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25TH JUNE, 1942.

WAR CABINET

OFFICIAL COMMITTEE ON POST-WAR INTERNAL ECONOMIC PROBLEMS

REVISED DRAFT INTERIM REPORT

Note by the Secretary

In connection with Conclusion 3 of the Minutes of the last meeting on 19th June, I circulate herewith the Revised Draft Interim Report and a note by the Chairman under cover of which it is proposed to circulate the Draft Interim Report, together with I.E.P.(42) 21 ("The Post-War Relation between Purchasing Power and Consumers' Goods" by the Treasury), to the Ministerial Committee on Reconstruction Problems. If no amendments are received within 3 days, the concurrence of members will be assumed and the documents will be presented to the Ministerial Committee.

(Sgd.). A. BASTER.
Secretary.

Richmond Terrace, S.W.1.
25th JUNE, 1942

PAPERS SUBMITTED BY THE OFFICIAL COMMITTEE ON INTERNAL ECONOMIC PROBLEMS

1. Interim Report of the Committee on:
"The Internal Economic Problems of the Post-War Transitional Period".

2. Memorandum prepared by the Treasury on:
"The Post-War Relation between Purchasing Power and Consumer Goods".

COVERING NOTE

1. The Interim Report of the Committee is submitted in fulfilment of the undertaking given in its Progress Report of 16th May, 1942 (R.P.(42) 11), to prepare a survey on "the major features of the general economic position in the years immediately after the war". It is, therefore, confined to the post-war transitional period, only touching on the immediate post-armistice problems and the longer-run problems of reconstruction, in so far as these are relevant to the consideration of the transitional period.

2. In considering this transitional period, the most important question is whether it will be a period of short supplies and of high demand for civilian goods (such as we are experiencing during the war), or whether we must be prepared to face the problems of deficient demand and of relatively abundant supplies, such as have accompanied periods of general trade depression in the past. The Memorandum by the Treasury is devoted to this question. After the last war, there was an inflationary period of excess demand and of short supplies, and many reasons are given in the Treasury document for believing that this war will be followed by a similar period of shortages and of threatened inflation, but of longer duration. The return of men from the armed forces to civil production will probably not be so rapid as after the last war; physical destruction (and the consequent need for replacement) of capital assets will be much greater; the restriction on the production and the purchase of civilian goods during this war has been more severe; there will be a greater volume of accumulated purchasing power ready for expenditure in civilian markets; the process of correcting our balance of payments by restricting imports or by increasing our exports will exercise a greater influence in curtailing supplies on the home market; and as a result of war developments, shortages in other parts of the world are likely to be more marked than after the war of 1914-18.

3. The Interim Report of the Official Committee has, therefore, been prepared upon the assumption that during the post-war transitional period shortages of civilian supplies and an excess of consumers' purchasing power will persist for a considerable time. Part I of the Report analyses the situation on this basis, and the conclusion is reached that the outstanding tasks of the transitional period will be

(i) to restore the balance of payments,

(ii) to restrain inflation, and

(iii) to promote the transfer of resources and, in particular, of labour, from war to peace-time employment.

4. In Part II the action necessary in various fields to achieve each of these three objectives is discussed in turn, while Part III deals very briefly with the bearing that such action will have on some of the long-term problems of reconstruction.

5. The conclusions of the Report are summarised as follows:-

(1) that the rehabilitation of export must be regarded as one of the prime objectives of post-war policy;

(2) that every effort must be made to continue the stabilisation policy;

(3) that, for a time, consumer rationing must be maintained;

(4) that such commodity controls as may be necessary must be continued;

(5) that in order to promote the transfer of resources, recourse must be had to the mechanism of allocation of materials;

(6) that special attention must be given to arrangements (which may have to be of a regulative character) for promoting labour mobility;

(7) that suitable opportunities should be taken to prepare the public for restraints and sacrifices that may be entailed during the transition period, if the more distant objectives of economic welfare are to be attained.

6. The Committee proposes to proceed with its work "on the assumption, not only that the policy of stabilisation should be continued as far as possible during the transitional period, but also that the preservation of a high and stable level of economic activity and of employment in subsequent years should be set in the forefront of our economic objectives".

(Signed on behalf of the Official Committee)

A.W. HURST.

Chairman.

4, Richmond Terrace, S.W.1.
24th June, 1942.

DRAFT INTERIM REPORT

INTRODUCTION

1. The object of this report is to present a broad survey of some of the salient economic problems with which this country will be confronted in the years immediately following the war, and of the deductions bearing on future policy to be drawn therefrom which we propose to adopt as the basis of future reports. The report is essentially a preparatory note. Separate memoranda of a more detailed character will be prepared on each of the main problems dealt with, and as the study thus proceeds, the Committee may introduce some differences of emphasis or method of presentation. To that extent, therefore, the conclusions should be regarded as provisional.

2. To get a clear perspective of the nature of these problems, a threefold classification is convenient:-

(a) There are the problems which will arise immediately hostilities come to an end.

(b) There are the problems which will arise because of the peculiar difficulties of the transition from war to peace.

(c) There are more fundamental problems concerning the objectives to be aimed at in the more distant period when these immediate difficulties are at an end.

3. The first class of problem, the problems of the morrow of the armistice, are for the most part problems of a highly technical nature, e.g. demobilisation, liquidation of war contracts, etc., and fall largely within the province of the departments which will be most immediately concerned. They are, therefore, most conveniently dealt with in a series of separate memoranda, the preparation of which is already well in hand.

4. Nevertheless, the nature of the measures which are to be put into operation at this point must necessarily depend in some degree upon the view which is taken of the conditions likely to prevail in the years immediately following. If it be thought, for example, that the years following the end of the war are likely to be years of economic depression, the demobilisation plan might differ widely from that which would be thought appropriate if conditions of active trade were to be regarded as more probable. Preliminary study seems to suggest that the conditions prevailing during these years would be of a highly novel and intricate character, presenting difficulties without precedent; and the problems which emerge are problems to which solutions must be found if we are to move forward without grave dislocation. It has, therefore, been thought desirable to devote this interim report chiefly to a study of the problems of the transitional period and the formulation of broad outlines of possible solutions.

5. Just as the solution of the problems of the armistice depends partly on the view taken of the problems of the transitional period, so solution of the problems of the transitional period will depend partly upon the view taken of more distant objectives. This is a matter necessarily

involving political issues upon which, at this stage, Ministers may not wish to make final pronouncement. This report, therefore, makes no attempt to go deeply into these questions. But in a final section, it has been thought desirable to set forth the way in which some of the transitional problems are related to the problems of the longer period, and to set forth explicitly in paragraph 59 one of the main assumptions concerning ultimate objectives upon which the work of the Committee is being based.

PART I

THE GENERAL NATURE OF THE PROBLEM

6. The main economic prob em during the war has been to transfer resources from use for inessential civilian purposes to use for the armed forces or for the production of munitions and other essential goods and services. The extent to which this mobilisation of resources has proceeded is illustrated by the following estimates of national expenditure (taken from Cmd. 6347):

	1938	1941	Change between 1938 and 1941
		£ millions	
Personal expenditure on consumption at cost of production	3,584	3,863	279
Expenditure on goods and services by public authorities	833	4,182	+3,349
Private net investment at home (including war losses made good)	406	- 493	- 899
Net investment abroad	- 55	- 798	- 743
TOTAL NATIONAL INCOME(1)	4,768	6,754	+1,986

Between 1938 and 1941, Government demand for goods and services rose by no less than £3,349 millions. In the same period personal expenditure rose by considerably less than the increase in the costs of goods and services for consumption, so that an appreciable decline (estimated at some 15 to 20 per cent.) in real consumption had in fact taken place. At the same time private investmant at home fell by £899 millions; for private enterprise at present is refraining from many capital extensions and is not fully replacing its fixed or working capital. The rate of decline of overseas assets also increased by some £743 millions a year as the community was enabled - by living on its foreign assets or by borrowing from abroad - to import considerably in excess of its exports.

7. The outstanding problem of the post-war transition will be to reverse all this - to transfer labour and other economic resources as smoothly as possible back to peace-time uses - to revive exports and the industries making for domestic consumption. This transition cannot, however, be smoothly carried out unless any great inflation or deflation of national income is avoided, and this is a problem of great delicacy. Fot if it is to be solved satisfactorily it is necessary that the rate of increase in other expenditure, including the overseas demand for our goods, should be properly related to the rate of decline in Government expenditure: at a time when there will be much purchasing power accumulated during

(1) Includes war risks insurance premiums and indirect taxes and rates other than those specifically on consumption.

the war and anxious to find an outlet, this will not be easy to bring about. Furthermore, as a result of the using up of capital assets abroad, we shall be faced with a severe deficit of the balance of payments which will have to be remedied if there is not to be a severe exchange crisis.

8. The ease with which this transition can be carried out will be affected by the way in which the war ends. If hostilities should, for example, continue in the Far East after they have been ended in Europe, the transition itself would be more gradual. For in this case, certain warlike activities would be diminished in intensity before the final conclusion of all hostilities, and the preliminary stages of economic and financial demobilisation would be carried out in a psychological atmosphere in which it would be easier to maintain the essential Governmental controls.

9. Indeed it goes without saying that many post-war economic problems must remain uncertain until it is clearer what will be the future course of events during the war and when the war is likely to end. The post-war shipping situation will constitute one of the most decisive factors in our economic position: whether the war ends with the present scarcity of importing capacity or whether, before the end of the war, American shipbuilding will have greatly eased the situation, is still a matter for speculation. Nevertheless, there are certain broad generalisations which may already be made.

10. For some time after this war, as after the war of 1914-18, there is likely to be a marked excess of demand over supplies for the majority of peace-time goods and services. Indeed, as is shown in much greater detail in a document prepared by the Treasury and submitted with this report, there is reason to believe that these inflationary tendencies will be more potent and last longer than after the last war. This may be best seen if demand is analysed under separate headings.

DEMAND FOR GOODS IN THE TRANSITIONAL PERIOD.

(a) Expenditure by Public Authorities:

11. If, as seems very probable, it should be necessary for this country after this war to retain for a time substantially larger armed Forces than after the last war, Government demands for military goods and services will continue at a high level. In addition very heavy expenditure from public funds will be necessary for physical reconstruction.

(b) Demand for Goods and Services for Personal Consumption:

12. During this war consumers' demands have been restricted with greater severity than during the last war. This has had a double effect. In the first place, consumers, being unable to buy their normal supplies of many commodities, have saved large amounts of money; and these sums, together with deferred credits under the income tax, will be available for post-war expenditure. In the second place, people will wish to purchase new stocks of clothing, furniture, household equipment, motor cars, and similar goods of which they have been starved during the war.

(c) Home Investment:

13. In the period after the war there will be a high demand for capital goods to re-equip and restock civilian industry and commerce. To some extent the State, by a careful timing and adaptation of the disposal or use of government-owned factories, machine tools and stocks, may be able to meet the special transitional demands of business for capital equipment without involving a demand for new production, but these government-owned resources will not all be suitable for peace-time demands. The post-war demand for capital goods will be very great: war damage to property will have to be made good, civilian industry re-equipped and arrears of demand for houses and business premises of all kinds will have accumulated: many of these demands will be urgent.

(d) The Balance of Foreign Payments:

14. There is a further factor which will add to the pressure of monetary demand. As suggested above, at the close of the war there will be a serious disequilibrium in our balance of payments with other countries. Whatever financial methods are adopted to rectify this it will be necessary to expand the volume of our export trade. This will represent an additional demand for goods and services in this country.

14a. All these considerations suggest that most of the elements of a sharp restocking boom will be latent in the situation.

SCARCITIES OF SUPPLIES IN THE TRANSITIONAL PERIOD.

15. On the other hand many civilian goods and services will be in short supply. The stocks in this country of most imported materials and foodstuffs will by the end of the war have been pared down to fine margins and unless the war lasts long enough for American shipbuilding to have replaced a great deal of the tonnage that has been sunk, replenishment will be slow. Of special importance will be the scarcity of certain raw materials such as timber and rubber, vital for reconstruction; materials of which the post-war rate of production overseas may for a time be below the pre-war level. Shortages here will delay recovery in other fields. As regards imported foodstuffs special difficulty may be expected from the shortage of refrigerated tonnage which will affect the supply of such foodstuffs as meat, butter, eggs and fruit.

16. The production in this country of some civilian goods and services will be restricted for want of adequate supplies of special types of skilled labour. Much labour will need to be retrained; much transferred geographically, before it is suitable for employment in expanding peace-time industries. Some factories have been closed down, their machinery moved and their premises used for storage or for housing other firms engaged on war production. It will take time to clear them and fit them out again with the proper machinery.

17. An outstanding example of an industry in which abnormally high level of demand will be combined with continuing scarcities of supply is afforded by Building. Reference has already been made to the accumulation of demands that is piling up during the war. Meanwhile the labour force in the

building industry will have been seriously contracted and will need to be increased very rapidly if the urgent needs of reconstruction are to be met. Certain types of skilled labour and certain building materials, in particular timber, are likely to be in seriously short supply.

BOTTLENECKS AND UNEMPLOYMENT IN THE TRANSITIONAL PERIOD.

18. These scarcities of many peace-time goods and services will be combined with an excess of resources in a number of war-time occupations. Certain raw materials such as aluminium, certain forms of capital equipment such as machine tools, and certain types of labour such as skilled engineering labour, will be in excessive supply.

19. Even if special measures are taken this lack of balance will lead to some unemployment, but if the situation is rightly handled, such unemployment need only be transitory, occurring in the first months following the armistice. It should, however, be clearly understood that unless it is possible to break down the 'bottlenecks', which are found to be holding up the expansion of particular kinds of civilian production, this unemployment may persist.

20. Such a situation will, however, differ fundamentally from that which normally obtains at a time of general unemployment. Then activity in the great majority of trades is slack and it is appropriate to give employment by expansionist financial measures which stimulate the demand for all goods and services. Such measures will be quite inappropriate in the post-war transitional period, with an already existing excess of demand over supply in a large range of civilian occupations. In such circumstances, only the rapid retraining and transfer of of those types of labour which are needed and careful control of the use of 'bottleneck' raw materials (such as timber in building or rubber in motor manufacture), coupled with measures for the speedy re-tooling of industry for peace-time purposes, will secure the rapid absorption of the labour displaced from war industries.

PART II

21. The preceding analysis suggests three outstanding tasks:

(i) The restoration of the balance of payments.

(ii) The restraint of inflation.

(iii) The transfer of resources.

The problems involved in the fulfilment of these tasks are discussed in the sections which follow.

(i) RESTORATION OF THE BALANCE OF PAYMENTS

22. It is commonly agreed that one of our major tasks in the period immediately following the war will be to wipe out the heavy deficit in the balance of payments. If we cannot do this the whole fabric of reconstruction is in danger and we run the risk of a failure to maintain essential imports and of a major internal inflation.

23. The main methods for meeting this situation, on the external side, have already been set forth in another document (R.P.(42) 2). But whatever international methods are adopted, important effects on our internal arrangements are necessarily involved.

24. It is improbable, that at least for some time after the war, we shall be able to dispense with limitations on imports. Even if the shortage of shipping should have disappeared it will be necessary to maintain restrictions on imports until other methods have been developed for the adjustment of the balance of payments.

25. But restrictions on imports cannot be the major instrument of equilibration. The chief imports of this country are foodstuffs and raw materials; supplies of which are essential for the standard of living; we must, therefore, rely in the main upon an expansion of exports.

26. In the early stages, at least, of this transition period the demand for our goods in overseas markets will be greater than we can satisfy. There will be no occasion to force our exports on those markets. Rather we shall have to decide which of the various markets it is most important that we should first serve. It will, of course, be of the utmost importance that we shall re-establish our trade connections in this period.

27. The subsequent expansion of exports, however, will require extraordinary measures. Raw materials will still be short. If all claimants on their use were to be allowed to participate in a general scramble, the rehabilitation of the export industries might be indefinitely delayed. If only with a view to securing adequate allocation for export, the retention of raw material control seems essential.

28. But this has a further implication. If export is to have priority, it follows that, for the time being at least, other things must go short. Certain forms of civilian supplies, especially textiles, will be short, and, if distribution is not to be disorderly, this means some prolongation of rationing of consumption.

29. At the same time, it is a matter for consideration how far the existing machinery for labour control and any special arrangements which may be devised in connection with demobilisation could be utilised to give priority in restoring labour supplies to the export industries. Some help might also be given to exports during the period by meeting part of the demand from the home market by the release of government-owned surplus stocks of manufactured goods (such as motor vehicles), leaving the newly produced supplies to be exported.

(ii) THE RESTRAINT OF INFLATION.

30. It has been suggested above that the period immediately after the war is likely to be marked by an excess of money demand over supply and the persistence of shortages. If the various controls which have been imposed during the war were immediately to be relaxed, there would be danger of grave inflation.

The Policy of Price Stabilisation.

31. The first question which, therefore, arises is whether the policy of price stabilisation is to be continued. It would doubtless be premature to decide that any rigid level of prices was to be maintained for there will be all sorts of forces operating at that time which may well compel some revision of our plans, but some decision is essential on the general question whether to continue the policy of stabilising the cost of living and the prices of goods of common use.

32. The policy of stabilisation involves the maintenance of maximum prices for a large range of raw materials and foodstuffs, at least as long as the period of excess of demand over supplies continues. This policy of price control will in turn necessitate the continuance of the controls over raw materials and basic foodstuffs into the transitional period. The possibility of maintaining this policy, however, rests primarily on three factors:-

(a) the continuation of a moderate wages policy which will not lead to such a rise in wage costs as to cause an ever increasing disequilibrium between costs and controlled prices;

(b) a decision to continue, if necessary, the policy of subsidising the cost of living;

(c) external conditions which do not cause the price of imported supplies of raw materials and foodstuffs to rise excessively against us.

33. It is impossible to foretell how high a level of subsidies the maintenance of the stabilisation policy would entail. In the transitional period costs are likely to fall; war risks insurance premiums on imported cargoes and on commodity stocks will presumably disappear; for a number of reasons, such as the absence of black-out difficulties and the replacement of less

efficient temporary labour the efficiency of production is likely to increase; without any decline in the level of wage-rates, wage costs will be reduced if less overtime is worked, finally the normal long-term improvement of technique is likely to continue and may be speeded up as a result of war developments. Indeed, these reductions in cost might be sufficient to enable the stabilisation policy to be continued without any actual cost to the Exchequer. It would, however, be too sanguine to rely upon any such early development. It is at present unknown what level of subsidies it will be decided to pay to British agriculture; but it is unlikely that they will totally disappear. There is also a danger that world prices of some materials and foodstuffs will rise, though such a tendency might be checked by a continuance during the transitional period of present arrangements for co-ordinated buying and co-ordinated use of shipping as between the United Nations.

