

ECONOMIC ANALYSIS OF GUARANTEED WAGES



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THE SECRETARY OF LABOR:

I have the honor to transmit herewith an economic analysis of guaranteed wages, which was prepared by Professors Alvin H. Hansen and Paul A. Samuelson, who were commissioned by the Bureau of Labor Statistics to make this analysis as part of its collaboration with the Guaranteed Wage Study of the Advisory Board of the Office of War Mobilization and Reconversion.

EWAN CLAGUE, *Commissioner.*

Hon. L. B. SCHWELLENBACH,
Secretary of Labor.

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A reprint of Appendix F from *Guaranteed Wages: Report to the President*
by the Advisory Board, Murray W. Latimer, Research Director

PREFACE

Upon the initiative of the Advisory Committee of the Office of War Mobilization and Reconversion in the study of guaranteed wage plans, the Bureau of Labor Statistics commissioned Professors Alvin H. Hansen and Paul A. Samuelson, of Harvard University, to prepare an economic analysis of guaranteed wages. This report was designed to supplement the description of guaranteed wage plans (Appendix C of the OWMR report and also reprinted separately as a Bureau bulletin), prepared by the Bureau for the Office of War Mobilization and Reconversion, and the exploration of the practical possibilities and problems in the extension of guaranteed wages, prepared by the Guaranteed Wage Study staff of the Office of War Mobilization and Reconversion. It appears in the Final Report of the Advisory Board of the Office of War Mobilization and Reconversion as Appendix F.

The present report is an economic analysis of the potential effects of guaranteed wage plans on the economy and the relation of guaranteed wages, if widely adopted, to economic security, business cycles, and the pattern of resource uses.

In accordance with arrangements described above, the Bureau of Labor Statistics also commissioned Professors J. M. Clark, of Columbia University, and Edward S. Mason and Sumner H. Slichter, of Harvard University, to comment on the analysis by Professors Hansen and Samuelson. These comments are included in the report.

The views expressed in all cases are those of the authors.

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APPENDIX F—ECONOMIC ANALYSIS OF GUARANTEED WAGES

I. INTRODUCTION

World War II brought full employment to the American people. The coming of peace holds forth the promise of a high level of job opportunities and production demand for some time to come. But no one can today forget how in the dozen years before Pearl Harbor the American economy was plagued with widespread unemployment and idle machine capacity—with an attendant loss of money income to all classes of society, and a reduction in human living standards so calamitous as to threaten the foundations of our democratic way of life. It is now abundantly clear that involuntary idleness cost the American people the equivalent of some \$300,000,000,000 of real income in the decade prior to the war. The tragedy, suffering, and frustration of the depressed 1930's will not, and need not, be permitted to recur.

It is not too much to say, therefore, that stability at high levels of employment and production will continue to be the number one domestic economic goal of all the community—business, labor, agriculture, and the Government.

Paradoxically, the United States, one of the youngest and most vigorous of all advanced national economies, seems throughout much of its recorded history to have experienced among the highest rates of unemployment of all the nations of the world. In the great depression following 1929 our percentage of unemployment exceeded that of all other nations, not even being surpassed by the German Weimar Republic. In the recovery years just preceding World War II we barely regained the 1929 level of real output, having wasted in unemployment a decade of potential improvements in our standard of living.

Even before World War I, the percentage range of unemployment in this country seems to have run about double that of a country like Britain. In addition to having greater amplitude of cyclical fluctuations (and somewhat more frequent business cycles), the American economy has also been char-

acterized by far greater seasonal swings. Besides, there is some evidence that the range of cyclical variation has been getting worse rather than better in the course of recent decades.

No single line of attack can be relied upon in the battle against depression. In addition to a full employment program, with its many-sided and continuing policies, the Government must be prepared with its social security and welfare measures to ameliorate the human burdens of unemployment. Nor can business, agriculture and labor stand by, passively relegating to the public authorities all responsibility and action designed to promote over-all stability in jobs and production.

One device aimed at mitigating the instability of production and pay rolls is the policy of guaranteed wages. It is the purpose of this report to give an economic analysis of proposals which have been put forward under this general heading.

BRIEF HISTORY OF GUARANTEED WAGE PROPOSALS

The programs initiated by private enterprise to moderate irregularities in production and employment actually antedate by well over a quarter of a century the explicit acceptance by Government (in the Employment Act of 1946) of its responsibility to combat depressions. Particularly after the sharp 1921 post-World War I recession in pay rolls and production, various forward-looking corporations began to institute voluntary wage guarantee plans of one sort or another. Others, without explicitly guaranteeing wages or employment, made strong efforts to smooth out the pattern of their operations so as to provide more continuous annual employment.

Some of these plans may have involved over-ambitious altruism. Others may have represented ill-conceived paternalism, covertly directed against the organization of unions and the development of collective bargaining. In any case, most of these

schemes were short-lived, many foundering on the rock of the great post-1929 depression. Does this mean that they were failures? Not necessarily. In an era when governmental unemployment insurance had not yet been enacted, these plans often aimed at softening the burden of unemployment for at least a limited time. They served as a first wall of defense against depression; the fact that these bulwarks were breached does not mean that they were not of considerable value. Also, in all fairness it should be said that the enactment of governmentally-provided unemployment compensation reduced the pressing need for the continuation of some of the plans.

While the great depression of the early 1930's spelled the end of many of the earlier guaranteed wage plans, it at the same time emphasized in the minds of everyone the great need for job security. And during the recovery years of the last decade, an increasing number of additional companies initiated new guaranteed wage plans.

Organized labor—in part stimulated by the late Franklin D. Roosevelt—begin to develop an interest in wage guarantees during the years just prior to World War II. At the present time, many guaranteed wage programs are embodied in management-labor collective bargaining contracts. Many unions in industries not covered by such contracts have indicated an intention to explore the possibilities of this device.

ORIGIN OF PRESENT STUDY

In 1944, at the peak of the war effort, several labor unions presented a request for a wage guarantee to the War Labor Board. The War Labor Board ruled against the establishment at that time of so important a new precedent in American labor relations. On the occasion of their refusal to grant the United Steelworkers' request, the board members indicated their interest in the proposal, and recommended that the whole problem be given careful study. Early in 1945, President Roosevelt requested that the Advisory Board of the Office of War Mobilization and Reconversion make a study of guaranteed wage plans as a means of regularizing production and stabilizing employment. In making its investigation into the whole problem of guaranteed wages, the OWMR proposed:

1. Examination of specific experience with guaranteed wage plans.

2. Analysis of methods and possibilities of regularizing production and stabilizing employment.

3. Inquiry on cost of various types of wage guaranties.

4. Analysis of economic effect of guaranteed wages.

5. Examination of relation of guaranteed wage plans to other economic measures also intended to stabilize or increase the national income.

In connection primarily with the last two of these points the authors of this report have been asked to make a general theoretical analysis of the economics of guaranteed wages and its relations to other policies. In doing so, we have not considered it fruitful to attempt a review of the voluminous literature on the subject, nor to present a well-rounded factual and quantitative picture of the status and prospects of guaranteed wages. This we can best leave to others. Early in our investigations it became clear that the greatest service we might hope to render lay in bringing under analysis and focusing attention on certain relatively neglected—but crucial—aspects of the problem.

Perhaps most important of these is the need for a critical examination of the repercussions of guaranteed wages upon the level of aggregate demand and upon the business cycle. Hardly less important is an examination of the economic principles and patterns of pricing which society needs to keep in view in order to achieve the most efficient use of our human and capital resources, the reduction of wastes of unstable production, and the equitable distribution of the burdens of unavoidable idleness. These two motifs—business cycle and aggregate demand aspects of guaranteed wages, and efficient, equitable use of our national resources—run through all our analysis, not only in their relationships to each other, but also against the background of other public and private economic policies.

We have not considered it our primary responsibility to spell out in any detail a specific program of action. We have been primarily concerned with general economic analysis. In chapter VI we do put forward certain recommendations, which we believe represent policies which are economically sound in the light of our analysis. Needless to say, these recommendations—and indeed all of our judgments and findings—are put forward only as

our own opinions as individual citizens and economists. They do not necessarily represent the opinions of the Advisory Board of the Office of War Mobilization and Reconversion, or the Washington Research Staff under the direction of Murray W. Latimer. In part our recommendations overlap or are similar to those in Mr. Latimer's final report.¹ It is a pleasure to acknowledge here the stimulus of discussion with him and his staff, even though we were not always able to agree fully upon final formulation of principle and emphasis.

DESCRIPTION OF GUARANTEED WAGE PLANS

Here at the beginning it is well to ask exactly what is meant by "guaranteed wages." No simple answer can be given because of the extreme variety of plans that one company or another has introduced under this general heading in the last quarter of a century. At the one extreme, we observe what is little more than a pious declaration of the company's intention to make efforts to stabilize its production so as to provide steady jobs and incomes. At the other extreme, a company may have signed a legal collective bargaining contract with a union agreeing to guarantee 45 or even 52 weeks of work per year to almost all of its employees.

Even the three best-known plans associated in the public's mind with the guaranteed wage—those of the Hormel, the Nunn-Bush, and the Procter & Gamble companies—differ materially in form and substance. Because there are so many descriptions of the various guaranteed wage plans available, we do not propose to discuss here (except very briefly) the different features involved in such plans, preferring to refer the reader interested in details and in particular concerns' plans to the voluminous literature on the subject.²

By a guaranteed wage plan, we shall not necessarily mean an annual wage plan. Conceivably,

¹ *Guaranteed Wages*, Report to the Advisory Board, Office of War Mobilization and Reconversion, January 31, 1947. See pp. 1-411 of this volume.

² The most comprehensive study prepared to date is the Latimer report. The National Industrial Conference Board, the National Association of Manufacturers, and Brookings Institution either have issued or will shortly issue studies on various aspects of wage guarantees; and Joseph Snider's book, *The Guarantee of Work and Wages* (Andover, 1947), is just out. See also the bibliography prepared by the U. S. Department of Labor, April 1945, entitled "The Guaranteed Annual Wage and Other Proposals for Steadying the Worker's Income; Selected References," and the popular book by J. Chernick and G. Hellickson, *Guaranteed Annual Wages* (University of Minnesota Press, 1945).

the employer's commitment to maintain workers' incomes might be for longer durations than a year—for example, over the whole of the business cycle. More often guaranteed wage plans are set up with a calendar year as the fundamental unit of time. But not infrequently, a firm may wish to guarantee employment for only 6 months or only for the whole of a season. Our analysis will apply also to such plans, but we exclude from our consideration programs concerned with insuring only a full week's work or any period less than, say, a quarter of a year.

The form of the guarantee may vary considerably: Some firms may insure a certain number of weeks' employment at unspecified job assignments and wages; or more often, there may be a guarantee of a certain number of specified pay checks—even if the concern should find that it has no duties for the workers to perform. Usually, if a firm has bound itself to continue a worker's income, it will cast about for some work for him to do, even if it is of a low-productivity character or of a currently unprofitable and unremunerative sort. But where even this is lacking, the corporation agrees to maintain the incomes of the workers who are included under the guarantee. The guaranteed wage becomes in this case the precise equivalent of 100-percent unemployment compensation, maintained for the duration of the guarantee.

Often the plan provides for the maintenance of income payments from week to week at a steadier rate than hours of employment, the overtime of some periods being balanced against the hours of underemployment through other weeks of the year.³ Under the Fair Labor Standards Act, any weekly hours of work in excess of 40 are usually to be paid for at a one-and-a-half overtime rate; but that act did provide for a partial relaxation of such penalty overtime rates in cases where a collective bargaining contract is in force guaranteeing certain minimum hours of total yearly employment.

Not infrequently, guaranteed wage plans are associated with various wage-incentive or profit-sharing programs. In addition to the steadily maintained periodic wage payments, there may

³ Some companies will lend their workers money in periods of underemployment, payable in subsequent periods of brisk employment. Such wage-advance schemes are related to, but distinct from, the guaranteed-wage plans discussed in this report.

also be supplementary bonus or wage payments at longer intervals of time. The total remuneration of the workers may be geared to their productivity, to corporate profitability, or to the value of production and sales.

So much for the form of the plan, whether it (a) guarantees employment, or (b) guarantees wage income, or (c) involves profit-sharing and various "flexible-wage" features. Equally important are the other various features and limitations of the guarantee, such as the following:

(1) Limitation of coverage. What workers are covered? Are only those who have been employed 2 years, 1 year, or 6 months covered? Or are only workers of certain skills and departments covered?

(2) Limitation of weeks per year. Are a full years' work and income (2,080 hours per year, 52 weeks at 40 hours per week) guaranteed? Or are only, say, 45 weeks of work guaranteed?

(3) Limitation on duration of guarantee. What is the duration and legal character of the guarantee? One prominent plan guarantees 48 weeks per year of work to all of its employees of more than 2 years' standing, but the guarantee is a unilateral one which the company reserves the right to discontinue at any time it may wish to do so. Other guarantees may run from the first of the year to the last, and may be embodied in a collective bargaining contract with a union. Still others may be binding upon the company, but terminable after it has given a year's or 6 months' notice.

The possible costliness, benefits, and other quantitative economic effects of guaranteed wages all depend very much upon the type of guarantees which are adopted—upon their degree of coverage, the hours guaranteed, and the duration of the guarantee. To avoid a tedious catalog of the various plans that are conceivable or now in force we shall find it convenient to outline a few possible guaranteed wage plans, in terms of which our exposition may be facilitated. This does not imply any approval of the particular details embodied in these examples. They are set out simply as hypothetical cases:

EXAMPLE 1: For each calendar or fiscal year, the company agrees—in a legally or morally binding fashion—to provide some number of weeks, say 45, of full-time pay (or its equivalent

spread over the year) to a specified group of workers, selected by seniority or length of previous service. The contract or agreement may, or may not, be renewed for the following year and its coverage and hours of guarantee may be altered, provided notice to that effect is given at least 3 months prior to the end of the contract year.

In this case, if the corporation encountered a sudden slump very early in the year it might be obliged to incur the costs of maintaining income for a period of almost a year. On the other hand, if the decline in its sales came late in the year, the company might be able to reduce its pay roll in very short order.

It would run the risk of having to maintain, on the average, substantial wage payments for something like 6 months after a decline in its revenues.

EXAMPLE 2: This is the same as example 1 except that the contract or agreement does not run from the beginning of one fiscal year to the beginning of the next. Instead, the guarantee runs on indefinitely—until the company gives 12 months' notice of its intention to discontinue the guarantee or change the extent of its coverage.

One could imagine a plan identical to example 2 except that the period of termination notice is reduced to, say 6 months.

EXAMPLE 3: This could be like either of the above two plans, but with the extra limitation that the employer's wage liability to workers laid off should never exceed in any year, say, 10 percent of the guaranteed pay roll. In most years, this would, in fact, provide 100-percent income security to all workers. But in a very bad year, when the number of idle workers became very high, then the employer's liability would have an upper limit. In this event, the laid-off workers would have to share in some manner the amount available for wage payments within the limitation of the 10 percent liability.

Obviously all sorts of variations could be attached to each of these illustrative cases. All three examples have this much in common: They enhance the job and income security of workers for at least a limited time into the future; and they involve the employer in the risk that, for a limited time at least, he may be obliged to maintain his wage outpayments even if his sales revenue falls

off sharply. However, the employer has not obligated himself to incur unlimited losses for an unlimited period; after the period specified under the terms of the contract, his guarantee terminates; and, of course, after these same periods of time, the worker may find himself jobless and without a current pay check.

