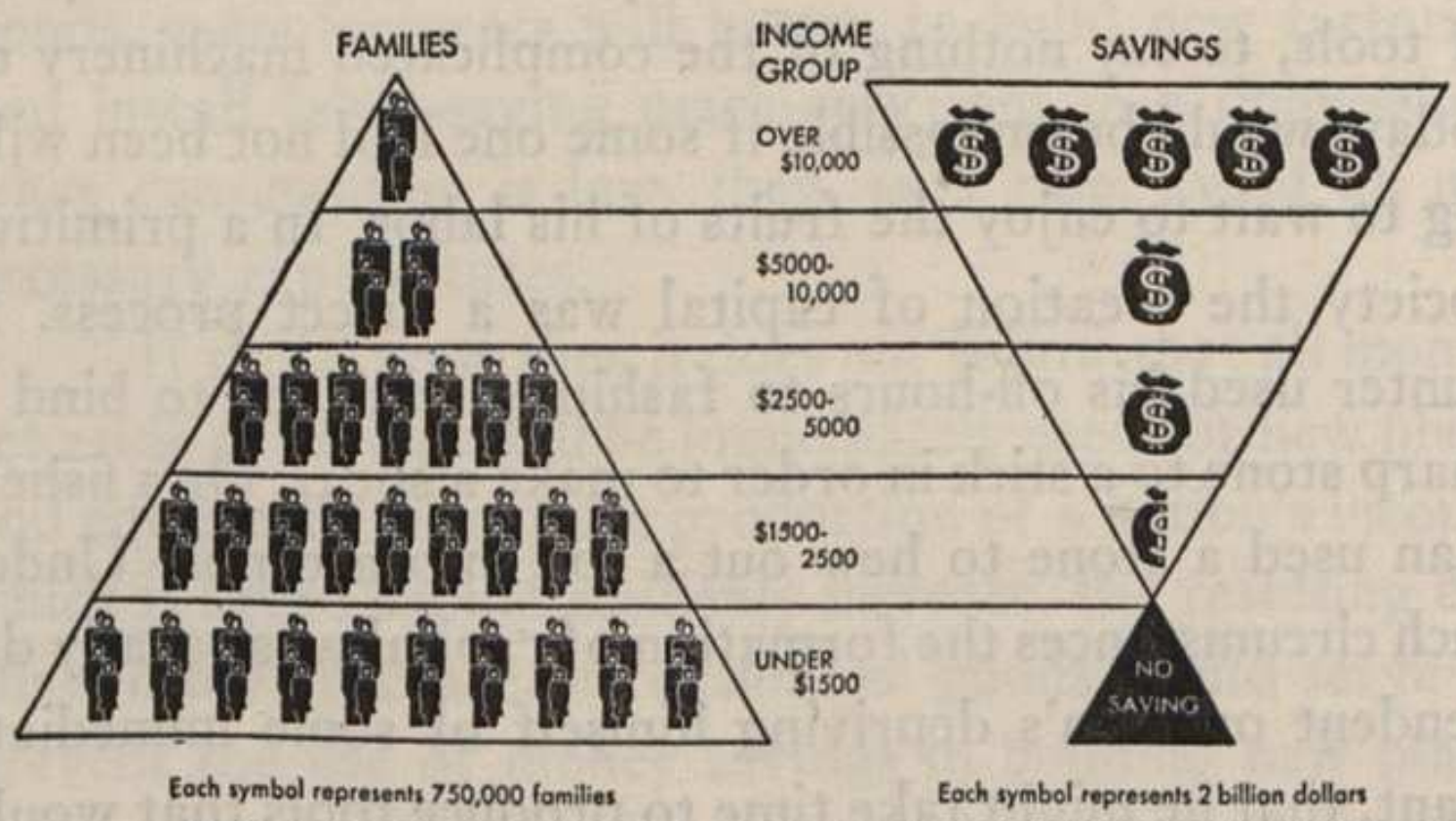
Many factors will influence a man in determining what share of his income shall be set aside as savings, but the most important of these is the size of his income. It is



practically impossible to save on a very low wage. But when an individual's earnings mount into the tens or hundreds of thousands, he finds it increasingly easy to save a substantial part of his income. Consequently, the greater the proportion of wealthy persons, the greater will be the

amount of savings. A glance at the following chart will reveal, for example, that out of a total of 15 billions of dollars of individual savings in 1929, no less than 12 bil-

SAVINGS OF NON-FARM FAMILIES



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lions were accumulated by the 10 per cent of the population possessing incomes of over $5,000. Families obtaining over $20,000 annually were able to save more than half of their total incomes, while those receiving less than $1,500 spent, on the average, more than they earned. It is scarcely surprising, therefore, that two-thirds of the savings of the American people should be made by the 2 per cent of the population having incomes of over $10,000 a year.

