SOME COMMENTS ON Prof. NURKSE'S CAPITAL ACCUMULATION IN UNDERDEVELOPED COUNTRIES

by

N. KOESTNER.

Prof. Nurkse's choice of the subject for the Commemoration Lectures of the National Bank of Egypt has been very timely and we must be grateful to the Bank for having published them for free distribution. The lectures give a remarkably lucid theoretical background to the problems of capital accumulation in underdeveloped countries which is one of the subjects constantly under discussion by the economic experts of U.N.O. and by different bodies of this complicated organisation.

It has gradually been forgotten during these discussions that there exist different types of "underdeveloped" countries and many receipes have been and are being offered based on the simplified assumption that an underdeveloped country is a *poor* country. When discussing underdevelopment, practically the whole of Asia, Africa, and South America, the Balkans, and a few other odd places are all classified as underdeveloped and thus different categories of countries facing quit different economic problems have been thrown into one pot.

To begin with, there still exist primitive, sparsely populated countries which can well be labelled "underdeveloped", and there still exist also enough "Kulturträgers" in other parts of the world who are eager to carry "civilization" to these parts, to develop the undeveloped ('underdeveloped" according to the new jargon) resources of these regions in the interests not of the aborigines, but of the "Kulturträgers" themselves. This process is well known and it does not matter much whether we call it colonialism, imperialism or by any other name.

(*) Prof. RAGNAR NURKSE: *Some Aspects of Capital Accumulation in Underdeveloped Countries*—National Bank of Egypt. Fiftieth Anniversary Commemoration Lectures—Cairo, 1952.

From the point of view of original inhabitants of such an "underdeveloped" country any colonization, no matter how "scientifically" conducted, means an intrusion of foreigners into the existing society, and even if it is not accompanied by fortright extermination of the aborigines, as happened in North America, it always brings disaster to the original possessors of the land by the limitation of their land utilization, by the introduction of alcohol, diseases, the destruction of wild life, and by the destruction of the legal structure of the society fitting the existing conditions of land cultivation, land tenure, and other features of the economy. If colonizers need capital and other help to "develop" a certain "underdeveloped" country, and look for foreign aid (as does United Kingdom at the moment in the interests of her colonies in Africa), one should not make oneself any illusions—the capital is needed to further the interests of the colonizing country (as in the case of the now famous groundnuts), and not in the interests of the aborigines. In all such cases, whether it be the Russian Turkestan or Siberia, Manchuria, Malaya, Congo or South Africa, we have to deal with a development process in a way *imposed* on the country concerned, of which the aborigines did not feel the necessity of importing either the capital or the technical advisers. The capital needed for development, mainly of the natural resources in the interests of some far-situated colonizing power, will normally be made available by this very power through local saving or through borrowing elsewhere. As the lands belonging to the aborigines will be either expropriated straight away or alienated by some scientifically established formulas (*) in favour of the intruders, the aborigines will be pauperized and thus the argument will be available that we have to deal with an "underdeveloped" poor country that offers a proper object for international financing operations.

An example taken far away from the atmosphere poisoned by the arguments about imperialism and colonial exploitation will perhaps contribute to the clarification of our idea. Even in

(*) A number of scientific statistical expeditions under the leadership of prominent statisticians were sent out to the Kazakstan (Kirghizia) to establish the areas of land necessary to support the Kazak nomads, and to define "superfluous" area that could be thrown open for Russian colonization.

Europe, to say nothing of other continents, one could find on the fringes of old civilisation vast areas where land was plentiful and could be had practically by taking possession. The villager was toiling the land in the most primitive manner, had plenty of food, comfortable shelter and clothing all produced by the family, would drink cream and not milk, and quench his thirst with thick beer brewed at home. Such a villager did not need capital nor technical aid from anybody and he was past master in exacting from the soil the highest quantity of food with the least effort, sowing perhaps only one tenth or less of his cultivable area and leaving the rest fallow in one or another form to recuperate its productive capacity.

Imagine now that the Planning Authority decided to open a mine in the neighbourhood and rushed tens of thousands of miners to the spot. There would at once be created a food shortage and it would be found that the country is under-developed. Tractors will be needed, drainage of land and other ameliorations. The local peasants would be found to be technically backward, their cultivation methods wasteful. "Superfluous" areas would be cut off from the village lands, and the peasants, incapable of adapting themselves to the new conditions, would fall into poverty, and would need aid in capital equipment as well as technical advice. A similar process has repeated itself often in any area of rapid development forced from outside.

Population growth will slowly force any society to work harder and eventually improve its methods of production to cope with the demand. The process will "finance itself" by accumulating the capital and experience. The last thousand years of well studied European economic history have demonstrated its mechanism. So far as international financing came into the picture, it served mainly to finance war.

The change that came with the advent of capitalism should not be misunderstood. Although outwardly it often appeared that capital-hungry negotiators came to the London City to obtain loans for development of their "underdeveloped" countries, it was the enormous pressure for expansion and need of food and raw materials experienced in the lending countries which made-the capital export possible and necessary. The development was thus sped up all over the globe, and it depended on local circumstances whether the result was an independent capitalistic community (U.S.A., Canada, Australia, S.-Africa, part of S.-America) or an "imperialistic" colonial expansion.

If there still exist underpopulated areas which are "underdeveloped" because their scarce population does not need any development, their development will be enforced from outside as soon as anything interesting for the developed countries can be found in these territories (wether gold in Alaska, oil and iron ore in Venezuela, or in Arabian desert, or cocoa, palm oil, rubber in different colonies elsewhere).

An eskimo or a pigmy of Central Africa is poor and underdeveloped only from a European point of view. If his hunting ground is large enough, he may lead a happy and contented life —so long as outside interference does not disturb the basis of his economy.

There exists, however, quite a different poverty in the world, not that of the contentment with primitive life of a sparce population living amidst plenty, but arising out of the *overpopulation*. Population growth, as we have mentioned, forces technical development and drives the people to work harder. If for a negro of Central Africa or for an eskimo, it is difficult to differentiate between work and play, a peasant in an overpopulated country must strain his energy to the utmost to produce the food for his family and the surpluses for the market with which to buy the rest of the necessities of life. The process of population growth has produced similar difficulties and sufferings all over the globe, and while in some parts solutions have been found in colonial expansion referred to above from its reverse side, and in simultaneous industrialisation, peoples of other countries, devoid of mineral wealth or where this wealth was unknown (Middle East oil !), have been straining their efforts mainly in the direction of extracting from the soil the utmost it could afford.