One point requires notice and emphasis at this place. While the letter of the guarantee may specify that the employer's liability ends after the date of termination, management and unions both are well aware that there will be considerable social pressure upon the employer to renew his guarantee and to maintain employment longer than specified in the contract. This explains why many financially strong companies, who do not doubt their own ability to finance guaranteed wages for the first year of a serious depression, are nevertheless reluctant to offer even a limited guarantee. Not without cause, they fear that such a limited commitment may put them on the spot after the period of guarantee is over. They realize that even those companies which guarantee nothing are under more or less powerful internal and external pressure to minimize lay-offs; but they also realize that such pressures are not brought to as sharp a focus as would be the case under a guaranteed wage plan. In the following discussion we shall, on occasion, have to go beyond the legalistic letter of the guarantee commitment to the further economic implications.

SOME PRELIMINARY OBSERVATIONS

Before discussing in detail the outline of our economic analysis in the following chapters, we shall do well to clear the air with a brief statement of certain fundamental preliminary conclusions.

First, the guaranteed wage is not a cure-all for the problem of business cycle unemployment—nor could it ever approach near to being one. Exaggerated claims, overstating its importance and advantages, do more harm than good. At the very beginning, we wish to state for the record—frankly and explicitly—that if it ever had to come to a choice between guaranteed wages and other important depression and anticyclical public and private policies, such as our system of unemploy-

ment insurance,⁴ our social security programs, or fiscal and monetary policy, then it would be guaranteed wages that would have to be rejected. We do not wish to be misunderstood. As will become abundantly clear from the pages that follow, we do not see any necessary conflict between guaranteed wages and other needed Government policies. On the contrary, it is to be hoped that guaranteed wages can be integrated with unemployment insurance so as to strengthen income security. Also, it is our view that guaranteed wages can be financed so as to contribute something toward moderating the excesses of boom and slump in the business cycle.

Second, although the primary motivation for guaranteed wages comes from wage-earners' fear of business cycle unemployment, our studies lead us to the following somewhat paradoxical conclusion. In a world of high effective demand and purchasing power, where there is no problem of chronic or depression unemployment—in such a world, guaranteed wages might make its greatest contribution: by stabilizing seasonal and other short rhythms in production and by equitably allocating the economic burden of the residual amount of unavoidable idleness and unemployment. This conclusion emphasizes all the more the importance of a full employment program, within the pattern of which the guaranteed wage can play a significant role. Under the present system of lay-off on short notice, the employer finds himself with insufficient financial incentive to undertake the costly efforts which are necessary for thoroughgoing stabilization. What are truly overhead costs to society often appear to the employer as avoidable variable costs, with the result that enlightened competition does not lead to the economically most efficient use of resources.

The view that the single individual firm, even a large one, can by good intentions and clever policies substantially contribute to solve the problem of the business cycle, we are compelled by economic analysis and all the available empirical data to

⁴There are, to be sure, many technical imperfections in our present unemployment insurance system: inadequacies of integration and uniformity between states, insufficient benefits in relationship to reserve accumulations, perverse cyclical aspects of merit or experience rating, etc. These should be remedied by legislation and practice. They should not be used as an excuse to attack unemployment insurance, or as an argument for substituting guaranteed wages or any other alternatives in place of unemployment insurance.

discard in the beginning. No one enterprise is secure enough or powerful enough to withstand and modify the great swings of general business activity.

In our judgment, there is scarcely more validity in the hope that gradually, by more and more firms voluntarily extending the scope of their stabilization activities, we shall approach finally to a condition of continuing high employment income and production. As we shall show later, there is every good reason for looking with approval upon a redoubling of the efforts of management, on its own initiative, toward ironing out its employment and production fluctuations. And when a considerable number of firms have carried through bold, imaginative, and well-conceived stabilization programs, considerable progress will have been made toward reducing the costs of economic idleness. But by far the greatest progress that will have been made is likely to be in connection with unemployment arising from seasonal and other rhythms of business activity of shorter duration than that of the business cycle.

From a dispassionate appraisal of the efficacy of guaranteed wages, the device would appear to be, by itself alone, a weak reed upon which to rely in an attack on such widespread unemployment as our economy has encountered in recent years. Indeed, it would be nothing less than tragic if, by management initiative or governmental and trade-union pressure, an ambitious program of guaranteed wages was undertaken without at the same time instituting other more important programs of government and business designed to promote high and stable levels of production, income and employment.

While it is conceivable that an ambitious program of universal wage guarantees would diminish the intensity of minor fluctuations, such as occurred in 1924 and 1927, there is danger that it might be financed in a manner that would intensify such deep and cumulative recessions as that of 1929. The relationship between guaranteed wages and the sharp recessions of the 1920-21 or 1937-38 type are by no means easy to appraise. If other governmental measures were not instituted to cope with depressions, sober quantitative appraisal of the relationship of pay rolls to corporate net worth shows that insolvency and bankruptcy could well be the price of any

guaranteed wage program which was not carefully limited in its coverage and duration. Business, even large business, is not the master of its fate where the business cycle is concerned.

On the other hand, we cannot be content to accept the chaotic status quo. For if we look at, say, the automobile industry, which very properly stands out in the public's mind as typifying the very essence of our industrial society, the picture we see is far from reassuring. Automobile production is an efficient undertaking, paying higher wages than the rest of the world and yet through greater productivity able to undersell all other countries on a free-trade basis. It is and has been a relatively profitable industry. An important part of its total output is under the control of three giant corporations, each of which has presented typical chapters in American industrial life: the self-contained growth of Henry Ford's great enterprise, the evolution after World War I of the vast General Motors Corporation, and the post-1929 emergence to full stature of the Chrysler organization. In addition the recent war has placed the remaining smaller independent producers in a comparatively favorable financial position.

But if we look more closely we see that it is an industry that lives dangerously. Stocks of finished cars and of parts and raw materials are literally measured in terms of days and weeks of production rather than in terms of months and years. The continuance of production hinges on a precarious scheduling of thousands of components produced in hundreds of separate plants. This elaborate division of labor and interdependence, which we hardly notice in ordinary times, makes for efficiency but at the cost of vulnerability—as was revealed in the postwar disorganization of the industry.

Despite the fact that the use of automobile services, as measured by passenger rides or gasoline consumption, fluctuates only moderately over the year and even over the ups-and-downs of the business cycle, the flow of automobile production proceeds in much more fitful jerks and starts, as dictated by the vagaries of consumer and dealer ordering and the march of the business cycle. In consequence, the employment record of the industry—the job experience of the workers attached to the industry—can almost be termed a shocking

one. Even in relatively good times workers often spend considerable time waiting to be called back to their jobs. In depression the production of autos and trucks may decline to a quarter of the prosperity levels.

To say that the situation is a shocking one is not to imply that any one group of individuals or organization is to blame or that the record of this industry is worse than that of many others. Different companies have at various times made determined efforts to iron out their fluctuations in production. The whole industry together has attempted to reduce seasonal variations by means of rescheduling the time of introducing new models and of holding auto shows. The results have been disappointingly meager. Clearly the historically developed institutional structure of the industry and of our unstable American economy must be blamed for the unsatisfactory character of the industry's performance with respect to production stability. Under the existing set-up no one company has the financial incentive or ability to provide steady jobs and income.

For a cure to the fluctuations in auto production over the business cycle, we must properly look elsewhere. But it is not too much to hope for, and to ask of management and labor, that measures be taken and practices be altered to moderate the incidence of irregular and seasonal employment and of economic idleness. This may require many far-sweeping changes in the organization of the industry: increases in inventories and storage facilities, limitation on undue coddling of consumers' desires with respect to modification of style and model changes, perhaps acceptance of lower hourly wage rates in exchange for higher annual earnings. Conceivably, such a program of thorough-going seasonal stabilization might even raise costs and prices to the consumer. None of these measures would be easy and none would be costless. But in a real over-all sense the costs are less than those of idleness under the present regime of instability, where the burden falls upon those least able to bear it, the workers.

Is it too much to hope that in the not too distant future all parts of the industry will look back and wonder that the present day wastes of idleness were even for an instant tolerated? We believe not. But in taking this viewpoint, we do not mean

to imply that such a happy state of affairs will come into existence simply by forcing the industry, through Government legislation or collective bargaining pressure, speedily to guarantee wages for substantially all employees. Unless a general, many-sided attack is made upon the problem of business cycle stabilization, together with a step-by-step industry-wide attack upon seasonal instability of production, guaranteed wage plans are likely to be so costly as to be doomed to failure.

It is this dilemma—that the present day deeply-rooted wastes of instability are economically intolerable but cannot simply be legislated out of existence—with which this report is concerned.

PROPOSED OUTLINE OF ANALYSIS

Of the five divisions of the study of guaranteed wages mentioned earlier, our report is naturally concerned with the final two: an analysis of the economic effects of guaranteed wages, and an examination of such plans in relation to other economic measures designed to stabilize or increase the national income. Such an analysis is a necessary supplement to a study of specific experience in different concerns and different industries.

The whole is more than the sum of its parts. Particular firms may have success with the guaranteed wage, in part because they are the only ones offering workers its advantages. The total economic impact of such plans might be negligible, or if overly ambitious or too "soundly" financed, the device might even prove harmful to over-all stability. If wage guarantees discourage investment commitments and if firms are induced to stabilize their employment at low levels in order to minimize lay-offs, the problem of reaching and maintaining full employment could conceivably be aggravated. Or if guaranteed wages had the effect of attaching workers to a single firm in subsidized idleness or inefficient production, then under certain circumstances national output and productivity might suffer.

Under the present wage contract, do the apparent money costs of hiring or laying off labor truly reflect the overhead social costs to society of maintaining the workers' standard of living? What should the relationship be between prices and wages in order that economic resources may be used most efficiently?

Perhaps more important still is the question of how guaranteed wages—on a limited or on a wide scale—affect the over-all level of aggregate demand. Would the mere act of guaranteeing employment create attitudes and behavior patterns sufficient to realize its stated objectives? We all know in a rough way that jobs make markets, and that markets for goods make jobs. Would the widespread commitment to maintain jobs automatically create the purchasing power necessary to make good such a commitment? Or to put the matter in another way, would the balance of aggregate demand in relation to our productive potential be improved; and would the basic factors causing fluctuations in investment—factors which underlie the business cycle—be compensated for?

Each one of these questions requires detailed over-all economic analysis. Each one leads inevitably to a consideration of other economic policies aimed at promoting economic security and stabilizing business activity.

In the chapter immediately following this introduction, we undertake to analyze the true economic cost of different kinds of idleness: to inquire how its amount is to be measured, to investigate how its burden is distributed between wages and property-returns, both in and outside of the industry concerned, and to examine the adequacy of incentives toward regularization.

Then in chapter III the interrelationships, comparisons, and contrasts between guaranteed wage programs and other public programs such as unemployment insurance and full employment programs are discussed.

Chapter IV presents an economic analysis of

the effect of guaranteed wages on the level of and fluctuations in aggregate demand. The results are found to differ depending upon whether the guaranteed wage program impinges on a society which is highly cyclical and fluctuating, or is reasonably stable at either a low underemployment or a high full employment level. In this analysis the effects of private reserve financing in contrast with the “pay-as-you-go” method of financing are examined.

While the problem of unemployment was quantitatively most pressing before the war, it cannot be permitted to overshadow the ever-present task of seeing to it that resources shall not only be used, but used efficiently so as to contribute toward the maximum satisfaction of individual and social economic wants and needs. Chapter V is concerned with the effects of guaranteeing wages upon the pattern of resource use and upon the structure of prices, wages, and costs. Here again it is necessary to distinguish among the different kinds of economic societies into which the guaranteed wage plans are introduced.

In chapter VI, we make a number of policy recommendations growing out of our analysis. Such guaranteed wage plans as may be introduced should be set up only after the possible dangers and limitations have been thoroughly canvassed. When this has been done, we believe that, under safeguarded procedures, the guaranteed wage can be made to contribute to a better and more efficiently functioning economic order, and that inducements such as those recommended in chapter VI looking toward more widespread experimentation and expansion are justifiable.

II. ANALYSIS OF THE ECONOMIC BURDEN OF IDLENESS

In this chapter we shall undertake to analyze in some detail the precise nature of the economic costs of unemployment and idleness. In the course of our discussion it will become clear that the problem of irregular production is more than the problem of general cyclical unemployment, although the quantitative magnitude of the latter has been such in recent years as to dominate our thinking and attitudes. To the degree that we are able to avoid serious breakdowns in the years ahead, problems (“labor mobility” for example) which seemed—and were—unimportant against the background of depression unemployment, will

take on a new significance. Thus we are concerned not only with depression unemployment, but with the problem as a whole, including daily, weekly, yearly, and longer-term irregularities and fluctuations in business activity, many of them avoidable.

SOCIAL VERSUS PRIVATE COSTS OF IDLENESS

But first let us note that the present system of hiring, employing, and paying labor is only one of many conceivable alternatives; and one which became widespread even in our own economy only in the last century. Before industrialization had

impersonalized our economic relations, it was probably the rule more often than not for a craftsman's helper to be hired by the year or season. Often, barring discharge for personal incompetence, the worker could even count upon some measure of job security and income maintenance even through hard times, the employer and employee tightening their belts together.

Even today in agriculture and some branches of small industry, the same relationship often prevails. And throughout all industry, large and small, executives and white collar workers are in good part assured of employment over all of the year and through most of the business cycle. It is perhaps not too hard to imagine an economic system in which the wage contract with all employees was more nearly like that with executives and white collar workers than like the present prevailing mode of wage payment and tenure.

Let us, however, consider the prevailing form of the wage contract and analyze its economic effects for whatever they may be. An industry with high seasonality may hire its workers for 7 or 8 months, leaving them idle during the off-season. Similarly, a concern sensitive to cyclical fluctuations may take on many new workers during the upswing of the boom, and conserve its resources during the depression by curtailing its wage payments.

Still, as was pointed out so clearly a score of years ago by Prof. J. M. Clark in his masterly *Studies in the Economics of Overhead Cost*:⁵

In a more general sense, however, there is a minimum of maintenance of the laborer's health and working capacity which must be borne by someone, whether the laborer works or not: that is, if it is not borne, if the maintenance is not forthcoming, the community suffers a loss through the deterioration of its working power which is at least equivalent to the cost of maintaining the laborer. Thus the burden is there in any case: it cannot be avoided. From this point of view it appears that a large part of the cost originally counted as wages represents an overhead cost which the laborer is responsible for covering as best he can, just as the employer is responsible for covering the overhead costs on account of capital. However, if the laborer fails to cover it the community does not escape the burden, and it is ultimately borne by industry in the shape of reduced productive power and damaged morale. And thus it comes back to the employer in any case.

⁵ John Maurice Clark, *Studies in the Economics of Overhead Costs* (University of Chicago Press, Chicago, 1923).

* * * The reason why the expenses of production, some of them, normally vary in proportion to output is simply because the terms of the wage contract are drawn in that way. The employer leaves the wage earner to care for his own overhead and the terms of the contract are not scientifically adjusted as, for instance, the contract for electric current is sometimes adjusted to the overhead costs of the ultimate producer. It may be that we shall find that our general system of wage payment is thoroughly unscientific and that a more scientific system may operate to improve the steadiness of employment in much the same way in which scientific rate systems have been used to increase the regularity of use of electric power plants (p. 16).

The fundamental discrepancy between true social costs of unemployment and apparent pecuniary private costs is of course accentuated by the form of the present wage contract. Without as yet going into the merits of such a proposal, let us suppose that by voluntary action or collective bargaining arrangements, firms were induced to provide income or work for their employees throughout all the year or all the business cycle. Then not only would the burden of the worker's maintenance be spread differently between the workers and the employers in the industry in question, and among the other workers and employers who make up the community at large, but in addition the use which the employer would make of labor might be different. Moreover his production or sales decisions might very probably be appreciably affected.