Since the relative number of individuals in the higher income groups increased more or less continuously from 1900 to 1929, it is only natural that the proportion of the national income set aside as savings should have risen during this period. This tendency was especially marked during the late twenties when the number of large incomes reached their peak.

The Importance of Savings

The fact that a large or even an increasing share of the nation's income goes into savings rather than into expenditures for living purposes does not necessarily indicate any weakness in our economic system. Even the simplest of tools, to say nothing of the complicated machinery of today, would be impossible if some one had not been willing to wait to enjoy the fruits of his labor. In a primitive society the creation of capital was a direct process. A hunter used his off-hours to fashion a club, or to bind a sharp stone to a stick in order to make a spear. Or a fisherman used a stone to hew out a log into a canoe. Under such circumstances the formation of capital was usually dependent on man's depriving himself of some immediate want, that he might take time to produce tools that would subsequently enable him to work more easily or more effectively.

Savings and Capital Formation

But in modern industrial society the creation of capital is not such a direct process. While it has generally been assumed that all money which was saved was automatically used for the construction of capital goods—such as factories, railways, machinery, and agricultural implements—no attempt has been made until recently to test this assumption scientifically. The third study of the Brookings Institution—**The Formation of Capital**—challenges this assumption.

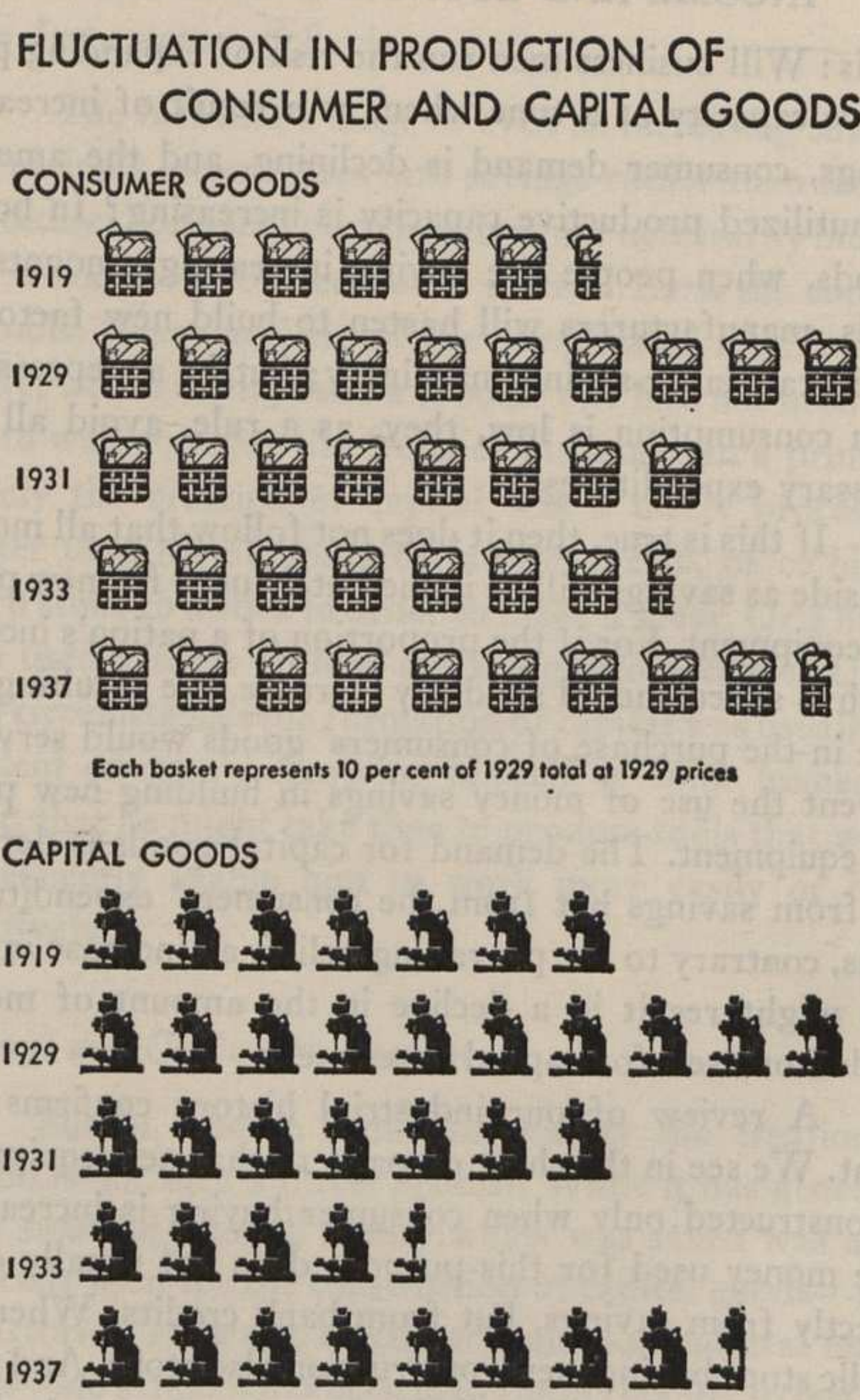
Obviously, money savings will be used to build new plant and equipment only if it pays to do so. The ques-