One can well imagine a very harmoniously developing community which produces not only all its food but also other necessities of life requiring some industrial processing, and eventually; as the population grows, finding itself facing a shortage in agricultural produce because the agricultural expansion is subject to the law of diminishing returns. If imports of food and other agricultural produce are impossible on big scale because of difficulties of communication (Mesopotamia), a situation develops where the community is forced to reserve more and more of its labour force for agricultural production, and thus gradually grows poorer in other amenities of life. On the technical side the result will be an over-exploitation of soil which will gradually deteriorate and the more so, the more highly the agricultural technique develops. It is the most efficient and complete irrigation system which was the cause of a deterioration of agricultural production and eventual total abandonment of wide areas of formerly productive soils and caused the eventual downfall and disappearance of great civilisations, and which threatens the economy of some other parts of the world at present. If natural conditions are more favourable, like in some densely populated valleys in Asia or in Egypt, such a disaster may not follow, but the population may live on starvation levels for centuries and be liable to disastrous famines from time to time.

It is a misnomer to call these densely populated poor countries underdeveloped : they are not underdeveloped but rather overdeveloped and have reached a position where the further development was prevented by natural barriers and where in some cases as a result of the deterioration of the soil a retrograde movement has taken place. Admittedly, the development has not been alike in the different areas that are comprised in this group of overpopulated countries and for this reason in the further comments we mainly have in view the Egyptian conditions. But we believe that on many occasions the comments are also applicable elsewhere.

To make it clearer what we mean, a few comparisons of conditions in Egypt with those in the U.S.A. deserve to be quoted.

The following were the yields in Egypt and U.S.A. in 1948 :

	U.S.A (per acre)	Egypt (per acre)
Cotton, pounds	311	578
Wheat, bushels	15	36

An estimate of the replacement value of *public* ameliorations of land, including dams, canals, etc. in Egypt is not available, but it can be safely put at well above £200m or over £33 or $95 per acre, thus more than double the total value of an acre of farm land in the U.S.A. Government upkeep of the irrigation system alone costs in Egypt about £E1½ million per year, and about £3-5 m. is spent yearly on new irrigation works, or about $1.50 a year per acre of cultivated land. Egypt uses at present as fertilizer about 20 kg. of nitrogen per acre of cultivated land against about 3 kg. per acre of cropped land in the U.S.A.

The picture changes, however, when we consider the density of farm population. Since in Egypt we do not possess figures on the total farm population, we take the population outside the towns at about 16 m., which gives approximately 2.7 people per acre of cultivated land. In the U.S.A. the number is about 0.02 per acre of total farm area or about 0.07 per acre of cropped area. *The whole problem may be said to be posed by this comparison.* As a result of extensive cultivation in the States, agricultural production per head of agricultural population amounts to over $745 in the U.S.A. and to approximately $60 in Egypt, *inspite of vastly superior labour intensity and much higher capital investment.*

It is the law of decreasing returns that is defeating the efforts of improving the lot of the people in Egypt. Marginal lands and marginal increases of productivity of the existing cultivated area are of course possible but only at a high cost which leaves no great promise for an improved living standard to those who toil the land. Capital investments of the type as usually are in minds of those studying the problems of agricultural development in poor overpopulated countries, in places far away from these countries, and recommending tractors, combines and other top achievements of extensive agriculture are quite out of place in Egypt and will aggravate the situation instead of bringing relief . they will most probably *reduce* the yields, and what is worse, make more people superfluous in a country already over-populated. These are commonplace truths that need no special verification or proof, since we have not yet met an expert who would not agree that if per any miracle, the population of this country were reduced by half or by two thirds, the remainder will at once be able to improve its standard of living if not two or three times so at least very considerably.

The great handicap of this country is exactly the fact that it is a country of very intensive agriculture and any new effort of increasing the production whether by applying more capital or more labour is giving diminishing and comparatively low returns. There are only a few fields where the returns are more promising and the improvements will prove to be profitable in the capitalist sense of this word. One comes regularly across reports from the U.S.A. that application of fertilizer pays itself eightfold. This is hardly the case in Egypt where fertilizers are used intensively and one may even suspect that a certain limit of their utilisation has been reached since at present prices the stocks of fertilizers remain unsold although credit for the purpose is not lacking. There cannot be any doubt that 100 pounds invested in a farm in the Middle West of U.S.A. will give higher returns than the same amount invested in agri-culture in Egypt.

The fact is not always realized that the same amount of labour and capital applied respectively in an extensive and an intensive agriculture do not yield the same results—the results are much smaller in the countries of intensive agriculture. From the point of view of abstract economics capital and labour should both, of course, be applied at the place where they yield the maximum results. This leads us straight to the conclusion that it is not the import of capital which is needed in the overpopulated countries—which is wasteful and can be used at home more profitably—but it is necessary to transfer the available labour to places where it can be applied with the optimum results. But this of course does not apply in the actual situation where each nation is jealously defending its own means of subsistence in a world tending to become overpopulated.

The problem of Egypt is overpopulation ; it can be relieved, but not solved by the incessant struggle for increased production to feed the number of people growing at a rate of one thousand a day and against the handicap of falling productivity of any new unit of labour applied. The figure of one thousand per day refutes by itself any argument that industrialisation is the solution. It is unthinkable that 100,000 or so newcomers can be industrially occupied every year in the light of the fact that the total occupied in the industry is less than 600,000.

It is agreed that by new large capital investments many a stretch of desert can be converted into fertile land. But informed opinion in this country is that a feddan of desert turned into cultivable land costs as much as a feddan bought in the most fertile part of the country. Thus the problem is still governed by the Law of diminishing returns. It is quite possible to invest further enormous amounts of capital in Egyptian agriculture, for instance, as it is actually being done by the force of circumstances, but there exists a fair probability that any new unit of product extracted by this means from the soil will cost more than the previous ones, and that as a consequence—no relief is offered to the producer, since per head he will produce less than before. In actual fact the statistical picture is that since 1939 the physical volume of agricultural production has tended to fall, notwithstanding the heavy investment in irrigation and other amelioration schemes. If these investments have paid dividends, it is because of favourable terms of foreign trade. Whenever the price trends will be reversed (*), a most awkward situation may be disclosed.

It is a pity that Prof. Nurkse has by-passed this fundamental problem of Egypt and of many other overpopulated poor countries.

(*) As they have recently.

***

We now may deal with some of the advices which Prof. Nurkse has to offer for partial relief to people whose standard of living has been forced down to starvation level by its growing numbers.

His first advice is that since there exists a hidden under-employment in the countryside, one could switch the unemployed part of the population to the production of capital goods, if only care is taken to keep the consumption of the population as low as before, by taxation or direct controls. From the point of view of abstract model economics this looks very reasonable and comparatively easy to apply. Unfortunately the economist has forgotten to consult the nutrition expert. If he had done so, he would have found that the model must be amended.