Today in a depression, a firm will for the most part not hire a man unless in some sense it expects to receive in value a return commensurate with his full wage. Not so does it act with respect to the machinery it owns. If, because of slack times, a piece of machinery can produce only a fraction of the value for which it was originally purchased, the firm will not thereby leave it in idleness. On the contrary, so long as the machinery can produce anything above its costs of operation (including of course any extra deterioration engendered by use) it will pay the firm to utilize the machinery.⁶

⁶ To some degree, therefore, we might expect some differences in entrepreneurial behavior of firms in such rare industries as shoe manufacturing, where much of the equipment is rented on leases of relatively short duration. Even here the changed form of the contract, from ownership to leasing, has important repercussions on how the various parties share the total social economic burden. An important qualification to the theoretical notion that firms do in fact disregard all truly fixed or overhead costs is indicated later. Often, in imperfectly competitive markets, they use full-cost considerations in their pricing—for rational and irrational reasons.

THE ECONOMIC COSTS OF IDLENESS

If an industrial worker has employment only 8 months a year and must lay off for 4, the true cost or economic burden to society is the amount of production which he is prevented from producing during the 4 months of idleness. Generally speaking, we should expect this to be roughly equivalent in value to the wage income that the worker loses by unemployment plus an additional wastage of capital and nonhuman resources as a result of the instability of production. Similarly, if a longshoreman works only a few days a week, the important costs to society are the foregone value of production and income on the days of enforced idleness.

Our earlier quotation from J. M. Clark gives an understatement of these true social costs, because the emphasis there is placed upon the necessary maintenance expenditure of the worker during periods of idleness. It is not improbable that an industrial worker capable of producing \$3,000 worth of output per year might, by practising stringent economies, be able to maintain himself and his family with their health, skills, and (more doubtfully) their morale intact on an expenditure of \$2,000 per year. Nevertheless, the true cost of a year's idleness of such a man is still \$3,000 and not \$2,000. And even if science were able to devise ways of costlessly putting men on ice, to hibernate during slack times like bears during the winter, the costs of idleness would still be the same.⁷

We feel it necessary to expound at some length these almost trite, fundamental economic principles because only in this way can a number of current misconceptions and distorted emphases be avoided. Thus, it is quite false to think that the social cost of instability would disappear completely if the employer were made to pay the workers' salary during periods of lay-off. Actually, this might be a highly desirable policy, because

⁷ This is all the more evident if we apply the argument to the less controversial and emotional problem of a nonhuman resource like land. If a 100-acre field neither gains nor loses in productivity by being left fallow for a season, can we say that there are no costs involved in its idleness just because no outlay on maintenance is required? The answer is "No." The potential crop of that year is lost forever. If the land actually goes to weeds and deteriorates through nonuse, the costs are that much greater.

If there has been a real change in society's desire or technology so that the land or worker now has a lower potential economic productivity, then the waste due to idleness is, of course, equal only to his new potential economic productivity.

the worker may be least able to bear the cost of idleness; and because society may deem it desirable for the employer to shoulder part of the cost in lower business profits, or wish the burden to be shifted in part forward to consumers and the general public in higher prices, or wish the burden to be shifted backward in reduced wage rates for all workers (including those who continue to hold steady jobs). But if the workers' incomes were maintained, though they are idle, the social wastage of productive resources would still be borne by society as a whole.

The total social cost is not changed in real product terms by different modes of sharing the burden of idleness. The social cost for the community as a whole will remain unless greater stabilization of jobs and production is achieved. It is not enough merely to transfer the burden from Peter to Paul. (Perhaps we should not say "merely" since it does make a great deal of economic, political, and social difference just how equitably or inequitably economic burdens are shared between the Peters and the Pauls of different economic levels.)

We do not deny that different modes of sharing the burden can have considerable repercussions on the total amount of the burden. For example, shifting part of the burden of depression unemployment from the workers to the Government may, depending upon the method of finance, reduce the amount of unemployment. Or making industry bear the costs of certain kinds of seasonal irregularity of employment may provide just the stimulus necessary to cause the introduction of effective stabilization programs.

In brief it is the effective carrying out of productive employment rather than merely the payment of wages that reduces the social costs of idleness and instability. Income maintenance without productive employment stabilization is only a half-way measure which transfers the economic burden of waste and minimizes its social impact, but fails to diminish it.

When, as above, we speak of the economic costs of idleness, we must be careful to distinguish between various kinds of idleness. Of course, no one can work 24 hours a day. The hours spent in sleep are not wasted, any more than is the time spent in leisure on Saturday afternoon and Sunday, or on holidays and vacations. We need not regard base-

ball pitchers who go hunting during the weeks following the World Series as wasting their time, any more than we would consider firemen on their way back from a fire or for that matter firemen playing checkers while waiting around for a new alarm, as being unproductive.

In other words there are unavoidable cessations of activity which are an intrinsic part of certain productive activities. All cost comparisons are relative. It would be pointless to compare our actual national output with that which could be obtained if the laws of thermodynamics were other than they are; or with what we could produce if no one required sleep and desired leisure; or with what would be producible if the seasons were constant. To the extent that work interruptions are unavoidable and intrinsic, it will make for clearer thinking if we avoid the term "idleness" and "economic waste."

Also, to the extent that curtailment of labor results in a reduction of human disutility or, what is almost the same thing, an enhancement of the utility of leisure—to this extent it would be obviously incorrect to regard the resulting loss of economic output as an equivalent total social waste. Thus, nobody laments the fact that our economic system fails to provide 84 hours a week of work for all, or fails to find work for a subway attendant in between stations. There are only so many activities that human beings can be reasonably expected to attend to at any one time.

Involuntary idleness such as is encountered over the business cycle or in many highly seasonal industries presents little or no saving grace in the form of reduced disutility. Rather does our measuring of the cost of idleness by the value of lost output understate the true loss. In addition there is an extra psychic loss inherent in unemployment itself. A man thrown out of work against his will is not on a vacation. In the present state of our society, work under reasonable conditions up to some 40 hours per week and 50 weeks per year is not a curse but a boon and a benefit. The social gain of transferring a man from frustrating involuntary unemployment to purposeful productive employment may even be greater than the value of the goods produced.

We may summarize our discussion of the overall economic cost of instability briefly as follows: (1) The primary economic cost is measured by the

loss of national output resulting from unnecessary idleness; (2) in addition there is a secondary cost involved in the individual misery and social disorganization which grows out of idleness itself

THE COST OF INSTABILITY TO THE WORKER

The intermittently employed worker suffers from instability primarily from the fact that his pay largely ceases during periods of unemployment. To some degree unemployment insurance benefits, home or work relief, and severance pay may help to keep his income from falling below an intolerable minimum; but only to a limited degree, since coverage is incomplete and of limited duration, and rates are deliberately set low in relation to full-time earnings.

It appears in general to be an empirical fact that workers subject to frequent lay-offs over the year and over the business cycle tend to fare badly in terms of average rate of earnings over the whole year and over the complete business cycle. But it is not at all obvious in theory that this should be so. It could be argued, and it is often argued, that competition in the labor market will cause higher hourly rates of pay to prevail in unstable occupations so as to compensate for their unsteadiness of employment. The mechanism bringing this about is supposedly the familiar one whereby workers refuse to go into industries offering less total compensation over time than prevails in those other industries which offer steady, full-time employment; and in refusing their supply, workers cause wages to be bid up in the highly fluctuating or irregular industries.

Before turning to the available statistics upon the subject, let us point out the rather artificial set of theoretical assumptions necessary to achieve this result. Firstly, the cyclical rhythms in activity of the industry in question must be of sufficient regularity so that workers deciding whether to enter or leave the industry can make some sort of an approximate calculation as to the hourly rate which will in the future yield average earnings comparable over time to stable occupations. Perhaps to some extent seasonal (building trades for example) and shorter rhythms are of sufficient regularity to be forecast by the workers to a limited degree, but the vagaries of the busi-

ness cycle and other fluctuations preclude even this possibility.

Furthermore, there is the second implicit assumption that job opportunities are so plentiful that workers can afford to pick and choose between different industries and occupations. During the past few decades, this has been far from the truth. Often workers have been faced with the choice of accepting precarious unsteady employment, or none at all. However, if high employment conditions should come to prevail, then this second hypothesis would become more nearly true.

Thirdly, an equalization of average earnings through changes in the supply of workers going into different industries implies that wage rates are set in different parts of the labor market by the operation of competitive supply and demand. Actually, and today this is so obvious that we need not elaborate, wages are to an important degree set by the forces of collective bargaining and are a resultant of the pressures exerted by union and management organizations.

Finally, there are always individual differences in ability, training, and opportunity, all of which tend to create inequality in the earnings of different kinds of workers. Even if all jobs were equally stable, we should still expect important, persistent differences in earnings in different fields. How then can we tell what part of the actual reported differences in earnings are due to different degrees of instability of work, and what part to other factors? The answer is we cannot, certainly not with quantitative accuracy.

One thing, however, is clearly apparent from statistics relating to annual hours and earnings in industries characterized by different degrees of cyclical and seasonal variability.⁸ There appears to be little tendency for hourly rates to adjust themselves in different American occupations so

⁸ The Washington staff of the guaranteed wage study has tried with little success to find occupations which are alike in all important respects except for varying degrees of stability of employment in order to make such estimates. The data examined were: (1) From the Censuses of Manufactures, 1929, 1933, 1935, 1937, and 1939: total pay rolls, numbers of employees month by month and average annual number of employees for selected industries. (2) From Bureau of Labor Statistics: average hourly earnings for industries selected for (1) and studies of annual earnings of employees in selected industries, published in the following issues of the Monthly Labor Review: February 1940, pp. 401-409; January 1940, pp. 172-182; April 1939, pp. 781-788; October 1939, pp. 921-931; December 1939, pp. 1470-1482; July 1937, pp. 29-37; July 1939, pp. 163-175; May 1936, pp. 1333-1335; December 1933, pp. 1398-1408; October 1940, pp. 823-833.

that average annual earnings over time are equalized in industries of different degrees of instability.

Some of the industries with most intermittent employment—especially those in rural agriculture areas of the South—also have the lowest hourly rates; while some of the highest hourly and weekly rates are to be found in lines of activity which are most stable in employment.

Logical purists may assert that the differences in average earnings over time are all due to other factors; and that hourly rates have adjusted themselves over what they would otherwise have been, not so as to equalize earnings, but so as to compensate for variability of employment. The form of this assertion makes it impossible for anyone either to verify or refute it. But such facts and analysis as have come to our attention incline us to the belief that any tendency for the hourly wage to rise so as to compensate for unemployment is only of a weak and partial character.

By and large, therefore, we incline to the conclusion on factual and theoretical grounds that the primary burden of instability of employment falls upon the worker and his family in the form of reduced average earnings over the long run. In terms of the equity considerations which underlie the modern insistence upon progressive taxation according to ability to pay and upon the social desirability of keeping up the standard of life of low-income families, placing the burden of unemployment wholly upon the worker represents the least desirable national policy, and one which aggravates to a maximum the onerousness of the given pattern of instability.

It does not follow necessarily from this that the best economic policy to remedy this situation would be one of raising standard hourly rates to whatever level is necessary to compensate for instability of employment. We do not say this merely because such a solution would involve extreme changes in the present wage set-up of American industry. Grave inequities may often justify drastic action. More important is the consideration that simply raising wage rates without reducing instability and idleness only shifts the burden off the worker's shoulders but may fail to reduce the economic dollar value of waste. This would tend to be true unless indeed there were some valid reason to expect that raising hourly wage

rates would by itself tend to reduce the average instability of production. Moreover, we need to consider the relative merits of raising wage rates and of changing the wage contract in the direction of guaranteeing longer periods of employment as means of promoting stable production.⁹

These questions we must defer until chapter V. But there is one aspect of the problem which deserves mention at this point. Under some circumstances raising the hourly wage rate may actually tend to increase the total of idleness—especially where the problem of “casual employment” is involved. By “casual employment” is meant primarily a condition where (a) workers are intermittently hired for short engagements, and (b) where the first worker who happens to present himself is likely to get the job. A surplus reserve of workers often results from higher rates of pay, especially if there is general unemployment.¹⁰

This line of reasoning is abstract and oversimplified. It should not be pushed too far. But it does indicate one aspect of reality, and it does indicate that any policy of raising wage rates should be accompanied by supplementary policies designed to reduce the total pool of unemployment.

Even if normal annual earnings were maintained in unstable jobs by means of higher rates of pay when working, there would still remain the evil of irregular earnings. An ideally calculating individual could perhaps be relied upon to budget his expenditure in equal amounts throughout the year; or in occupations subject to much longer rhythms, over the whole cycle. But for ordinary human beings spending patterns tend to follow closely upon their current income, so that uneven income payments result in ups and downs in living standards.

Added to the evil of variability of work and pay, there is the attendant feeling of insecurity. Without some tangible advance guarantee, for every worker who is actually fired a number of others may quake in their boots. Living apprehensively from day to day, the worker cannot

efficiently make financial plans for the future, cannot undertake advantageous long-run commitments with respect to home ownership, life insurance, and other desirable forms of personal consumption and saving.

To be sure, formal and informal seniority practices already serve to ameliorate, in part, the universal fear of unemployment. But there still remains a large residue of insecurity, which, taking the long view, we must regard as partly unnecessary. This shows that there may even be merit in those limited guarantee plans which do not go much beyond explicitly guaranteeing job security to those who already in fact largely enjoy it. The mere announcement effects may be reassuring to some degree.

The question may be raised whether stabilizing employment and income over time and reducing job insecurity will serve to increase or reduce the average propensity to consume out of a given income. The answer to this question, which has a bearing on the problems discussed in chapter IV, depends upon a nice weighing of conflicting quantitative tendencies. On the one hand when people are reduced from a high income level to a lower one, they probably still try to maintain as best they can the higher standard of consumption to which they have become accustomed. Therefore, because of the “ups” in the “ups and downs” of income, there is a tendency for average saving to be lower and the average propensity to consume to be higher than with stable incomes. On the other hand the persistent fear of unemployment tends to cause people to try to save more out of a given income.

He would be a rash man who would venture a confident definitive answer to the question of which tendency is the stronger, no satisfactory statistics being available. Since there appears to be no strong presumption upon either side, we may tentatively cancel out of our appraisal any claim that guaranteeing wages will have stimulating or hampering effects upon saving habits. (To some extent steady wages improve the credit position of workers and enable them to invest in consumers capital goods such as housing and autos. Such an increase in investment implies a higher rate of effective demand.)

Guaranteeing employment to a limited number of employees raises some of the same policy prob-

⁹ A further drawback to raising hourly rates is that workers differ in their lay-off experience according to seniority and other matters.

¹⁰ A classic case is that of the London dock and wharf workers, analyzed almost 40 years ago by W. H. Beveridge in his significant work, *Unemployment: A Problem of Industry* (1909 and 1930), p. 107.

lems involved in excessive seniority provisions.¹¹ Admittedly, we need not argue that everyone must be dragged down to the level of insecurity of the least fortunate. Having granted this, however, we must still go on to point out the possible evil of carrying seniority and wage guarantees to a favored group so far as to create in effect an economic caste system, in which one fortunate privileged group is protected completely from the vicissitudes of economic life, at the expense of throwing the full burden on those left without protection. Some underemployment for all may be preferable to total unemployment for a minority. If there must always be an irreducible minimum of the working force unemployed, it would be far better for their numbers to be made up of a revolving group of different people, with no appreciable group being unemployed for very long. During the 1930's, those who had been unemployed the longest had the greatest difficulty in finding jobs after business demand began to recover. They were beginning to form part of the so-called hard core of unemployables, until the high level of wartime demand melted the core and proved their employability.

This points a possible way out of the dilemma that giving security to the majority may inequitably and cumulatively concentrate insecurity upon an unlucky minority: the maintenance of a high level of over-all effective demand by bold public policies will serve to help those recently hired employees who lack seniority and who cannot qualify for guaranteed wages.