tion is: Will business men run the risk of expanding productive capacity at a time when, as a result of increased savings, consumer demand is declining, and the amount of unutilized productive capacity is increasing? In boom periods, when people are buying increasing amounts of goods, manufacturers will hasten to build new factories and install labor-saving machinery; but in a depression, when consumption is low, they, as a rule, avoid all unnecessary expenditures.

If this is true, then it does not follow that all money set aside as savings will be immediately used for new plant and equipment. For if the proportion of a nation's income which is saved should suddenly increase, the resulting decline in the purchase of consumers' goods would serve to prevent the use of money savings in building new plant and equipment. The demand for capital goods is derived not from savings but from the consumers' expenditures. Thus, contrary to the prevailing belief, an increase in savings might result in a decline in the amount of money needed or used for capital investment.

A review of our industrial history confirms this point. We see in the chart on page 16 that new equipment is constructed only when consumer buying is increasing. The money used for this purpose does not usually come directly from savings, but from bank credits. When the public stops buying, new construction also stops. And what is more conclusive, it reveals that the *rate of growth* of new plant and equipment is closely linked with changes in consumer buying power—which it follows—and that the trend of capital construction is frequently directly opposite to that of money savings.

The amount of savings available for investment, for



example, rose rapidly between 1922 and 1929; but the volume of securities floated for building new plant and equipment showed no such increase. In 1929 there was a

reservoir of savings available for investment amounting to 15 billion dollars, while the sum actually invested in new construction and mortgages was only about 5 billion. The excess went either into the stock market, where it contributed to the unhealthy boom prices and was ultimately lost, or into foreign loans, which were also larger than was desirable. Since 1929 there has been practically no demand for capital expansion, and the surplus funds have in part stagnated as bank deposits, in part been used to finance government deficits, and in part to bid up the prices of securities.

The Basic Defect

The source of our economic difficulties, then, is evident. There is no physical obstacle to the full utilization of our productive capacity. The difficulty is to be found rather in the unequal distribution of income and a resulting excess of savings as compared with consumptive expenditures. Our diagnosis is not complete, however, until we learn why it is that the tendency toward a concentration of wealth and over-savings has been more marked in the post-war period than in earlier years.

Throughout the first century and a quarter of our national existence our savings were not large enough to supply funds for all of our needed capital equipment. The deficiency was made up by borrowing from foreigners and through bank loans. Our railways, for example, were built largely with British funds, and supplied—at one stage—with British equipment. In the past twenty years the situation has been sharply reversed. The tremendous profits

made during the war provided more funds than were required for domestic plant expansion.

Price Stabilization

Added to this was another factor, making for an increased concentration of wealth. The twenties were marked by unprecedented technological progress. Productivity *per wage earner* in the manufacturing industries increased by more than 25 per cent between 1922 and 1929. Under a system of free competition, the pressure of competition would force business men to reduce prices in proportion to the increased efficiency of their plants. The only factor which might keep prices up would be a tendency for increased wages to counterbalance the decline in other costs. But let us see what actually happened to prices and wages during the boom years.