A human being in abstract economics will work when, in a mental exercise, it is ordered to do so. An actual man must be fed a number of additional calories, to enable him to perform additional physical work. The average man needs 1700 calories per day to keep alive. For any physical work he must absorb food producing about 6 times as many calories as he has to produce in work. A man carrying earth from the bottom of a canal in a basket needs, say, 150 calories an hour which for 8 hours represents 1200 calories of extra food requirements. If we consider that one third of the population of a village is superfluous, we may take it that $\frac{2}{3}$ of the population needs full ration, and $\frac{1}{3}$ needs only to be kept alive on starvation level. There will be, of course, no such strict differentiation, the people on the average consuming, say, $\frac{1}{3} \times 1700 + \frac{2}{3} \times 2900 = 2500$ calories a day. If one third of the people is taken away, to dig a canal, the total population will need a daily working ration of 2900 calories. Thus the food requirement will increase by 16 %, or taking into consideration that the "starving" part consuming only 1700 calories, was taken from the village and gets the starvation ration from the village as before, the Government must contribute to their food, 1200 calories, or 41 %. In addition, the administration, etc., of the canal construction will cost at least 25 % of the calory cost of workmen, or $2900 \times 0.25 = 725$ calories per workman which also must be found by the Government. Thus, in calories, the Government will get from the village for capital investment 1700 calories and must supply itself 1200 + 725 = 1925 calories or about 53 % of the total new investment expenditure in our example.

The example is hypothetical and dos not pretend to be in agreement with the nutrition and working standards of this country (*), but obviously whenever the government of a poor country borrows money abroad for carrying out a capital project, the contribution it extracts from its own people is of similar dimension. Thus there is no 100 % local financing possible on the theory of the superfluous population in the villages harnessed to capital works. Prof. Nurkse admits that there will be differences to cover, but ascribes them to frictional factors and to leaks in enforcing the scheme. In actual fact there is a fundamental gap of the same order as the possible extraction of the "calories" from the village.

The argument may be met, of course, by the statement that history is full of examples where the State forced starving workmen to work and perform large capital works until they succumbed to their fate. Canals have been built by many rulers virtually with the bones of forced labourers in many parts of the world (not excluding Egypt). But is such a proposition worth considering, and should the very bones of those for whose wellbeing the promoters of capital investment are catering, be cruelly sacrified to this new Moloch ?

Prof. Nurkse deals further with the observed fact that capital investment in a poor country often proves to be a failure because its products find no market, the purchasing power of the population being too small. There is great truth in the statement, and one of the most outstanding failures of this nature was observed in Bulgaria between the two wars. The Government pursued a very active industrialisation policy and granted all kinds of favours to new industrial undertakings The strongest impetus of all was given to industry by the exchange restrictions of the 30ies. The ultimate result was a severe industrial crisis during which a government investigation

(*) The average consumption in Egypt according to the F.A.O. was in 1950 2,360 calories.

revealed a practically total overcapitalisation in all branches of industry. To relieve the situation a ban on new investments was imposed and this—in an outspokenly "underdeveloped" and poor country. The explanation was, of course, that owing to the small production per head of the village population suffering from heavy overpopulation and representing nearly four fifths of the total, there was no internal market to absorb the goods offered. Where could the electric bulbs of a local lamp factory go, if one could pass in the evening a totally electrified village having only one or two electric lights burning in the local inn, while the bulbs in the houses would be switched on occasionally a few times a week?

Prof. Nurkse's solution is that of Jean Baptiste Say: production creates its own market, provided you produce goods required by the market. Thus increase your production proportionally.

We are in complete agreement with Prof. Nurkse on this point and strongly believe with Tugan-Baranovsky that all overproduction, if observed, is partial. Let us investigate, however, where the source of trouble exactly is that faces the overpopulated ("underdeveloped") countries whenever they embark on industrialization. What exactly do we mean, when we say that newly established industries lack markets? The market for these industries obviously is to be found among existing producers, i.e. farmers and artisans in the first place. Since the new factories by their competition are forcing the existing artisans into starvation, it is the agricultural population among which the newly established industries should find their market, and since the peasants produce so little per head, they have little to offer in exchange. Thus, to break the vicious circle of the lack of market, it is necessary and sufficient to start by—*increasing the agricultural production*. For obviously, if a shoe factory is established and absorbs a certain number of villagers as workmen, and if otherwise the conditions of production in the village remain the same, only so many calories, i.e. purchasing power, will become available as was represented by those workmen and their families who left the village. Since they have gone from semi-starvation into full work, the purchasing power of the village will not only be not able to absorb the total production of the shoes, but will even not be able to purchase shoes for the countervalue of workmen's food requirements—the surplus available for exchange against shoes being equal only to the semi-starvation ration of workmen who left the village.

The process of capital accumulation, i.e. of establishing new industries, is in principle therefore possible only if an additional increment is first available in agriculture. The other possibility is the *replacement of imported goods* by local production. It is on this latter basis that the industry in Egypt, and so far as we can judge, also in other "underdeveloped" countries, has been primarily expanding. Sugar, textiles, cement, mechanical industries—all have established themselves mainly on the place carved out of the import market at the expense of foreign exporters. A smaller rôle in the market creation was played by competition with locally established handicrafts.

Now, this replacement process can go comparatively far in a poor country, and may replace a very considerable amount of imports. It has been going on for more than half a century and has produced another very ackward phenomenon more or less on a planetary scale. A country like Egypt producing cotton for export, but having reduced its imports of cotton goods to bore trifles (the same having happened in India, Argentina, Brazil and many other countries) is bound to lose its market for cotton which the importing countries previously needed to produce cotton goods for export. Thus the export market for cotton shrinks and there appears a "balance of payments gap". It would be only too natural that the very need of exporting cotton also shrinks as local production develops, but this is not the case : the newly established local industries need also foreign raw materials and fuel (and, of course, there is the need for imported machinery). The shift from imports of manufactured goods to that of raw materials and food by countries which previously exchanged foodstuffs and raw materials for manufactures is one of the factors which are bound to aggravate the monetary transfer difficulties all over the world : while the previous situation in crude lines was one of selling food and raw materials against manufactures, now a cotton producing country, say, having replaced its imports of manufactures by locally produced goods wishes to sell her cotton against food for her industrial population, and for raw materials for other industries, and for fuel. The countries buying cotton lack those goods and have difficulty in procuring them, since the supplying countries also do not need their manufactures. This new schematical vicious circle arising out of the industrialisation of "under-developed" countries obviously exists in actual fact at least since the first world war.