34. The continuation of the policy of stabilisation does not necessarily involve the stabilisation of every particular price. At the end of the war the prices of manufactured goods (e.g. of clothing) are likely to be abnormally high in relation to the prices of other goods (such as certain controlled foodstuffs). It will probably prove desirable to maintain a stability of the general cost of living index by allowing certain prices to rise as the prices and cost of other goods are reduced.

35. It is also a matter for consideration whether the production of "utility" goods, such as "utility" clothing, should not be continued into the transitional period. Such a policy would help to keep prices from rising and would enable accumulated shortages of goods such as clothes and furniture to be met as efficiently and as speedily as possible.

The Control of Demand.

36. If the policy of price stabilisation is to continue, certain other measures are also necessary. It is not enough to fix prices. It is necessary also to control demand. This principle has various applications.

(a) The restriction of money demand.

37. During the war the general level of demand has been held in check by high levels of direct and indirect taxation and also by the influence exerted by the National Savings campaign. Direct taxation has greatly restricted the spendable incomes of the rich, and has now been extended so as to affect the incomes of a large number of wage-earners. Heavy indirect taxes have not only held in check the demand for the goods and services directly taxed, but have withdrawn in taxation large sums of money which might otherwise have been available for expenditure on other objects. If prices are to be kept stable, some continued use of the fiscal instrument is necessary. During the period of inflated demand and short supplies, taxation should be maintained at a high level; and it will also be important to secure a continuance of large scale voluntary savings by the public.

38. A similar principle might be observed in the repayment of deferred income tax credits. If these sums are withheld during the period of general scarcity, and are released as abundant supplies appear on the market, they will

contribute to the stabilisation of the general conditions of supply and demand.

(b) Rationing.

39. But the restriction of money demand in general will not be enough, at any rate during the opening stages of the transition. It will almost certainly be necessary in certain cases to maintain more direct control of consumption. Both for the reasons mentioned above in connection with the problem of the rehabilitation of exports and in order to maintain equitable distribution, it will be necessary that, for some time, certain rationing schemes should be continued.

40. This conclusion is reinforced by the consideration that some prolongation of rationing will be necessary in order to facilitate the provision of relief to Continental Europe.

41. Such a policy would not involve an indefinite commitment to this form of regulation. As supplies increase, so rations could be enlarged, and as the point at which supply was once more equal to demand was approached, rationing could be abolished altogether. What is important is that if the general principle of stabilisation is to be adopted, the public should be educated to realise that some continuance of existing control is necessary.

(c) The allocation of materials.

42. Direct control of consumption, however, is not in all cases the most appropriate instrument for restricting demand. In many cases (e.g. that of timber) the most effective instrument at present for the restriction of civilian demand is through the appropriate Raw Material Control and it will probably be impossible to maintain an orderly development during the transitional period unless the Controls are themselves continued. These Controls will be needed to make allocations of the scarce materials among the various civilian uses according to their relative urgency.

43. Such peace-time allocation of raw materials will, however, raise certain difficult problems. In war-time all activities are directed as far as possible to one specific aim - the development of the greatest possible war effort, but in peace-time there are a multitude of economic objectives; and it is difficult, if not impossible, to reduce all these to a common measure for the purpose of priorities. In many cases it may prove necessary to distinguish only between a few broad groups - such as the export trade, "utility" goods, and other home market goods - though the problem of the later sub-division of supplies within these broad groups would, however, require careful attention. Then there will be the further difficulty of providing for allocations not only to existing firms but also to new businesses which may be established after the war. Even though raw materials are scarce, new firms must be at liberty to start in order to be ready for the time when output must expand. Men and firms returning from war service must not find every avenue to enterprise blocked.

(d) Limitation of Supplies.

44. Finally, it must be noted that there are at present in existence a series of controls which restrict consumption by direct operation on the output of manufactured products - in particular, the direction of production operated by the Board of Trade. Clearly, the main object of policy after the war must be to remove limitation of supply. But in so far as these regulations permit a control of demand for scarce materials or manufacturing capacity, any measures for their relaxation must be carefully co-ordinated with general stabilisation policy. Reference has already been made in paragraph 14 to the demand for capital goods which will arise after the war. It is presumed that to the extent that our fiscal resources allow such capital demand to be met, funds will be made available although there will be serious technical problems to be solved if this is to be done without impairment of the gilt edged market.

(iii) THE TRANSFER OF ECONOMIC RESOURCES.

45. The foregoing discussion has been concerned with measures which would be consequential on any decision to continue the stabilisation policy. But stabilisation is not an end in itself. The prime objective of policy, as already stated, must be to transfer resources from the service of war to the service of peace; and indeed it must be recognised that to some extent the two aims are in conflict. For there can be no doubt that the release of pent-up money demand at the end of the war will work in a way to promote transfer. The high demand for the products of peace-time industry which occurred after the last war caused the boom, but it also eased the absorption of demobilised men. If now we attempt to bring about the transition without such a price boom and all that followed in its train, we must be careful to provide mechanisms which will take the place of these drastic influences.

46. To do this, it will be necessary to take special measures to break down bottlenecks. The limiting factors on the expansion of demand in peace, as in war, will almost certainly prove to be the shortage of certain plant, certain key products and certain types of labour. Some use of the method of priorities, both for materials and for labour, will be essential if these obstructions are to be rapidly overcome. For example in connection with the demobilisation plan, attention should be given to arrangements for the early release of men whose special skill can provide the speedy rehabilitation of branches of industry having this pivotal position in relation to the whole economy.

47. The need for geographical and occupational transfer of labour will not be confined to the immediate post-war period. Experience between the two wars has shown how structural changes in demand, in productive technique or in the channels of trade may leave persistent pockets of "special" unemployment. No doubt similar structural changes will be found to result from the present war and to occur in the more distant future. And the need for definite Government action to bring about the transfer of labour in order to absorb such unemployment will be increased by certain long-term trends in the population. As a result of the serious decline in the birth-rate over the last few decades our working population is coming to consist of a higher and higher proportion of older workers and, after a few more years, the total working population will begin to decline: no action that can now be taken can have any appreciable bearing on either trend for, at any rate, the next fifteen years. Old

workers are naturally less mobile than the young and, moreover, the less rapidly a population expands the more difficult it becomes to adjust labour supplies between declining and expanding industries by concentrating the entry of juveniles into expanding industries. For this reason it is probable that the actual transfer of older workers from one occupation or region to another will become more and more necessary.

48. It is obviously desirable that action taken during the transitional period to promote the mobility of labour should be framed with reference to this long-term need. Considerable experience has already been gained in the inter-war period of the geographical as well as the occupational difficulties involved. The prevalence of unemployment during this period in certain heavy industries largely concentrated in particular areas in the North and West, while the development of new industries was taking place in the South-east, raised many acute problems and it has been suggested that Government action should be taken to secure a better distribution of the industrial population in future. Such proposals raise wide and important issues going beyond the scope of this report, but their bearing on the problem of the mobility of labour is obvious.

49. A better distribution of industry will do much to ease the geographical difficulties, but it will in no way reduce the need of extensive provision for retraining of the unemployed in new occupations. Great importance will no doubt be attached to this matter in the review of the schemes of social insurance and allied services now taking place.

PART III

LONG-RUN PROBLEMS

50. The earlier paragraphs of this paper have given reason for believing that a continuation of many of the discomforts of the war economy will be inevitable during the transitional period. As long as serious shortages of consumers' goods persist, certain war-time restrictions and controls must be maintained, if an orderly development of economic life is to be achieved.

51. But the acute shortages of the transitional period will not last for ever. As the channels of trade re-open and resources are transferred, so gradually something more like equilibrium should be established. Thereafter, there should be hopeful possibilities, not only of restoring, but also of progressively raising our standards of living. For there is no reason to doubt that technical progress after the war, as in past years, will enable real production to be steadily increased. Indeed, the war will in many ways have speeded up the process of technical invention and discovery, and may thus indirectly make possible a more rapid development of technique in certain civilian industries and occupations. It will, of course, take time to make good war damage to houses, to productive equipment and to other forms of capital; but this process should not take longer than a few years; and thereafter, if industrial activity can be maintained, it should be possible year by year to increase and to improve the community's capital equipment and thereby progressively raise the national income. If we are to obtain the food and raw materials that we need from overseas we shall have to devote a larger proportion of our productive power to producing goods for export. We must therefore raise our total production appreciably above the pre-war level before we can improve on our pre-war standards of consumption. But there is no reason to doubt that our productive capacity can be increased within a comparatively short time to the extent that is requisite for this purpose. The early prospect is arduous but the distant vistas offer great opportunities.

52. These long-term possibilities will, however, partly depend on the policy which is adopted during the transitional period and partly on factors which do not lie wholly within our control. In the first place we must solve the difficult problem of our balance of payments so that we are able to obtain from abroad - on not too onerous terms - the food and raw materials upon which our prosperity must continue to depend. The solution of this problem depends mainly upon external conditions and international arrangements which have already been discussed at length in another document (R.P.(42) 2). But this problem will not be satisfactorily solved unless during the transitional period internal measures are also taken to restore and to expand our export trade, even though these measures entail the continuation of restrictions in the home market.

53. It has already been observed (paragraphs 45 to 49) that one of the main problems of the transitional period will be to transfer economic resources from the contracting occupations of war-time to the expanding occupations of peace. Unless this transfer can be smoothly carried out, it will be impossible effectively to remove the shortages which will exist in the transitional period; and unless sufficient

transferability of resources is maintained thereafter, it will be impossible to take full advantage of technical progress to raise standards of living in subsequent years.

54. In a similar manner, the successful continuation of the policy of stabilisation during the transitional period would aid the maintenance of stability and prosperity in subsequent years. After the last war, an uncontrolled restocking boom was followed by a severe economic depression; and although the sharp burst of economic activity and of rising prices which occurred at that time may have somewhat facilitated the process of demobilisation, it greatly complicated the problem of maintaining a stable level of economic progress in subsequent years. In the later years of reconstruction after this war, it is essential to prevent economic depressions and the widespread wastes of economic resources in idleness and unemployment, which are the normal accompaniments of such depressions. In fact, all the solid improvements in standards of living which we may hope to achieve after the transitional period are dependent upon the successful avoidance of large-scale unemployment; and the restraint necessary for the maintenance of stabilisation during the transitional period will be well worth while, if for no other reason than that it should facilitate the maintenace of stability in subsequent years.

55. During the transitional period of shortages, the policy of stabilisation will require a continuation of price controls and of restraints on civilian purchases. But this period of shortages will pass; and the continuation of the policy of stabilisation will then, from time to time, require the adoption of measures to encourage and promote, rather than to restrain, civilian consumption. Various financial and economic measures should be considered, the object of which would be to maintain a high and stable level of demand for goods and services in general. It will be necessary at the same time to ensure that this high and stable level of demand is translated effectively into a high and stable level of trade activity and of employment, and that economic life is so organised as not to impede the necessary expansion of production.

56. One of the most important of our post-war economic problems will be that of the physical reconstruction of damaged property. It will probably be agreed that rebuilding should be planned with a view to the preservation of amenities, the promotion of public health and the reduction of costs of production. There is, however, another important aspect of this problem. Physical reconstruction may be so timed and so planned as to aid in the policy of stabilisation. In the early post-war years, when our building capacity will be insufficient to meet the demands upon it, it will presumably be necessary to control building activity so as to prevent a competitive scramble and secure due priority for more important and urgent reconstruction work. But it will also be essential to enlarge our building capacity and for this purpose to secure the entry into the building industry of a large number of additional workers. Both the rate and the scale of the expansion to be aimed at should be carefully planned in the light of the needs of physical reconstruction on the one hand and of the requirements of economic stability on the other.

57. In addition to the planning of physical rebuilding and the improvement of housing conditions, it would probably be agreed that there are other ways in which the social services should be developed. The objectives of social and economic improvement would be difficult in conditions of widespread unemployment, of low production and of a reduced national income; but the maintenance of a high and stable level of economic activity would greatly ease their sttainment and would reduce the financial burden of the necessary public expenditure.

58. For all these reasons the Committee propose to proceed on the assumption, not only that the policy of stabilisation should be continued as far as possible during the transitional period, but also that the preservation of a high and stable level of economic activity and of employment in subsequent years should be set in the forefront of our economic objectives.

CONCLUSION

59. If the argument of the preceding sections is correct, the following conclusions seem to suggest themselves:

(1) that the rehabilitation of export must be regarded as one of the prime objectives of post-war policy;

(2) that every effort must be made to continue the stabilisation policy;

(3) that, for a time, consumer rationing must be maintained;

(4) that such commodity controls as may be necessary must be continued;

(5) that in order to promote the transfer of resources, recourse must be had to the mechanism of allocation;

(6) that special attention must be given to arrangements (which may have to be of a regulative character) for promoting labour mobility;

(7) that suitable opportunities should be taken to prepare the public for restraints and sacrifices that may be entailed during the transition period, if the more distant objectives of economic welfare are to be attained.

60. As was indicated at the beginning, this report makes no claim to be an exhaustive treatment, even of the subjects with which it deals, and there have been deliberately omitted from its range a number of problems which will be of great importance, even in the transition period e.g. the problems of deconcentration, disposal of stocks, control of the capital market, and the improvement of industrial efficiency. On all these and other matters, further papers are in active preparation.

23rd June, 1942.

THE POST-WAR RELATION BETWEEN PURCHASING POWER AND CONSUMERS GOODS

NOTE: This memorandum does not purport to deal with our long run post-war economic position. It is concerned with the post-war transitional position and offers reasons for expecting that, whatever may be the course of events afterwards, the transitional period of shortage, involving a prevailing high demand for labour, will be longer than it was after the last war.

It is hoped to present shortly, with the aid of the Central Statistical Office, some statistical data bearing on our long run economic position on certain assumptions.

I. Introductory.

1. The experience of the last post-war period supplies the most natural starting point for an examination of the probable economic trend after the present war. It is true that in many important respects the conditions on this occasion are likely to differ materially from those which prevailed last time. These conditions are liable moreover to be affected by a large variety of factors, including the future course, the duration, and the manner of termination of the war, which cannot at present be foreseen. For these reasons it is important to scrutinise critically all generalisations suggested by the analogy of 1919-1922. None the less, this is the only experience which is at all relevant to our future problem; and, in the absence of any other, it inevitably determines the impressions that are instinctively formed. It seems desirable, therefore, to begin with a brief review of the outstanding features of the last post-war experience, followed by an examination of the main respects in which different conditions are to be expected after the present war.

II. The Last Post-war Period.

2. The Armistice of November 1918 was followed after a brief period of hesitation, by boom conditions, both at home and in export markets, which lasted from early in 1919 until the summer of 1920. There was a widespread "re-stocking" movement; that is to say, traders and business men generally set themselves to rebuild to normal levels stocks which had been depleted during the war. Similarly, there was a considerable expenditure on plant by industrialists endeavouring to turn their works round from war-time to peace-time purposes, or to overtake arrears of renewals that had accumulated during the war. There was also a wave of active buying by the consuming public, both at home and abroad. Behind this general activity of demand, there lay a superabundance of purchasing power in the hands both of the business community and of the general public. These boom conditions, coupled with the rapid removal of wartime controls, entailed a sharp increase of prices. This caused serious unrest at the time, and helped to aggravate the troubles that arose in the subsequent depression. None the less the boom helped greatly while it lasted to smooth the process of demobilisation. Some four million men were discharged from the armed forces in the eighteen months after the armistice; yet at no time did the number of ex-service men in receipt of "out-of-work" donation rise to 400,000. Trades and industries catering for civilian needs had to absorb not only the great bulk of the men demobilised from the forces, but also large numbers of work-people who had been employed in making munitions. This colossal task which had given rise to serious apprehensions beforehand, was accomplished with a remarkable measure of success. Until the summer of 1920, public opinion in Great Britain, as in the United States, and indeed generally throughout the world, was

mainly preoccupied not with unemployment, but with the rise in the cost of living, profiteering, the "vicious spiral", and other symptoms of a boom.

3. This boom broke in the summer of 1920, and by 1921 the prevailing conditions were those of depression throughout British industry. Prices and wages fell heavily, and unemployment reached large-scale dimensions. But though the depression was severe for a time, it was not very prolonged. The process of recovery became clearly marked during 1922, and continued steadily until by the spring of 1924, a condition of considerable activity had been reached. The incompleteness of this recovery reflected in part a failure to regain the export markets which had been lost during the war; a failure which was to become more clearly marked in subsequent years. During these particular years (1922-24) the British coal-mining industry, which was later to become the centre of depression, received advantitious aid from the decline of Continental coal production resulting from the occupation of the Ruhr. None the less, the contrast between "sheltered" and "unsheltered" industries had been recognised as early as 1923 as constituting the crux of the British post-war industrial problem. The extent of the recovery during these years was perhaps obscured at the time by the fact that the unemployment figures seemed more serious than they really were to minds that were influenced by statistical standards derived from the very different pre-1914 trade union percentages.

4. The fluctuations of activity between 1919 and 1924 were not, of course, uninfluenced by the policies, financial monetary and economic, that were pursued during this period. In the sphere of public finance, policy was dominated by the objective, which was unquestioningly accepted in all quarters of restoring a balanced budget at the earliest practicable moment, coupled with the subsidiary objective of maintaining equilibrium at a steadily falling level of revenue and expenditure. Taxation was only gradually reduced from the high war-time levels. Expenditure was quickly and drastically curtailed; the subsidies which had been given, e.g. for bread and coal, to check the rise in the cost of living were soon withdrawn, as part of this policy, and the process of retrenchment was carried further in 1922 by the application of the "Geddes Axe".

5. Another branch of financial policy exerted an important influence on the course of events. During 1919, the attempt was made to "fund" the large volume of short-term debt which had accumulated during the war, and the Victory and Funding Loans were issued with this object in view. Credit policy was directed so as to facilitate these funding operations; and conditions which it is fair to regard as "cheap money" conditions were maintained for a considerable time despite the inflationary movement that was in progress.

