

CHAPTER I

GENERAL OBSERVATIONS.

§ 1. **Mutual dependence between production and consumption.** Before proceeding to analyze the symptoms and causes of the present crisis, a few theoretical observations are necessary to enable us to understand better some fundamental facts concerning the world crisis. First of all we must remember that all economic activities may be divided into two large spheres, viz. that of *production*, concerned with the creation of utilities, and that of *consumption*, concerned with their appropriate destruction (for the ultimate purpose of the satisfaction of human wants). There must be a constant equilibrium between production and consumption, for it is impossible to consume more than has been produced and to produce permanently more than can be consumed. Under the Capitalist economic system not only is the extent of consumption determined by the extent of production, but the extent of production is vice-versa also determined by the extent of consumption through its influence on the development of prices.

Under the Communist system, production, relying on statistical data, determines beforehand the quantity of goods to be allotted to consumption. From this it follows clearly that production under the Capitalist system is far more vulnerable to any changes of consumption. If consumption declines, production must decline too, for otherwise overproduction and a crisis result. It is therefore important to examine the question of factors which determine the power of consumption.

"Consumption should conform to human wants", say the Communists; "to each what he deserves", say the Collectivists or Socialists. Under the Capitalist, individualist order of society the *consumption power* of individuals (or households as individual consumption units) is determined by their income, expressed in money economy in terms of money. *Money income* is thus the intermediate item through which the distribution of commodities is effected. This way of distribution can be, of course, opposed to the above mentioned Communist postulate of distribution according to human wants, for on one hand many wants of a large majority of mankind must remain unsatisfied, whereas on the other hand many people draw an income far surpassing the amount required to satisfy their wants. But in the same way it may be also opposed to the Collectivist postulate of distribution according to deserts, for many incomes, such as income from inherited wealth, have obviously not been deserved by the effort and work of their possessors.

In this connection it might be objected that even productive organizations (manufacturing industries) are consumers (of raw materials, fuel etc.), without receiving an income, for yield or surplus of undertaking is not the same as income. That is true, but it must be remembered that these productive organizations consume only for the purpose of producing new goods, destined to serve further consumption, and so the process goes on until complete consumption by the last member in this chain is achieved. Every production must therefore, either directly or indirectly (for we must leave the intermediate stages aside), end in the *ultimate consumption* by some consumption unit, drawing an income (i. e. either a single individual or a household), and it must see in this consumption its ultimate aim. In other words income pays either directly or indirectly for the whole production, with the sole exception of products consumed by the producers themselves, and not put on the market (self-sufficient economic units). Without this ultimate consumption the preceding consumption would be

useless, and the latter is thus only of an intermediate nature. Thus the statement that the total of all incomes determines the total of production is correct.

On the other hand it is undoubtedly true that there is no income without production, for the simple reason that real income is nothing but production which has reached the stage of distribution. Production and income, and therefore also consumption, are mutually interdependent. The restraint or suppression of production frustrates consumption, the decline of consumption destroys production.

§ 2. Dependence of production on the method of the distribution of income. But this does not exhaust the question of the dependence of production on other factors. Total production does not depend only on total consumption, but — probably even to a larger degree — on the *distribution of income* as well, which in its turn has influence on the extent of consumption. If all incomes were equally large, we would achieve quite a different volume and character of consumption from those resulting from the existing inequality of income. The largest consumption and therefore the possibility of the largest production might be achieved by a complete equalization of incomes, leading to a complete equalization of consumption. Needless to say, this equalization would also change the nature of this consumption: consumption of luxury articles would decline and might temporarily disappear altogether, whereas consumption of necessaries would increase.

A serious deviation from the principle of the equality of income must lead to decreased and inadequate consumption (underconsumption), which cannot be substituted by a partial increase of consumption in a few particular cases (overconsumption). There were times when this inequality contributed towards the progress of mankind, for only in this way could the accumulation of stock and reserves be achieved, i. e. the acquisition of means of pro-

duction (machinery and other auxiliary capital), which led to a further growth of production. In those times new means of production were needed to satisfy consumption, whereas to-day consumption and the question of better sales have become the chief object of our solicitude.

Complete equality of income, however, is impracticable and even undesirable, for it would not actually lead to the highest possible prosperity (i. e. to maximum production and maximum consumption). Absolute equality is not insisted upon even by the principle of Communism (consumption according to wants) or by that of Collectivism (consumption according to deserts), to say nothing of Capitalism. The possibility of unequal incomes and thus also of consumption offers the best scope for rewarding efficiency, i. e. an exceptional performance of work. Without the necessity of such rewards of merit we could perhaps arrive at complete equality of distribution, providing the most favourable ground for maximum consumption, but it is quite certain that we would not achieve maximum production, for without the incentive of extra pay maximum efficiency could not be obtained, and thus even maximum consumption would not be achievable. The most favourable ground for maximum consumption assures by no means actual maximum consumption. But our aim must be the achievement both of maximum consumption and of maximum production. It follows that it is not the existence of inequality of income as such which is unsound, but only the existence of *excessive inequality of income*. For it is this excessive inequality which prevents the full satisfaction of wants by depriving a large number of people of the opportunity of satisfying them, although these wants could be satisfied in view of the adequate aggregate income. On the other hand a certain number of people draw incomes which are far in excess even of their least important wants. A large part of these incomes not only is not consumed, but even cannot be consumed, and this spare money is left to capitalization.

Thus the extent of ultimate consumption and therefore also of corresponding production is substantially restricted, and this restriction is carried out in favour of future increased production, necessitated by the said capitalization, i. e. acquisition of machines, tools and appliances, factory buildings and other investments.

§ 3. Static and dynamic inequality of income.
Inequality of income is not, however, an uniform conception. We must carefully distinguish between static and dynamic inequality. By *static inequality* is understood that state of affairs which from time immemorial was the origin of the difference between the rich and the poor. It does not influence production unfavourably, because it adapts itself to conditions as they exist and as they existed before.

On the other hand *dynamic inequality* occurs, when the rich, or at any rate the fairly well-to-do, average consumers turn into poor and weak consumers, so that through this inequality they are excluded almost entirely from the ranks of consumers. This inequality affects production most unfavourably. Having made arrangements to satisfy the wants of these consumers, who subsequently have unexpectedly ceased to consume, production had reckoned with a consumption which did not materialize. The term of dynamic inequality, detrimental to production, does not therefore include every movement or change in the distribution of income, leading to greater inequality, especially not a change which turns a poor man into a rich one, as in this case production would on the contrary profit from this unexpected increment of consumption. Detrimental to production is only the *reflex movement*, i. e. the effect of impoverishment implied in inequality. These fine distinctions of the meaning of inequality are, in my opinion, very important, especially as people are apt to generalize and to consider as a rule every inequality of income as one and the same social phenomenon. We shall have to refer to it therefore even later on.

These introductory remarks were necessary for a better understanding of my chief thesis that the present economic crisis is a crisis of consumption and of distribution, and not a crisis due to deflation, as maintained by some authorities.