Thus the proportional development of production à la Say meets its difficulties, both inside and outside the "under-developed" countries, and there is hardly any doubt that the proportionality is very difficult indeed to achieve, and what would on superficial observation look like proportionality may be found on closer analysis to be a disturbing factor reaching far beyond the boundaries of the country in question. It goes without saying that the industries of "underdeveloped" countries can seldom count on any foreign markets and thus are unable to cater for imported part of their raw materials themselves.

From the point of view of abstract analysis it would thus appear to be more or less irrelevant whether or not industrial development takes place in an "underdeveloped" country : in both cases it will be one and the same factor which will enable the country to improve its standard of living—*the increase of agricultural production per capita.* It is of less importance whether the surplus product is exchanged for more foreign or for more locally produced goods.

In the totally overpopulated countries of the Orient with high rate of increase, the flow of surplus agricultural population towards the industry has always represented only an infinitesimal factor of relief. In Egypt the increase in industrial population between the two censuses 1937-1947, a period where the great wartime development took place, amounted to 215.000. Between 1947-1951 the increase was 81.000 (*). Supposing that

(*) If we have understood the statistics correctly.

two members of family of five were actively engaged in industry, the wartime increase gives an approximate increase in total industrial population of 538,000 while the total increase of population amounted to 3.2 m. Such favourable conditions are exceptional, however, and an industrial boom of wartime dimensions will not repeat itself in time of peace.

As soon as the per capita increase of agricultural production is admitted as the major goal, it has also to be admitted that the goal is unattainable so long as populaton growth : in Egypt the population growth has actually overtaken all the gains in production since the great modern irrigation works were initiated. The real problem requiring solution is therefore the problem of population : if it is solved by emigration, birth control measures, or any other imaginable means it will be found that the problem of "underdevelopment" is non-existent.

***

The source of the capital in the process of the "replacement industrialisation", as we may conveniently call the process described above, is also rather an irrelevant matter. It may be, perhaps, admitted that the process normally starts by foreign capital lured by high profits, the cost of transport, high tariffs, and (recently) the transfer difficulties all contributing to the profitability. Later on, local capital becomes interested and the process continues through savings of the companies, and gradual "repatriation" of foreign capitals which find their activities more and more hampered by exchange, price, and other controls, and by the unfavourable political atmosphere.

The indusiry being thus once established, finds itself very soon hitting the market ceilings, which retards the development and causes a permanent depression. The way out, as has been argued above, can only be found in enhanced agricultural production which thus remains the key to the whole problem. In a country like Egypt depending for its very life on one single source of water, the large scale capital investment in agricultural improvements has obviously to be undertaken by the State, since the investment must be on a very big scale and hardly produces any profit at all and thus does not attract private investors. Financing individual farmers is in addition legally insecure for private capital which still remembers its bitter experiences in the 1930ies.

Prof. Nurkse's special service to this country is that he has pointed out the preponderant rôle incumbent on the State in connection with capital accumulation in "underdeveloped" countries, and has put into a proper perspective the necessity for local saving even in case of gratis capital flowing into the country from abroad. It was necessary to remind us that grants coming from abroad may induce a disinvestment, and that favourable terms of trade may not serve any good purpose, if the increment accruing to the country is not directed to a proper use.

Although prof. Nurkse does not believe in the eternal dollar shortage, he lets the same ghost in through the back door, as he himself admits, by introducing a new villain, the 'demonstration (or incitation) effect". We readily admit that the American neckties and beach shirts are competing most successfully with more simple and fitting local patterns, especially in the "underdeveloped" countries, and that we have become slaves of American radios, gramophones, and motorcars. It is perhaps not quite useless to stress also the verso of this coin. The greatest demagogue of the last century, Ferdinand Lasalle, called "die verfluchte Bedürfnislosigkeit" ("the damned lack of needs") the greatest enemy of the advancement of the labouring classes. We may say, perhaps, that the lack of needs, torpor, and inertia is the first enemy to be overcome by the poor peoples of the East before they can start on the road of real progress. If the "demonstration effect" is capable of rising some new needs, it will also force people to look for means of satisfying them, i.e. force them to work for a purpose. One of the greatest enemies of progress, already wellknown in Southern Italy, to say nothing of the East, is the "dolce far niente", the attitude that if I have already food for to-day, I need not work. It was observed during the recent building boom in provincial towns that increased wages were only aggravating the labour shortage—as wages were increased, the masons preferred to stay away from work more days in the week. The "imitation effect" may induce such people to acquire the habit of saving.

It appears, however, that prof. Nurkse does a disservice to the theory of comparative costs by dismissing it through another back door, if we may say so, by admitting that the dollar shortage or the balance of payments gap may become permanent as a result of imitation and other such effects.

This conflict between the theory and practice arises out of his adopting the classical theory of comparative costs, but not the classical concepts of money and of the balance of payments (although this latter concept was hardly very clear in the mind of the classics). The theory of comparative costs has a meaning only if one accepts the dependence of living standards on the productivity of labour. The modern "gaps" arise as a result of rigid exchange rates combined with more or less free internal inflation which is not used as an instrument of forced saving but rather for the purpose of keeping the standard of living above the real productivity levels. The "gaps" appear therefore as a result of some countries striving to obtain dollar goods to supplement the product of their own labour without offering any countervalue in exchange. To say that these "gaps" are persistent or permanent, is to admit that in some ways assistance is and will be permanently forthcoming from the countries living within their means, and saving. If means of payment are not available in form of goods (including gold) and services, a "gap" in balance of payments can only arise if the foreign supplier grants a credit or sends the goods for nothing. Since nobody had ever thought of gratis supplies in times before 1914, poor countries had usually a favourable foreign trade balance to enable them to defray their "invisible" obligations arising from borrowing and imports of capital from wealthy countries. This situation was considered normal and no demonstration effect could ever disturb in a permanent manner the balance of payments. Disturbances occurred, of course, as a result of poor harvests, political upheavals, etc., but they were temporary per force.

Perhaps the best example of such a "classically" sound monetary policy of a poor country is that of Tzarist Russia which kept the rouble stable from the beginning of 1890ies until well into the first World War, being able to finance in the meantime a big capital investment program, a major war and one large and some smaller famines (during which a finance minister coined the now famous statement : "We shall go hungry but we shall export (grain)"). Of course, there was a big flow of foreign capital and foreign credits to the country during the period, encouraged by the reliability of the debtor during the previous hundred years.

If the situation has now changed, it is not as a result of demonstration or imitation effect, but the phenomenon is entirely due to a new political constellation. The international insecurity has brought private international lending and investment practically to a standstill ; and although some countries still publish certain figures showing private capital movements, they record either movements of fugitive capital (from unsafe poor countries to safer wealthy countries) or investments in the interest of power politics. Intergovernmental grants and lendings are p o l i t i c a l by their very nature. If some poor, and especially some impoverished, countries live beyond their means, it is not because they like to imitate some wealthy countries, but they are able to do so only because it is in political interest of the wealthy countries to support them. To maintain the contrary is to mix up the cause and effect.