6. This, however, was only a passing phase. By the end of 1919 it had been decided to follow the course proposed by the Committee on Currency and Foreign Exchanges After the War ("The Cunliffe Committee") which may be roughly summarised as a policy of gradual monetary deflation with a view to the re-establishment of an effective gold standard. The most precise recommendation of the Cunliffe Committee was that the fiduciary note issue should be limited by law, and thereafter gradually reduced by making the actual maximum reached in any year the legal maximum for the year following. This recommendation was adopted by Treasury Minute in December 1919; and since the limitation of currency could not be effective without a corresponding curtailment of bank credit, credit policy had to be adjusted to this decision. Credit conditions became accordingly more stringent, the process culminating in

an increase of the Bank Rate to 7% in April 1920. This was quickly followed by the collapse of the boom; though how far this result was due to the restriction of credit, how far to a natural exhaustion of the "re-stocking" process, and how far to the contemporary slump in the prices of primary products overseas, is a question which necessarily admits of argument. It is to be noted that up to this point the chief public criticism passed upon the policy pursued was that the application of the brake of dear money was unduly slow and hesitating.

7. Although the inflationary trend was definitely reversed within a few months, Bank rate was maintained at 7% for over a year. This may have been a material factor in the intensity of the depression in 1921. The prolonged maintenance of dear money was attributable to a combination of three influences (1) the adoption of the policy of the Cunliffe Committee; (2) the fall in the exchange value of sterling; (3) the course of events in other countries, particularly the United States.

8. The pound which had been "pegged" during the war at an exchange-rate with the U.S. dollar of $4.76½ was unpegged in March 1919. It fell quickly and heavily, reaching a level of $3.20 within a year, from which it made a recovery which was for some time hesitating and chequered, reaching $4 in May 1921, but falling back to $3.60 in July 1921. To raise this exchange rate, with a view to the ultimate restoration of the gold standard on the basis of the traditional gold value for the pound, was widely regarded as an important objective of monetary policy; and the pursuit of this objective, which was accomplished in 1925, exerted an influence in the intervening years, varying in strength from time to time on internal credit policy.

9. In the United States, the course of trade was very similar to that in Great Britain. There was the same early boom and inflationary tendency, though the rise of prices, as was natural in view of the fall of the pound, was less marked. There was the same reversal of in the summer of 1920, following on tighter credit conditions which culminated in a rise of the New York rediscount rate to 7 per cent in June of that year. There was the same sequel of a heavy fall of prices and an intense depression; there is the same possibility that this depression may be largely attributable to the fact that the rediscount rate was also maintained at 7 per cent. for about a year; and there was a somewhat similar foreign exchange complication, in that the maintenance of dear money was largely due to the fact that the United States had been losing gold. Finally, in the United States, also, there was a comparatively early recovery. This began sooner, being evident early in 1922, and was more decided than the recovery in Great Britain. There was no loss of pre-war export markets by the United States to impede and obscure the extent of the internal recovery; and by March 1923, a condition of high productive activity had been reached, with renewed inflationary symptoms which were the signal for a contraction of credit. It seems probable that the United States recovery in 1922-23, was a major influence in causing the recovery in Great Britain.

10. In the belligerent countries of the European Continent, the inflationary trend was not reversed in 1920, but continued in the ensuring years with a gathering momentum, until it culminated in some countries in a complete currency collapse, and in others in a depreciation of the value of the currency to a small fraction of its previous value.

11. It is of some interest to consider briefly the course of publicly financed capital expenditure, (commonly described as expenditure on "public work") during the period under examination in Great Britain. The total expenditure of local authorities financed by borrowing was as follows:-

	(£ millions)			
	1920-21	1921-22	1922-23	1923-24
Housing	52.2	81.7	29.6	11.3
Roads	3.6	6.2	9.0	8.3
Other Purposes	38.6	40.8	33.0	32.4
TOTAL	94.4	128.7	71.6	50.0

In the phase of slump, road bulding programmes, for which the development of motoring offered substantial scope, were pushed forward, largely with the object of mitigating unemployment. The above figures show, however, that house-building was the dominating factor in the volume of public works expenditure. The house-building activity was attributable to the housing policy initiated in the boom phase in order to make good the acute housing shortage left behind by the order. It reached its peak in the slump years. In 1922 it underwent a very sharp curtailment as the result of changes in policy prompted by the increasing preoccupation with retrenchment. Thus whatever public works expenditure may have contributed toward mitigating unemployment during 1921, the ensuing recovery took place despite a substantial net curtailment in the volume of this expenditure.

12. Commercial policy did not exert an important influence on the trend of activity during this period. A limited range of industries was protected against overseas competition by the Safeguarding and Key Industries Measures; and by the retention until 1924 of the McKenna duties. But these represented comparatively minor exceptions to the general rule of the maintenance of a Free Trade policy.

13. For the present purpose it seems unnecessary to carry the story in any detail beyond 1924. The prolonged malaise that ensued in British economic life was largely attributable to a cause associated with the war, namely, the loss of export markets by industries such as coal and cotton, which were so highly localised that it was not easy for their redundant labour-force to obtain alternative employment. An important influence may also have been exerted by the restoration of sterling to its pre-war exchange parity in connection with the return to the gold standard. But such influences differ in kind from those, such as the movement to "re-stock"which represent more or less normal reactions to war conditions, as such; and there is no similar presumption that they are likely to be repeated. It is pertinent to observe that the rough similarity between the British and American trends which had prevailed until 1924, was replaced for some years by a broad contrast between unemployment in Great Britain and abounding prosperity in the United States.

14. The foregoing analysis may be summed up as follows. In the course of trade activity in Great Britain between 1919 and 1924, three phases can be distinguished:-

(1) a phase of inflationary boom conditions, marked by rapidly rising prices, during which demobilized labour was absorbed on a very large scale. The main impetus to this inflationary trend was supplied by the need to re-stock both at home and abroad, and to overtake arrears of plant renewals. An essential underlying condition was a superabundance of purchasing-power. The movement was

further stimulated by the maintenance of easy credit conditions in the interest of funding operations, by the removal of war-time controls, by the withdrawal of subsidies to the cost of living, by the fact that none the less the budget was not yet balanced, and by the heavy fall in the exchange value of sterling;

(2) a phase of general depression, beginning in the summer of 1920, which though severe and accompanied by a heavy fall of prices and wage-rates, was not very prolonged. This may have represented in part a natural reaction, after "re-stocking" had been largely accomplished from the preceding boom. But it was probably intensified by the fact that the stringent credit conditions which had been employed to check that boom were maintained for over a year, by the effect on purchasing-power of drastic budgetary retrenchment, and by the repercussions of a similar depression in the United States;

(3) a phase of substantial recovery, especially in production for the home market, which began in 1922. A major influence in promoting this recovery was probably the more complete recovery that set in in the United States; and the fact that the recovery was slower and less decided here was probably partly due to the recovery in the exchange value of sterling and to the credit policy pursued with that object in view.

It is evident from this review that the widespread impression that the Armistice was quickly followed by a prolonged period of uninterrupted depression as far from being accurate even as regards Great Britain; while in most other belligerent countries, the prevailing trend for many years was either towards inflation (as on the European Continent) or one of exceptional trade activity (as in the United States).

III. Probable Differences in the Next Post-War Period.

15. Any attempt to forecast the respects in which the conditions after the present war may be expected to differ from those after the last war must be largely speculative in character, and open to varieties of judgment. We cannot tell as yet when the war will end, how it will end, what sort of a world it will leave behind, or even whether it will end, as did the last war, at approximately the same time throughout the world. All these uncertainties, and more especially the last, have an important bearing on the present problem. It is possible, however, that these uncertainties affect the degree rather than the character or the direction of the differences which are to be expected; and that the latter can be indicated with some degree of confidence. They may be considered under two broad heads, internal and external respectively.

A. Internal.

16. (1) It seems probable that the process of demobilisation, both from the armed forces and from war production will be less sharp and sudden after this war than after the last. The outlook is complicated by the possibility that the war may end at widely separated times in different parts of the world; so that operations may continue, say, in the Far East after peace has been re-established in Europe. In that case, the demobilisation of some of those absorbed in the war effort, those in particular concerned with defence against air attack or invasion, might have been undertaken before the final end of the war. But apart from this possibility, it would seem prudent to assume that we may find it necessary to maintain armed forces of considerable strength for at least some years after the war is over. It seems unlikely that we shall be in a hurry to reduce the Air Force to small dimensions, and the production of certain types of armaments such as aeroplanes and tanks may well be continued on an important scale. This probability will be increased if the international political outlook remains clouded for whatever reason.

(2) A second difference arises from the physical destruction which has been caused by air bombardment during the present war, the scale of which may possibly become materially greater before the war is over. Capital assets of a large variety of kinds - houses, factories, warehouses, shops, public utilities - will need replacement, and we shall be faced as a consequence with a substantial task of physical reconstruction and re-building. In so far as an abnormally large volume of work of this capital character has to be undertaken, the consequences are likely to be similar to those of war-time armament expenditure; i.e. purchasing power will be generated without a commensurate increase in consumers goods. It is true that the magnitude of the task may not prove so great in practice as is often supposed. The available data relating to War Damage claims suggests that the losses so far caused by air bombardment are on a smaller scale than might have been expected. It is important, moreover, to remember on the other side that one of the factors which underlay the housing shortage of the 1920's, and the prolonged demand for additional houses, is not likely to exert the same influence in the next post-war period. This was the abnormally rapid growth in the number of family units, which was largely a reflection of the fact that the annual number of births in the United Kingdom was at its maximum early in the century. Despite the war-time destruction, therefore, it is possible that new houses will not be required on a larger scale than after the last war. The importance of the factor of greater physical destruction depends, therefore, mainly on what happens during the remainder of the war.

(3) War production is absorbing a larger proportion of our productive resources than was the case in 1914-18, and, apart from essentail foods, the supply of goods available for meeting civilian demands is being more drastically curtailed. There was no parallel in the last war to the present Limitation of Supplies Orders, or to the scheme for concentrating industry. So far as consumers' goods are concerned, the depletion of stocks is likely, therefore, to be more marked and more widespread when the war ends than it was in 1918; and it is also probable, especially in view of the large number of factories which are now being used as warehouses, that it will take longer to restore the production of goods for civilian purposes to normal dimensions, to overtake arrears of capital maintenance and renewal.

(4) The excess of accumulated purchasing-power which is banked up under war conditions but which is likely to be thrown upon the market when peace is restored, will probably be much larger upon this occasion. After 1918 there was no very marked tendency to encash the savings certificates which had been accumulated during the war. It would be unsafe to assume that this experience will be repeated, in view of the greater extent to which the satisfaction of pressing needs has been postponed owing to the unobtainability of goods. Further, the arrangement under which part of the sums which the State is now taking from the taxpayer are being credited to him, will serve to increase the volume of purchasing-power liable to be directed to the purchase of consumers' goods. This tendency is likely to be accentuated by the strenuous efforts that are being made during the war to keep down the prices of essential goods in order to prevent the development of a prices-wages spiral; for this means that a smaller part of the redundant purchasing-power that is being created is absorbed in buying goods at inflated prices.

(5) This redundancy of purchasing-power is not likely to be absorbed as quickly as it was after the last war by drastic measures of financial retrenchment. Some of the war-time subsidies, notably those to cover inceases in farming costs, will probably have to be retained in the post-war period, in order to avert an increase in the cost of living. On the other hand it will not be easy to maintain the high war-time rates of taxation, having regard to the extent to which they fall on the smaller income ranges and the extreme severity of their application to the higher ranges. It may well be that for such reasons, coupled with the fact that budgetary equilibrium is no longer so universally accepted as an imperative requirement of sound finance, unbalanced budgets will persist for considerably longer than after the last war. Apart from this possibility moreover, there is likely to be a considerable volume of Government expenditure, e.g. the compensation payments under the War Damage Acts, which, though not forming part of the annual budgetary expenditure, will serve none the less to increase the purchasing-power at the disposal of the community.

B. External.

(6) The balance of international payments with which we shall emerge from the present war is likely to be seriously adverse; and we shall be faced with an imperative need to restore this balance to equilibrium within a reasonable period, either by increasing our exports or by curtailing our imports. The pressure upon us in these directions will be made the more urgent by our loss of exchange resources and by the large sterling balances which India, the Dominions, and foreign countries will have accumulated. In so far as we succeed in increasing exports, the productive capacity available for producing goods for the home market will be correspondingly reduced. A reduction of imports would also serve to reduce the supplies of goods with which the needs of the home population could be satisfied. In either case, therefore, the process of correcting the adverse balance will exert an influence tending to maintain an excess of demand over supply. There was no tendency of this character after the last war. We entered that war with a highly favourable balance of payments, which represented, as it were, fat that we could afford to lose. We emerged from that war with the loss of something like one quarter of our former export trade, and we never made this loss good; but we were not as a consequence under any compelling need to curtail our imports, the volume of which in fact tended to increase.

(7) It is not only in this country that the intensity of the war effort, as measured by the proportion of productive resources absorbed by war purposes, is much greater in the present war than in that of 1914-18. It is certain that before the war ends, this will be true as a general world phenomenon. In the United States the production of various types of goods for civilian purposes, notably for example, automobiles, is already being drastically curtailed. There was no parallel to this in the last war. Again, though Japan was technically a belligerent in the last war, her economic life was not seriously involved in war production; and she emerged in 1919 with a greatly increased capacity to produce for export. Thus, so far as industrial products at least are concerned, prevailing world conditions of shortage seem likely to be more prolonged after the present war.

(8) Active military operations have already spread over a far wider area than during the last war, and have entailed a greater degree of destruction and economic dislocation. Although there will be less physical damage to be made good in

France and Belgium, there will be much more in Russia and the Far East. Moreover, the possibility cannot be excluded that the world output of several primary commodities, notably tin, rubber, and oil, may be seriously reduced for a considerable period by military developments before the end of the war is reached.

(9) There is also the possibility, which it is not easy at present to assess, that the present war will leave behind it a greater degree of political and social confusion than the last. In 1918 the Central Powers and their Allies collapsed suddenly and very nearly simultaneously, and the military collapse was associated with political revolutions. For the most part, however, these political revolutions took a form in which an orderly Government was promptly substituted for the previous regime, and it was only in a comparatively limited area in Eastern Europe that economic reconstruction was seriously impeded by political chaos. It cannot confidently be assumed that this experience will be repeated. It may be that unsettled political conditions will interfere far more seriously after the present war with the revival of peace-time production over a large part of the world.

17. It will be readily appreciated that all the foregoing differences tell in the same direction, from the standpoint of the question under examination. Each of them will tend to prolong the period during which the prevailing conditions must be expected to be those of an excess of purchasing-power over the supply of goods. The process of demobilisation is likely to be more gradual and less complete; there will be more physical damage to make good, a greater exhaustion of stocks to be replenished, a greater diversion of industrial plant to war production to undo, a larger banking-up of purchasing power in the hands of consumers with larger unsatisfied wants, a more pressing need to devote more of our productive capacity to export work, and a greater difficulty in obtaining supplies from overseas. These tendencies will probably be reinforced by budget deficits continuing for considerably longer than after the last war, and by more severe conditions of general world shortage. It is impossible at the present stage to evaluate the strength of these various influences; but the longer the war lasts, and the more its future course is marked by unexpected developments, the greater is their importance likely to become.

18. It remains, however, to consider possible influences of a somewhat different character from those examined, namely, those which may arise from the gradual long-run trend of economic development, and those connected with changes in ideasand policy.

IV. <u>The Long-Run Economic Trend</u>.

19. The main influence to be considered under this heading is that of the continued advance in industrial productivity arising from technological improvement which, moreoever, has probably become more rapid, taking the economic system as a whole, than it was formerly. The productive capacity of the industrial countries of the European and North American Continents was certainly far larger at the outset of the war than was required to sustain the standard of living that actually prevailed. In some countries an important fraction of this productive power was wasted in the form of the unemployment, or partial employment, of plant and labour; and the services of a large and growing number of persons were absorbed in functions such as advertising and sale-promotion, which were of doubtful social utility and could certainly be largely curtailed without any material injury to the standard of life. In other countries an important

fraction of the productive power was devoted to large-scale preparations for war; and the success of Nazi Germany in particular in building up an overwhelming military strength without any very marked lowering of her living standard, although she had not the advantage of the possession of international capital assets, suggests that the margin of productive power which a modern industrial country wastes in one way or another, is larger than has hitherto been realised. This wasted margin must have grown considerably in the inter-war period. If, therefore, the shortages to be overtaken after the present war will be, for the reasons previously given, more serious and more widespread than they were in 1918, it can be argued on the other hand, that modern societies will be more powerfully equipped for overtaking them.

20. A special feature of the technological progress of the last generation was its marked extension to the production of many agricultural commodities. During the last ten years before the present war a pronounced condition of over-supply became apparent for a large range of agricultural commodities, leading to the accumulation of vast surpluses. War conditions have led to the disappearance of many of these surpluses, and it is not unlikely that substantial inroads may be made into those that still remain before the war is over. None the less, the probability suggested by the available statistical data is that abundant supplies of certain basic agricultural commodities, notably wheat and cotton, will be available to meet the world's post-war demands. After the last war there was a prevailing scarcity of wheat for several years; and in this respect at least it seems probable that the situation after the present war will be more favourable to consumers.

21. Thus the influence of the long-run economic trend will be in the opposite direction to that of the considerations enumerated in the preceding section. It seems unlikely, however, although the matter does not permit of a conclusive judgment, that this will be strong enough to reverse the conclusion, to which those considerations point, that a longer period during which demand generally will tend to exceed supply is to be expected. The larger available margin of productive power that is normally wasted will not affect the problem until it has been effectively directed to the production of peace-time goods; and this is likely to take a considerable time. The prospect of a more abundant supply of certain agricultural commodities is uncertain and limited in scope; and its significance is rather that it may make it easier to check a serious inflationary development during the phase of "boom" than that it is likely to bring that boom to an early end. On the whole, therefore, it seems reasonable to regard the long-run trend as a factor tending to qualify rather than to alter the prospect, suggested by the previous analysis, of a longer period of a prevailing excess of purchasing-power; though subsequently, of course, it may well become once again a factor of dominating importance.