In concluding this discussion of the evils of job insecurity, we must point out that this is not a matter of concern only to the workers involved. The employer is vitally affected by the workers' mental state in this regard. On the one hand, from a realistic hard-boiled viewpoint there is little doubt that fear of losing one's job sometimes acts as a whip to spur the worker on to more efficient production. Fear of discharge for cause certainly acts in this direction. But fear of lay-off is quite another matter, except to the extent that the order of retention of men and rehiring is made to depend upon demonstrated efficiency. Even

¹¹ It is not at all paradoxical that even recently hired workers tend to favor seniority rules. They hope to possess seniority themselves some day.

in the fairly rare industrial situations where labor is in fact laid off in order of inefficiency and rehired in order of efficiency, there is always the counter tendency that tense and insecure workers may over the longer run be less efficient rather than more efficient producers.

Neither of these last points is so telling as the fact that increasingly in modern industry formal or informal seniority rules determine the order of a worker's lay-off, rather than his own effort and productivity. No worker feels that the chances of retaining his job are primarily dependent upon his own efforts. But all the workers together often feel—rightly or wrongly—that by their behavior they can stretch out the work to be done and prolong the average period of employment of the whole group. In order to make jobs last they will consciously or unconsciously slow down their efforts—with detrimental effects upon productivity, costs, and profits. And such is the group solidarity of any set of men working in close contact that even those workers with high seniority and no fear of unemployment will actively and passively pursue these same tactics; for just as young workers look forward to the time when they will have gained seniority and act accordingly, so too do the old-timers remember back to the days when they were at the bottom of the ladder. Besides, rarely does one have so much seniority but that he is outranked by someone else, and even his job may be thrown in jeopardy whenever there is a really deep falling off in business activity. Given the above set-up, increasing the worker's feeling of security by means of guaranteed wage plans may contribute to an increase in labor productivity.

This completes our brief survey of the ways in which the economic burden of unemployment tend to fall with heavy weight upon the workers; through (1) reduced earnings, (2) loss of opportunity for useful and satisfying activity, with attendant costs to the community at large, (3) through variability of the receipt and expenditure of income, and (4) through a widespread feeling of insecurity and tension among both those employed and those unemployed.

We turn now to an examination of the burden experienced by the employing industry.

THE COST OF INSTABILITY TO INDUSTRY

The burden of unemployment falling on the workers is only part of the total story. Heavy unemployment causes national income to fall sharply. During such times industry is operating at low capacity levels. The rewards to property decline.

Historically, there seems to have been a rather remarkable constancy in the proportionate division of the total national income between personal effort (wages, salaries, and personally earned entrepreneurial profits) and property income (interest, net rents, and profits combined). It appears that the burden of heavy unemployment tends to be parceled out in something like the same proportion between property and labor income.

If we take property income as a whole, probably similar conclusions can be drawn in the case of seasonal and other noncyclical idleness. If these irregularities cause an annual loss of national income and product of some billions of dollars, an appreciable fraction takes the form of lower earning returns to property income receivers. Success in a thorough-going stabilization program would mean more stable and probably higher profits over the cycle as well as higher wages. Therefore, both labor and management have a mutual stake in ironing out irregularities in production and employment.

We have seen that the average take-home pay tends to be decreased by instability of employment in different industries. What may we infer about the profit rate in industries which are subject to the greatest fluctuations in activity? Can we expect that the effective maintenance of guaranteed wages would be at the expense of the profits now earned by variable industries?

To the extent that any wage or job guarantee induces, accompanies, or follows upon successful stabilization of production, the second question answers itself. If steady production at a high level tends to increase labor efficiency and to reduce expensive turn-over, the program may much more than pay for itself. But if we must assume that guaranteed wage income is maintained in industries that are still subject to irregularities of demand and production, the answer to the question of whether the burden will fall on profits is not so simple. It depends in part upon the answer

to the first question as to how profit rates have in the past accommodated themselves to differing degrees of instability.

If we select those industries with the greatest cyclical or seasonal fluctuations and compare their profit rates with steadier industries, there does not appear to be any strong relationship between profits and instability. For the period 1935-39, which includes a recession as well as years of expansion, the average profit rate of 10.1 percent for all durable goods hardly differs from the 9.8 percent for all nondurable goods. Automobiles, one of the most strongly cyclical and seasonal industries, has among the highest rates of profit, whereas iron and steel, also a cyclical industry, has rather low profit rates.¹²

If industries which had previously been stable were suddenly to become cyclically or seasonally irregular, then profits would immediately be affected adversely. Something like this probably happened as a result of the unexpectedly deep depression of 1929-33, profits in many lines being very hard hit. But by and large, unstable industries have a history of being unstable. When capital chooses between going into the canning industry and some other line, it does so with the expectation that supplies and operations will there be bunched into a relatively few months of the year. Similarly, an industry like baking is expected to be fairly stable, both seasonally and cyclically.

To the extent that these expectations are correct—and they certainly are not necessarily so—there is a tendency for profit rates to be equalized (over the cycle and year) by the competitive movement of capital between and among industries. That being the case, the residue of the economic burden of idleness that is not thrown upon the workers in the given industry—this residue is not borne by the industry's capital. Instead it is shifted forward and backward to workers and investors elsewhere.

In overcrowded lines of activity where rivalry is very keen and profits are chronically low, the cost of even customarily expected fluctuations in production may not be allowed for in price setting. Many of our industries with the greatest

¹² Unpublished study of Office of Price Administration, entitled "Return on Net Worth, Before and After Taxes, 1936-44, 2,500 Leading Industrial Corporations."

amplitude of seasonal fluctuation happen to meet this description at least in part. However, for the most part, the low profits experienced in these fields ought properly to be kept analytically separate from the fact of seasonality of operations. Were the same total level of demand to be spread evenly over the year or cycle, while at the same time the conditions of over-entry into the industry and past excessive investment were yet to prevail, we might still expect profits to be low. A real exception to this statement is provided by the case in which people are encouraged to overinvest their capital in an industry because of the appearance of high profits during the short-lived busy season. This would be the counterpart of a similar possibility in the labor field, where workers overcrowd an industry because of short-sighted concentration upon the transitory high hourly rates to be earned for a few months of the year or a few years of the cycle.

Other fields are to be found such as durable consumer goods and chain department stores where operations show a distinct seasonal and cyclical pattern but where profits are nonetheless fairly high. In many markets one or a few firms occupy a strategic position of dominance by virtue of efficiency of operation, advertising, research, trade marks, patents, and so forth. New firms are not able to come in and compete away the monopoly or quasi-monopoly returns of these concerns.

From the analysis of the last section, a few tentative hypotheses may be drawn as to the possible effect of introducing guaranteed wages upon the profit position of unstable industries. Depending upon the variability of the industry and upon the limitations placed upon the guarantee, we could expect profits to fall in the short run after the plans are first put into effect—unless indeed the plans induced an increase in efficiency. In the longer run, and to the extent that capital can be made mobile, capacity and output would gradually shrink in the more variable industries.

More and more the burden would then be shifted forward to the consumer through higher prices, or backward upon wage rates in general—not through actual pay cuts, perhaps, but through a slowing up of the rate of increase of real wage rates. Part of the burden might well fall upon monopoly profits. In fact the cut might be covered by increased efficiency.

Nevertheless the case should not be overstated. Even if profit rates were equalized over all industries in the long run, we could not conclude that profits would necessarily escape all the burden of the extra costs entailed by guaranteed wages. True, the rate of profit in the particular unstable industries would be relatively unaffected. This does not preclude the very real possibility that the “equilibrium rate of profit” would be lower under a regime of over-all guaranteed wages than under the present form of the wage contract where labor can be made a variable monetary cost. There is no reason why the historical proportion between labor and property income would necessarily be preserved in the face of so drastic an institutional change. In technical terms, the “imputed net productivity” of capital depends very much upon wage rates, collective bargaining, labor “productivity,” taxation and other cost conditions. Under guaranteed wages, we cannot tell with certainty whether equilibrium profit rates would rise or fall. Any possible effects upon profits would have further repercussions on consumption, saving, and investment propensities, as we shall see in chapter IV of this report.

Probably, as we have seen, workers now directly bear the major cost of instability. Also, it is clear that the portion which workers do not bear may in part be shifted off the shoulders of the employers directly concerned to consumers and to industry in general. But still there remains some element of cost to the industry directly involved. Is it not to the selfish advantage of the industry itself to regularize its activities by means of stabilization programs? The answer is—to some degree—yes. Doubtless industry is already pursuing many such policies; the observed degree of irregularity of operations in our economy is by no means the maximum conceivable.

Doubtless, too, much more remains to be done in this connection. Business management is far from omniscient. Custom, ignorance, and inertia play a role in preventing companies from actively undertaking policies which are to their own maximum long-run profit advantage. Often companies are not fully aware even of their own irregular pattern of operations; many devote far less attention to stabilization programs than to other aspects of sales promotion, product development and

research, quality control, and cost accounting. The pressure of management groups such as the American Management Association, the Chamber of Commerce, and the Committee for Economic Development, and the pressure of organized workers through collective bargaining, and of government and the public-at-large, is all to the good in spurring corporations on to studying the problem of further stabilization programs. Engineering and efficiency studies have time and again shown that the surface is as yet hardly scratched. When every corporation of any size has a major executive and sizeable staff working creatively upon this problem—then and only then can we expect even the self-interest of the corporation, to say nothing of the economy at large, to be well served.

We can expect that the obvious stabilization policies, which hold out immediate economies with little cost and no risks, have already been exhausted in large part. What is needed is for management to display with respect to thorough-going stabilization efforts the same venturesomeness and imagination that it displays in promoting a new product or in risking the construction of a new plant.

And yet, despite the above exhortation, there are good reasons to believe that under present commercial and financial institutional set-ups, the hard-boiled single enterprise has only a limited motive to pursue extensive stabilization policies. During the last 25 years, good will, effort, initiative, and intelligence have been applied again and again to the problem. Yet plan after plan for voluntary stabilization has petered out or become a casualty of business depression. With a loose labor market and wages a variable cost, irregular production is not always expensive production.

This condition may not last. While it would certainly be premature to conclude that the business cycle is a thing of the past, nevertheless, both public and private enterprise have learned much; and today there is widespread recognition and determination that we must do everything in our power to prevent such catastrophic declines in national income and production as characterized the slump which followed 1929.

In any event, the longer that high employment conditions are maintained, the greater will be the

immediate dollar-and-cents incentive to regularize any remaining instability of productive activities. Depression conditions in the labor market have left corporations with a heritage of personnel policies, which however appropriate they may have been in the years of labor surplus before the war, may prove extremely costly in a high-employment economy.

Let us take the automobile industry as a case in point. Suppose manufacturers bow down to the seasonal character of auto demand once the immediate postwar backlog of demand has been partially filled, and in consequence are able to provide only some 8 months' work to the average employee. What will the result be? Will workers be compelled to lay off for 4 months, living on unemployment-insurance benefits and previous savings, and borrowing, or on relief? Probably not, if jobs are really plentiful. Then, when auto production is again resumed, many will be called but few will answer. Large numbers of workers will have been attracted by job offers with other concerns. Any firm with unstable employment would have to raise wage rates and undertake costly recruitment policies to keep a suitable labor force.

During depressions the cost of labor turn-over to an employer consists primarily of the costs to be incurred in securing and training a new worker. In modern mechanized industry, where a premium is placed upon general intelligence, manual dexterity, and basic training in the use of nonspecialized machinery, it is not at all impossible that the expense of training new workers is a good deal less than would appear from many exaggerated accounts. After not many weeks, a worker transferred to a new department or hired for the first time, may be nearly as efficient as he is ever likely to be; especially since the novelty of a job often elicits an enthusiasm and zeal which wears off with continued experience. Possibly this explains why the alleged reduction of cost of labor turn-over has been so ineffective in the past as a spur to stabilization. But in a full-employment economy, every employer will be pitted against every other employer in an effort to secure more labor in a tight market. Labor laid off may

be lost forever. From any one firm's viewpoint, labor separations then tend to give rise to labor shortages rather than simply to labor turn-over.

This leads us to stress once more that production stabilization and the guaranteed wage involve much more than business cycle unemployment.

III. THE GUARANTEED WAGE IN A BROAD SECURITY PROGRAM

Substantial security of income or employment, or both, is everywhere more and more recognized as a primary goal of modern democratic societies. This goal cannot be achieved by any one method. In all modern societies many institutional arrangements, programs, and procedures have been adopted, designed to contribute to stability of income or employment. Among the most important of these are (a) a variety of social security measures and (b) various programs to stabilize employment in the individual firm and for the economy as a whole.

DIFFERENT PATTERNS OF JOB SECURITY

Employment contracts under modern conditions typically are terminable without notice or upon so short notice as to give virtually no security of tenure. Nevertheless a substantial proportion of modern workers feel fairly secure in their jobs. In many cases it may be assumed that employees of long standing regard their positions as more or less permanent. Such employees are not likely to fear dismissal for cause. In general, they are not likely to be greatly concerned about lay-offs, except in the case of wholly unforeseen catastrophes of a character which are not regarded as very probable. It appears true that human beings are prone to be unduly optimistic and to underestimate risks of a character which they are not in the habit of facing more or less continuously. By and large, employees of long standing probably experience a feeling of security greater than is in fact justified by the course of events.

Employees who feel a sense of security in their job by reason of long tenure are likely to underestimate the importance of unemployment insurance, and related measures, as means of ensuring some degree of income security. For these employees it is security and continuity of the job

The following chapters undertake to show the relationship between guaranteed wages and other programs; also, the direct relationship to the over-all level of aggregate demand and unemployment, and to the efficient use of resources in a high-employment economy.

already held that is really important, not the easing of transition to a new job.

But a large proportion of employees are not in this favored position. Typically their tenure of employment with any one firm is relatively brief. For many workers, a job is, even at best, a comparatively temporary thing. Lay-off or voluntary separation is a continually recurring experience. Workers who are accustomed to only short-period job tenure doubtless fall into different categories with respect to reemployment experience. Some, by reason of the character of their occupation, adaptability, resourcefulness, etc., expect easily and quickly to find new employment. In the transition to a new job, unemployment insurance plays an important role.

In bad times, however, reemployment, even for the alert worker, becomes difficult if not impossible. Unemployment insurance becomes then an important means of support, just as it is for those workers who encounter difficulty at any time in finding new work. It provides, however, only a fraction (usually 50 to 60 percent) of normal earnings, with maximum limits ranging from \$13 to \$28 per week; while the maximum duration of benefits runs for only 14 to 26 weeks. It can serve as an important stop-gap for seasonal and transitional unemployment under conditions in which opportunities for reemployment are reasonably good—that is, in a relatively buoyant labor market where aggregate demand is on a fairly satisfactory level. In addition, the dismissal wage can help to bridge the gap in the event of technological unemployment, consolidation of firms, or a secular decline in a firm's business.

A considerable proportion of the American labor force, even though at times laid off, does not typically change jobs. Such workers regard themselves as "attached to a firm" even though they experience frequent and fairly long periods of unemployment. Thus, in the automobile in-

dustry in the period of 1935-39, workers were employed on the average for only about 75 percent of full time.¹³

The table below gives a quantitative picture of the number of workers of different years' service with a large public utility system. In 1929, when jobs were plentiful, the turn-over of workers was very high. Consequently, the percentage of workers with less than 1, 2, or 5 years of service was relatively high. During the depression, the picture was changed greatly. Few workers had been recently hired, and the number "separating" from the company was relatively small. Workers with 5 years' service began to be the rule rather than the exception, so that even workers with high seniority rating would have faced lay-offs if further widespread contraction of operations had become necessary.