If the world has now reached a stage of development where one mighty country is willing and able to give gratis economic support to other countries, and if it even looks on some counts to be a profitable business to do so, the conclusion is not justified that under a world government the same would continue on heavy scale. Another modern rigidity is responsible for this—closed frontiers. The world resources and "living space" are now the monopoly of individual states. Supposing that a world super-state comes into existence to-morrow and that it will be a democratic institution, it will decree the freedom of migration which was one of the features of the 19th century. Freedom from want generously declared some time ago by two responsible statesmen will never be attainable. What may be attained, if freedom of migration is declared, will be not freedom from want, but equitable distribution of resources—perhaps a nivellation in poverty. If access to countries with underdeveloped resources like Canada, U.S.A., Siberia, South America, some parts of Africa and Australia will be open to all world citizens, a more equitable distribution of productive facilities will result and there will be less need to send food overseas to starving areas. Admittedly this in present circumstances is only a mental experiment.

There is one rather sad point that recurs time and again in prof. Nurkse's lectures and which is bound to add to the general pessimism of those studying the problem. Practically every ray of hope the lecturer shows us is combined with application to the toiling masses of coercion, restrictions on consumption, increased taxation, etc... Whether it is the redirection of labour force from villages to dig canals, or industrialization à la Japan or Soviet Russia, or the forced saving on starvation levels by means of inflation or stricter taxation, it is always the toiling man who has to suffer additional (if sometimes only relative) burdens. One eventually begins to wonder, for whom after all are these sacrifices to be made? Isn't it the working man and his family of whose welfare one should think first when embarking on any investment scheme?

To end these remarks it is perhaps worth our while to remind of one great source of capital formation that is not given any prominence by prof. Nurkse—the rent. The over-populated poor countries of the East are at the same time countries of big landlords, of extreme poverty and extreme wealth. This wealth in most cases has its source in land rents. If this wealth is kept idle, is wasted in luxuries or is transferred for investment or spending to the wealthy countries of the West, probably the major part of nation's savings will not be productively employed. Ways and means should exist to harness these savings in national interests. In Egypt the agrarian reform has already channeled some of the accumulating rents in a proper direction, but it is obvious that it is by offering proper facilities to investors in general that further progress in this direction will be made.

N. Koestner.

A SOCIO-ECONOMIC ANALYSIS OF THE KEYNESIAN THEORY

by

A. M. HASSAN, Ph. D. (Econ.)

Faculty of Commerce, Cairo University.

PROLOGUE.

Theories are the invention of people who are in their lives profoundly affected by the dynamic forces prevailing in their society. They are but the echo of the inventors and the reaction of their impulses to their environment. In other words, economic theories are good records of the working forces on the stage of the social and political drama. They cannot, thus, be dealt with in a vacuum. An accurate study of any of them must take into consideration the socio-political order prevailing at the time, as well as the background of the economic opposing interests. In this way one can realize to what extent any theory could succeed in solving a certain economic problem occurring in a certain place at a certain time.

The following is an endeavour to analyse the Keynesian theory in keeping with that line of thought.

1.—Socio-Political and Economic Background.

The Keynesian theory came to light at a time when the economic order of most of the nations was disrupted by the Great Depression of the early 1930's. Millions were unemployed everywhere, business was slack and a large amount of balances was idle.

The depression did not occur suddenly. It was the result of accumulated unchecked forces. Since the 1914-War, the world was passing a period of dislocation and change, or, if we may quote Pigou's words, the world was entangled in a dwindle period, tottering between boom, slump, doldrums and slump again, a vicious circle in the non-integrated structure.

In a free-economy, or an economy of uncertainty, there is no restriction to idle resources being accumulated, which result in a gradual reduction in consumption and increase of the unsold stocks. This is what was actually in process. Wealth was accumulated in the hands of a few whose propensity to consume was low, while a large number of people, with a very high propensity to consume were left poor. What was taking place in one country was also in process between the industrially powerful countries and the agricultural poor ones, as free international transaction worked against raw producing countries, reducing thereby their propensity to consume in the long run.

On the whole, the position became one of over-production from the point of view of businessmen and producing countries and under-consumption from the outlook of the working classes of people and the debtor countries.

The economic break-down thus revealed the inherent disintegration and disequilibrium in the standing economic order.

Such unstable conditions had their repercussion on the socio-political arena. The franchise system in the world was truly widened and some nations got their independence since the war. But the people and nations were still sharply divided and national incomes and international wealth were badly distributed. This caused a strain on the internal and external social relations.

The struggle between socialism and labourism on one hand, and liberalism and conservatism on the other was intensified. Behind each forces there was a philosophy persisting to dominate the scene. The former was interested in transforming the means of production to the hands of the State, while the latter, per contra, believed in a society motivated by self-interest and dominated by the freedom of exchange, or in other words, the maintenance of the existing *status quo*.

With unemployment ranging between 11.7 millions and 20.5 millions between 1930 and 1935 while the world real income was highly depreciated (1), new forces appeared in the scene. Being based on a new philosophy of the State, the prophets of the new forces made all justifications for its interference to alleviate social, economic and even political disorders. Different as they were, Fascism and Labourism, worked hard to make the State the planner for society and the governor of its destiny. But their opponent ideology was feared to lead to a disastrous clash.

2.—Philosophical Background.

In this period of confusion, tension and uncertainty, the Keynesian theory was formulated to create an atmosphere of confidence in the weary free exchange system. It was an attempt to restore security against unemployment without the blunders of war. Continuous wars give one the impression that they became the means to alleviate such a system from its disintegration. They accidentally appeared twice in the first half of this century, each one seven years after a pressing depression.

The Keynesian philosophic background is not fundamentally different from those built on individualism. This might be the reason why it looks like manna from heaven to the capitalist defenders, who hold the view that capitalism is not a stagnant system but rather flexible. and can change its form to suit new developments without need of any revolutionary change. Keynes made it clear that "if orthodox economics is at fault, the error is to be found not in the superstructure..., but in a lack of clearness and generality in the premises" (2). He found "no reason to suppose that the existing system seriously misemploys the factors of production which are in use" (3). The success of any system or theory depends on its suitabilities to the environment into which they are projected. One should not

(1) The figures were for 32 countries as given by E. Varga in his *Two Systems*, p. 73. The Report of the Delegation on Economic Depression, Part I, L. N. gave a figure of 25 million industrial workers being unemployed throughout the world at 1932. See p. 21.

(2) Keynes, J. M.: *The General Theory of Employment*, p.v.