V. Ideas and Policy.

22. The course of economic events after the war may be greatly affected by policy. It would obviously exceed the proper scope of this paper to attempt a systematic forecast of the policy that is likely to be pursued, the more so because it may be affected in turn by the diagnosis that is accepted as to the probable course of events. None the less there are some matters, so highly relevant to the problem, upon which differences in the objective situation and differences in prevailing ideas between the two post-war periods are so likely to result in difference of policy, that it seems desirable to take account of them.

23. In the first place, there has been an important change in the general attitude towards the maintenance of economic controls. After the last war, there was a prevalent and strong desire to sweep away the whole system of war-time controls as rapidly as possible with a view to the restoration of normal peace-time conditions. The indications are that this desire will be at any rate less strong, less unqualified and less sweeping after the present war. There is, indeed, a more widespread scepticism as to whether our pre-war arrangements represented the natural and normal economic system, and as to whether accordingly it is either desirable or practicable to aim at re-establishing them with the fewest possible changes. If, moreover, the conditions at the end of the war are marked by an acute shortage of shipping and other key factors, there is likely to be a fairly general recognition of the need to maintain a considerable measure of control over our economic life for such purposes as the prior satisfaction of more urgent needs and the re-building of our capacity to produce for export.

24. The wholesale removal of controls in 1919 served to stimulate the inflationary developments which marked the "boom" period, and it may thus have contributed something by way of reaction to the severity of the slump that followed. Although the forces tending in the inflationary direction are likely, as the preceding analysis has suggested, to be stronger after the present war than they were last time, the greater readiness to accept the continuance of controls, may help to make it easier to hold these forces in check.

25. In this connection, however, another aspect of the problem should be mentioned. A condition of things in which the supply of purchasing-power tends to exceed the supply of available goods, does not imply that unemployment will be negligible. The transfer of production from a war-time to a peace-time basis will give rise, just as the reverse process does, to unbalanced production, "bottle-necks" and hold-ups; and many workpeople may find themselves unemployed for a time, not because the demand for the products of their industry is insufficient, but because production is insufficient somewhere else or because the supplies of imported materials are insufficient. Such obstacles to the speedy restarting of industry may be more serious after the present war than they were after the last. It may take a considerable time, for example, to restart many of the factories which have been closed down under "concentration" schemes. Shortages of certain materials, e.g. rubber, may also be severe. Apart from such "bottle-neck" problems, the reabsorption in peace-time economic life of large numbers of persons from the fighting services and from war production entails difficult problems of personal adjustment, and a small percentage may remain unemployed as a consequence, despite a strong demand for labour in general.

26. The problems of post-war policy will be made more complicated and more difficult by special unemployment of this latter character. The remarkable success with which vast numbers of demobilised soldiers and workpeople were absorbed in civilian economic life within the eighteen months that followed the Armistice of 1918, may have been greatly aided by the intensity of the re-stocking boom and by its inflationary accompaniments. The rise in selling prices kept well ahead of the rise in costs of production, and, though this carried other evils in its train, general business conditions were so profitable, or so apparently profitable, that employers were anxious to engage additional labour, and could afford to pay less regard than they might otherwise have felt bound to do, to its

efficiency for the work in question. If controls designed for such purposes as preventing an undue rise of prices and restraining home consumption with a view to rebuilding an adequate volume of exports, are retained for a considerable period after the present war, the result may be to slow down the rate of re-absorption. This will not necessarily be a disadvantage; the process of demobilisation itself may, as has been indicated, be less sharp and sudden, so that a less rapid rate of re-absorption may prove to be all that is required. But if this possibility is not realised, and demobilisation is effected with a rapidity comparable to that of 1919, some conflict of objectives may possibly arise; and the task of avoiding inflation may be made more difficult by ill-judged pressure for general removal of restrictions when in fact other measures would be appropriate and adequate to meet the case.

27. In regard to monetary policy, there have also been changes both in prevailing ideas and in the objective facts of the situation, which may have an important bearing on post-war developments. As has been seen in Section II the severity of the comparatively short-lived slump in 1921 in Great Britain and in the United States may have been partly due in both countries to the continuance, for a considerable period after the inflationary trend had been reversed, of the high money-rates which were established in 1920. It seems unlikely for various reasons that an influence of this kind will operate after the present war. The delay in reducing money-rates until the middle of 1921 was largely attributable in both countries to exchange considerations. The United States had been losing gold to Spain and Argentina, and appeared to be threatened with a loss of gold to Japan. In view of the embarrassing magnitude of the gold reserves which the United States now possesses, it is most unlikely that any difficulty would be caused by a future outflow, even if it should occur. The continuance of dear money in Great Britain was explained partly by its continuance in the United States, and partly by the desire to raise the gold value of the pound; and, as will be suggested later, there is no reason to suppose that the latter complication will affect policy after the present war. It must be remembered, moreover, that according to the traditional view, gold movements or foreign exchange tendencies were regarded, as was natural under gold standard conditions, as the proper determinant of credit policy. The idea that in the event of an industrial depression the chief aim of credit policy should be to promote industrial recovery had hardly begun to win acceptance in 1920 or 1921.

28. In view of these various changes, it may be assumed that if, after the present war, an initial post-war "boom" should be followed by a sharp set-back, credit policy would be adapted far more quickly so as to make its contribution to preventing this set-back from developing into a severe depression. How important this contribution would prove in practice is perhaps a somewhat speculative question, particularly if it were to be supposed that the initial phase of boom had been accompanied by a serious inflationary movement. None the less, there is at least a possibility that, under altered monetary conditions, any future <u>analogue</u> to the slump of 1921 might be much less severe.

29. The prevailing trend of activity over a longer period may also be affected by the probable differences in monetary conditions. As has been suggested in Section II, the contrast between British economic <u>malaise</u> and American prosperity between 1923 and 1929 was probably attributable partly to the loss of export markets by old-established and highly localised industries, and partly to the difficulties entailed by the restoration of the pound to its time-honoured parity with gold, and consequently with the dollar. Since we have now been off the gold standard for more than ten years, no particular parity possesses the sanctity that formerly attached to $4.86. The

maintenance of exchange stability may, it is true, be regarded as an important objective; and this may exert an influence on internal policy. But it is one thing to resist a depreciation of the exchange, and quite another to bring about a large appreciation such as was effected between 1922 and 1925. There seems no reason to suppose that exchange appreciation will be a serious factor in the problems of British economic life in the next post-war decade.

30. It seems equally doubtful whether there will be any parallel to the other main factor which played a part in our malaise between 1923 and 1929, namely the loss of export markets by highly localised industries. We must expect, it is true, that our export trade in many lines will be adversely affected by the stimulus that the war has given to the development of manufactures in undeveloped countries. On the other hand, most of our principal industrial competitors are engaged, or are likely to become engaged, in war production in a degree far more comparable with our own proportion than was the case in the last war. Moreover, the restoration of equilibrium to our balance of payments will be a vital objective of our policy, in a sense in which this was not true last time; so that we may expect a greater concentration of effort on the promotion of export trade. Finally, it seems unlikely that any loss of export trade will be concentrated in the same degree as in the last post-war decade on industries of the same highly-localised character. There is no reason, therefore, to suppose that it would give rise to an equally difficult problem of large-scale unemployment concentrated in particular areas.

VI. Conclusion.

31. The analysis in Section III led to the conclusion, qualified but not overborne by the counter-balancing considerations examined in Section IV, that the phase of "boom" after the present war is likely to be longer, and might prove considerably longer, than after 1918. This conclusion is subject, of course to the reserves that must necessarily attach to any attempt to forecast post-war conditions. On the other hand, its practical significance is perhaps greater than may appear at first sight, and is heightened by the considerations discussed in Section V.

32. It was observed in Section II that the popular impression that the last war was followed almost immediately by a prolonged depression is far from accurate. The depression which reached its nadir in 1921 was not in fact more prolonged than the boom which preceded it. The recovery which began in 1922 was, it is true, in Great Britain, hesitating and incomplete. But in the United States, the story was very different. There, the recovery of 1922 led within a year to conditions of full activity which were maintained without serious interruption until the end of 1929. Indeed, the trend of economic activity in the United States in the post-war decade may be farily summed up as ten years of exceptional trade activity, broken only by a sharp but short-lived slump, lasting from the summer of 1920 until early in 1922. The severity of this short-lived slump was partly due to circumstances that need not be repeated. What is perhaps more important, the divergent experience of Great Britain after 1923 was also due to circumstances that need not be repeated. So far as the trend of industrial activity is concerned, though not necessarily in other respects, there seems no reason why our experience after the present war should not resemble the last post-war experience of the United States more closely than our own.

33. It is important, however, that this conclusion should not be misinterpreted. The presumption that arises from the analysis summarized in the preceding paragraph is that, notwithstanding the possibility of a temporary setback to an early post-war boom, the period between the cessation of hostilities and the time when a persistent and general tendency for supply to exceed effective demand reasserts itself as a major source of economic difficulty may be considerably longer than two or three years. But this does not mean that no serious economic dangers are to be apprehended. On the contrary, problems of shortage may be no less formidable than problems of over-supply. These problems will, of course, be most serious in the immediate post-war period. During the remainder of the war, shortages of essential goods may become more acute and more widespread, so as to entail a more substantial degree of deprivation than exists at present. It will take time to overcome these shortages, particularly in view of the probable need to divert shipping and supplies to meet the needs of liberated countries in Europe and elsewhere. On the other hand, there is a danger that the present mood of readiness to accept sacrifices may give way when the war is over to an impatient demand for the restoration of pre-war standards; and this might prove a source of friction which would in turn impede the restoration of our productive power.

34. It is possible, however, that problems of shortage may persist for a more extended period; not because our productive capacity is likely to be insufficient once it has been restored, but because we may find ourselves unable to sell enough in world markets to purchase the large imports of food and raw materials that are essential to maintain our pre-war standard of living. This raises the problem of external economic relations which lies outside the scope of the present Memorandum. The Continental inflations of the 1920's serve, however, to indicate how serious and prolonged the dangers might be, if that problem is not satisfactorily solved. Inflationary conditions, as has been pointed out above, persisted in several countries for many years after the last war was over; and in most cases a major underlying cause was lack of means to buy from abroad.

35. It is obvious, of course, that the reservations that must be made for the unforeseeable and the unknown become greater as the period is extended. For this reason the second of the conclusions summarised below must be taken as subject to a greater margin of uncertainty than the first. It is inevitable, however, that post-war planning should be based in some degree on certain hypotheses as to the probable economic trend; and it is suggested that the working hypotheses adopted for this purpose should be as follows:-

(1) that after the cessation of hostilities, an initial phase of "boom", accompanied by the risk of an inflationary movement is to be expected, and that this phase is likely to last longer than it did in Great Britain after 1918;

(2) that there may be a still longer period, before a persistent tendency for supply to exceed effective demand reasserts itself, as distinct from temporary trade set-backs; and that during this period, if no satisfactory solution is found for the external economic problem, inflation may remain our most serious danger.

36. The moral would seem to be that while we must be prepared from the outset with appropriate measures for such

special unemployment as may arise from the maladjustments of the transitional period, the main problem of that period will not be that of stimulating the effective demand for goods and services, but rather of controlling and directing it, so as to ensure the orderly recovery of our economic life, including adequate production for export. As however, the length of this transitional period must necessarily be a matter of uncertainty, it is desirable that the plans that are prepared should have a high degree of flexibility in particular as regards timing.

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S E C R E T.

I.E.P.(42)11. COPY NO. 34

18TH APRIL, 1942.

WAR CABINET.

OFFICIAL COMMITTEE ON POST-WAR INTERNAL ECONOMIC PROBLEMS.

FUTURE WORK OF THE COMMITTEE.

Note by the Secretary.

By direction of the Chairman I circulate herewith a memorandum by the Economic Section of the War Cabinet Offices on "The Future Work of the Official Committee on Post-War Internal Economic Problems", for discussion at the next meeting of the Committee on 23rd April (Item 2 of Agenda).

(Signed) A. BASTER

Secretary.

Richmond Terrace, S.W.1.

18th April, 1942.

THE FUTURE WORK OF THE OFFICIAL COMMITTEE ON POST-WAR INTERNAL ECONOMIC PROBLEMS.

(Note by the Economic Section of the War Cabinet Offices).

1. In the discussions on the programme of work of the Committee, reference has been made to studies embracing a wider view of economic problems than can be expected to arise directly out of the departmental studies which are at present being undertaken. The purpose of this note is to discuss the objects which such wider studies might cover and the way in which they may best be developed.

2. It is suggested that such general studies serve two main functions:-

(i) One of the main objects of the Committee is, no doubt, to see that each department is aware of the plans which other departments are making for reconstruction, so that, as far as possible, these different policies may be appropriately adjusted into a well knit whole. The procedure adopted by the Committee has this purpose in mind, since (a) each department has undertaken, in preparing the paper for which it is responsible, to consult the other departments most closely concerned, and (b) in certain cases (e.g. the planning and timing of public works), special interdepartmental sub-committees have been constituted. But there are certain interconnections of a rather general character between the various policies that may be adopted by various departments for various purposes; and it is suggested that one or two separate papers on such inter-relationships between various problems would be useful to the Committee as a background for the discussion of particular departmental proposals. The paper on Raw Material Controls recently prepared by the Economic Section is an example of this type of study.

(ii) It would no doubt be wrong for the Committee to attempt to decide between long-term economic issues of a highly controversial nature; but certain broad economic objectives are now more or less universally accepted, and the attainment of these objectives will affect the immediate post-war transitional problems as well as the longer period problems of economic policy. On the external side, the erection of a permanent apparatus for eliminating disequilibria in balances of payments and providing expansion is generally regarded as desirable. Similarly, on the internal side, while there is manifestly no agreement

concerning the general question of collectivism versus private ownership, it may be conjectured that such aims as the stabilization of employment, the promotion of a higher standard of life and the elimination of obstacles to expansion are objectives on whose desirability all men of goodwill would be agreed. It is suggested that studies of the implications of some of these generally accepted economic objectives might help to bring into perspective a number of the departmental enquiries into specific issues. The paper on the prevention of unemployment (I.E.P.(41)3) prepared by the Economic Section is an example of this type of study.

3. There are a large number of possible studies of the type mentioned in section (i) of paragraph 2 above (i.e. on the interconnections between the different economic problems which will need to be solved after the war). The following is merely an illustrative list of some of the main topics of this character on which it might be useful for the Committee to have papers prepared:-

(i) The Economic Section is in the course of preparing a document describing the forms of, and interconnections between, existing wartime controls over the economic system. This paper should, by supplementing the study which has already been made of the Raw Material Controls, help the Committee to obtain a broad perspective of the system of controls with which we shall start the reconstruction period.

(ii) The interconnection between price policy, consumer rationing, raw material controls and import policy is very close. Part of this subject has already been covered in the paper prepared in the Economic Section on the Raw Material Controls; but it might be useful to prepare a further paper on the more general issues involved.

(iii) The work which is being done in another Committee on external economic relations must necessarily have great relevance to the work of this Committee. For the adoption of a particular type of currency or commercial policy may facilitate or may make impossible the adoption of particular forms of internal economic policy. A paper on the main implications for internal policy of the adoption of different types of external economic policy should help to make the discussions of this Committee as realistic as possible.

4. There are a number of further studies which might usefully be prepared on those generally accepted economic objectives to which reference has been made above (section (ii) of paragraph 2):-

(i) The paper on the prevention of general unemployment (I.E.P.(41)3) was confined almost entirely to a discussion of the long-term problems involved, and had little reference to the special difficulties of preventing unemployment which are likely to arise in the first stages of post-war transition. The Committee, in discussing the paper on these long-term problems, suggested that a second paper on the immediate problems of the transition might be useful.

(ii) It is generally agreed that after the war, both in the immediate post-war period and in the longer run, measures must be taken to ensure social security and a minimum standard of living to all classes of the community. There is, however, a large variety of types of measure which may affect this problem - (e.g. wage policy, price control, taxation, extension of social services, etc.). Moreover, many of the methods which may be advocated for the attainment of a minimum standard of living (e.g. wage policy) may have favourable or unfavourable effects upon the solution of other problems (e.g. the prevention of unemployment). It is suggested therefore that a paper on the various methods of raising standards of living and of the economic implications of these various methods should be useful to the Committee.

(iii) It is generally recognised that in the post-war world, if demobilised labour is to be absorbed and the great scarcities of goods are to be met without inflation, the utmost must be done to obtain an expansion of production of goods for export and for civil internal consumption. The successful solution of many post-war economic problems depends upon obtaining conditions which are favourable to economic expansion rather than restriction of production in the various peace-time branches of economic activity. Many of these conditions (which depend inter alia upon financial policy, price policy, wage policy, raw material control, industrial organisation) will no doubt be covered incidentally in various departmental papers now in preparation, such as the paper at present being prepared in the Treasury on post-war financial policy; but it might prove useful to the Committee to have a paper on the general issues involved.

5. The papers proposed above would in no way suggest the actual administrative action which should be undertaken by the various departments concerned. Their purpose would be to discuss some of the broader economic considerations which the departments will wish to bear in mind in formulating proposals for administrative action. They might also throw some indirect light on the question of the relative priorities which should be placed upon the particular enquiries now being undertaken by the different departments.

16TH APRIL, 1942.

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S E C R E T.

U.S.E.(42)4th Meeting. COPY NO. 45

WAR CABINET.

OFFICIAL COMMITTEE ON POST-WAR EXTERNAL ECONOMIC PROBLEMS AND ANGLO-AMERICAN CO-OPERATION.

DRAFT MINUTES of a Meeting held in the Conference Room, Richmond Terrace, S.W.1., on FRIDAY, 26TH JUNE, 1942, at 11.0 a.m.

P R E S E N T:

Sir Alfred W. Hurst,
Reconstruction Secretariat.
(In the Chair).

Sir Richard Hopkins,
Treasury.

Sir Donald Fergusson,
Ministry of Agriculture and Fisheries.

Mr. N. B. Ronald,
Foreign Office.

Sir Quintin Hill,
Reconstruction Secretariat.

Mr. P. A. Clutterbuck,
Dominions Office.

Mr. G. L. M. Clauson,
Colonial Office.

Mr. W. D. Croft,
India Office.

Mr. W. F. Crick,
Ministry of Food.

Mr. Clay,
Board of Trade.

Miss Schufeldt,
Board of Trade, Relief Section

Mr. E. M. Nicholson,
Ministry of War Transport.

THE FOLLOWING WERE ALSO PRESENT:

Sir Frederick Phillips,
Treasury.