Percent of workers with varying lengths of service in a large utility system

Year	Percent of workers			Number of separations as a percent of average number of workers
	With 1 year or less	With 2 years or less	With 5 years or less	
1929.....	25	38	61	31
1932.....	1	2	33	10
1936.....	9	12	17	7
1938.....	2	10	22	7½
1941.....	19	26	36	12

In strongly organized industries, workers are less vulnerable than formerly to dismissal, or discharge "for cause." So long as times are good, union workers with seniority are also protected from lay-offs in a wide variety of industries where contraction of output is a gradual affair involving only the more recently acquired workers. There are other industries, however, where technology requires whole plants and units to be shut down when output is contracted. In such industries, even strong union organizations cannot protect workers with high seniority rating from being

¹³The average weekly hours of automobile workers for the 1935-39 period, using Bureau of Labor Statistics data weighted by the Bureau's employment indexes, were 36.1. These were the average weekly hours for employees working. Total labor force was estimated from numbers of employees reported to the Federal Bureau of Old-Age and Survivors Insurance, with a correction for inclusion of nonproduction workers. The automobile labor force appears to have averaged about 18 percent more than the average force at work, so that average weekly hours for the whole force averaged about 30.6.

intermittently laid off—even in years of fairly high business activity.

The demand for a guaranteed wage is likely to be strong in industries of this type. Such workers, to be sure, not infrequently take advantage of unemployment insurance and job opportunities offered elsewhere in the interim period of temporary unemployment. Yet a large proportion more or less regularly experience temporary unemployment each year, and await a return to their old job without obtaining, in the interim, work elsewhere. To repeat, it is particularly for workers of this character that the guaranteed wage plan makes a strong appeal. These workers are, in a sense, "attached to a firm," yet the number of days worked per year is low. The conditions of the industry prevent or make difficult a high ratio of days worked to working days in the year. If the firm could diversify its production so as to dovetail employment throughout the year, a high ratio of days worked to working days could be achieved. In view of the character of the modern labor contract, it is probable that most employers have not yet seriously tackled the job of giving steady employment to workers regularly attached to their firms. If the labor contract were on the guaranteed basis, these firms would be compelled to explore to the utmost ways and means of finding steady work for those "attached to their firm."

GUARANTEED WAGES AND STABILIZED EMPLOYMENT

Where unemployment is primarily a matter of seasonal fluctuations, and other types of work interruptions of a short-term character, the guaranteed wage plan seems to be peculiarly suitable as a device to help solve the problem of job security. If under such conditions the guaranteed wage became the rule for all competitors in an industry, more and more those competitors would survive who proved most resourceful in the development of stable, year-round employment. At first, doubtless, relatively little progress would be made and the guaranteed wage might prove to be a heavy burden on the industry. This might involve a rather drastic readjustment of prices or wage rates or both. Eventually, however, as more and more firms increasingly solved the problem, costs would be reduced. Accordingly prices could be lowered

again or wage rates raised, or both. The net social gain would be steady year-round employment for the workers and an enlarged real income for the community as a whole.

A LIMITED GUARANTEED WAGE

In what has been said above, the assumption is made that the guaranteed wage would be applied to all, or nearly all, the workers employed by the firm. But even firms with short-run irregularities in employment have a certain residue of workers who are continuously employed. If the concept of the guaranteed wage were applied only to these workers, the plan would become at once more feasible, but also would accomplish relatively little. Similarly, with respect to industries afflicted with cyclical unemployment, a guaranteed wage which involved only that residue of workers which a firm can reasonably expect to hold through even a deep and prolonged depression, would become highly practical, but correspondingly also of less value.

Nevertheless, even this limited concept deserves consideration. It would indeed not solve the problem of either income or job security. These difficult goals must be attacked from a great many angles. The guaranteed wage is only one among many approaches to the problem. Indeed, if too much were attempted by this method, other more promising methods might be seriously impaired. The guaranteed wage, we believe, does have its place as a part of a larger program. Even the minimum concept of the guaranteed wage referred to above could achieve something of substantial value. If each firm gave assured employment to that fraction of its peak employment which experience indicates to be feasible and practical, a formally recognized status of security might be given to an appreciable fraction of the entire labor force. This would, at any rate, be something to start with. The problem would then be sharply posed: if such a fraction of workers were protected under the guaranteed wage status, what could then be done (1) to provide in other ways (dismissal wages, unemployment insurance and over-all stabilization policies) as much security as is possible for the uncovered employees, and (2) to expand gradually the number coming under the guaranteed wage plan.

THREE ROADS TO JOB AND INCOME SECURITY

Comparison may usefully be made between (1) the guaranteed wage plan, (2) unemployment insurance, and (3) a full employment program. In making this comparison it will be helpful to assume that each measure is a part of a general pattern in which each reinforces and supplements the others as means to provide security for workers. Thus considered, what can each of these three approaches contribute to the problem of security?

The full employment program aims to provide security by ensuring a good market for labor services. The goal is adequate aggregate demand, so that workers can readily find and obtain jobs. This plan does not guarantee a job to any individual. It provides a favorable market in which he may seek a job. The mere fact that the aggregate demand for goods and services is sufficiently high to ensure a good market for labor services, will not prevent fluctuations in employment in seasonal industries. It will not prevent shifts taking place between industries and between regions. A man living in town X may not be able to get a job in his particular skilled occupation in town X; or anywhere if his skill has become obsolete, or his demands exorbitant. Aggregate over-all demand does mean, however, that job opportunities are in general plentiful throughout the Nation. A man cannot sit on his front porch and expect just the job he wants to come to him. But if he is alert and active, the market is favorable. Labor is in good demand throughout the country. There are many job opportunities from which one may choose. And retraining programs, employment offices, travel allowances, and adequate housing facilities (essential parts of a complete full employment program) should make the task of transfer to new jobs and other regions relatively easy.

Such in brief is the goal or function of a full employment plan for job security. It does not guarantee a job, and at best there will be unemployment. In particular there will be seasonal, technological, and transitional unemployment. The plan thus falls short of adequately meeting the problem of security. Something more is needed.

The unemployment insurance program aims primarily at a minimum of income security, and does not directly attack the problem of job security. The program assumes that workers will become unemployed for all sorts of reasons—seasonal fluctuations, fluctuations in the business cycle, changes in technology which throw people out of work, structural changes which adversely affect certain regions, shifts in population, foreign competition, etc. The program is not designed directly to remove any of these causes of unemployment. It is designed merely to ensure a temporary minimum income to workers who are out of a job. As a by-product, the program does indeed, it is now believed by most economists, make some contribution (if properly financed) toward the maintenance of aggregate demand. But at best its contribution to the maintenance of purchasing power is relatively limited, and its main function is to provide a minimum income to those out of work. To repeat, the program is designed to give minimum income security, not job security. The income received is not paid in return for work. The payment is made basically in accordance with the principle of partial income maintenance,¹⁴ not in accordance with the principle of productivity.

If now we extended unemployment insurance (industry or firm financed) far beyond the limits which are now actually applied in practice to the point of full coverage of wage income for the period of a year or perhaps a minimum of 40 weeks of the year, instead of only 50 or 60 percent of wages for 14 to 26 weeks, we should have arrived, at least in terms of the income receipts of the protected individuals, at the same point as the guaranteed annual wage. Under the guaranteed wage, of course, the worker not only receives a continuous income payment during the period for which the wage is guaranteed; he may also be subject to the call of the employer for the performance of work.

From one point of view the guaranteed wage can be looked upon as 100 percent unemployment insurance, for at least a limited time. But it is often more than that, especially where it involves

“guaranteed work” as well as income. It carries the principle of merit (or experience) rating to its ultimate degree; the whole burden of maintaining the worker is assumed by the employer. Any use he can make of the workers is all to the good since his labor costs go on anyway. Under the unemployment insurance plan, the worker is obligated, in return for income payments, merely to register at the public employment office and actively to seek work if it is available. If work is found, the insurance payments cease and wage payments begin. Under the guaranteed wage, wage payments continue with or without work, but the worker is under obligation to work whenever the employer so directs. And especially if the guaranteed wage is integrated with unemployment insurance, as we suggest, he will also be under obligation to seek work elsewhere.

The guaranteed wage plan, accordingly, as opposed to the principle of unemployment insurance, tends in the direction of bringing work to the worker in the employer's establishment. Unemployment insurance, through the unemployment exchanges, seeks, on the other hand, to send the worker to the job wherever it may be. This difference can, however, easily be exaggerated since an employer under the guaranteed wage also may seek to place his idle employees in jobs elsewhere and with other establishments.¹⁵

Nevertheless, the guaranteed wage tends rather more than unemployment insurance toward fixity of jobs in regions and establishments to which work must be brought. The maintenance of labor mobility is no easy matter; yet much could be done to keep productive resources fluid in reference to changes in technology and in demand. Employment offices, operated in conjunction with unemployment insurance, if effectively managed, aim to promote the movement of workers from old establishments and regions to new ones as dynamic changes in products and in wants arise. Under the guaranteed wage plan the main effort is to provide work for the worker on his old job or at least in the firm to which he is attached; under unemployment insurance the emphasis is placed upon connecting up workers and jobs in any firm offering suitable work, preferably in the

¹⁴ A rough calculation suggests that unemployment compensation covers less than a fifth, and possibly not much over a tenth, of the wage loss from all unemployment. The system is much more effective in compensating total unemployment wage loss in good times than in bad.

¹⁵ See our policy recommendation in chapter VI calling for an integration of unemployment insurance benefits and guaranteed wages.

region where the worker is located, but if not there then elsewhere, at least within reasonable limits.

To sum up, a full employment program is designed to maintain, within reasonable limits, adequate aggregate demand. Emphatically, it will not guarantee every worker a continuous job. It does no more than to ensure plentiful employment opportunities—a brisk demand for labor. And in order to achieve reasonably full and sustained employment, a fairly high degree of labor mobility is required. A full employment program must therefore include, as a part of the plan, retraining provisions, travel allowances, and adequate provision for working-class houses where jobs are available.

Nevertheless, at best, there will still be seasonal, technological, and transitional unemployment. A full employment program, therefore, leaves many workers unprotected unless supplemented by a well-developed scheme of unemployment insurance. Social security is therefore necessary, in order that at least a minimum income will be received by those workers who suffer the effects of the unavoidable unemployment which is a by-product of the manner in which production is carried on under modern conditions. This insurance of a minimum of income, since a job cannot continuously be guaranteed to everyone, is the right of all workers, and is so recognized in all modern democracies.

IV. GUARANTEED WAGES, OVER-ALL EFFECTIVE DEMAND, AND THE BUSINESS CYCLE

INTRODUCTION AND BRIEF SUMMARY

The subject matter of this chapter, the quantitative effects of guaranteed wages upon total demand and upon business cycle fluctuations, is intrinsically complex and can only be analyzed in rather technical terms. Perhaps it is for this reason that the voluminous literature on guaranteed wages scarcely scratches its surface. Nevertheless, no economic analysis of guaranteed wages could be complete without coming to grips with the question as to how effective such plans can be in reducing over-all unemployment and in moderating the business cycle.

For readers who are not interested in the technicalities of analysis, a few of our more important findings may be briefly sketched. However, to ap-

Within the framework of a full employment program, supplemented by unemployment insurance, a highly important function can be served by the guaranteed wage. There are already a substantial number of persons, including professional and salaried workers and some wage-earners, who have achieved a fair degree of job security, if not in a formal guaranteed wage, at least in its practical equivalent. This group could doubtless be enlarged even without a full employment program. Standing alone, however, without the protecting influence of a steady, brisk demand for labor, any widespread expansion of unlimited guaranteed wages might encounter serious difficulties. Within the pattern of a realizable high employment program of sustained aggregate demand, the guaranteed wage could be extended to include a fairly high proportion of workers in the labor force. For some firms or industries the number of weeks guaranteed might be 40, for others 45, and for others 50. The guaranteed wage, safeguarded in view of the risks involved and properly integrated with unemployment insurance,¹⁸ could play a significant role as a means of providing income security. Most important of all, however, is the task of securing continuing high levels of employment. Income security cannot take the place of steady productive employment.

praise their validity, there is no escape from the more detailed analysis which follows this section.

In this chapter we do not consider governmental programs of any kind. If the guaranteed wage were to be a governmentally financed program, that would be one thing; and the economic and political implications of such a plan would then need to be examined. But this is not our concern in this chapter. We consider here the economics of a privately financed guaranteed wage. How would a privately financed guaranteed wage, taken by itself, affect (a) the fluctuations of the business cycle, and (b) the level of effective demand, production and employment over the cycle. It is important, we repeat, for the reader to remember

¹⁸ The problem of integration is discussed in ch. VI.

that the problem before us is concerned exclusively with the economic effects of a privately financed guaranteed wage.

Those who concentrate upon the expansionary effects of guaranteed wage payments, to the neglect of how these payments are financed, come out with an exaggerated notion of the efficacy of wage guarantees to combat depression and unemployment.

It is not inconceivable that the guaranteed wage could be the means of inducing (by providing worker security and in other ways) a higher man-hour productivity. But there is no evidence from experience that increases in productivity, as such, tend to iron out the cycle or to raise the level of employment over the cycle. Increases in productivity are important from the standpoint of raising the standard of living, but not from the standpoint of eliminating the cycle. Guaranteed wage payments (whether they induce increased productivity or not) may, however, help to iron out the cycle if they are financed from reserves accumulated in good years and paid out in bad years; or they may, to some extent, raise the level of employment in the depression phase, through the redistribution of income when financed on a pay-as-you-go basis.

The fact that a guaranteed wage plan might more or less "pay for itself" is certainly significant. But only insofar as the plan redistributes income over time, or else redistributes income between economic groups, will it have any effect either on the stabilization of employment or in raising the level of employment. Our tentative conclusion is that the guaranteed wage, by itself, is not likely to prove very effective either as a means of stabilizing the cycle or of lifting the level of employment over the cycle, although the guaranteed wage may be partially effective in regularizing seasonal employment.

With respect to the redistribution of income, nobody can say just what percentage of the financial costs of guaranteed-wage plans will fall on corporate stockholders rather than on consumers or wage earners. Except to the extent that the costs fall upon net corporate savings (without affecting dividends or interest outlay, or net corporate outlays on plant, equipment, or inventories), guaranteed wages may be regarded as a form of personal income redistribution. Such a

redistribution may be highly desirable on social grounds. But the available statistical data showing (a) how people in different income classes allocate their extra dollars between saving and consumption expenditure, and (b) the relatively small proportion of the total national income flowing to the high-income groups, suggest that such redistributions are of somewhat limited quantitative significance in raising the level of over-all purchasing power.

Apart from such personal redistribution and its relatively limited effect, we conclude that in periods when net investment outlays for the economy as a whole are deficient, causing a decline in employment and in business profits, the guaranteed wage may, indeed, for a time maintain consumption expenditure. For this to be true in these circumstances, the payments would have to be financed from accumulated business reserves previously set aside to cover guaranteed-wage payments in the subsequent depression, or else from current undistributed profits and depreciation charges not invested in plant, equipment, or inventories. Under the assumptions made (apart from redistribution of personal income via lower wages or higher prices), these would be the only methods of finance, government support being ruled out. But the amount of guaranteed wages that could be financed from depression business profits and surplus would be quite limited, even though no account were taken of possible unfavorable effects on the economy which such losses might entail. And if the amounts set aside in reserves in boom years are large enough to cover the risk involved, new problems are encountered which are rather serious. While moderate reserve accumulations could help to iron out the cycle, large reserves (as we shall see in the discussion which follows) might seriously intensify the savings-investment problem. Thus, either way, there are, we believe, rather severe limits to the extent to which the guaranteed wage can iron out the cycle or raise the general level of employment over the cycle.