(3) *Ibid.* p. 379.

be misguided by the existance of a certain rentier aspect in the capitalist system because it was just "a transional phase which will disappear when it has done its work" (1), declared Keynes. On the whole, if individualism "can be purged of its defects and its abuses it would be the best safeguard of personal liberty" (2).

The Keynesian philosophy is thus a liberal one and its major purpose is to "buttress political liberalism with a new economic program and to fortify this economic program with a new political economy" (3). Private ownership was accepted on the assumption that it is the result of profit motive which canalise human actions to the best channels for the whole and which, if disposed of, there would not be any assurance that human motives would not be directed to other harmful directions. In the same manner the Keynesians approved interest—taking as it is the inducement—factor to save (4). To limit its harmful effect, it should be on a lesser scale than advocated by the classicals. Keynes wanted "the aggregate return from durable goods in the course of their life" to be just enough to "cover their labour-costs production plus an allowance for risk and the costs of skill and supervision" (5). Even inequalities of wealth and income were justified on social and psychological grounds, but not to be of such large disparities as those in existence (6).

The Keynesian disapproval of the classical assumptions and resolutions was based largely on the divorce of the latter from the realities of life. The Classicals based their economics on the micro—than the macro-analysis with the result that they were driven away to hypothetical anealogies. They disagreed in the presence of involuntary unemployment with the result that they come to a wrong conclusion that the economic system is self-adjusting and needs no planning or intervention from outside. It may well be that the classical theory, declared

(1) *Ibid*, p. 367.
(2) *Ibid*, p. 380.
(3) DILLARD, D.: *The Economics of J. M. Keynes*, p. 318.
(4) KEYNES, *op. cit.*, p. 379.
(5) *Ibid*, p. 376.
(6) *Ibid*, p. 374.

Keynes, "represents the way in which we should like our Economy to behave. But to assume that it actually does so is to assume our difficulties away" (1). The main problem that is threatening to disrupt the capitalist politico-social and economic structure is the cyclical crisis and it is no use blaming the inflexibility of the wage system, because employment is not a function of one single factor but of more than one. If labourers resist any reduction in their wages as a result of price fall, one has to remember that "'the real wage earned by a unit of labour has a unique (inverse) correlation with the volume of employment (2). Besides, it is for the interest of the Capitalists that the propensity to consume must not sink in the first place, and it would be to their real benefit to adhere to a policy calling for full employment, even if they have to sacrifice for it. This is because of the existing prima facie case that if employment increases "the reward per unit of labour in terms of wage-goods must, in general, decline and profits increase" (3).

Keynes, contrary to the Classicals did not made his assumptions in a vacuum but went on to examine the mechanism of the institutional and other subjective factors which determine any socio-economic behaviour. Social practices and institutions, though not unalterable, have a certain bearing on the distribution of wealth and income and also the manner of investment and consumption. Thus one cannot neutralise or ignore the significant part played by these subjective factors. It would also be futile to treat the individual in isolation and think that he comes to this decisions uninfluenced by his status or simply through pecuniary measures, weighing average of quantitative benefits and multiplying them by quantitative probabilities (4). Keynes thought that there was no proof of this strict mathematical calculation in deciding personal political or economic action (5).

The Keynesian disapproval of the classical mathematical

---

(1) *Ibid*, p. 34.
(2) *Ibid*, p. 17.
(3) *Ibid*, p. 17.
(4) *Ibid*, p. 161.
(5) *Ibid*, p. 162.

sense dit not divert them from applying other mathematical arguments based on hypothetical assumptions. They invented their "Investment Multiplier" which was a formula combining the degree of propensity to consume with that of investment. They defined it as being equal to a reciprocal of one minus the marginal propensity to consume. Following this formula one would find out that the amount of the multiplier should run from one to infinity. This would mean that any small portion of investment would result, by successive movements, in creating a case of full employment ; and on the contrary any disinvestment, however small, would result in a case of everyone being unemployed ; neither case proves to be factual. This fault compelled the Keynesians to suppose that the multiplier lies between 1.5 and 10 only (1).

The problem of unemployment and its direct relation to the propensity to consume drove Keynes to be sympathetic with the pre-classical doctrine of Smith and Malthus : that everything is produced by labour "aided by technique, natural resources and by the results of past labour..." (2). One has to note, that accepting labour as the sole factor of production and that other factors are just helpers, did not list Keynes as a Marxist, because he was not. Keynes included in labour "the personal services of the entrepreneur and his assistance" (3). This consideration of labour as the sole factor of production was rather a revolt against the traditional liberal teachings which Keynes tried to preserve. Keynes went on to take "the unit of labour as the sole physical unit" required for measurement in the economic system. But all this did not turn Keynes to suggest any radical policy in the course of distribution. He was more interested to find out how to fill the gaps in the classical analysis and implement a solution of the disturbing state where "full, or even approximately full, employment is of rare and short-lived occurrence" (4).

The Keynesians are not socialists and could not be mistaken by their call for State interference in the economic field, or

(1) DILLARD: *op. cit.*, p. 87.
(2) KEYNES: *op. cit.*, p. 213.
(3) *Ibid*, p. 213.
(4) *Ibid*, p. 250.

their acceptance of central planning and mass welfare expenditure. Their leaning on the State was logical from their macro-analysis and their acceptance of the influence of the subjective factors. In the Robinson Crusoe situation, the State did not exist, but it exists in social life and plays an influential rôle and thus, it has to be accepted to play its part in solving the unemployment problem. The Keynesians are truly critical of conservatism but mostly because its representatives offered no practical or distinguished novel measures for safeguarding capitalism (1). If they have little choice, they would rather rally themselves behind bourgeois politicians than the "boorish proletariat" (2). Keynes said frankly that, if one had to choose between totalitarianisms, he would choose the tyranny of money rather than that of ideology (3). Thus it is not surprising that the Keynesian thesis appeals to the Social Democrats, Liberals and Monopalists (4).

In spite of the fact that the Keynesian theory wanted to reform capitalism, without attacking its existing institutions and thus, appeared not to be biased by class struggle, its solutions are partial. Keynes did not agree on restraining wages during a depression, but in the mean time, he did not advocate a high-wage rate which would mean an increase in the power of labour compared with the owners of capital. He centralised his analysis on the problems which were disturbing the capitalist section as interest rate, profit expectations and the supply of money (5). His booklet on war finance commended him as the gallant defender of the rich who could not pay for the war against the workers, the "war-profiteers" who are "taking advantage of the war to increase their consumption" (6) The Keynesian thesis was, in a sense, "essentially conservative and oriented towards a preservation of the status quo," declared Dillard (6).