Mr. J. M. Keynes,
Treasury.

Professor L. Robbins,
Economic Section,
Offices of the War Cabinet.

Mr. J. Meade,
Economic Section,
Offices of the War Cabinet.

Mr. R. F. Harrod,
Prime Minister's Statistical Office.

Mr. A. Baster.....Secretary to the Committee.

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S E C R E T

U.S.E.(42) 4th Meeting. COPY No. 41

8TH JULY, 1942.

WAR CABINET

OFFICIAL COMMITTEE ON POST-WAR EXTERNAL ECONOMIC PROBLEMS AND ANGLO-AMERICAN CO-OPERATION.

DRAFT MINUTES OF MEETING HELD ON 26TH JUNE, 1942.

CORRIGENDUM.

Page 1, second paragraph.

"SIR DONALD FERGUSSON ..... said ....."

Delete - second sentence, lines 6 - 8.

Substitute - "He preferred a system of regulation of production and marketing reviewed if necessary every five years."

Subject to the above amendment, it is requested that the Draft Minutes in your possession be regarded as FINAL.

4 Richmond Terrace, S.W.1.

8th July, 1942.

COMMUNICATION OF DOCUMENTS TO OTHER GOVERNMENTS.

MR. CLUTTERBUCK asked if the scheme for the International Regulation of Primary Products (U.S.E.(42)10) could be cast in a form which would be suitable for transmission to Dominions representatives in London. MR. CROFT said the proposal was of special interest to India and the question might arise of sending a copy of the document to the Government of India before the conversations with the Americans had reached an advanced stage. MR. KEYNES said he had had these considerations in mind in drafting the document. THE CHAIRMAN said the question of communicating documents of the Committee to other Governments would be one for Ministers.

INTERNATIONAL REGULATION OF PRIMARY PRODUCTS. (U.S.E.(42)14).

SIR DONALD FERGUSSON, in elaborating his note on the scheme for the International Regulation of Primary Products, said that from his experience in the Ministry of Agriculture and his knowledge of conditions in other countries he was convinced that the scheme would not commend itself to the Americans and would not work. He preferred a system of restrictions on production, reviewed if necessary every five years. MR. KEYNES said that if such a system were generalised it would be against the interests of this country. MISS SCHUFELDT said her Department felt some practical objection to the scheme on the ground that primary production would of necessity have to be strictly regulated in the period just after the war. MR. CLAUSON said his Department did not disagree fundamentally with the scheme. After a general discussion, IT WAS AGREED:-

(1) That Sir Donald Fergusson and Miss Schufeldt should prepare a considered note of their objections and present it to Mr. Keynes, who would then consider how far these objections could be met by generally acceptable amendments of U.S.E.(42)10.

(2) In default of agreement the note should be presented to the Committee together with the final version of U.S.E.(42)10 for approval and eventual submission to Ministers.

AGENDUM: MEASURES OF INTERNATIONAL ECONOMIC CO-OPERATION. (U.S.E.(42)13).

MR. KEYNES said that what was wanted was a practical list of subjects for discussion with the Americans. Mr. Pasvolsky had already suggested a list, which was being studied in the Treasury and was quite a different document from U.S.E.(42)13. SIR RICHARD HOPKINS suggested that it was necessary to clear up the matter of the agenda for the Anglo-American conversations, first giving special attention to the directions in which we wished the conversations to go, and to consider U.S.E.(42)13, in which subjects were classified on general principles, at a later stage. SIR FREDERICK PHILLIPS said that discrimination in international trade and international cartels would have first place in the American list. MR. NICHOLSON said that in any classification of schemes for international collaboration it would be essential to consider how far organs of war-time collaboration could be used, after appropriate changes, for peace-time purposes. After a general discussion, IT WAS AGREED:-

(3) That the Treasury should expedite their preparation of an agenda for the Anglo-United States conversations.

(4) That the question of the appropriate classification of subjects for the purpose of U.S.E.(42)13 should be taken up afterwards.

(5) That the question of the programme of further studies to be initiated by the Committee should be taken up when the note mentioned in Conclusion (1) of minutes of U.S.E.(42)2nd Meeting, had been circulated.

(6) That the Board of Trade should prepare material for the Committee on the regulation of international cartels.

NEXT MEETING. (7) That the next meeting of the Committee should be called by the Chairman as soon as sufficient progress had been made with any of the above matters.

Richmond Terrace, S.W.1.

27th June, 1942.

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S E C R E T

I.E.P.(42) 24 and 25 COPY NO. 2

WAR CABINET

OFFICIAL COMMITTEE ON POST-WAR INTERNAL ECONOMIC PROBLEMS.

CORRIGENDA.

I.E.P.(42) 24: Post-War Wages Policy.

Page 12, paragraph 19, sub-para. 4; lines 13 to 17.

Delete:- "On the other hand there is reason to fear that those responsible for the National Savings Campaign have been too ready to invite workers to save their war-time earnings in order that they may draw them out and have a good time when the war is over."

I.E.P.(42) 25: Demobilisation and Resettlement.

Last page

The table showing the numbers of the employed civil population, should follow the Supplementary Note on the Size of the Demobilisation Problem, and not the appendix.

Richmond Terrace, S.W. 1.

23RD JUNE, 1942.

This DRAFT MINUTES are circulated for a... it is requested that any comments be forwarded by NOON, 30 JUN 1942 after when concurrence will be assumed.

SECRET

U.S.E.(42) 3rd Meeting. COPY NO. 47

WAR CABINET

OFFICIAL COMMITTEE ON POST-WAR EXTERNAL ECONOMIC PROBLEMS AND ANGLO-AMERICAN CO-OPERATION.

DRAFT MINUTES of a Meeting held in the Conference Room, Richmond Terrace, S.W.1, on Tuesday, 23rd June, 1942 at 11.0 a.m.

PRESENT:

Sir Alfred W. Hurst, Reconstruction Secretariat. (In the Chair).

Sir Richard Hopkins, Treasury.

Sir Frederick Leith-Ross, Chief Economic Adviser.

Mr. G.L.M. Clauson, Colonial Office.

Mr. W. D. Croft, India Office.

Mr. E. M. Nicholson, Ministry of War Transport.

Sir Donald Fergusson, Ministry of Agriculture and Fisheries.

Mr. Henry Clay, Board of Trade.

Mr. P. Liesching, Dominions Office.

Mr. W. F. Crick, Ministry of Food.

Mr. E. Baring, Foreign Office.

THE FOLLOWING WERE ALSO PRESENT:

Mr. J. M. Keynes, Treasury.

Sir Frederick Phillips, Treasury.

Professor L. Robbins, Economic Section, Offices of the War Cabinet.

Sir Hubert Henderson, Treasury.

Mr. R. F. Harrod, Prime Minister's Statistical Office.

Mr. J. Meade, Economic Section, Offices of the War Cabinet.

Miss Schufeldt, Board of Trade Relief Section.

Mr. A. Baster ..... Secretary to the Committee.

AGENDA: Item 1. National Regulation of Primary Products U.S.E.(42)12.

During a general discussion of the scheme in U.S.E.(42) 10 in the light of the amendments proposed in U.S.E.(42)12 further amendments were suggested which Mr. Keynes undertook to consider.

IT WAS AGREED:

(1) That the document after revision by Mr. Keynes should be printed and circulated to members of the Committee and that if any further alterations of substance were proposed the Chairman should call a further meeting.

SIR RICHARD HOPKINS suggested that if there appeared to be a real difference of opinion about the proposals this should be made clear to Ministers. SIR DONALD FERGUSSON said that he would set down any objections he felt to the scheme in a paper for the Committee. The question whether this indicated such a difference of opinion as should be brought to the notice of Ministers could then be considered.

Next meeting.

IT WAS AGREED:

(2) That the Committee should meet next on Friday, June 26th, at 11 a.m., in the same place in order to consider Mr. Harrod's paper on "Classification of Measures of International Economic Collaboration" (U.S.E.(42) 13 - already circulated).

4 Richmond Terrace, S.W.1.

24th June, 1942.

M. McDougall

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S E C R E T

U.S.E.(42) 3rd Meeting. COPY NO. 69

WAR CABINET

OFFICIAL COMMITTEE ON POST-WAR EXTERNAL ECONOMIC PROBLEMS AND ANGLO-AMERICAN CO-OPERATION.

DRAFT MINUTES of a Meeting held in the Conference Room, Richmond Terrace, S.W.1, on Tuesday, 23rd June, 1942 at 11.0 a.m.

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Reconstruction Secretariat.
(In the Chair).

Sir Richard Hopkins,
Treasury.

Sir Donald Fergusson,
Ministry of Agriculture and Fisheries.

Sir Frederick Leith-Ross,
Chief Economic Adviser.

Mr. Henry Clay,
Board of Trade.

Mr. G.L.M. Clauson,
Colonial Office.

Mr. P. Liesching,
Dominions Office.

Mr. W. D. Croft,
India Office.

Mr. W. F. Crick,
Ministry of Food.

Mr. E. M. Nicholson,
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THE FOLLOWING WERE ALSO PRESENT:

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Sir Frederick Phillips,
Treasury.

Mr. R. F. Harrod,
Prime Minister's Statistical Office.

Professor L. Robbins,
Economic Section, Offices of the War Cabinet.

Mr. J. Meade,
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4 Richmond Terrace, S.W.1.

24th June, 1942.

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WAR CABINET

OFFICIAL COMMITTEE ON POST-WAR INTERNAL ECONOMIC PROBLEMS

DEPARTMENTAL STUDIES

Note by the Secretary

By direction of the Chairman I circulate this memorandum on "Post-War Wages Policy" by the Ministry of Labour and National Service, in fulfilment of Item VII(d) of the Programme of Work appended to I.E.P.(42) 19.

(Signed) A. BASTER.

4/5, Richmond Terrace, S.W.1.
11th June, 1942.

POST-WAR WAGES POLICY

Note by the Ministry of Labour and National Service

PART I

INTRODUCTION

1. It is impracticable at the present time to attempt to formulate a definite Government policy for post-war wages without a clearer view of possible developments in the post-war industrial system. For example, it is not yet possible to foresee how soon or how far private industrial undertakings will be free to control the nature and volume of their production. The extent of State direction and control of the movement of labour and choice of employment and the changes to be made in social services, particularly the provision for the unemployed, will affect the settlement of the terms and conditions of employment. In the political field, too, there will be potent forces at work which are likely to affect wages policy. It is impossible to foresee the nature and force of the public reaction to a successful conclusion of the war, but if the experience of 1918 is any guide it can be assumed that there will be insistent demands for large-scale organisation by the State of schemes of work and control of profits. These demands will not be as easily dismissed on this occasion as was the programme put forward by the Trade Union Movement in 1919 for the nationalisation of mines, transport, shipping and electricity supply and for the elimination of private profits

from the shipbuilding and engineering industries. Demands have already been put on record as a basis for action in a resolution of the Trade Union Annual Congress in 1941 which include the improvement of the status of economic security of the workers, the control of financial interests and the speedy provision of continuous employment for all workers.

2. In the fifth point of the Atlantic Charter expression is given to a "desire to bring about the fullest collaboration between all nations in the economic field, with the object of securing for all improved labour standards, economic advancement, and social security". In the fourth point of the Charter it is stated that an endeavour will be made, "with due respect for their existing obligations, to further enjoyment by all States, great or small, victor or vanquished, of access on equal terms to the trade and to the raw materials of the world which are needed for their economic prosperity". This presumably means that the costs of our own export industries will have to be adjusted to international costs of production. The possible reaction on our long term wages policy is obvious.

3. The home situation will undoubtedly be affected by new international relationships and by the extent to which co-operation, through the International Labour Office organisation, is effective in securing recognition of minimum standards and the need for maintaining in the post-war period international co-operation on economic and social problems. An International Labour Conference was held in the Autumn of 1941 in New York, followed by a meeting of the Emergency Committee of the Governing Body in London in April, 1942, and it is clearly the hope of the International Labour Office to play an effective part in securing international standards in relation to minimum wage levels and hours of work.

The Conference passed a number of resolutions which have been printed in Cmd. 6331. It "emphasised the necessity for the promulgation of laws where necessary fixing minimum rates of wages in order to ensure to the workers the means of satisfying the essential requirements of human beings who undertake their work in the conditions and with the exigencies of our present civilisation". It further expressed the view that "the International Labour Organisation should be in a position to give authoritative expression to the social objectives confided to it, in the rebuilding of a peaceful world upon the basis of 'improved labour standards, economic advancement and social security'".

4. Wages policy cannot, therefore, be considered in isolation from the general trend of public affairs and any attempt, at the present stage, to lay down fixed lines of policy would be fruitless and might prove, in the light of events, a definite hindrance to rapid adjustment of ideas to meet new conditions. Furthermore, close consultation with industrial interests, which has been maintained during the war on all questions of industrial policy, must be continued into the post-war period. The special importance of effective collaboration between public authorities and workers' and employers' organisations during the transition from war economy to peace economy was specially emphasised by the International Labour Conference at New York.

5. It is possible, however, to indicate some of the practical considerations to be borne in mind in the transition from war to peace and to set out shortly some of

the major problems in connection with wages policy which are likely to arise in the immediate post-war period. It is desirable to look at these problems in the light of past history and Parts II, III and IV of this paper accordingly record briefly the general outline, as follows:-

Part II - Wages Policy following the last war, 1918 to 1920.

Part III - Pre-War Conditions.

Part IV - War-Time Wages Policy.

In Part V an attempt is made to set out some of the problems which may have to be considered after this war with certain observations on them.

PART II

WAGES POLICY FOLLOWING THE LAST WAR - 1918-1920

6. At the close of the war of 1914-1918 a period of industrial dislocation and of severe unemployment was anticipated and to meet this possibility the first act of the Government was to convene a national conference of representatives of employers' organisations and trade unions before which the Prime Minister placed a proposal that, as a first step towards the restoration of general confidence, the rates of wages prevailing in each trade or industry in any district at the date of the Armistice should be maintained for a limited period. As a result of the negotiations the Wages (Temporary Regulation) Act, 1918, was passed on 21st November, 1918. The Act carried out two main objects:-

(a) It continued for six months, as statutory minimum rates, the standard rates existing at the date of the Armistice or such other rates as might be substituted for the standard rate by an arbitration award or by a voluntary collective agreement approved by the Minister of Labour; and

(b) it repealed the provisions of the Munitions of War Acts prohibiting strikes and lockouts and discontinued compulsory arbitration except as regards differences about what was the standard rate or whether another rate should be substituted for the standard rate.

The arbitration tribunal set up under the Act (The Interim Court of Arbitration) was, in effect, the war-time Committee on Production with additional members. The Act was twice extended, but terminated in September, 1920. Under it claims for advances of wages were numerous and in some instances serious stoppages of work resulted, but a very large number of disputes, far in excess of the number of stoppages, were settled by arbitration, conciliation or voluntary agreement.

A fuller description of the Wages Policy adopted after the last war will be found in Part II of the Nuffield College Memorandum circulated as I.E.P.(42) 3.

PART III

PRE-WAR CONDITIONS

Voluntary Collective Bargaining

7. The strength of the system of collective bargaining in this country is the result of a gradual development over many years. As long ago as 1894 a Royal Commission expressed approval of the development of voluntary conciliation boards which had already proved successful on a small scale. The rate of progress depended upon adequate organisation and mutual confidence but by 1914 most of the staple industries in the country had adopted a system of settling terms and conditions of employment by joint agreements. In 1917 the Whitley Committee was appointed and in a series of reports proposed the formation of National and District Joint Industrial Councils to regulate wages and conditions. At the same time the Committee reported against compulsory arbitration and urged continuance of a system whereby industries settle their own differences with resort, where necessary and by mutual agreement of both sides, to voluntary arbitration. This policy was enacted in the Industrial Courts Act, 1919.

8. In the period 1918 - 1939 voluntary collective bargaining was extended over a wide field with the approval of successive Governments and of industrial organisations. The Balfour Committee on Industry and Trade dealt with the subject fully in their final report in 1929 and said:

> "However imperfect they may be and however open to criticism may be some of their results, we are convinced that on the whole the methods of collective bargaining and settlement of wages questions which have grown up spontaneously in accordance with the circumstances of different trades are vastly preferable to any uniform cast-iron system imposed by law. There is abundant evidence that this view is shared by the representative organisations both of employers and employed in the principal industries."

The strength of the system lies in its adaptation to the needs and circumstances of particular industries and to the encouragement it affords to those with knowledge of practical problems to rely on self government.

Wages Legislation

9. In some industries it has been necessary for the State to intervene to the extent of providing machinery for the establishment of minimum terms and conditions of service.

(a) The Trade Boards Acts, 1909 and 1918 provide for the establishment of Trade Boards whose duty it is to fix minimum rates of wages which are enforceable under penalty. The Minister of Labour can apply the Acts to any trade in which he is of opinion that "no adequate machinery exists for the regulation of wages throughout the trade and that having regard to the rates of wages prevailing in the trade it is expedient that the principal Act should apply to that trade".

The Acts at present apply to some 50 trades which (before the war) employed some 1,500,000 persons. There is nothing in the Acts to prevent individual contracts or collective agreements for the payment of wages at rates in excess of the statutory minimum rates.

(b) The Coal Mines Minimum Wage Act, 1912, (passed for the purpose of terminating a national stoppage of work) provided for the setting up of Joint District Boards for the purpose of fixing minimum rates of wages for the various classes of workers in the industry. The Boards consist of representatives of the owners and of the men with an independent chairman. The machinery set up under the Act is still in existence, but the minimum rates have been effective only to a limited extent, owing to their having been fixed generally at a lower level than the operative rates arranged from time to time as the result of collective bargaining.

(c) Under the Agricultural Wages (Regulation) Act, 1924, minimum rates of wages in agriculture in England and Wales have been fixed by Agricultural Wages Committees for each county or (in some cases) part of a county, and statutory effect has been given to these rates by orders made by a Central Agricultural Wages Board. The Central Board was not empowered to alter any rates fixed by a Committee, but in certain limited cases (e.g., default of a Committee) the Board could itself fix minimum rates. The Agricultural Wages (Regulation) Act, 1940, amending the Act of 1924, provides that a national minimum wage may be fixed for men by the Central Board after consultation with the Committees. The minimum rates fixed by the Committees must be such as to ensure that no man of full age employed whole time shall receive less than the national minimum wage; and the Committees are required to have regard to the national minimum wage when fixing minimum rates for other classes of workers.