We do not wish to overstate or overemphasize these somewhat pessimistic conclusions. Indeed, in the discussion that follows they are qualified at many points. Nonetheless, we must once again stress the limitations of the guaranteed wage as a remedy for the business cycle, and emphasize

the need for a well-rounded full-employment program including both public and private policies designed to keep our economy stable at a high and growing level of real income.

JOBS AND MARKETS

Let us begin our detailed technical analysis by considering the simple view that guaranteed wages and employment maintain incomes and jobs, that steady incomes mean steady sales of business, which in turn give rise to high and steady employment. In short, jobs make markets, markets make jobs, and so forth, indefinitely. According to this view, a serious depression like that of the early thirties is nothing but a vicious circle; for one reason or another, the public and business has become frightened enough to contract spending; this initial contraction of spending has resulted in reduced levels of business sales and consumers' incomes; and this situation tends to perpetuate itself at low levels of national income and high levels of unemployment.

Some such theory as this is widely held both by many conservatives and many liberals. The latter say, "All we have to do to cure such a situation is to prime the pump for a little while. Once the system gets back on its feet the Government pump priming can stop because the new circular flow of income-sales will be able to maintain itself at high levels of employment."

We believe it fair to say that the majority of modern economic experts reject this view just as they reject its oversimple conservative version which goes something like the following: "Any depression can be temporary if businessmen and the public will keep their heads and realize that prosperity is just around the corner. The Government should steer clear of the whole situation, except for a little necessary emergency action. Then, if people will only act upon the assumption that conditions are fundamentally all right, and if they will only 'buy now' instead of later, the corner of prosperity can be permanently turned."

The majority of modern economists, let us repeat, do not believe that such a theory squares with the monetary, statistical, and historical evidence accumulated by students of the business cycle. They find themselves forced to reject the assumption that, like Gilbert and Sullivan's all-powerful Mikado (all we have to do is declare jobs

guaranteed, and ordering that this be done is just as good as if it were done.

We do not deny that there is a germ of truth in the above viewpoint: Pessimism and reductions in spending do involve some elements of the vicious circle character, and the descent into a depression is of a cumulative, self-aggravating nature. But fundamental facts of economic life are ignored by this overly simplified theory. The fact is that people do not spend all their income on consumption goods and services. Retail sales by business to the public constitute only a part of the total national income produced at high levels of employment. Around one-eighth of national income,¹⁷ when employment is high, has throughout our history of the last half century gone into the form of investment goods or net capital formation. And it is capital formation that basically represents the difference between prosperity and depression. All the available statistical evidence shows conclusively that capital goods and durable consumer goods experience the greatest amplitude of variation over the business cycle. Moreover, this variation spreads throughout the economy, in particular affecting the volume of nondurable consumption expenditures and replacement capital expenditures, and so it has a magnified effect on aggregate outlays, income and employment.

For the purpose of this report, it is not necessary to enter upon the controversy as to just what the long-run prospects for investment are, or just what in the past have been the primary causes of investment fluctuations. It is enough to record the fairly substantial agreement of economists that among the important factors affecting investment behavior are scientific inventions, technological innovations, population movements and growth; changes in tastes; relations between different elements in the price, cost and wage structure; interest rates and availability of capital; investor psychology and businessmen's expectations; attitude, legislative acts and policies of government; governmental public works and public development projects; and so forth.

Now it is not at all clear how much, if at all, the guaranteeing of wages as such would affect

¹⁷ If one preferred to relate gross investment to gross national product, the ratio of investment to national product would be far higher.

the sum total of these factors in a manner favorable to the maintenance of the high levels of total outlays necessary for full employment—if, without guaranteed wages, otherwise adequate demand were inadequate. It is not even as yet clear in what direction or to what degree the over-all balance of saving and investment would be affected by the widespread adoption of the guaranteed wage.

WILL GUARANTEED WAGES STABILIZE CONSUMPTION?

But cannot the following limited case be made for guaranteed wages: Would not the widespread adoption of such plans at least succeed in stabilizing consumption, with the effect that fluctuations in national income would then be confined to the relatively small sector of the economy—the capital-goods industries? Also, would not the successful maintenance of consumption moderate, at least in the short run, some of the wide swings of investment—those dependent upon the level of current business sales? Finally, would guaranteed wages raise the total level of consumption over the cycle, and so also lift the average level of investment?

These are separate but related questions. The answer to the first is fundamental and prepares the way to an answer to the others. If it can be shown that guaranteed wages would stabilize the level of consumption, much (though far from enough) will indeed have been proved. For under the present system of wage and job tenure, fluctuations in the relatively minor (say, one-eighth) part of our economy concerned with net investment give rise to “multiplied and amplified” fluctuations in consumption as well. Thus if full employment net national income in the postwar were about \$160 billion, and net investment were to drop away to nothing, the loss to the economy would not simply be around one-eighth of national income—or some \$20 odd billion.¹⁸ As workers and property-owners in the capital-goods industries lost income and contracted their consumption ex-

penditure, there would be set in motion a chain of cumulative contractions in income which might be two or three times as large as the initial decline in investment expenditures. In short, a relatively small failure in investment outlay tends to result, under our present system, in considerably larger changes in total income, because of the “secondary” contraction of jobs and consumption expenditure.

If the consumption outlays could smoothly and instantly rise whenever investment declines, we should not experience any general decline in aggregate demand in a prolonged depression. But this is simply not possible. Individuals will not suddenly change long-established customs and habits with respect to the disposition of their incomes between consumption and saving merely because, from the social standpoint, the turn in the cycle calls for an increase in spending out of a reduced income. Thus an offsetting increase in consumption cannot and does not occur. Worse than that, consumption actually falls off when investment declines, since unemployment and declining business prospects induce a decline in private spending patterns.

This induced decline in consumption could indeed be avoided if, by some “magic,” substitute income payments could be found to take the place of the declining capital-goods pay rolls. These substitute income payments, since they do not correspond to any productive output, would be in the nature of “transfer” payments. Ideally, they might be financed out of the stream of saving which always characterizes full-employment income levels. By this “magical operation” the income flow would be maintained even though net investment should fall to zero and cause considerable primary unemployment. In short, the savings stream, instead of financing new investment, would be transferred to idle workers and the owners of idle resources. Total consumption would thereby be maintained.

Perhaps a bald statement of the problem in these terms may help to reveal the lack of realism involved in over-simplified assumptions with respect to the maintenance of consumption and employment. Unfortunately, economic analysis of guaranteed wages does not seem to substantiate the claim that this device would, as a first approximation, necessarily tend to maintain consumption for

¹⁸ Even when gross investment is positive in the sense that some capital goods are being produced, net investment may well be negative if the total value of capital goods output is less than the amount of capital goods being used up. In view of the fact that gross and net investment differ only by the fairly constant magnitude of capital consumption or depreciation, absolute changes in gross and net investment can be used interchangeably for purposes of business cycle analysis.

any appreciable period of time at the appropriate full employment levels, i. e., roughly at seven-eighths¹⁹ of the full-employment level of net national income.

To illustrate the point, let us consider the case where investment opportunities are only such as to replace existing capital. It is not enough then for all employers in the consumption goods industries to undertake guaranteed wage plans. Rather, all employers—in both consumption and capital-goods industries—must carry through with such guarantees. Total consumption and saving typically depends upon total national income (at least as a first approximation) in such a way that in order to ensure a volume of consumption equal to seven-eighths of full employment national income, the actual amount of national income accruing to people must be eight-eighths of the full employment level. If investment opportunities are for the moment moribund, where is the “missing eighth” to come from?²⁰

If investment opportunities are temporarily in large part saturated—plant and equipment having been built up during the preceding boom period to about as far as prevailing technology justifies, and if houses, hotels, office and commercial buildings have been constructed to the extent (and in fact often farther than is) justified by growth and the requirements of prevailing standards—then investment outlays will decline even though consumption expenditures could, in some manner, be stabilized at the boom level. And, if this is so—and the experience of business cycles for 75 years supports this analysis—then the producers of capital goods will not be able to continue to operate at levels adequate to maintain their pay rolls or to pay guaranteed wages to their employees. And when the market for the capital-goods industries drops out, then a large fraction of the market for consumers goods will also disappear. This is the situation which cannot be waived by the over-simplified theory which holds that jobs provide pay rolls, pay rolls provide markets, and

¹⁹ This includes local community and other governmental services (education, for example) financed from personal taxes. In modern communities this is one important way in which consumers spend their incomes.

²⁰ All through this analysis we are assuming, it is to be remembered, that the guaranteed wage is financed by private industry and not by the Government. If consumption were automatically maintained by Government outlay, the case would be entirely different.

markets in turn provide jobs. The overly simplified version did indeed fit reasonably well into a primitive economy where capital goods played no significant role. And it is for this reason, basically, that primitive economies, while poor, nonetheless rarely suffer from unemployment.

If the “missing eighth” continues to be lacking, how can consumer outlay be kept up to the maximum level reached in the boom? This is the crucial question: by what method of financing is the wage guarantee to be maintained? And yet throughout most of the literature on guaranteed wages, this whole problem is either neglected completely or passed over lightly. To remedy this defect, the rest of our chapter will analyze in some detail the effects of different methods of finance—pay-as-you-go and reserve.

If a guaranteed wage plan keeps a man from being laid off and makes possible the maintenance of his income, then it is not unreasonable to expect that it will result in an increase in his consumption purchases over what they would otherwise have been in the absence of such a plan. So far, so good—but we have not carried the analysis very far if we stop with the expansionary effect of guaranteed wage expenditure.

If the Government were paying the bill, not out of tax revenues, but by the printing of crisp new dollars or by loan-financing, that would be one thing. The discussion of the implication of such a policy, together with relevant comparisons with other antidepression programs (which might be more justifiable and promising), would take us very far afield and far beyond the scope of our present study. When only private finance is involved, it is necessary to give attention to some important factors which offset the favorable income maintenance effects, as we shall see.

BUSINESS CYCLE STABILIZATION AND PRODUCTION EFFICIENCIES RESULTING FROM GUARANTEED WAGES

Before entering upon a discussion of reserve and pay-as-you-go financing, we must digress to consider a point which is given considerable weight in the literature of guaranteed wage plans. Such programs, it is claimed, often more than pay for themselves because of the production efficiencies resulting from lower labor turn-over, greater

labor efficiency, and fuller utilization of capital. Especially in connection with the ironing out of seasonal and irregular fluctuations is this likely to be the case. If the general business cycle is not brought under control, it is more doubtful that the increase in efficiency will be nearly as great as the costs of maintaining income payments in the face of conditions which fluctuate independently of the firm's control.

However, in any case there may be some savings in cost to offset against the expense of guaranteed wages. The question will inevitably be raised, therefore, as to whether widespread guaranteeing of wages cannot by itself iron out the business cycle, or at least maintain income steady throughout the cycle, and do this without any net cost to the business community. The remaining paragraphs in this section aim to throw light on these questions and clear the ground for the analysis of reserve and pay-as-you-go financing.

If the savings in cost through increase in efficiency were very important, the individual employer would be helped to finance his guaranteed wage, but it would not necessarily solve the problem of unemployment for the economy as a whole. Increased labor productivity, meaning among other things that less employment is provided by a given volume of output, would raise the same problems of unemployment and purchasing power as technological inventions. About this there is a large literature, the consideration of which would lead us rather far beyond our immediate task. The mere reference to this literature is, however, sufficient to show that in the absence of a positive full employment program, it cannot safely be assumed that technological and other developments designed to increase worker productivity, would automatically increase and stabilize aggregate employment and aggregate demand in the economy as a whole.

If the guaranteed wage could induce an increase in productivity sufficient to cover its cost, this would be a great social gain leading, as with all advances in efficiency, to a potentially higher real income; and in an expanding economy in which technologically displaced labor quickly became reabsorbed, this potential would actually be realized. But the mere fact that a guaranteed wage plan or an invention "pays for itself," will not alone tend to reduce the fluctuations of the cycle.

There is no evidence from past experience (nor could it be expected on grounds of general analysis) that gains in productivity tend to have this effect.

Nevertheless, it is possible for the cost-savings of guaranteed wages to be used in such a way as to promote stability over the cycle—that is, by investing the financial cost-savings in good times into a reserve fund out of which payments are made in depression. This leads us into the whole problem of pay-as-you-go and reserve financing. After we have analyzed these devices, we shall return to efficiency cost-savings.²¹

TWO METHODS OF FINANCE

There are two methods by which widespread guaranteed wage plans could be privately financed. First, there might be some sort of reserve plan, according to which funds would be collected during the expansionist boom phase of the business cycle; and then during the contractionist depression phase of the cycle, these funds would be dispersed in the form of guaranteed wages. This same reserve principle is already in effect in connection with our Federal and State unemployment compensation program. The best case could be made for the anticyclical reserve method of financing if our economic system could be regarded as suffering only from cyclical swings above and below some "normal high-employment" level.

The second general method of financing guaranteed wages, is that of so-called pay-as-you-go. In contrast to the anticyclical reserve plan, in any given year the costs of guaranteed wages would be approximately balanced by current charges against sales or business gross income. Such a plan would involve relatively small payments in the boom years and therefore relatively small costs. In depression years, however, the payments would be large and the redistribution of current income would be considerable. The question to which we wish the answer is how much the payment of currently financed guaranteed wages might so redistribute income as to raise the level of consumption expenditures (or in more technical language the consumption function) and thus increase total aggregate outlay beyond what it other-

²¹ See below, footnote 26, p. 445.

wise would have been in the depression period. How would the cost be distributed between business net savings, wages, and consumer prices?

PAY-AS-YOU-GO FINANCE

Except for the earlier discussion of any possible induced increases in productivity, pay-as-you-go financing necessarily involves a process of redistribution of income between the various claimants to the national income—a redistribution which would fall mainly in the depression phase when large guaranteed wage payments would be made.

How such a redistribution affects aggregate demand is one of the most difficult questions in the whole field of economic analysis. At the present time, there does not exist sufficient theoretical and factual knowledge to permit a confident or precise answer. It involves the same perplexing problem as that of the incidence of the taxes raised to finance our whole social security program; or for that matter, of the incidence of corporate and business taxes in general.

As we have already noted, we assume that any increase in productivity induced by the guaranteed wage has already had its effect in total real income. The problem to which we address ourselves, therefore, is the redistribution effect of the guaranteed wage. Three extreme positions can be stated, with the truth probably lying somewhere in between: (1) The cost of guaranteed wages is borne completely by profit-receivers through reduced earnings of their properties; (2) the cost is shifted forward completely to consumers; (3) the cost is shifted back onto workers, who lose in wage rates what they gain in steadier income.

A survey of the literature on social security taxation would show widespread doubt that most of the increase in pay-roll costs could, except in the shortest run, be at the expense of corporate profits. Economists who have written on this subject seem rather to incline to the belief that the primary incidence would be on wages or on consumer goods prices. We would be rash to attempt a pronouncement on this difficult quantitative question, since not even the two of us would be in perfect agreement as to our rough guesses.

In depression when profits are already low or negative, the heavy extra costs of guaranteed wages are perhaps even less likely to fall in large part on capital. This conclusion is reinforced

when we remember that guaranteed wages are to be superimposed on a system of developed collective bargaining, where already labor is attempting to keep wages high and is already taking some advantage of management's ability to pay.

But let us first, for the sake of the argument, suppose that the cost of guaranteed wages does fall largely on profits. Then wage income will be larger, and dividends smaller. Since the bulk of dividends does not go to poor widows and orphans, there will probably be some favorable effect upon the propensity to consume. But the extent of this should not be exaggerated. The difference between the average propensity to consume²² (and to save) of the rich and poor is known to be very great. But the available evidence from governmental family budget studies seems to suggest that the marginal propensities to consume (and save)—and it is only these which are relevant—differ less sharply between rich and poor than do the average propensities. Dollars redistributed from wealthier common stockholders to workers add something to total consumption purchases, but less than is usually supposed. Nevertheless, to the extent that such a transfer is feasible consumption is thereby increased.