(1) DILLARD : *op. cit.*, p. 318-319.
(2) *Ibid*, p. 319.
(3) KEYNES : *op. cit.*, p. 373.
(4) EATON, J. : *Marx Against Keynes*, p. 14.
(5) DILLARD: *op. cit.*, p. 320.
(6) KEYNES, J. M.: *How to Pay for the War*, p. 21.
(7) DILLARD: *op. cit.*, p. 326. See also in the same meaning KLEIN, L. R.: *The Keynesian Revolution*, p. 167.

Failing to furnish a specific politico-social backing to his theory, except of course some scattered fragments of liberalism, Keynes left it in an unsafe position. It could be exploited by opposing political parties. It is not full employment as such that matters, but to what end, is the crux of the problem. The Keynesian thesis could well give a new basis for a new workable liberalism (1) striving for social reform. But in the mean time, it could furnish a totalitarian with an excellent tool for a war economy.

3.—The Keynesians and the Functions of the State.

The Keynesians agreed to give the State a big rôle in the economic and social field, more than any liberal theory had allowed before. It was on this issue that some writers considered the Keynesian theory as a revolutionary one. The limitation of the rôle of the State under the classical theories was understandable, so long as economics was "regarded as a science of the relations between man, nature... (with) the State (requiring) consideration only at the level of application and not as a part of the subject matter of the science" (2). Extending the State functions was sought for as the "only practicable means of avoiding the destruction of existing economic forms in their entirety and as the condition of the successful functioning of individual initiative" (3).

When the Keynesians returned to State help, their eyes were focussed on the damaging effect of accumulation on employment and the insecurity of the capitalist system in life of uncertainty. With the paradox of poverty in the midst of plenty, certain measures had to be taken to stop what might be the outcome of such a condition. To protect the existing Status, certain measures had to be taken not through the doubtful use of force but rather through engaging the idle hands in some work or another. In the past the fraction of unemployment was small and wealth was widely diffused, but through the processes of the free exchange system, it became

---

(1) DILLARD: *op. cit.*, p. 325.
(2) SWEEZY, P. M.: *The Theory of Capitalist Development*, p. 239.
(3) KEYNES: *The General Theory of Employment*, p. 380.

concentrated in a few hands and large numbers were forced to idleness without any fault of their own. If feudal landlords found a way to engage their vassals in constructive schemes, the new capital owners could not be less capable of doing the same and thus avert a class-war.

The Keynesians did not discuss the worn out functions of the State. The rôle of the State to execute law and carry its order, guarantee civil rights and defending society from invasion were taken for granted. But the new rôle of the State was based fundamentally on sustaining full employment, within the framework of society. Redistribution of ressources, reorganising the means of production and carrying any social reforms, should then be directed to fulfil that aim but not to be used to realise any politico-social equilibrium. By thus widening the scope of State function, it could precipitate the needed environment" which the free play of economic forces requires, if it is to realise the full potentialities of production" (1).

The suggestion of letting the State control the supply of credit was accepted by a considerable number of businessmen. The success in the capitalist system came through the ploughing into the economy of what was produced by it. But the increase in complexity and uncertainty in the socio-economic field created a state of cautiousness and holding idle, large balances, which work in deflationary way and widen the gap between actual and potential production. And as capital is not a self-subsistent entity, but rather associated with consumption, thus any reduction in the rate of interest must have the effect of increasing income and accelerating the propensity to consume. But Keynes denounced influencing the rate of interest as of doubtful effect. The measure he preferred was to call up on the State to direct and organise investment because it "is in a position to calculate the marginal efficiency of capital goods" (2). The same line was followed by Hansen (3). Keynes insisted that "The only radical case for the crisis of confidence which affect the economic

---

(1) KEYNES: *op. cit.*, p. 397.
(2) *Ibid*, p. 164.
(3) HANSEN, A. H.: *Fiscal Policy and Business Cycles*, p. 391.

life of the modern world would be to allow the individual no choice between consuming his income and ordering the production of the specific capital asset" (1).

The second function of the State underlined by Keynes was the execution of a scheme of public works. Such a scheme would have a large effect on the aggregate employment (2). They should be carried on, he emphazised, without any notice to their utility. To support his argument, Keynes justified the old practices of governments who built pyramids, cathedrals or even waged wars (3). He went on to say that, even digging holes in the ground would achieve the purpose, if nothing else could be done. We have to accept the carrying on of constructive schemes "as an inevitable result of applying to the conduct of the State the maxims which are best calculated to "enrich" an individual by enabling him to pile up claims of employment which he does not intend to exercise at any definite time" (4).

The Keynesians agreed on the State carrying on a scheme of public works not for the intention of improving social welfare and raising the material standard of the people, but rather "to reform capitalism to a system of full employment" (5). When full employment is thus maintained, there is no assurance from the Keynesians that these schemes should be continued. The extent of such a policy, as "the intelligent politico-social policy needed", as a Keynesian adherent puts it, is "not necessarily (to) be either too great, or too small. It could be just right" as not to infringe any damage to private entreprisers (6). It looks fine to find out some Keynesians suggesting that constructive projects should be useful from the point of view of economic welfare but as there is no assurance that such a course could be taken, because of the lack of a suitable ideology to hold on the theory very firm, we might find ourselves indulged in an awkward position following the natural course

(1) KEYNES: *op. cit.*, p. 161.
(2) *Ibid.*, p. 127.
(3) *Ibid*, p. 131.
(4) *Ibid*, pp. 129-131.
(5) KLEIN: *op. cit.*, p. 168.
(6) *Ibid*, p. 169.

and decline to anarchism and war (1). The conditions of the world to-day emphazised this conclusion and to avert an expected crisis a rearmament race is taking place. Keynes himself felt this difficulty after the experience of the 1930's and declared that : "It appeared to be politically impossible for a capitalistic democracy to organize expenditure on a scale necessary to make the grand experiment which would have my case except in war conditions" (2).

Keynes submitted a social programme as a third function for the State to assure a high stage of consumption. Such a programme should be carried out, stated Keynes "to defeat the dark forces of time and ignorance which envelop our future" (3). One cannot depend here on private enterprise to take the initiative because there "is no clear evidence from experiences that the investment policy which is socially advantageous coincides with that which is most profitable" (4). Consumption expenditure such as relief payments on health, family allowances, different kinds of pensions and grants to education in addition to the injecting of new spending, however, on the propensity to consume, could be viewed as investment in human beings which could also be beneficial whatever the type of society.