The Agricultural Wages (Regulation) (Scotland) Act, 1937, established machinery consisting of district committees and a central Wages Board for minimum rate fixing in Scotland generally similar to that of the Act of 1924 in England. Under the Act of 1937 in Scotland the Department of Agriculture had, however, power to direct a district committee to reconsider a minimum rate. The Agricultural Wages (Regulation) (Scotland) Act, 1940, transferred this power to the Scottish Agricultural Wages Board. The Board is also empowered by the Act of 1940 to vary the decision of a district committee after taking into consideration any representations made by the Committee.

(d) The Road Haulage Wages Act, 1938, Part I, provides machinery similar in principle to the Trade Boards for fixing the minimum remuneration of some 250,000 workers engaged in the road motor transport industry (Goods). Under Part II of the Act certain classes of road haulage workers may complain to the Minister of Labour that remuneration is unfair. Unless the complaint is otherwise disposed of, it is referred for settlement to the Industrial Court, which can make a binding award.

(e) An entirely novel form of State intervention in industrial relations was made by the Cotton Manufacturing Industry (Temporary Provisions) Act, 1934. Its purpose was to make temporary provision - for a period of three years - for enabling statutory effect to be given, in certain circumstances, to rates of wages agreed upon between representative organisations of employers and workers in the weaving section of the cotton industry. Serious deterioration of trade had led to disregard of collective agreements which had formerly been generally observed and the industry was faced with the possible collapse of the whole system of collective bargaining. Briefly the Act enables the Minister of Labour to extend to the whole of the weaving section of the industry the results of collective

bargaining between representative organisations but he is in no way responsible for the terms of the agreement or required to intervene in the negotiations between the organisations.

The machinery of the Act was used and orders were made in 1935 and 1937. When war broke out there was under consideration the question of extending the scope of the Act to other sections of the cotton industry. Although, in these circumstances, the Act has been continued year by year, further occasion for its use has not arisen because of the provisions of Part III of the Conditions of Employment and National Arbitration Order, 1940 (see paragraph 13 below).

10. As indicated above the policy in peace-time has consistently been to encourage voluntary collective bargaining and not to intervene in the settlement of wages and working conditions except for that purpose or for the purpose of preventing the payment of unfair or exceptionally low wages. This policy has, moreover, been consistently supported by the industrial organisations of employers and workers.

Under pressure of war there have been temporary modifications of this policy, as described in Part IV of this Paper.

PART IV

WAR TIME WAGES POLICY

Development under the first War Government.

11. The problems and difficulties of wage regulation in war-time were keenly remembered from the last war by workers, employers and the Government. In 1939 the Government took the first steps towards minimising the risk of industrial friction by adopting a policy of price control and consulting the National Joint Advisory Council (representing the Trades Union Congress and the British Employers' Confederation) on the question of "slowing down the tempo" of wages increases. The approach to the Advisory Council was made personally by the Chancellor of the Exchequer in December, 1939, when he explained the effects of the war on supplies, the danger of inflation and the policy of price control (particularly of items entering into the cost of living index), and suggested that an increase in the cost of living ought not necessarily to involve an increase of wages rates. The immediate reaction of the trade union side of the Council was that before assenting to any form of wages control they would need to be assured that there would be equality of sacrifice among all sections of the community and that more attention would need to be given to the question of (i) profits, (ii) the resources of taxation, (iii) the relative levels of remuneration in different industries and (iv) the practicability even in war-time of transferring purchasing power from the better to the less well remunerated members of the community. They undertook to consider the matter carefully and subsequently entered into private conferences with the employers with the object of reaching agreement on the question raised by the Chancellor. (At this time (December, 1939) the cost of living had risen some 12% above the September, 1939, level and the average level of rates of wages had risen by less than 4%).

Development under the second War Government.

12. Before the National Joint Advisory Council were ready to reply to the Chancellor, there occurred the grave military situation of May, 1940, and the formation of a new Government, whose first Act was to take power in the Emergency Powers (Defence) Act, 1940, to require all persons without distinction "to place themselves, their services, and their property" at the disposal of His Majesty. The new Minister of Labour immediately invited the advice and assistance of the Council as to the exercise of the new powers taken by the Government. The first use of this power was after consultation with the Council to make Defence Regulation 58A, which provided inter alia that, in determining the terms upon which services should be performed, the Minister should have regard to collective agreements between organisations of employers and trade unions.

13. The National Joint Advisory Council reached agreement, in June, 1940, on the question put to them by the Minister of the best means of removing wages problems from the field of controversy during the critical period following May, 1940. The Council's advice (which was unanimous) was to the effect that wages regulation should remain with the voluntary joint machinery in the various trades and industries, but should be supplemented, in cases in which disputes arose, by compulsory arbitration without stoppage of work. This advice was accepted and effect was given to it in July, 1940, by Parts I and II of the Conditions of Employment and National Arbitration Order, 1940 (S.R.O. 1940) No.1305). The Order contains a provision prohibiting a strike or a lockout unless the dispute has been reported to the Minister and has not been referred for compulsory arbitration within 21 days of the report being made. The policy of the Government has been to continue to deal with disputes on the basis of co-operation with the organisations in industry, to refer disputes to compulsory arbitration only after other means of settlement have been exhausted, and to take legal action only in cases in which it can rely on the support of the constitutional elements among the workpeople and in which the objects of those concerned are definitely mischievous. Nevertheless, the anti-strike provision has had a substantial deterrent effect and, whether owing to this or other causes, the average of time lost owing to stoppages of work is considerably less than in the last war.

At the same time, in accordance with a recommendation by the National Joint Advisory Council, Part III of the Conditions of Employment and National Arbitration Order provided that all employers should observe terms and conditions of employment not less favourable than the terms and conditions which have been settled by machinery of negotiation or arbitration "to which the parties are organisations of employers and trade unions representative respectively of substantial proportions of the employers and workers" in the trade or industry in the district concerned. Any question as to nature, scope or effect of the recognised terms or as to whether any employer is observing them may be reported to the Minister and dealt with as if it were a trade dispute under Part I of the Order. Part III of the Order is in effect an extension and generalisation of the provisions of the Cotton Manufacturing Industry (Temporary Provisions) Act, 1934, which is mentioned in paragraph 9(e) above. Under this Part of the Order only nine cases - each relating to a single employer - have been referred to the National Arbitration Tribunal for settlement, but there is no doubt that the provision has had considerable effect in inducing employers at large to conform to the obligations voluntarily assumed by those employers who participate in collective bargaining.

14. By May, 1941, the official cost of living figure had risen to 28 per cent. above the level of September, 1939. Since May, 1941, the figure has remained practically stationary. Meanwhile the average level of full-time weekly rates of wages has risen slowly to about 28 per cent. above pre-war (as at end of March, 1942). Owing to the longer working hours and the more frequent working of night-shifts and the extension of systems of payment by results, total earnings have of course risen more than rates of wages. Periodical returns of earnings are not available, but special enquiries by the Ministry of Labour and National Service have shown that between October, 1938, and July, 1941, average total earnings rose by 42.3% as compared with an increase of 18% in average rates of wages. Resort to compulsory arbitration has been on a relatively small scale and the vast majority of wages adjustments have been effected by the machinery of voluntary collective bargaining without any kind of Government intervention. The policy of the Government in regard to the stabilisation of prices and regulation of wages is concisely summarised in a White Paper (Cmd.6294) issued in July, 1941.

PART V

POST-WAR WAGES POLICY

General Considerations

15. As stated in paragraph 1 of this memorandum it is not possible to formulate a Government wages policy to meet post-war conditions without knowledge of the social and industrial changes which may take place. On the one hand, there may have to be considerable control of employment accompanied by some restriction on the right of workers under peace conditions to refuse employment or to choose the terms of employment.

On the other hand, in so far as control of industry is relaxed so as to encourage and restore private enterprise and to create favourable conditions for the employer to compete in the available markets, the workers are entitled to their pre-war freedom to sell their labour to the highest bidder and to refuse employment under certain terms. The role of the State may then be confined to minimum wage legislation, State unemployment insurance, and other payments for the relief of distress.

Industrial policy generally will have to be related to the problem of creating increasing consumer demands abroad and at home, and of securing over a period a rising standard of living with increased leisure and increased purchasing power in wages and earnings. Such a policy is by no means inconsistent with the objective of reduced costs per unit of production. Experience shows that with increased efficiency of management production costs can be reduced while wages are increased, and any additional margin in wages over the essential living expenses is available to create new demands. The role of the State must therefore be to promote stability and to keep in check forces which would operate to the disadvantage of rising standards. So far as wages movements are concerned, the following are some of the problems which are likely to arise.

Restoration of Pre-War Practices

16. Under the Restoration of Pre-War Trade Practices Act, the trade practices which have been or may yet be departed from during the war are to be restored after the war, except where agreements are made to the contrary. The Act is not directly concerned with wages, since the trade practices with which it is concerned are defined as rules, practices or customs with respect to "the classes of persons to be or not to be employed" and "the conditions of employment, hours of work or working conditions". The most frequent and most controversial changes of practice with which the Act is concerned are undoubtedly those connected with the many aspects of the dilution of skilled labour and the demarcation of work between different classes of workpeople. The Act does nothing more than re-establish temporarily - that is, for a period of 18 months after the war - the practices which existed immediately before the war. No doubt large numbers of workpeople who have benefited by a change of practice will find that, during the period of its operation the Act may operate to their disadvantage; but the benefits they have had during war-time were only made possible by the sacrifices made in the national interest by those classes of workers who had established and maintained practices before the war.

As already stated, the Act does not deal directly with wages but it is bound to have reactions on wages policy and practice. Other influences will also be at work, but the effect of the Act taken alone would be to increase the wage costs per unit of production.

Collective Bargaining

17. Perhaps the major question of wages policy will be whether there should be any State regulation of wages (other than in industries to which minimum wage regulation may have to be applied) or whether wages should be determined by collective bargaining. This issue has been raised at frequent intervals during the war and is still a matter of discussion. On the one side it is argued that one of our greatest dangers is from inflation due to wage increases and that in order to keep control in the field of finance, especially at a time when employers have little immediate financial interest in stabilising wages, the State ought to have some additional machinery to prevent excessive rises in wages while at the same time stabilising prices. On the other hand, it is pointed out that the system of collective bargaining which is deep-rooted in the industrial structure of the country has so far proved successful under war conditions, that both sides in industry have shown a real sense of responsibility in handling the matter, that direct State control involves a danger of strikes directed not against employers but against the State, and that the experience of State control in the last war does not constitute a happy precedent. So far the increase in the average level of full-time weekly rates of wages since the war began has not exceeded the rise in the cost of living and in so far as earnings have been increased owing to longer working hours, over-time, night work and payment by results, the State has gained through increased production.

After the war the dangers of inflation may be just as great as, if not greater than, during the war and there may be strong pressure to introduce State control of wages. The decision will no doubt be taken largely on war-time experience, but if adequate steps can be taken to maintain stabilisation of prices, there seems to be no reason why the system of

collective bargaining, supplemented in certain cases by statutory machinery, should not be allowed to find a solution for the adjustment of wages and conditions in the immediate post-war period. It would be more difficult to justify State control after the war than during the war, because of the general desire for liberty of action, but if there should be a tendency for wages to rocket upwards some system of State control might have to be imposed.

Compulsory Arbitration

18. The advantages and disadvantages of a system of compulsory arbitration were often discussed before the War. Such a system was tried in some other countries, but was never put into operation here except during the last war. During the war the system has on the whole fulfilled its object, and the Government will have to decide whether they will seek to continue it after the war. It is fairly clear that it could only be maintained with the general agreement of the national employers' and workers' organisations, but the Government would probably have to give a lead in the matter, and they may decide that it would be in accordance with their post-war policy generally at least to attempt for a time some system of compulsory arbitration.

Compulsory arbitration has been introduced under war conditions primarily as a short-term policy to avoid loss of production due to trade disputes. A long-term post-war policy for the settlement of disputes must rest on some other basis than that of avoiding loss of production; for example, in the export trades the competitive power of industry may be of at least equal importance.

After the war we may well have great difficulty in recovering our export markets. A series of lengthy industrial disputes would have a most detrimental effect. Industrial disputes certainly retarded our progress after the last war. For instance, at the end of 1918 a prolonged strike of iron moulders, and a consequent shortage of castings, reduced employment in the engineering and metal industries; in the Autumn of 1920 the decline in employment was accelerated by a shortage of fuel resulting from a strike in the coalmining industry between the 18th October and the 4th November. A still more serious strike in the coalmining industry took place in the Spring of 1921 when the stoppage was prolonged for over 3 months and resulted in a scarcity of fuel which greatly accentuated the effects of the depression in trade; several important industries largely dependent on coal were brought almost completely to a stop. There is therefore no doubt about the need for avoiding lengthy stoppages of work after this war, but it is another question whether any system of compulsory arbitration is the best means of achieving that object.

It is hardly practicable either in war or in peace to prosecute large numbers of men if they insist on withdrawing their labour in order to force their demands. In war-time, however, the loss of production resulting from stoppages of work is regarded by public opinion as almost a criminal offence, and nearly all the stoppages which have occurred have been contrary to the advice of the Trade Unions. Controls of all sorts are commonly accepted as necessary in war-time, and there is a limitation on employers' profits. In ordinary peace-time conditions the Government would not have the same backing from public opinion, and the Trade Unions would naturally claim to reassert their hard-won rights to withhold labour as a means of securing their objects. Moreover, the Government might well

find itself in a much weaker position if it were brought into a direct relationship with workpeople on questions of terms and conditions of service than if full reliance were placed upon the influence of representative organisations of employers and workpeople.

The more immediate issue is whether the Government should attempt during the immediate post-war period to continue the system of compulsory arbitration. This will depend largely on the extent to which other war-time restrictions (on employers as well as on workers) are maintained and on the degree of success the Government achieve in the effort they must make to arouse public opinion to the conviction that the immediate post-war years are no less critical for the future well-being of the country and demand no less the re-adjustment of ideas and, if necessary, the sacrifice of individual freedom than the period of the war itself. If the need for the continuation of national unity and sacrifice is properly appreciated by the nation, it should be possible to secure the recognition by both sides of industry of the desirability of maintaining the principle of compulsory arbitration for a transition period immediately after the war. Even so, if there is any serious challenge to the continued prohibition of strikes or lock-outs when industry has ceased to be on a war footing, it will soon be made evident that the power to [illegible] individuals for an offence under some Regulation or Act of Parliament is not an effective instrument for dealing with an organised movement.

Price Stabilisation

19. The question of price stabilisation is to be dealt with primarily in the Treasury memoranda, but the question is of vital importance in relation to wages policy. Our general object after the war should be to avoid, so far as possible, violent fluctuations in the cost of living while maintaining a rising standard of consumption. We must seek to avoid a repetition of the 1919 boom followed by the depression of the ensuing years. So far as wages policy is concerned, therefore, there would be great advantage in continuance of a policy of price stabilisation for at least 18 months after the end of the war.

In the immediate post-war period, earnings of individual workers will fall as over-time is reduced, and the weekly income of many households will be further reduced as women leave industrial employment. At the same time, heavy income tax liabilities will continue for some time. A reduction of income will call for radical re-adjustment of working class expenditure and savings, and the situation should not be prejudiced further by the withdrawal at too early a date of the control of prices of commodities - especially those which are included in the cost of living index figure.

Subsidisation of food prices has, during this war, been on such a large scale that its indefinite continuance on the present scale may not be possible. Great difficulties will, however, undoubtedly arise when the subsidies are withdrawn, especially in view of the inevitable reduction of earnings mentioned in the preceding sub-paragraph, and it may well prove necessary to withdraw them gradually. The price structure must eventually find a new economic level, and if experience shows that we shall be unable, after this war, for a considerable period to obtain command of a supply of goods sufficient to attain the general standard of living whichh prevailed before the war, it is preferable from the point of

view of wages policy that the cost of living should rise gradually rather than that the cost of living should be stabilised but money income reduced.

In this connection it is pertinent to raise the question of controlling the release of post-war credits which have been accumulated under the income tax arrangements, under E.P.T. and through the National Savings campaign. In the first place it may not be possible after the war to maintain the present sdale of savings out of money income even if household income were maintained at the war-time level, and the cost of living index and the prices of goods not now controlled may be forced up in consequence. If in addition credits were released too suddenly, they might create a false impression of prosperity and especially if they were released at a time when consumers' goods were in short supply they would inevitably create an inflationary movement. On the other hand, there is reason to fear that those responsible for the National Savings campaign have been too ready to invite workers to save their war-time earnings in order that they may draw them out and have a good time when the war is over. If, as appears almost inevitable, it will be necessary to "freeze" these credits for a considerable period after the end of the war and only allow releases on proved need, would it not be wiser to explain this policy now in order to prevent the disappointment and discontent which will inevitably arise if a "freezing" Order is made before public opinion has been prepared? If public opinion is unprepared, such an Order might well lead to industrial disputes and demands for higher wages in order to compensate for the failure of the Government to repay the income tax contributions which had been promised after the war. It is understood that the Germans have faced this difficulty and have provided that the "Iron Savings Accounts" of wage and salary earners shall be subject to one year's notice of withdrawal.

Guaranteed Week's Wages

20. Under the Essential Works Orders, which will probably cover between 6 and 7 million workers by the end of the war, all these workers are guaranteed a week's wage at time rates irrespective of whether they are fully employed or not. The continuance of the Essential Works Orders themselves has been examined in the paper on Labour Controls (I.E.P.(42) 2) but the question of continuing a guaranteed week might conceivably be separated from it.

In the view of many, a guaranteed week is one of the essential elements in social security and many workers who have enjoyed this guarantee for the period of the war will be unwilling to give it up. It may be hoped that some industries which have had experience of the system during the war will adopt it by voluntary agreement, but the Government will have to decide whether to continue the system in its own industrial establishments or through Government Controls maintained after the war, and whether, in relation to private enterprise, the adoption should be left to voluntary agreement or should be imposed by Statute.

Minimum Wage Regulation

21. An account has been given in Part II of this paper of minimum wage regulation in operation before the war. During the war a few additional Trade Boards have been established. Should there be any extension of such legislation after the war or should reliance be placed on

collective bargaining?