Retail prices showed practically no change between 1922 and 1929. Wholesale prices, particularly of manufactured goods, dropped slightly during the period, but the decline was not comparable to the increase in productivity of labor. Whatever decline occurred in wholesale prices was absorbed by the marketing process, and the ultimate consumer reaped no benefit. It should not be assumed, however, that all the profits resulting from the failure of prices to fall in accordance with increased efficiency went to the owners of capital. In the manufacturing industries it is estimated that higher wages absorbed about 40 per cent of the gain, lower prices a like amount, with the balance going for profits. Considering the relatively small number of stockholders, even this division served to accentuate the concentration of income in the hands of a privileged few.

The Trend Toward Monopoly

But why did this inflexibility in prices not occur in former-times? It is apparent that some new factor or factors have arisen to prevent the competitive system from functioning normally. Indeed, the tendency toward rigid prices had its beginnings as far back as fifty years ago, and exists in practically all industrial countries. It is a direct result of the development of three new types of business organization. The first and most important of these is the unified monopoly or trust, where a single concern dominates the market sufficiently to be able to set prices more or less at will. The second is the cartel, found chiefly in Europe, under which a group of producers agree to control production with a view to stabilizing prices. The third, the trade association, is essentially an American development; such associations usually seek through informal cooperation to stabilize conditions in an industry without exercising a rigid control over output.

All of these combinations may be regarded as the normal development of the trend toward large-scale enterprise, which in turn is based on the greater efficiency of mass production. When a corporation finds itself in a position to fix prices, it usually seeks to establish them at a level which will yield the highest possible profit. This may not lead to exorbitantly high prices, for the company must consider the volume of sales which may be obtained at a given level. But there is a tendency to take a short-sighted view and seek the highest possible profit from year to year, rather than to look for larger ultimate profit through a gradual expansion of the market. Where governments have

either entered or sought to control business, there has also been a tendency toward price stabilization.

Profits

If we have been correct in asserting that many business concerns have failed to pass on by lower prices to the consumer the advantages gained from technical improvements, we should expect to find that profits and dividends increased more rapidly during the post-war period than the volume of business, wages, or salaries. And such indeed was the case. Both the volume and the rate of profits in manufacturing industries advanced considerably from 1922 to 1929. The rate of increase was the greatest, moreover, in the largest and more efficient corporations.

LINES OF PROGRESS

OUR diagnosis is now complete. We have found the root of our difficulty in a concentration of income brought about by the price-fixing policies of monopolies and trusts. Our problem now shifts from that of diagnosis to that of prescription. How can the flow of income to various classes in society be modified so as to increase consumer buying power and stimulate a greater volume of production? What approach to this problem is most likely to lay the soundest basis for economic progress?

Merely to redistribute our existing income equally among the entire population would obviously not solve our problem. If the whole of America's national income had been thus divided up in 1929, each person would have received about $625, or approximately $2,800 per family. While this is substantially more than was obtained by most American families during that year, it was not, as we have

already observed, enough to provide a satisfactory standard of life. If we are to fulfil the basic needs of the American people, it is evident that the total national income will have to be expanded far beyond the present level. This indicates that our primary task is that of discovering a means of increasing production.

Taxation and Income Division

One of the most widely discussed methods of achieving a more satisfactory division of income is that of taxation. This has definite promise, but does not meet all of the problems. The obligations of the government to care for jobless men and women during periods of economic stress is accepted today by all advanced countries. But the permanent support of any considerable portion of the population in idleness would be clearly wasteful. An increase in real living standards can only come by putting persons to work in useful occupations, whether employed by the government or by private industry. Much the same may be said with regard to social insurance. Protection against the uncertainties of modern life may be necessary as a matter of permanent policy, but it does not constitute a final answer to our problem. Insurance is merely a device for transferring the risks of life from the shoulders of individuals to those of society as a whole; it cannot in itself bring about any substantial increase in general living standards.

Public Works

Government public works are in a somewhat different category. Here work is performed and wealth created. It is evident that there are certain services that can be more

satisfactorily furnished by public than by private enterprise. These include the postal service, public schools, highways and waterways, public parks and buildings, forest and reclamation projects, and, to a certain extent, gas, electricity, and municipal transportation. Beyond this somewhat restricted field, however, it is difficult to find enterprises that do not conflict fundamentally with private interests. This means that any gigantic program for giving employment through government-financed projects must either include a certain amount of "boondoggling"—i.e. enterprises whose usefulness is scarcely equal to the effort expended upon them—or interfere with private business. The question is not so much whether a given form of public works is useful or not—presumably all such projects are useful in the broadest sense—but whether the labor and capital might not be more valuably employed. As long as millions of Americans have an inadequate diet, are improperly clothed, and are compelled to live in unsanitary and unsightly dwellings, we are not reaching the heart of our problem by building roads, public parks, post offices and eliminating grade crossings—valuable though these services may be.