Not all corporate profits are paid out in dividends. Some go to that other silent partner of business enterprise, the government. Conceivably a shift from profits to wages might lower tax revenue and, other things being equal, contribute to larger depression loan financing and so to a slightly higher level of over-all expenditure; in other words to a slightly higher level of effective demand. It should, however, not be hard to find other more obvious ways of expansion if depression and unemployment call for expansionary fiscal policies.

A considerable part of profits goes into net corporate saving, representing undistributed profits or additions to earned surplus. Part of the increase in guaranteed pay rolls might be expected to come out of such net corporate saving. (This is true even in deep depression, when net corporate saving may be negative if dividends are being paid out in excess of current earnings; because of guaranteed wages the figure might become

²² "Average propensity" refers to the proportion of income consumed (and saved). "Marginal propensity" refers to the proportion of any small additional increment of income which is consumed (and saved).

algebraically more negative.) An increase in the payment of wages at the expense of corporate net saving would, taken by itself, tend to raise the level of total effective demand. But this conclusion would be true only on the assumption that there would not at the same time be adverse effects upon the corporation's inducement to invest.

In time of deep depression, most firms do not even replace much of their depreciating equipment. Yet they still, on their income statements, include charges to depreciation reserves as an item of cost to be subtracted from gross earnings in arriving at net profit. But these depreciation charges are expenses that, at the moment, involve no outlay. It would therefore be wrong to conclude that a firm which was suffering business losses was necessarily flooding the community with purchasing power. A more meaningful measure of a firm's expansionary or contractionist influence, taking all factors into account, would be the difference between its gross investment expenditures (including replacement outlays) and its gross saving (including depreciation); or, what comes to the same thing, the difference between its net investment and its net saving.

With net and gross investment already cut to the bone, in a period of depression a further reduction in earnings (and net saving) might not have any very significant effect upon net investment. But in the first years of recovery from a depression, or during the first years of descent into depression, there might be some counterbalancing adverse effects upon investment—although not necessarily dollar for dollar. These adverse effects might arise *ex post* simply because in an imperfect capital market many firms must depend upon their own funds for their investment outlays.

Probably more important would be the effects on expectations aroused—the adverse effects upon investment decisions at all phases of the cycle. During the boom, businessmen will be somewhat wary of undertaking certain doubtful marginal investments if they expect to be unable to cut their pay roll when times become bad. The harmful total effects upon the average level of net investment over the whole business cycle could conceivably be greater than the quantitative reduction in net business saving. Or less. No one can say.

We may sum up the case usually considered most conducive to an expansionary effect of guaranteed wages—where the costs fall completely on profits—by saying that stimulus to the level of purchasing power and effective demand is of somewhat doubtful quantitative magnitude over the business cycle as a whole. In depression times, the quantitative effects may be somewhat more important, but still should not be exaggerated.

Let us turn now, more briefly, to the more realistic case where a considerable part of the cost of guaranteed wages is assumed to fall on wages or upon the consumer's real income. If only seasonal or short rhythms of particular industries are being considered against the background of a full-employment society, such a method of meeting the costs may lead to a more nearly optimal system of pricing and use of economic resources. But from the standpoint of business cycle fluctuations, such a method of bearing the costs of guaranteed wages is fairly neutral in its over-all effects upon production and (real) effective demand.

If the cost falls upon wages or raises consumer goods prices, then income is being shared by those who are employed with those workers who would be without pay if it were not for the guaranteed wage. If such benefited workers are not already in high-paid industries and do not already have high current incomes (apart from the guaranteed wage) this whole process may involve some redistribution of income from average income receivers to those who are more needy. Just as with schemes for sharing work through reduced hours, this redistribution might result in some slight increase in the propensity to consume for the community as a whole. However, the point made earlier concerning the smaller difference between marginal propensities of different income classes would apply here with even greater force—since the difference between incomes is in this case relatively small.

The guaranteed wage would amount, in these circumstances, to a sharing of the income between those productively employed and those unemployed. In other words, those who are earning incomes at productive employment would be defraying the cost of the guaranteed wages. This is all the more true in view of the fact that under depressed conditions, profits could cover no appre-

cial part of the cost. Thus, the guaranteed wage, under these circumstances, would in fact be a "share-the-income" program. In place of a "share-the-work" plan, we would have a "share-the-income" plan. There would occur a shift of income among the wage-earner and consumer groups with no sizable effect upon the aggregate propensity to consume.

We may conclude, therefore, that a pay-as-you-go financing of guaranteed wages which does not fall on profits would result in little change in the level of income determination at the different phases of the business cycle. With real investment fluctuating over the cycle, real total consumption (all groups in the economy considered) would not remain stable, and real income would still fluctuate more than the absolute variation in net investment. Only to the extent that the cost can be saddled on to corporate profits, and more specifically upon corporate saving and not upon investment, will the guaranteed wage plans have any appreciable expansionary effect upon the level of over-all production and employment.

This does not quite exhaust the analysis of guaranteed wage financing on the total level of effective demand. As yet no mention has been made of the possibility that the enhanced security engendered by guarantee plans might cause workers to save less over the cycle, and to purchase with their savings more durable goods such as autos and houses. This is a possibility, and to the extent that it is effective, it would work toward some strengthening of the average level of effective demand.

Can a similar case be made out for the proposition that the guarantee device will cause employers to cast about for new productive activities and thereby raise the average level of employment? As far as a single concern is concerned, there may be something in this. If a locomotive or other capital-goods producer were to take on a consumers-goods line, such as breakfast food, he would no doubt smooth out the variation of his employment and production. But for the economy as a whole, little or nothing has been gained. The average income elasticity of demand and the over-all fluctuations in income are the same as before. Similarly, if an auto company, to make work for its own employees, cancels subcontracts with suppliers and begins to make its own parts, there is no over-all gain. If the beer industry, by heavy

advertising, gains at the expense of the bakery or confectionery trade, the over-all situation is the same. Only too often, the devices which seem to stabilize one concern's production are at the cost of somebody else's destabilization.

The only true exceptions, from a business cycle point of view, are policies which involve additional net investment for the community as a whole, or an expansion of consumption standards. "Producing for stock" is one stabilization device frequently mentioned by writers on guaranteed wages. Such a policy does involve net investment. How important can this factor be over the business cycle? The answer is somewhat discouraging, except for brief cycles. Production for stock might in 1930 have kept employment from slipping off as rapidly as it did. But such positive net investment in inventories is only too likely to result subsequently in commensurate disinvestment, making 1932 and 1933 even more depressed. A brief recession in business believed to be temporary might be bridged by this device. But a sharp inventory recession of the 1921 or 1938 type is likely to be accompanied by so much price uncertainty as to render this device relatively ineffective.

We must also not lose sight of the fact that many of the policies of businessmen that lead to larger total investment and employment do not give rise to much employment within their own plants. When railroads order new equipment, the extra jobs are not provided for railway labor. When a merchant or manufacturer "buys for stock" the task of guaranteeing jobs is eased for his suppliers but not for himself. It is true that he is somebody else's supplier, and that if all together pursue expansionist policies, all together may benefit. But it is not less true that anyone who holds back will also benefit from the expansion of the others; and it is somewhat Utopian to rely upon collusive decision-making by business as a body or upon altruistic social planning by isolated businesses.

The figures of seven-eighths consumption and one-eighth saving are given by way of illustration. They should not be interpreted literally, especially since in many downswings of the business cycle, autonomous net investment (caused by advances in technique and the like) will not disappear completely. Less than one-eighth of the full employment income level would then have to be made

up by guaranteed wage programs in order to keep total consumption stable.

There is also the further possibility that some appreciable part of net investment expenditure is not "autonomous" but is "induced" by, or is dependent on, the level of consumption or income. According to this type of argument, if guaranteed wage plans succeeded in keeping consumption at a higher level, then an appreciable amount of net investment would be induced (over what there would otherwise have been).²³

The weakness in this argument stems from the fact that a given stationary level of national income, no matter how high it is, cannot on balance be supposed to include any continuing net—as distinct from gross or replacement—investment. It is only the change in the level of income that induces net investment. When the stock of capital has become adjusted to any new level of income, no matter how high, net investment would again disappear²⁴—in the absence of technological changes and interest rate variations.

These rather long-run considerations will not seem decisive to the adherent of guaranteed wages as a business cycle cure. He will ask, "Isn't the business cycle a short-run phenomenon? Would not the maintenance of consumption lead to induced investment (over what it would otherwise have been) for at least the few years that a depression usually lasts?"

The answer to both of these questions may well be in the affirmative. But this does not mean that the temporary, once-and-for-all, induced investment effects of consumption maintenance can be regarded as raising the average level of demand and employment over the whole cycle. What is

²³ In technical terms, some economists would assume a "marginal propensity to invest" (out of income) as well as a marginal propensity to consume. This would tend to increase the "multiplier" effects of a given increase or decline (as the case may be) in autonomous investment or autonomous consumption. But so long as the two marginal propensities add up to less than one, then guaranteed wage plans will incur some over-all losses (payments for idle labor) whenever autonomous investment declines. However, those writers who assume large marginal propensities to invest and large multipliers, seem to imply that the historical changes in autonomous investment (the "multiplicands") were correspondingly smaller—in order to lead to the same observed fluctuations in total national incomes. Therefore, to such writers the "losses" resulting from guaranteed wage plans would tend to be correspondingly smaller.

²⁴ This situation means that there are no changes in technology involving new processes of production or new products for consumption. Changes in methods of production or in products would often require new autonomous investment, which would cause a rise in national income.

gained in investment during the depression is likely to be at the expense of investment during subsequent periods. By virtue of induced investment effects, guaranteed wage plans may have some stabilizing effects on the cycle—by expanding depression demand at the expense of the following boom-time demand. In this it resembles reserve financing, which we are about to discuss, with the difference that reserve financing usually fills in the trough of depression at the expense of the previous rather than the subsequent peak. But neither method is likely to expand demand appreciably over the cycle, unless Government loan financing or private corporation net savings are used to finance the guaranteed wage plans. Moreover, as we have seen, any favorable induced investment effects must be set against the unfavorable effects upon net investment and venture capital resulting from the recognition by potential risk-takers that guaranteed wage plans are likely to increase their costs and risks.

One final point favorable to the guaranteed wage. Over time, the consumption standards of people increase as people get used to higher levels of living. Any success achieved in maintaining high real incomes tends to breed further success. Unlike induced investment effects, "induced consumption" effects may be permanent rather than transient or once-and-for-all.

Once employment is guaranteed, labor becomes in the nature of an overhead cost rather than a variable cost. We should at least explore the possibility that this might lead to a pricing policy over the cycle which would make for greater stability of production. The beginner in economic theory is taught that really fixed costs should, at least in the short-run, be disregarded in output decisions and price formation; any business should not be refused which can at least earn something more than variable costs. If a large part of labor is no longer a variable cost, this might permit downward flexibility of prices to rather low levels.

In more advanced courses in economic theory (particularly those dealing with so-called "administered" prices and monopolistic competition) we are taught that "full" costs (including both overhead and variable costs) actually have an important influence on price formation, and this more sophisticated analysis appears to be in line with business practice and business opinion. In all like-

lihood, this pattern of "full-cost pricing" tends to characterize those semi-monopoly fields where industry is likely to guarantee wages. Therefore, it is something of an academic exercise to investigate the effect of flexible downward prices which abstractly might be related to the conversion of labor costs from a variable to a fixed cost.

Twenty years ago most economists would probably have considered such downward price flexibility a highly effective way of meeting depression. Today we are not so sure. The modern economy (given our present-day institutions) does not seem to go through price deflation painlessly or easily. Still there is this to be said for the kind of downward price flexibility referred to above in connection with the guaranteed wage. Such price reductions would not, it is assumed, be accompanied by wage reductions or any substantial decline in worker income, so that one of the worst aspects of a deflationary spiral would not be present. Still, increasingly it is the modern viewpoint that the price elasticity of demand is much lower in depression periods than used to be thought the case. Consequently, we should think it unwise to attach too great quantitative importance to the phenomenon under discussion even if it were likely—which it is not—that prices will show the proper cyclical flexibility rather than perverse flexibility.

RESERVE FINANCING

We must now analyze the possible effects of reserve financing. This method has most significance, and is most likely to be resorted to, in a society subject to pronounced cyclical swings. If, on the contrary, employment is reasonably stable, whether at a high level with low unemployment or at a relatively unsatisfactory level with chronic unemployment, one year is very much like another, so that there can be little shifting of the financial burden over time.

A gradual and experimental introduction and extension of the guaranteed wage plan might be financed in part on a self-liquidating basis. A gradual expansion of the program as experience justified might be accompanied by cost reductions which could "carry" the reserve plan without resort to higher prices or wages lower than could otherwise be paid. On this basis, it is likely, however, that progress toward the guaranteed wage

would be slow and would probably be largely restricted to firms whose employment experience is in any event favorable. If anything substantial were going to be achieved, it is probable that there could be no escape from a program involving, for the great majority of firms, the accumulation of reserves financed out of profits, wages, or higher prices. Without substantial reserves, the program would be discredited by a wave of defaults at the first onslaught of any considerable volume of mass unemployment.

An examination of the experience of various firms in the 1929–34 depression reveals how costly different guaranteed wage plans might have been. The high employment commitments of the late 1920's would have entailed heavy cost outlays all through the early and middle 1930's. If guaranteed wages had then been in existence, in a real economic and accounting sense, the men necessary to produce the high 1929 outputs would frequently have cost the companies in the thirties more than the total wages actually paid out to them at that time. Prudent bookkeeping would have suggested that this expense be recognized in 1929 as part of the cost of that year's output, and that funds be set aside to meet this contingent, but nonetheless necessary, deferred expense.

Accordingly, if we mean by a guaranteed wage program something more than a cautious and tentative introduction by a few firms with highly favorable employment experience, we must envisage a substantial program of financing—in other words, the accumulation of large guaranteed wage reserve funds. Now it is just this problem which we need to face in assessing the feasibility of the guaranteed wage plan, unsupported by governmental financial assistance. How would the accumulation of large guaranteed wage reserves affect the functioning of the economy?

An analysis of the impact of the guaranteed wage system (financed on the reserve basis) upon the flow of income and expenditure involves a consideration of the manner in which such a program withdraws funds from the income stream on the one hand, and pours funds into the income stream on the other. If we envisage a highly fluctuating society, and if we concentrate attention for the moment exclusively on cyclical unemployment, it follows that a guaranteed wage reserve plan will, for the economy as a whole, withdraw funds

from the income stream in boom years, and pour back approximately equivalent funds in the depression years. The same problem of "incidence" of the costs arises here as under pay-as-you-go; but the timing is different.

If we assume that the annual charges to the reserves are financed largely from higher consumer prices or lower wages, it follows that the level of consumer expenditure would be less than otherwise in the boom years, and higher than otherwise in the depression years. The "reserve method" lops off the boom and fills in the valley of depression. It is a method of redistributing expenditures over the time span of the cycle. The reduction of expenditures in the boom period might reduce employment, or it might merely have the effect of holding down price inflation.

In technical terms, the accumulation of reserves during prosperous periods tends to exert a deflationist influence at that time by reducing the effective propensity to consume and increasing "average thriftiness" or the effective propensity to save. The spending of the reserves in the depression period exercises an expansionist effect by raising the effective propensity to consume at that time.