The Keynesians did not seem to care much for the concepts given in the latest development of the classical theory, considering the maximisation of welfare. Their limit for spending is the attainment of a state of full employment from the entrepreneur's point of view. The *Beveridge Plan* of 1942 and the *British Employment Policy* of 1944 were designed on these lines. Their main object was to supply certain social welfare services and thereby limit the propensity to save of the lower income groups and influence an increase in the propensity to consume. The *White Paper on Employment Policy* revealed that intention in saying that the standard rate

---

(1) Klein states that "the economic law of motion of capitalism will take us down the same road that Germany followed so recently." Cf. *Ibid*, p. 167.
(2) Quoted by DILLARD: *op. cit.*, pp. 129-130.
(3) KEYNES: *op. cit.*, p. p. 155.
(4) *Ibid*, p. 157.

of contribution for a social insurance scheme "would be assessed on the basis of a forecast of the average level of unemployment, in such a way as to keep the social insurance fund in balance over a number of years" (1). One can then understand why a social programme on the Labour Government scale was much criticised and accused of aggravating the State of inflation and keeping high the rate of taxation, while in the meantime, expenditure on rearmement did not receive the same criticism.

4.—The Keynesian Fiscal Policy.

While being liberal, in some way or another, in their employment policy, the Keynesians seem to be lending more to conservatism in their fiscal policy. Keynes frankly showed the responsibility of the inequality of wealth and income in aggravating the state of unemployment if not contributing to it (2). He added that the removal of some of these inequalities would play a significant part in keeping high the propensity to consume and helping the growth of the aggregate wealth. In spite of that, the measures advocated by Keynes in the fiscal field did not work in that direction.

To Keynes, State socialism which would embrace most of the economic life of the country is undesirable (3). But the State could determine the aggregate amount of resources devoted to certain investments and also it could fix the rate of reward to those who own them. The State should not, according to the Keynesians, rely only upon taxation and use it for social ends. The fulfilment of the Keynesian plan could be carried, in addition to taxation, by means of public loans. That solution was most appealing to capitalist America which financed its New Deal projects, and built most of its post-war schemes and armament programmes through loans.

Dillard stated that "the greatest stimulation to employment will result when a public construction program financed by borrowing replaces a public relief program which was paid four out of taxation" (4). The least stimulation would be,

(1) Employment Policy, Cmd. 6527, p. 23.
(2) KEYNES: *op. cit.*, p. 130.
(3) *Ibid*, p. 378.
(4) DILLARD: *op. cit.*, p. 108.

according to him, when the programme is financed wholly by taxation. The main point of argument here is that expenditure of funds collected by taxation does not increase the aggregate propensity to consume because such an attitude is but a substitution of private expenditure by public expenditure. But this is a misrepresentation of the fact, because it was assumed in the beginning that there were more idle balances than necessary and, thus, taking them by taxation, not only increased the aggregate propensity to consume, but also would relieve the State of any obligation of repayment of loans and their interest. The loan arguments might be accepted, if the individuals were already employing these balances, but in a less rational way, or expecting to use them in the near future. In addition, while the Keynesian solution would benefit the rentier class and increase their power of accumulation, it is feared that the loans and interest repayment would start another cyclical movement as a result of expected increasing idle balances.

Transferring the Keynesian thesis from peace needs to war necessities, one would find that the same trend in their outlook in championing voluntary and compulsory savings, contracting loans, increasing consumption taxes in addition to increasing those normally applied.

When submitting his resolutions for full employment, Keynes tried to be neutral, on the assumption that tax rates remained unchanged (1). But this does not mean that Keynes did not give any concrete idea about different types of taxes. Keynes righly assumed that any increase of individuals' income would be automatically followed by an increase in their propensity to consume, but in a lesser degree. That means that increasing income stimulate savings and widen the margin of idle balances. This is true under the assumption that the individual has satisfied his immediate primary needs.

There are two ways of looking at the taxation system from the point of view of employment : the first is the depressing effect of taxation on risk-taking and the other is its influence when intended to redistribute income and wealth. Keynes

(1) *Ibid*, p. 122.

looked as if he did not sympathise with taxation, in one place, but seemed to agree with it in another. He admired the use of direct taxation since the end of the 19th century to remove the great disparities of wealth and income (1). But carrying such a policy much further would embody the implications of increased evasion and thus diminish "unduly the motive towards risk-taking". Such taxes used to be taken into consideration and seem to be hampering big scale investment (2). Keynes left the argument there without developing it, but one cannot fail to find that he disagreed with the taxes that would paralyse the profit motive.

On a simple analysis, Dillard looked at all taxes as having a deflationary effect (3). Such might be true only if the government, when collecting the taxes, intended to have a budgetary surplus. Apart from that, considering the normal behaviour of the State and the individual, we find that the former is not keen to keep in the treasury more than that what it intends to spend, while the latter, on the majority, keeps certain amount of his income reserved in his coffer. Dillard, being a Keynesian, went on to argue that "highly progressive taxation is an element that tends to depress business confidence and inhibit spontaneous optimism" (4). This conclusion depends on the manner of the tax, the condition of society and the state of employment. There is more evidence that higher taxation, for instance, on monopoly and quasi-monopoly profits and on the income groups, who retain enough margin after the tax, would not deter business or individual activity, if the yield of the tax was fully expended. It means that the writer is mixing up income taxes and profits taxes. In the case of unemployment when the purchasing power falls down, the differences between income groups get wider than in the case of full employment. High taxation, which would be spent on a wide scale, would play a double rôle, by increasing the propensity to consume and thus stimulating investment and by reducing the gap between different income groups.

(1) KEYNES: *op. cit.*, p. 372.
(2) *Ibid*, p. 309.
(3) DILLARD: *op. cit.*, p. 112.
(4) *Ibid*, p. 112.

Keynes truly followed the social trend of using taxation as a measure to retain more equal distribution of wealth and income. But his argument was based on the employment aspect. '"If fiscal policy is used as a deliberate instrument for the more equal distribution", declared Keynes, "its effect in increasing the propensity to consume is, of course, all the greater" (1). This is so. The propensity to consume in the low income groups is must higher than amongst the high income groups. The amount of income which might possibly be left idle in the hands of the rich will, most probably, enter immediately into consumption, if it is given to the poor. The rise in the propensity to consume may also prove to be "positively favourable to the growth of capital" (2) and thus capital owners should not fear such taxes on the long run. Keynes was not then a social reformer who advocates redistribution for the sake of social justice, but only as a measure to save capitalism from slipping into chaos. Accordingly, Keynes would, most probably, stop using fiscal policy for the cause of redistribution at any stage, when full employment is attained.

The Keynesian thesis, I feel, cannot succeed, in the long run, and become capable of bridging the gap of inequality between classes or even distribute the socio-economic burdens of taxation according to the people's capacity. But still, it has to be given most time and study before one can come to definite conclusion about it.

A. M. HASSAN.

---

(1) KEYNES: *op. cit.*, p. 95.
(2) *Ibid*, p. 393.