The most important element in social security would be the establishment for all workers of a minimum standard of living, and if the need were proved it might be necessary to extend minimum wage regulation to occupations not now covered. Apart from coalmining and the catering trades for which proposals are now under consideration, there is, at present, little evidence of the need for such legislation. A more immediate question in this country is the relation of the wage levels in the different industries (see para. 26).

Family Allowances

22. This subject will have to be considered in connection with Post-War Wages Policy. The Treasury have recently issued a White Paper on the subject, and no doubt its relation to the Social Services is being examined by Sir William Beveridge's Inter-departmental Committee on the future of those Services. This is hardly the place to set out the arguments for and against family allowances, but the Committee will wish to consider whether this is a feature of post-war wages policy which they should bring to the notice of the Ministerial Committee.

Compulsory Enforcement of Voluntary Agreements

23. Before the war there was advocacy in certain quarters of a widespread extension of the principle embodied in the Cotton Manufacturing Industry (Temporary Provisions) Act, 1934, referred to in paragraph 9 (e) above. The national employers' and workers' organisations were not in favour of such a general extension and the principle was never adopted by any Government before the war, except in relation to the cotton industry. The principle has, however, as explained in para.13 above, been embodied in Part III of the Conditions of Employment and National Arbitration Order of July, 1940, and is now operative, though very few cases have been reported under this Part of the Order. The Government will have to decide whether this portion of the Order (i) should be terminated on the cessation of hostilities, (ii) should be allowed to lapse when the Defence Regulations cease to be operative, or (iii) should be embodied in permanent post-war legislation.

So far as the workers are concerned, the principle has the advantage of protecting their agreed terms and conditions of employment against attack by individual employers, e.g. in the less well organised industries or under economic pressure during periods of slump. On the other hand, in so far as legislative backing to agreed conditions induces a reluctance to make adjustments to meet changed circumstances, it may lead to more unemployment during periods of depression. Further, it may substitute reliance on machinery provided by the State for action by Trade Unions on behalf of their members, and, in the long run, weaken the position of Trade Unions in making agreements. So far as employers are concerned, the principle has the advantage of protecting good employers against under-cutting by bad employers, though as a counterpart it tends to give large combines the power of forcing small employers out of production by the adoption of a high wage standard.

Automatic Adjustments of Wages to Changes in the Cost of Living

24. It has been the practice in several industries to fix wages automatically according to a sliding scale based on the

cost of living index. At the present time this system applies to about 3 million workers. The question may well arise after the war as to whether this system should be extended more generally or should be reduced in extent, and the Government may be expected to give a lead in the matter.

The system has certain great advantages. It tends to reduce disputes within industry since wage adjustments take place automatically, and, moreover, it provides that workers do not suffer financially from any changes in the financial policy of the country or through international economic and financial operations.

On the other hand, the system is open to certain grave objections, especially if it were applied on too large a scale. Under the normal system of collective bargaining there is a "lag" between the raising of wages following a rise in the cost of living, or reduction following a fall. This "lag" tends to prevent excessive rises and falls in wages and thereby tends to even out trade cycles. For instance if there were no such lag, a rise in the cost of living would immediately be followed by a rise in wages which, in themselves, would immediately produce further rises in the cost of living. Further, in so far as the cost of living figure represents taxation (as it does at present in relation to the taxes on tea, sugar, etc., and the purchase tax) it is unreasonable that workers who are remunerated on a sliding scale should escape what is intended to be a universal indirect tax; conversely, if an indirect tax is remitted, it is unreasonable that workers should not participate in the benefits.

A further argument against automatic adjustments of wage rates to changes in the cost of living is that any such system would handicap any efforts to produce an equilibrium in the international economic position after the War by adjustments of exchange rates. For instance, if other countries come to compete with this country more severely in foreign markets, and the demand for British exports declines, Britain must do without some of her former imports. Either British wages must fall, and fewer imports be bought although their price remains the same, or British currency must decline in value, and the price of foreign goods in terms of British money rise, while wages remain constant. In either case the result is a rise in the cost of living relatively to British wages, any attempt to offset which by a rise in wages can only start the whole process over again. There is no escape from one or other of these courses, and a blind seeking after a sliding-scale policy must not only jeopardise international adjustment but land this country in a fruitless and disastrous attempt to catch its own tail.

Women's Wages

25. One question which it will not be possible to burke after the war is the relation of women's wages to men's wages, both generally and in the same industry or on the same work. This raised the fundamental question of whether wage is primarily a payment for the value of work down or a payment to meet social responsibilities.

The Government policy in the past has been to rely on the results of collective bargaining and in relation to its own staff to follow those results. To attempt to alter this policy would be a change of the first magnitude both for the Government and for industry, but women will have taken a larger part in this war than on any previous occasion in the country's

history and their demand for a better status in relation to men, as reflected in a more comparable level of wages, will be even stronger than after the last war.

Effect of wages policy on policy for prevention of "slumps"

26. In order to prevent a recurrence at intervals after the war of periods of depression it has already been suggested to the Committee in I.E.P. Paper (41) 3 that financial measures should be taken to expand and to stabilise at a high level the general demand for goods and services. But the favourable effects of such financial policy would be offset if (i) it were accompanied by restriction and monopolistic devices in industry and in distribution, which caused an increased demand for goods and services to be met by a rise in prices rather than by an expansion of production, or (ii) money wage-rates began a rapid upward rise whenever the demand for labour was really good; if such a rise took place, the financial policies of expansion would have to be abandoned in order to avoid the vicious spiral of inflation.

The continuation of a policy of moderate changes in wage levels even in times of active employment or severe depression in peace-time, is therefore an essential element in a successful anti-depression policy, and it will be necessary to consider how this object should be achieved. Under any system of voluntary collective bargaining it would be necessary to rely very largely on the moderation and breadth of outlook of both employers and the Trade Union leaders. Employers and Trade Union leaders would have to be convinced that moderation in pressing general demands for reductions in wages on the one hand or for higher wages on the other was essential to the maintenance of employing capacity and social security. Also Trade Union leaders would have to be convinced that

(i) the policy would not rule out all increases in wages, especially for the lower-paid workers, in individual industries,

(ii) the Government were taking adequate steps to curtail employers' excessive profits and to prevent monopolistic devices in industry,

(iii) so far as progressive rise in the standard of living is made possible by technological advance, increased demand, and other causes, the workers will be entitled to a full share in the improvement in the way of higher wages, shorter hours, better social services, etc.

It may be thought that it would be impossible for Trade Union leaders to accept and act upon these assurances under any system of private enterprise and free competition. There might, however, be hope of success if the principle were put forward by the State as part of an orderly system of post-war planning, designed to provide social security and to remove the danger of industrial depressions, and agreed after full consultation with the Trades Union Congress General Council and the British Employers' Confederation. It would also be desirable, if possible, to get the principle agreed between the leaders of all political parties as an essential feature of post-war reconstruction and so removed from the field of party politics.

Sheltered and Unsheltered Trades, and International Standards

27. Before the war there was disparity in wage levels between sheltered trades which were not open to world competition and unsheltered trades, and though no trades are now unsheltered, the pre-war disparities in basic rates have not entirely disappeared. The export trades in the immediate post-war period will probably secure a ready market for their goods and may be able to raise their wage standards without State assistance. No doubt steps will be taken to create additional demands by raising standards in backward countries. If, however, world conditions were to be stabilised on the former competitive basis the old inequalities would tend to recur. We cannot allow the export trades to become once again the Cinderella of British industry offering the lowest wages, and it may well be that an attempt must eventually be made to adjust differences in wage levels with a view to securing recognition of the value to the community of the services of various classes of workers.

The exact nature of the problem and its solution will largely depend on new adjustments in international economy. No doubt the immediate post-war problem will be the world supply and distribution of goods needed for the personal needs of large masses of population who have suffered from several years of deprivation. Every country will also have huge demands for materials to make good the devastation of war. This country must develop its overseas markets, particularly in view of the loss of our income from overseas investment. Failure to do so must result in either a reduction in the pre-war standard of living or a drastic transfer of population from this country to countries which can offer opportunities of development. Steps must be taken in the direction of greater equality between standards of living and the burdens on industry in the competing countries. The solution may perhaps lie in the formation of much larger economic units and the adoption of measures to ensure approximately uniform standards of living within each large unit. The wages aspect of these problems may appear to be only incidental to world planning, but any plans for the post-war world which do not provide economic security and a reasonable standard of living for wage earners in all industrialised countries will be doomed to failure.

Ministry of Labour and National Service.

8th June, 1942.

I.E.P. (41.) 3	General Unemployment.
I.E.P. (42) 11.	Future Work of Committee
I.E.P. (42) 24.	Post-War Wages Policy.
I.E.P. (42) 26.	Draft Report of I.E.P. to R.P.

Committee Section.
Mr Olley.

Mr. Harrod

I.E.P. (41) 3 is at present in the country. Mr. Olley can get it by tomorrow morning if you require it.

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S E C R E T.

I.E.P.(42) 26.

17TH JUNE, 1942.

COPY NO. 8

WAR CABINET.

OFFICIAL COMMITTEE ON POST-WAR INTERNAL ECONOMIC PROBLEMS.

DRAFT INTERIM REPORT.

"THE INTERNAL ECONOMIC PROBLEMS OF THE POST-WAR TRANSITIONAL PERIOD".

In connection with Conclusion 2 of the Draft Minutes of the meeting of the Committee on 11th June, 1942, I circulate herewith a revised draft of Document I.E.P.(42) 22.

(Signed) A. BASTER

Secretary.

Richmond Terrace, S.W.1.

17th June, 1942.

DRAFT INTERIM REPORT.

INTRODUCTION.

1. The object of this report is to present a broad survey of some of the salient economic problems with which we shall be confronted in the years immediately following the war, and to obtain instructions on certain matters of policy which must be observed in drawing up further plans. The report is essentially a preparatory note. Separate memoranda of a more detailed character will be prepared on each of the main problems dealt with, and as the study thus proceeds, the Committee may introduce some differences of emphasis or method of presentation. To that extent, therefore, the conclusions should be regarded as provisional.

2. To get a clear perspective of the nature of these problems, a threefold classification is convenient:-

(a) There are the problems which will arise immediately hostilities come to an end.

(b) There are the problems which will arise because of the peculiar difficulties of the transition from war to peace.

(c) There are more fundamental problems concerning the objectives to be aimed at in the more distant period when these immediate difficulties are at an end.

3. The first class of problem, the problems of the morrow of the armistice, are for the most part problems of a highly technical nature, e.g. demobilisation, liquidation of war contracts, etc., and fall largely within the province of the departments which will be most immediately concerned. They are, therefore, most conveniently dealt with in a series of separate memoranda, the preparation of which is already well in hand.

4. Nevertheless, the nature of the measures which are to be put into operation at this point must necessarily depend in some degree upon the view which is taken of the conditions likely to prevail in the years immediately following. If it be thought, for example, that the years following the end of the war are likely to be years of economic depression, the demobilisation plan will differ widely from that which would be thought appropriate if conditions of active trade were to be regarded as more probable. Preliminary study seems to suggest that the conditions prevailing during these years will be of a highly novel and intricate character, presenting difficulties hitherto without precedent; and the problems which emerge are problems to which solutions must be found if we are to move without grave dislocation towards the happier days which we all hope are ahead. It has, therefore, been thought desirable to devote this interim report chiefly to a study of the problems of the transitional period and the formulation of broad outlines of possible solutions.

5. Just as the solution of the problems of the armistice depends partly on the view taken of the problems of the transitional period, so solution of the problems of the transitional period will depend partly upon the view taken of more distant objectives. This is a matter necessarily involving political issues upon which, at this stage, Ministers may not wish to make final pronouncement. This report, therefore, makes no attempt to go deeply into these questions. But in a final section, it has been thought desirable to set forth the way in which some of the transitional problems are related to the problems of the longer period, and to set forth explicitly one of the main assumptions concerning ultimate objectives upon which the work of the Committee is being based.

6. The report falls into three parts. In Part I the problem is stated. In Part II the various measures which seem to be necessary are discussed. In part III an attempt is made to show the connection between these measures and the problems of the more distant future.

PART I.

THE GENERAL NATURE OF THE PROBLEM.

7. The main economic problem during the war has been to transfer resources from use for inessential civilian purposes to use for the armed forces or for the production of munitions and other essential goods and services. The extent to which this mobilisation of resources has proceeded is illustrated by the following figures of national expenditure:-

	1938	1941	Change between 1938 and 1941
		£ millions	
Personal expenditure on consumption at cost of production	3,584	3,863	279
Expenditure on goods and services by public authorities	833	4,182	+3,349
Private net investment at home (including war losses made good)	406	- 493	- 899
Net investment abroad	- 55	- 798	- 743
TOTAL NATIONAL INCOME(1)	4,768	6,754	+1,986

Between 1938 and 1941, Government demand for goods and services rose by no less than £3,349 millions. In the same period personal expenditure rose by considerably less than the increase in the costs of goods and services for consumption, so that an appreciable decline (estimated at some 15 to 20 per cent.) in real consumption had in fact taken place. At the same time private investment at home fell by some £899 millions; for private enterprise at present is refraining from many capital extensions and is not fully replacing its fixed or working capital. Investment abroad also declined by some £743 millions a year, as the community was enabled - by living on its foreign assets or by borrowing from abroad - to import considerably in excess of its exports.

8. The outstanding problem of the post-war transition will be to reverse all this - to transfer labour and other economic resources as smoothly as possible back to peace-time uses - to revive exports and the industries making for domestic consumption. This transition cannot, however, be smoothly carried out unless any great inflation or deflation of the national income is avoided, and unless the disequilibrium of the balance of payments is speedily remedied. And this is a problem of great delicacy. For if it is to be solved successfully, it

(1) Includes war risks insurance premiums and indirect taxes and rates other than those specifically on consumption.

is necessary that the increase in other expenditure must take place substantially at the same speed as the decline in government expenditure; and at a time when there will be much purchasing power accumulated during the war and now anxious to find an outlet, this will not be easy to bring about. Furthermore, as a result of the using up of capital assets abroad, we shall be faced with a severe deficit of the balance of payments which will have to be remedied if there is not to be a severe exchange crisis.

9. The ease with which this transition can be carried out will be affected by the way in which the war ends. If hostilities should, for example, continue in the Far East after they have been ended in Europe, the transition itself would be more gradual. For in this case, certain warlike activities would be diminished in intensity before the final conclusion of all hostilities. Moreover, these preliminary stages of economic and financial demobilisation would in this case be carried out in a psychological atmosphere in which it would be easier to maintain the essential Governmental controls.

10. It goes without saying therefore that many post-war economic problems must remain uncertain until it is clearer what will be the future course of events during the war and when the war is likely to end. For example, the post-war shipping situation will constitute one of the most decisive factors in our economic position. Whether the war ends with the present scarcity of importing capacity or whether, before the end of the war, American shipbuilding will have greatly eased the situation, is still a matter for speculation. Nevertheless, there are certain broad generalisations which may already be made, although the march of events is yet uncertain.

DEMAND AND SUPPLY OF GOODS IN THE TRANSITIONAL PERIOD.

11. For some time after this war, as after the war of 1914-18, there is likely to be a marked excess of demand over available supplies for the majority of peace-time goods and services. Indeed, as is shown in much greater detail in a document prepared by the Treasury,/ and circulated independently of this report, there is reason to believe that these inflationary tendencies will be more potent than after the last war. This may be best seen if demand is analysed under separate headings.

(a) Expenditure by Public Authorities:

12. If, as seems very probable, it should be necessary to police Europe or other parts of the world, Government demands for military goods and services will fall less rapidly than after the last war. Moreover, expenditure of public funds for purposes of physical reconstruction will necessarily be very heavy.

(b) Demand for Goods and Services for Personal Consumption:

13. During this war consumers' demands have been restricted with greater severity than during the last war. This has had a double effect. In the first place,

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/ Footnote reference.

consumers, having been unable to buy their normal supplies of many commodities, have saved large amounts of money; and these sums, together with deferred credits under the income tax, will be available for post-war expenditure. In the second place, people will wish to purchase new stocks of clothing, furniture, household equipment, motor cars, and similar goods of which they have been starved during the war.

(c) Home Investment:

14. In the period after the war there will be a high demand for capital goods to re-equip and restock civilian industry and commerce. To some extent the State, by a careful timing and adaptation of the disposal or use of government-owned factories, machine tools and stocks, may be able to meet the special transitional demands of business for capital equipment without involving a demand for new production. But these government-owned resources will not all be suitable for peace-time demands; and the increase of the post-war demand for capital goods will be very considerable. War damage to property must be made good; civilian industry will need to be re-equipped and to make good arrears of capital investment; the demand for housing will have accumulated in a similar manner; civilian industry and trade will require to be restocked.

15. At the same time it must be presumed that funds for such capital demands will be made available, although there will be serious technical problems to be solved if this is to be done without impairment of the gilt-edged market.

(d) The Balance of Foreign Payments:

16. There is a further factor which will add to the pressure of monetary demand. As suggested above, at the close of the war there will be a serious disequilibrium in the balance of our payments with other countries. Whatever financial methods are adopted to rectify this, it will be necessary to expand the volume of our export trade. In so far as this policy is successful, the increase in our exports will represent an additional demand for goods and services in this country.

The total effect of all these considerations suggests that most of the elements of a sharp restocking boom are latent in the situation.

SCARCITIES OF SUPPLIES IN THE TRANSITIONAL PERIOD.

17. While demand is thus expanded, many civilian goods and services will be in short supply.

18. There will be scarcities of imported raw materials and foodstuffs. At the end of the war shipping will be short, unless American shipbuilding has had time greatly to change the present situation. The overseas production of some raw materials, such as rubber, will be low. Our own stocks of certain raw materials, vital for the reconstruction period, will also be low. Thus scarcities of timber for building or of rubber for motor-car manufacture, will delay the period when civilian supplies will meet post-war demands. Imported foodstuffs will, for similar reasons, remain in short supply; and this will be particularly true of those foodstuffs, such as meat, butter, eggs and fruit, the import of which depends upon refrigerated tonnage.

19. Furthermore, the production of some civilian goods and services will be restricted for want of adequate supplies of special types of skilled labour. Much labour will need to be retrained or to be transferred geographically before it is suitable for employment in expanding peace-time industries. Again, some factories have been closed down, their machinery moved, and their premises used for storage or for housing other firms engaged on war production. The space will have to be cleared and the machinery re-installed before peace-time production can start again.