In order to make this point clear, let us assume that the government has launched a gigantic PWA, putting ten million men at work on utterly useless projects at a wage of, say, six dollars a day. The government would be spending nearly 20 billion dollars a year for wages; the PWA workers would have a vastly increased buying power; but no additional food, clothing, houses, or automobiles would have been created, nor could these be produced if all the idle manpower was engaged in non-productive government enterprises. The result would be that the PWA workers

would obtain goods that previously went to the regularly employed portion of the population, but the country as a whole would be no wealthier than before. The forty million who are employed would merely be digging into their pockets to aid the ten million who are now jobless, and we would not be utilizing our idle capacity to increase living standards for all.

Raising Money Wages

A more direct means of expanding the purchasing power of the lower income groups is through an increase in money wages. Belief that such action will eliminate the basic causes of cyclic depressions has always been one of the fundamental principles of the American Federation of Labor, and, indeed, played an important rôle in determining the policies of the NRA. Even before the crisis, the doctrine of high wages as the guaranty of American prosperity was widely accepted by business groups as well as by the official labor movement. Although the argument is similar, we have here really two separate contentions: (1) that an increase in wages is necessary to bring about recovery in a period of depression; and (2) that high money wages are essential for promoting permanent economic progress.

Increased Wages under the NRA

Perhaps the most satisfactory way of examining the first of these contentions is by analyzing the wage-raising program of the NRA. The theory underlying this program was extremely simple. An increase in wages, it was urged, would expand the buying power of the masses and thereby bring about a larger volume of production, which, in turn,

would put more men at work. These newly employed men would spend their wages for additional goods, and thus set into motion the perpetual wheel of recovery. The increase in money wages was not looked upon as a measure of reform, but rather as a device for stimulating the entire economic system.

It was generally recognized that prices were bound to rise along with wages. But it was hoped that higher prices could be deferred until the working class had enjoyed the benefits of their increased wages. The President himself stated this clearly when he declared at the time of the passage of the Recovery Act: "We cannot hope for the full effect of this plan unless, in the first critical months, and, even at the expense of full industrial profits, we defer price increases as long as possible."

Despite the fact that wages were expected to rise more rapidly than prices, it was not believed that profits would suffer permanently. On the contrary, the view was widely expressed that the greater volume of business which recovery would bring would increase industrial earnings, even though the profit on each item might be reduced. In theory this was sound enough, because many industries were operating at 20, 30, or 40 per cent of capacity, and any increase in activity greatly decreased the burden of fixed overhead charges. Actually, however, many serious obstacles were encountered. Irrespective of the prospect of increased earnings, it was necessary for many business concerns to advance the money for wages many months before the returns of the enlarged sales could be obtained. Some establishments had sufficient surplus on hand to pay these wages out of their own funds. But there were many companies whose financial situation was so precarious after

years of depression that they could not even borrow the money. Since the NRA had no control over prices, it was perhaps inevitable that these concerns, and probably some which were not so hard hit, should seek to recoup the wage increases by a simultaneous rise in prices. In fact a considerable increase in prices occurred in June and July, 1933, in anticipation of the advance in wages. Thus instead of prices lagging behind wages, as the President had requested, the reverse tended to be true.

Obstacles to Increasing Money Wages

Many of the obstacles encountered in the attempt to expand mass buying power through the NRA codes were perhaps exceptional. The situation at the time was peculiarly suitable for an increase of prices equal to or exceeding the rise in wages. But in a competitive system an advance in wages is always difficult to obtain. Most business men find payrolls not only to be the largest element in their costs, but also the most flexible. If an employer can reduce the amount paid to his workers, he immediately has an advantage over his competitors. Whatever the effect of low wages may be on the economic system as a whole, an individual business enterprise is undoubtedly the gainer if it can reduce its wages below the market rates. Similarly, most concerns hesitate to raise their wages above the level of their competitors, lest they be underbid in the struggle for markets. Under the competitive system it is only to be expected that each concern shall pay the lowest amount possible for labor and raw materials. Only where employers believe that high wages pay dividends in increased efficiency are they likely to advance wage rates willingly.