20. An outstanding example of an industry in which an abnormally high level of demand will be combined with continuing scarcities of supply is afforded by Building. At the conclusion of the war, there will be additional demands on the building industry for repair of war damage and the making good of arrears. This demand would be additional to normal peace-time demands on the building industry. Meanwhile, the labour force in the building industry has been seriously contracted as a result of the war. This may need to be increased very rapidly if the urgent needs of reconstruction are to be met. Certain building materials, and in particular timber, are likely to be in seriously short supply.

BOTTLENECKS AND UNEMPLOYMENT IN THE TRANSITIONAL PERIOD.

21. These scarcities of many peace-time goods and services will be combined with an excess of economic resources in a number of war-time occupations. Certain raw materials such as aluminium, certain forms of capital equipment such as machine tools, and certain types of labour such as skilled engineering labour, will be in excessive supply.

22. Even if special measures are taken, this lack of balance will lead to some unemployment. If the situation is rightly handled, such unemployment need only be transitory. But in the first months following the armistice, some unemployment is inevitable; and unless it is possible to break down the 'bottlenecks', which are found to be holding up the expansion of particular kinds of civilian production, this unemployment may persist.

23. Such a situation will, however, differ in a very important particular from the conditions which normally obtain when unemployment is present. In a time of general unemployment, when activity in the great majority of trades is slack, it is appropriate to give employment by expansionist financial measures which stimulate the demand for all goods and services. Such measures will be inappropriate in the post-war transitional period, with an already existing excess of demand over supply in a large range of civilian occupations. In such circumstances, only the rapid retraining and transfer of those types of labour which are holding up peace-time industry, and plans for the economising of 'bottleneck' raw materials, (such as timber in building or rubber in motor manufacture), and measures for the speedy re-tooling of industry for peace-time purposes, will serve to promote reabsorption.

PART II.

24. The preceding analysis suggests three outstanding tasks:

(i) The restoration of the balance of payments.

(ii) The restraint of inflation.

(iii) The transfer of resources.

The problems involved in the fulfilment of these tasks are discussed in the sections which follow.

(i) RESTORATION OF THE BALANCE OF PAYMENTS.

25. It is commonly agreed that one of our major difficulties in the period immediately following the war will be the equilibration of the balance of payments. If we cannot do this the whole fabric of reconstruction is endangered. We run the risk of a failure to maintain essential imports and a major internal inflation.

26. The main methods for meeting this situation, on the external side, have already been set forth in another document (R.P.(42) 2). But whatever international methods are adopted, important effects on our internal arrangements are necessarily involved.

27. It is improbable, for some time after the war has ended, that we shall be able to dispense with limitations on imports. Even if the shortage of shipping should have disappeared it will be necessary to maintain restrictions on imports until other methods have been developed for the adjustment of the balance of payments.

28. But restrictions on imports cannot be the major instrument of equilibration. The chief imports of this country are foodstuffs and raw materials, supplies of which are essential for the standard of living. We must, therefore, rely upon an expansion of exports rather than upon restriction of imports as a means of restoring the balance of payments.

29. To do this, however, will require extraordinary measures. Raw materials will still be short. If all claimants on their use were to be allowed to participate in a general scramble, the rehabilitation of the export industries might be indefinitely delayed. If only with a view to securing adequate allocation for export, the retention of raw material control seems essential.

30. But this has a further implication. If export is to have priority, it follows that, for the time being at least, other things must go short. Certain forms of civilian supplies, especially textiles, will be short, and, if distribution is not to be disorderly, this means some prolongation of rationing of consumption.

31. At the same time, it is a matter for consideration how far the existing machinery for labour control and any special arrangements which may be devised in connection with demobilisation could be utilised to give priority in restoring labour supplies to the export industries. Certain demands on the home market during the transitional period might also be met through the release of government-owned surplus stocks of manufactured goods (such as motor vehicles), while the newly produced supplies, as and when they come forward, were reserved for the export markets.

(ii) THE RESTRAINT OF INFLATION.

32. It has been suggested above that the period immediately after the war is likely to be marked by an excess of money demand over supply and the persistence of shortages. If the various controls which have been imposed during the war were immediately to be relaxed, there would be danger of grave inflation.

The Policy of Price Stabilisation.

33. The first question which, therefore, arises is whether the policy of price stabilisation is to be continued. It would doubtless be premature to decide that any rigid level of prices was to be maintained for there will be all sorts of forces operating at that time which may well compel some revision of our plans. But some decision is essential on the general question whether the attempt is to be continued to maintain stable the cost of living and the prices of goods of common use, or whether the existing policy shall be changed.

34. To maintain the policy of stabilisation it would be necessary, as at present, to maintain maximum prices for a large range of raw materials and foodstuffs, at least as long as the period of excess of demand over available supplies continues. This policy of price control would be simplified in so far as the controls over raw materials and basic foodstuffs are continued into the transitional period. The possibility of maintaining this policy, however, rest primarily on three factors:-

(a) the continuation of a moderate wages policy which will not lead to such a rise in wage costs as to cause an ever increasing disequilibrium between costs and controlled prices;

(b) a decision, if necessary, to continue the policy of subsidising the cost of living;

(c) external conditions which do not cause the price of imported supplies of raw materials and foodstuffs to rise excessively against us.

35. It is impossible to foretell how high a level of subsidies the maintenance of the stabilisation policy would entail. In the transitional period costs are likely to fall for a variety of reasons: as shipping scarcities diminish, freight rates are likely to be reduced; war risks insurance premiums on imported cargoes and on commodity stocks will presumably disappear; for a number of reasons, such as the absence of black-out difficulties and the replacement of less efficient temporary labour, the efficiency of production is likely to increase; without any decline in the level of wage-rates, wage costs will be reduced if less overtime is worked and the normal long-term improvement of technique is likely to continue and may be speeded up as a result of war developments. Indeed, these reductions in cost might be sufficient to enable the stabilisation policy to be continued without any actual cost to the Exchequer. It would, however, be too sanguine to rely upon any such early development. It is at present unknown what level, if any, of subsidies it will be decided to pay to British agriculture; but it is unlikely that they will totally disappear. There may be rises of the overseas prices of our imports and of internal wage rates which will make it necessary to continue price subsidies for a considerable period.

36. The continuation of the policy of stabilisation does not necessarily involve the stabilisation of every particular price. At the end of the war the prices of manufactured goods (e.g. of clothing) are likely to be abnormally high in relation to the prices of other goods (such as certain controlled foodstuffs). It will probably prove desirable to maintain a stability of the general cost of living index by allowing certain prices (e.g. those of subsidised foodstuffs) to rise as the prices and cost of other goods (e.g. clothing) are reduced.

37. It is a matter for consideration whether the production of "utility" goods, such as "utility" clothing, should not be continued during the transitional period. Such a policy would help to keep prices from rising, and would enable accumulated shortages of goods such as clothes and furniture to be met as efficiently and as speedily as possible.

The Control of Demand.

38. If the policy of price stabilisation is to continue, certain other measures are also necessary. It is not enough to fix prices. It is necessary also to control demand. This principle has various applications.

(a) The restriction of money demand.

39. During the war the general level of demand has been held in check by high levels of direct and indirect taxation. Direct taxation has greatly restricted the spendable incomes of the rich, and has now been extended so as to affect the incomes of a large number of wage-earners. Heavy indirect taxes have not only held in check the demand for the goods and services directly taxed, but have withdrawn in taxation large sums of money which might otherwise have been available for expenditure on other objects. If prices are to be kept stable, some continued use of the fiscal instrument is necessary. During the period of inflated demand and short supplies, taxation should be maintained at a high level.

40. A similar principle might be observed in the repayment of deferred income tax credits. If these sums are withheld during the period of general scarcity, and are released as abundant supplies appear on the market, they will contribute to the stabilisation of the general conditions of supply and demand.

(b) Rationing.

41. But the restriction of money demand in general will not be enough, at any rate during the opening stages of the transition. It will almost certainly be necessary in certain cases to maintain more direct control of consumption. Both for the reasons mentioned above in connection with the problem of the rehabilitation of exports and in order to maintain equitable distribution, it will be necessary that, for some time, certain rationing schemes will have to be continued.

42. Such a policy would not involve an indefinite commitment to this objectionable form of regulation. As supplies increase, so rations could be enlarged, and as the point at which supply was once more equal to demand was approached, rationing could be abolished altogether. What is important is that if the general principle of stabilisation is to be adopted, the public should be educated to realise that some continuance of existing control is necessary.

(c) The allocation of materials.

43. Direct control of consumption, however, is not in all cases the most appropriate instrument for restricting demand. In many cases (e.g. that of timber) the most effective instrument at present for the restriction of civilian demand is through the appropriate Raw Material Control. In these cases it will probably be impossible to maintain an orderly development during the transitional period unless the Raw Material Controls are themselves continued. These Raw Material Controls will be required to make allocations of the scarce materials among the various civilian uses according to the urgency of various requirements, and, thereby, to prevent an abrupt rise of price of the material or a disorderly scramble among purchasers.

44. The peace-time allocation of raw materials will, however, raise certain difficult problems. In war-time all activities are directed as far as possible to one specific aim - the development of the greatest possible war effort. But in peace-time there are a multitude of economic objectives; and it is difficult, if not impossible, to reduce all these to a common measure for the purpose of priorities. In many cases it may prove necessary to distinguish only between a few broad groups - such as the export trade, "utility" goods, and other home market goods - in order to make allocations between these categories. The problem of the later sub-division of supplies within these broad groups would, however, require careful attention. On top of this there will be a further difficulty in that it will be desirable to provide for allocations not only to existing firms but also to new businesses which may be established after the war. Even though raw materials are scarce, new firms must be at liberty to set up in order to be ready for the time when output must expand and exservicemen and firms turning from munitions must not find every avenue to enterprise blocked.

(d) Limitation of Supplies

45. Finally, it must be noted that there are at present in existence a series of controls which restrict consumption by direct operation on the output of supply of manufactured products - in particular, direction of production operated by the Board of Trade. Clearly, the main object of policy after the war must be to remove limitation of supply. But in so far as these regulations permit a control of demand for scarce materials or manufacturing capacity, any measures for their relaxation must be carefully co-ordinated with general stabilisation policy.

(iii) THE TRANSFER OF ECONOMIC RESOURCES.

46. The foregoing discussion has been concerned with measures which would be consequential on any decision to continue the stabilisation policy.

47. But stabilisation is not an end in itself. As has been argued above, the prime objective of policy must be to transfer resources from the service of war to the service of peace; and indeed it must be recognised that to some extent the two aims are in conflict. For there can be no doubt that the release of money demand would work in a way to promote transfer. The high demand for the products of peace-time occupations which occurred after the last war caused the boom. But it also eased the absorption of demobilised men. If we decide to attempt to bring about the transition without a price boom, we must be careful to provide mechanisms which will take the place of these drastic influences.

48. To do this, it will be necessary to take special measures to break down bottlenecks. The limiting factor on the expansion of demand for peace, as on the expansion of demand for war, will almost certainly prove to be the shortage of certain key products or certain key labourers or the required type of plant. It would seem, therefore, as if some use of the method of priorities both for materials and for labour would be desirable if these congestions are to be rapidly relieved; and it is a matter for consideration whether in connection with the demobilisation plan attention should not be given to arrangements for the early release of men whose special skill can provide the speedy rehabilitation of branches of industry having this special position in relation to the whole economy.

49. The need for geographical and occupational transfer of labour will not be confined to the immediate post-war period. Experience between the two wars has shown how structural changes in demand, in productive technique or in the channels of trade may leave persistent pockets of "special" unemployment, and that it is necessary positively to promote the transfer of labour in order to absorb such unemployment. It would be over sanguine to expect that no serious structural changes will occur after the present war. There is, moreover, another reason why the problem of labour mobility is likely in the post-war world to be more severe than before. Past changes in population have been such that the working population will come to consist of a higher and higher proportion of older workers, and that the total working population will cease to grow. Old workers are naturally less mobile than the young. Moreover, the less rapidly a population expands, the more difficult it becomes to adjust labour supplies

between declining and expanding industries by concentrating the entry of juveniles into expanding industries; and for this reason it is probable that the actual transfer of older workers from one occupation or region to another will become more and more necessary.

50. It is therefore a matter for consideration whether more permanent measures for the promotion of labour mobility might not be usefully initiated during the transitional period. There has been considerable experience of training schemes and of schemes for the geographical as well as the occupational transfer of labour in the period between the two wars. In this connection, any remodelling of the social services may perhaps play an important part and the payment of benefits or assistance to the unemployed might be combined with the extension of machinery for the retraining and for the geographical and occupational transfer of the unemployed.

PART III.

LONG-RUN PROBLEMS.

51. The earlier paragraphs of this paper have given reason for believing that a continuation of many of the discomforts of the war economy will be inevitable during the transitional period. So long as serious shortages of consumers' goods persist, certain war-time restrictions and controls must be maintained, if an orderly development of economic life is to be achieved.

52. But the acute shortages of the transitional period will not last for ever. As the channels of trade re-open and resources are transferred, so gradually something more like equilibrium should be established. Thereafter, there should be be hopeful possibilities, not only of restoring, but also of progressively raising our standards of living. For there is no reason to doubt that technical progress after the war, as in past years, will enable real production to be steadily increased. Indeed, the war will in many ways have speeded up the process of of technical invention and discovery, and may thus indirectly make possible a more rapid development of technique in certain civilian industries and occupations. It will take time to restore war damage to houses, to productive equipment and to other forms of capital. But this process should not take longer than a few years; and thereafter, if industrial activity can be maintained, it should be possible, year by year, to increase and to improve the community's capital equipment. The immediate prospect is still arduous. But the distant vistas are bright.

53. These long-run possibilities will, however, in many ways be conditioned by the policy which is adopted during the transitional period. In the first place, we must achieve a permanent restoration of equilibrium to our balance of international payments in such a way that does not too seriously raise the cost of the imported foodstuffs and raw materials, upon which our prosperity must continue to depend. The solution of this problem depends upon many considerations, which have already been discussed at length in another document, (R.P.(42)2). But this problem will not be satisfactorily solved unless, during the transitional period, internal measures are taken to restore and to expand our export trade, even though these measures entail the continuation of restrictions in the home market.

54. It has already been observed (paragraphs 46 to 50) that one of the main problems of the transitional period will be to transfer economic resources from the contracting occupations of war-time to the expanding occupations of peace. Unless this transfer can be smoothly carried out, it will be impossible effectively to remove the shortages which will exist in the transitional period; and unless sufficient transferability of resources is maintained thereafter, it will be impossible to take full advantage of technical progress to raise standards of living in subsequent years.

55. In a similar manner, the successful continuation of the policy of stabilisation during the transitional period would aid the maintenance of stability and prosperity in subsequent years. After the last war, an uncontrolled restocking boom was followed by a severe economic depression; and although the sharp burst

of economic activity and of rising prices which occurred at that time may have somewhat facilitated the process of demobilisation, it greatly complicated the problem of maintaining a stable level of economic progress in subsequent years. In the later years of reconstruction after the war, it is essential to prevent economic depressions and the widespread wastes of economic resources in idleness and unemployment, which are the normal accompaniments of such depressions. In fact, all the solid improvements in standards of living which we may hope to achieve after the transitional period are dependent upon the successful avoidance of large-scale unemployment; and the restraint necessary for the maintenance of stabilisation during the transitional period will be well worth while, if for no other reason than that it should facilitate the maintenance of stability in subsequent years.

56. During the transitional period of shortages, the policy of stabilisation will require a continuation of price controls and of restraints on civilian purchases. But this period of shortages will pass; and the continuation of the policy of stabilisation will then, from time to time, require the adoption of measures to encourage and promote, rather than to restrain, civilian consumption. Among the measures which will be appropriate for this purpose are the appropriate planning and timing of public expenditure on capital works, so that such expenditure may be stimulated when private demand is slack; and various other financial and economic measures should be considered, the object of which would be to maintain a high and stable level of demand for goods and services in general. It will be necessary at the same time to ensure that this high and stable level of demand is translated effectively into a high and stable level of trade activity and of employment, and that economic life is so organised as not to impede the necessary expansion of production.

57. One of the most important of our post-war economic problems will be that of the physical reconstruction of damaged property. It will probably be agreed that rebuilding should be planned with a view to the preservation of amenities, the promotion of public health and the reduction of costs of production. There is, however, another important aspect of this problem. Physical reconstruction may be so timed and so planned as to aid in the policy of stabilisation. In the early post-war years of acute shortages, it will presumably be necessary to restrain building activity, in order to prevent it from exercising undue strain on our limited resources. But when general shortages have disappeared and labour and raw materials for building have become more plentiful, the speeding up of physical reconstruction may be able to play a useful part as a means of stimulating activity if a general depression should threaten to develop.

58. In addition to the planning of physical rebuilding and the improvement of housing conditions, it would probably be agreed that there are other ways in which the social services should be developed. The objectives of social and economic improvement would be difficult in conditions of widespread unemployment, of low production and

of a reduced national income; but the maintenance of a high and stable level of economic activity would greatly ease their attainment and would reduce the financial burden of the necessary public expenditure.

59. For all these reasons the Committee intends to proceed on the assumption, not only that the policy of stabilisation should be continued as far as possible during the transitional period, but also that the preservation of a high and stable level of economic activity and of employment in subsequent years should be set in the forefront of our economic objectives.

CONCLUSION.

60. If the argument of the preceding sections is correct, the following conclusions seem to suggest themselves:

(1) that the rehabilitation of export is to be regarded as one of the prime objectives of policy?

(2) that an attempt should be made to continue the stabilisation policy;

(3) that, for a time, consumer rationing must be maintained;

(4) that the mechanism of commodity controls must be kept in being;

(5) that in order to promote the transfer of resources recourse must be had to the mechanism of priority, both in regard to labour and material supply, and that special attention must be given to arrangements (which may have to be of a regulative character) for promoting labour mobility;

(6) that suitable opportunities should be taken to prepare the public for any restraints and sacrifices that may be entailed during the transition period, if the more distant objectives of economic welfare are to be attained.

61. As was indicated at the beginning, this report makes no claim to be an exhaustive treatment, even of the subjects with which it deals, and there have been deliberately omitted from its range a number of problems which will be of great importance even in the transition period - the problems of deconcentration, disposal of stocks, control of the capital market, and the improvement of industrial efficiency. On all these matters, further papers are in active preparation.

17th June, 1942.