Indeed, experience has shown clearly that we cannot rely on voluntary increases in money wages for our needed expansion of consumer buying power. Wage increases are usually obtained only as a result of pressure from organized labor, or when there is an actual scarcity of workers. And since business concerns tend to pass on their increased costs to the consumer, a boost in wages usually brings no net gain to society as a whole. One group of workers merely profits at the expense of the remainder of the population. As a matter of fact, wage earners constitute a smaller proportion of the American consuming public than is generally realized. Out of a total population in 1930 of over 122 million, nearly 45 million dwelt on farms while an additional 14 million lived in towns of less than 5,000 inhabitants. Even a considerable part of the urban population of 63 million are non-wage earners. Thus the workers likely to be affected by a program of wage increases do not constitute more than 40 per cent of the gainfully employed. Nor are they necessarily the group which is most greatly in need of increased buying power. The per capita income of the farm population was only $273 in 1929, and in many regions, particularly in the South, it averaged much lower. Obviously any plan which is to bring permanent economic progress to the United States must benefit the farmer as well as the wage worker.

This is not to imply, of course, that an increase in wages is not economically desirable. On the contrary, a study of wages and prices over the past century reveals that the gradual rise in living standards during that period is attributable both to advancing money wages and declining prices. Unfortunately, however, it is difficult to convince the average employer regarding the desirability of

high wages. Where better wages have been won through the pressure of organized labor, the cost in terms of social struggle has been so high as to call in question the desirability of concentrating solely on this goal.

Fortunately this is not necessary. Adding to the number of dollars in a man's pay envelope is not the only way of increasing his buying power. If his weekly wage remains unchanged and the prices of the things which he buys decline, he is as well off as if he had obtained a raise in pay. There have been extended periods in American history—particularly between 1865 and 1895—when precisely this happened, and these were relatively good years for American labor.

Lowering Prices

If we would turn back a century to the writings of the classical economists, we would find that they faced the problem of income distribution, and that they too recognize the necessity of continually expanding mass purchasing power. It might be helpful for us today to recall their solution of the problem. They pointed out that under a system which operated under the incentive of private profits, each business manager will strive in every possible way to reduce his costs. He may achieve this by installing more modern machinery, by organizing his business more intelligently, or by building a larger, more efficient plant.

Having reduced costs he has two choices before him: He may continue to sell at the old price and pocket the difference between his old costs and the new ones. Or if he is ambitious, he may seek to increase the volume of his business by cutting his prices—hoping that by expanding his market he may make even greater profits than if

he had kept his prices up. Since larger sales make possible even lower costs, he will usually choose the latter plan—at least this was the theory of the great economists of the 19th century.

Thus, according to theory, the pressure of competition should gradually reduce the selling prices of commodities and thereby stimulate consumer demand. And unlike wage increases, this method of expanding buying power is fully in line with the principles of our existing economic system. Reduction of prices when accompanied by a corresponding cut in costs does not threaten the profits of a business concern. Indeed, it is the gateway to increased earnings. Instead of modifying or "reforming" of the capitalistic system, the policy of price reduction, if carried out, would restore that system to working efficiency.

Wages Must Be Maintained

But this method can only be successful if the general level of wages is maintained while prices decline. If wages are cut in proportion to the reduction in prices, there will be no increase in mass purchasing power and no expansion in the demand for goods. Needless to say this simple fact has been ignored by many business managers. To many of these, wage cutting has appeared to be the easiest way of reducing costs and of gaining a competitive advantage over rival companies. This line of reasoning is sound as long as only one concern practices this policy, but it falls down when, as in 1930-1932, all business concerns begin to cut wages simultaneously. If all wages are cut by, say, 20 per cent, the buying power of a large section of consumers will be reduced by 20 per cent. Moreover, since competitors are almost certain to cut their wages by at least as

much, no advantage is gained over them. As a matter of fact business as a whole is worse off than before, because there are certain fixed costs, notably interest and overhead, which cannot be reduced as readily as prices and wages.

Fortunately, although there is always strong pressure upon managers for the reduction of wages, there are also pressures for stabilizing or increasing them. When business is good, skilled labor is usually somewhat difficult to obtain. Moreover, labor organizations have tended to grow in strength in recent years, and have made it increasingly difficult for business concerns to reduce wages even in periods of depression. From the standpoint of the basic principles of the competitive system, labor's firm opposition to wage cuts has proved distinctly helpful.

Advantages of Price Reduction

Perhaps the chief advantage of price reduction as against wage increases as a means of stimulating consumer buying power lies in the fact that everyone is a consumer, while less than half of us are wage earners. Millions of individuals who do not earn their living by wage labor would share in the benefits of lower prices. A 10 per cent reduction in the cost of living would mean that every person could buy as much as he does now with 90 cents on each dollar, leaving him with one-tenth of his income to spend for the things which he has always wanted. This would necessitate an immediate increase in production of at least 10 per cent.

It is true that the rich consume more than anyone else, and that their gains from lower prices would seem to conflict with the need for redistributing income. The fact is, however, that while the rich as individuals consume far

more than the poor, the total outlay for living expenses of families receiving more than $100,000 in 1929 was only 6 per cent of the aggregate amount spent by all American families—though their income was 11 per cent of the total. On the other hand, families earning less than $3,000 exercised half of the buying power of the country.

Can Our Economic System Meet Our Needs?

Inherent in our findings is a basic challenge to the American people. Can we, within the limits of our resources and without a drastic change in our economic or political order, provide a standard of living at least as high as we have known in the peaks of prosperity in the past? Can we go beyond this and give every citizen a standard equal to that of the so-called "middle class" in 1929? The answer is, yes, provided we make certain adjustments.

We possess an unutilized plant capacity capable of increasing materially the living standards of the masses. But to fill the unsatisfied needs of the 92 per cent of our families who are now below the $5,000 level would not only absorb all of our existing idle capacity, but would require a considerable expansion of our productive equipment. Since the failure to make use of our full capacity is attributable to the lack of buying power on the part of the consumers whose wants and needs are the greatest, it is evident that anything which increases that buying power will stimulate production. Taxation is a possible means of redistributing income, although tax-supported public works tend to stimulate the production of non-essentials as contrasted with such primary wants as food, clothing, and shelter. The general raising of wages as a device for redistributing income also has definite possibilities. Its weakness

lies in the fact that over half the population, including many of the poorest groups, are not wage earners.

Consumer buying power would also be increased if industry revised its price policy and passed on to the ultimate consumer all of the benefits which it obtained from technological progress. This method has an advantage over the others in that it does not run counter to the profit motive, but actually gives promise of greater profits through increased business activity. A reform of this type would not be an attack on the capitalist system, but a return to the very logic upon which that system was justified by the classical economists of the 18th and 19th centuries.

Nevertheless, the practical application of the program of price reduction implies a direct attack on one of the chief abuses of the profit system as we know it today—the trend toward monopoly and industrial combinations for the purpose of stabilizing prices. The growth of this tendency can be traced in the past fifty years in the emergence of trusts, pools, cartels, trade associations and holding companies. Even governments have frequently aided in this process on the theory that they were promoting "business stability." Whatever the purpose lying behind this trend, the result has been a concentration of wealth and economic power which has become the chief barrier to present-day economic progress.

We cannot attain our ultimate objective as long as these abuses remain. The underlying purpose of business is to serve people; indeed only as it serves people can it serve its own best interests. If an enterprise merely serves a small group cautiously, restricted at every turn lest the owner's advantage might be lessened by passing on the benefits of new knowledge or better methods, it will find its own de-

velopment stunted by lack of opportunities. True economic progress implies something far broader than this. It must be compatible with the wealth of our resources, with the power inherent in modern scientific knowledge, and with a skilled and intelligent labor force. And above all we must realize that the economies of mass production can only be realized in an economy of mass consumption.

Opening New Markets at Home

There are those who look to the opening of some new market, or to some new invention to furnish the stimulus to lead the world out of the existing depression. They point to the growth of the West as the primary factor in overcoming the crisis of the 70's, and to the commercial development of the automobile and the radio as an important element in the prosperity of the 20's. Today we have no more continents to exploit and apparently no great new invention which is likely to regenerate our economic life. This does not mean, however, that we must resign ourselves to a period of economic stagnation. We have untapped wants within our population sufficient to absorb the fruits of technological development for years to come. Merely to put the common necessities of food, clothes, and houses within the reach of the millions who are undernourished, shoddily clad and sheltered in the filthy tenement of the city or the weather-beaten shack of the country, would open up a tremendous field for business expansion. With abundant natural resources, an ample supply of financial capital and an apparent surplus of trained workers, we could furnish at least these necessities if our system of distribution were readjusted along the lines indicated.

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