Taken as a package, this double-barreled program is socially desirable. But if the period of so-called prosperity is like that of 1936 or 1937, in other words not one near to full employment, the deflationary influence of reserve accumulation is, taken by itself, a factor reducing employment, consumption, and in all likelihood capital formation as well. However, if the prosperity period is one characterized by manpower shortages, by too much effective demand, and a tendency toward inflation, then the enforced reduction of consumption is all to the good.

We need not treat in detail the mechanics of the process whereby reserves are accumulated and dispersed, because this problem has been widely discussed in the literature on social security. If guaranteed wage reserves consisted simply of building up of cash or bank deposits in good times and their dispersal in bad times, the process would be relatively simple. The quantity of money would not necessarily have to undergo any changes but its rate of activity or velocity would be lessened in good times and increased in bad.

If reserves are treated as trust funds investable only in Government bonds or similar gilt-edge securities, the mechanics might be slightly different but the final effect substantially the same. As a matter of fact so long as the Federal Reserve banks or the commercial banks are willing to buy or sell considerable volumes of Government securities, these assets possess many of the liquidity properties of money. If, in depression, the bonds accumulated in the reserve funds were bought by the banks, then the stimulus to effective demand resulting from guaranteed wage disbursements might appear as an increase in total bank deposits rather than simply as a change in the velocity of money. In good times, if the growing reserve funds absorbed Government bonds held by the banks, the result would be to curtail the volume of deposits during the boom below what it would otherwise be.

Any thoroughgoing discussion of this problem would have to take account of the effects upon the interest rate structure of both the accumulation and deaccumulation of such reserve funds. Broadly speaking, these secondary reactions upon the interest rate structure and the capital markets are to some degree perverse. The accumulation of reserves in good times would to some measure tend to raise capital availability and lower interest rates, so that some of the enforced reductions in consumption would seep over into investment rather than curtailing over-all demand.²⁵ Similarly in depression, attempts to liquidate reserve funds might have some upward effects upon interest rates and consequently, some depressant effects upon investment. However, these secondary effects can be minimized if reserve funds are confined to Government bonds. Moreover, the

²⁵ So long as the funds are not hoarded, there is always the possibility that some of the purchasing power diverted away from consumption will filter into investment. (It has been argued along similar lines that raising taxes in excess of Government expenditure to retire debt may prove not to be deflationary if the owners of retired Government bonds plough the money back into productive investment expenditure.) In a perfect capital market, where the favorable effects upon investment can only take place through a reduction in the interest rate, this secondary reaction to a primary reduction in the consumption schedule would in all likelihood be quantitatively smaller, dollar for dollar, than the original primary effect. This for two reasons: the doubtful responsiveness of investment to reduced rates of interest, and the adverse effect on investment outlay of reduced consumption sales. To the degree that the actual capital market is an imperfect one, always subject to informal rationing, investment may react somewhat stronger to larger loanable funds than if the investment rate alone were involved. This modifies but hardly alters our conclusion.

monetary authorities can easily, and should, take account of any perverse interest and other effects of reserve accumulation and deaccumulation and take appropriate action.

A new possibility would arise if governmental fiscal policy could be assumed in the years ahead to be effective in preventing inflation when the economic system is operating at full employment. Whenever private investment demand was excessive, fiscal and monetary policy, on this assumption, would curtail the excess. In such an environment, the widespread accumulation of guaranteed wage reserves would reduce to some degree the need for alternative deflationary monetary and fiscal policies. If carried to excess, however, such reserve accumulations might have to be offset by actual expansionist governmental policies.

There is no assurance that the level of income and employment over the entire cycle would be any larger under reserve financing. Among other effects, the program would bring about a redistribution of income, partly from profits, partly from consumers in general, and partly from productively employed workers to workers who, if there were no guaranteed wage plan, would cease to draw wages. If carried out on a relatively modest scale—one which would not seriously distort price-wage relationships—the effect would be to level off more or less the boom demand and to raise the effective demand in the depression period. But if really huge reserves were accumulated in boom years, adequate to pay annual wages to a large part of the labor force in a depression as serious as that beginning in 1929, the boom could easily be converted into a depression. Reserves of the magnitude required would cause a serious distortion in the economy. Some would prefer to state this distortion in terms of the wage-price structure, others in terms of a concealed tax on consumers and wage-earners, and still others in terms of a savings-investment problem.²⁸

²⁸ If technological cost savings from the guaranteed wage plan (assuming for the moment that such plans do increase man-hour productivity) were placed in a reserve fund during the boom phase of the cycle and paid out in the depression phase, the effect would be a redistribution of income over time. The total income payments made to individuals in the boom would be made less than would otherwise have been the case; and during the depression the income payments would be increased. Financed as here assumed, out of increased productivity, there would result no redistribution of income between individuals, and no absolute reduction in corporate profits or corporate net savings. If however, the gains in productivity were nil or inadequate to cover the guaranteed wage payments, the added costs would have to

Apart from these theoretical considerations is the practical matter that actuarial calculations of the unemployment risk are not feasible. The reserves that are built up might prove too large. In this event the accumulation of reserves would amount to a compulsory savings scheme not simply in the boom years, but also over the entire cycle. Aggregate demand might thus tend to become deficient over the long run and create a condition of underemployment. (Of course if the long-run factors were inflationary, such compulsory saving would tend to be a stabilizing factor.) Finally, in a growing society, the setting aside of reserves, even though actuarially exact, nevertheless would still result in the growth of reserves over the cycle, and to this extent, would tend to aggravate the problem of maintaining adequate levels of aggregate demand.

On the other side, the inability to make reasonably accurate actuarial calculations of the risk involved might result in wholly inadequate reserves. Unemployment insurance reserve funds, though they undertake a very limited liability compared with a comprehensive guaranteed wage program, have had to be supported in various countries by the Government treasuries. While large reserves have been built up in the State unemployment funds in the United States, a serious and prolonged depression could easily bankrupt many of them. A guaranteed wage plan, even one limited to 40 weeks per year, could be considerably more costly than unemployment insurance. The reserve funds, to withstand a serious depression, might have to be far larger than those needed for unemployment insurance. Put to the test, guaranteed wage plans might need Government support even more than unemployment insurance. Thus, what was intended to be a scheme based on private industry financing might face default under the stress of serious depression, or else be compelled to call upon Government support. This risk

come either out of corporate net savings or else from a redistribution of the income of individuals.

Only the reserve method of financing is capable of redistributing the income over time, i. e., from boom to depression. Such redistribution over time has nothing to do per se with the question where the funds come from, whether from: (a) gains in productivity or (b) redistribution of income between individuals and social groups. If the reserve method of financing is not used, gains from productivity will necessarily be passed on in the form of (a) larger income payments, (b) increased outlays on plant and equipment, or (c) larger corporate retained earnings. But none of these, apart from reserve financing, would tend to iron out the cycle.

serves to stress all the more the importance of limiting the employer's liability, as suggested in chapter VI below.

It would not be possible to calculate with any high degree of accuracy the actuarial risks involved in introducing guaranteed wage plans in different industries even in a society committed to a program of sustained full employment, and prepared to use fiscal, monetary and other measures to achieve this goal. A number of countries, including England, Canada, and Australia, have issued white papers on employment policy proclaiming high and stable levels of employment as a deliberate aim and responsibility of Government. The United States Employment Act of 1946 does not go quite that far. All the British countries referred to above have recognized the difficulties involved, and none is confident of anything more than moderate success. Thus, even with the best of good will and favorable circumstances, no one knows what degree of success may attend these plans. We know that the war has left us the heritage of innumerable distortions, and these will plague us for many years to come.

Let us suppose, however, that we have surpassed this difficulty—that experience has, in fact, demonstrated a high degree of success with a stabilized full-employment program for a period sufficiently long to warrant general confidence. Some fluctuations there would nevertheless be, but more moderate and presumably fairly well under control. Cyclical fluctuations of employment would be mild, yet relatively large in the heavy capital-goods industries. Seasonal and transitional unemployment would also be experienced.

In the "ideal" society described above (and we repeat that we have no illusions that such a society can quickly be realized) guaranteed wage plans, privately financed, might tend to moderate any remaining cyclical swings, and to facilitate an attack on seasonal unemployment. Transitional and frictional unemployment might be intensified if the guaranteed wage had the effect of reducing labor mobility.

Within the framework of the society envisaged above, cyclical unemployment might become a more or less manageable risk, and accordingly, the reserve funds needed to meet the financial lia-

bility involved would not need to be large. In this event there would develop no long-run problem of excessive compulsory saving in the form of reserve funds. The reserves accumulated in the good years would be dispersed in the relatively low years. This leveling process would tend to smooth any remaining swings in the cycle.

A buoyant labor market, such as that here assumed, would moreover be favorable to an attack on the problem of seasonal unemployment. Employers would be stimulated by the introduction of the guaranteed wage to find year-round work for their employees. It is one thing to place such a responsibility upon employers in a society such as the one we are living in, with its grave uncertainties with respect to the stability of the market and the adequacy of aggregate demand. It is quite a different matter to introduce the guaranteed wage in seasonal industries in a society in which, within reasonable limits, the adequacy of aggregate demand is assured. The development of supplementary lines is feasible in an expanding and buoyant society, whereas it might only supplant the product of some other producer in a limited market in which there was not work enough to go around. Seasonal unemployment might be largely eliminated in a full-employment economy. But even so, this important goal could not be reached unless ingenuity and resourcefulness were brought to bear on the problem. The guaranteed wage might offer a powerful financial inducement to employers to find steady year-round work for their employees. The technical job of dovetailing short-run fluctuations in employment is no mean managerial task, but a sustained high level of aggregate demand would provide an environment within which the job could be attacked with high promise of success.

We have spelled out these various prospects of the guaranteed-wage program within the framework of a society which had achieved a high and stable level of aggregate demand, not because we think such a society is going to be reached tomorrow or the next day, but rather to lay bare the difficulties confronting the guaranteed-wage program. The conclusion is not that the guaranteed wage must await the dawn of a perfect society. The conclusion is rather that we must take account

of its limitations, and especially avoid procedures that may defeat the very purposes which it is intended to achieve.

Having in this chapter analyzed the effects of guaranteed wages upon the problem of business-cycle unemployment, we turn in the next

V. GUARANTEED WAGES AND EFFICIENT USE OF RESOURCES

The problems to be discussed in this chapter are of a rather abstract and general nature. Nevertheless, the theoretical analysis involved, even though briefly stated in this report, is, we believe, important in an over-all consideration of the guaranteed wage.

THE MERIT-RATING CONTROVERSY

In chapter II it was shown that the economic cost of idleness to the community could be primarily measured by the loss of output which it entails.²⁷ Suppose that a particular industry or line of activity has a record of great instability of production and employment. How should its prices and costs then be set?

This identical question was involved in the extensive discussion of merit (or experience) rating in connection with unemployment compensation. The original Wisconsin Unemployment Insurance Act, drawn up under the strong influence of John R. Commons and economists of his school, required employers with unusually poor records of stability to pay higher rates of taxation. Those demonstrating unusually good continuity of employment were granted lower rates—in much the same way that steel-frame buildings, relatively immune to fire risk, are granted low fire-insurance rates.

Two principal considerations are usually invoked to justify this procedure. First, and perhaps of least importance, is a feeling that fairness (justice or equity) implies that an employer should have to pay only for the evil which he creates, but that he should be made to pay for that. This particular argument is a highly controversial one. Numerous writers, perhaps even the majority, have dissented, arguing that it is the essence of social insurance (in contrast to private

²⁷ Our earlier discussion also dealt with the additional evil arising out of the effect of idleness itself on the worker and community, and also upon the problem of equitably sharing the costs involved in idleness between different individuals and groups.

chapter to a consideration of its influence upon the pricing system as it relates to the efficient use of economic resources. Even if the problem of depression were brought under control there would still remain the challenge of seasonal and other irregularities in production.

insurance) that there be a sharing of burdens between groups; the essence of merit rating, on the other hand, is the perverse principle of "to him that hath, shall be given."

The second argument in favor of making the industry bear the costs of its own instability has usually been the more important one. Under such a system, management is supposed to be encouraged to stabilize its operations. It is financially penalized if it does not stabilize; it is rewarded to the extent that it does. There is certainly something to this; as we saw in our earlier discussion of the present wage contract, labor appears to each firm as an avoidable variable cost. Current practices therefore tend to warp and distort the socially desirable adjustments of production.

We do not wish to enter upon the details of this controversy. It is enough to note that the opponents of merit rating point to empirical data to show that employers are typically not able to do much about their own instability. Experience, it is said, seems to indicate that employers' reactions to higher penalty rates are not sufficiently sensitive (particularly in response to the rather moderate differences in rates usually involved in merit rating) to be very significant. Further, it is argued that employers with steady records are not usually better planners but are more often the lucky beneficiaries of special market situations (often of a monopoly type).

This economic controversy finally burned down in the years after 1935 when the Social Security Act was passed. The theoretical honors, if one may judge from the literature, seem to have gone against merit rating. Nevertheless, in recent years merit rating has been introduced in modified form by almost all States, principally as a one-way street making for reductions in taxation and tending to keep unemployment reserves from growing so rapidly during the high-employment wartime years—that is, during precisely the time when such reserve accumulation might contribute

toward the fight against inflation and excess aggregate demand. This, and not the establishment of effective differentials spurring planning for stabilization, has become the primary function of merit rating.

BUSINESS CYCLE VERSUS OTHER IDLENESS

When we turn to guaranteed wages, which is equivalent almost to 100-percent unemployment compensation borne completely by employers, what was previously a rather stale academic exercise becomes a really vital economic problem. Should the form of the wage contract be changed so as to raise, substantially, the costs of production of unstable firms?

A quite different answer must be given to this question depending upon the kind of instability involved. We saw, in the last chapter and earlier, that a typical business concern cannot really do very much by itself to moderate the cycle, and often what it can do represents no corresponding net gain for society as a whole but rather only changes the place where instability appears. We also saw that widespread guaranteed wages by all employers together are scarcely likely, taken alone, to prove a quantitatively important stabilizing factor in an economy subject to wide swings of investment, which in turn have a cumulative effect on income and employment.

The John R. Commons view that the price of each commodity should be made to bear the cost of the idleness which it involves—we do not say causes—cannot validly, we believe, be applied to unemployment of the business cycle type. In this chapter, we wish to consider whether or not a similar conclusion would hold with respect to unstable industries which operate in a continuing high employment economy; or to unstable industries which operate in an economy whose general over-all activity is steady but at a relatively low level involving considerable chronic unemployment.

At the risk of being wearisome, let us repeat once more why the problem of business cycle unemployment differs from that of seasonal or other irregular rhythms. The unstable sector of our economy is predominantly the capital goods industries. To argue that costs and prices should be raised in such industries flies in the face of certain com-

monly accepted programs for fighting depression—programs which stress the need to reduce construction costs, interest rates, and capital costs in general so as to stimulate investment outlays. It would be bad social accounting to discourage employment in the capital goods industries by saddling additional costs on these industries. Such a procedure is only too likely to reduce the total volume of capital goods outlays over the cycle, thereby leaving the system at a lower average level over the entire cycle.

The same matter may be put in still another way. When unemployment is the alternative to an industry's employment of a worker, the true social (opportunity) cost of hiring the worker is nil. Let us suppose that we undertake to saddle—in the form of an overhead—the financial cost of an idle worker upon the industry in question. If indeed, it were true that the capital goods industry were characterized by a high degree of perfect competition, in the short-run these increased overhead items would not cause any increase in the selling price of the product (a capital good) since under perfect competition the selling price would be forced, in periods of falling demand, down to a level below full unit costs. This means that saddling the extra labor cost (in the form of an overhead item) need not necessarily result in curtailment of output. Instead, it would cause the short-run burden to fall heavily upon the industry's stockholders. This might well be better than having it fall upon the workers, but is not necessarily better than spreading the burden of depression more widely on the community as a whole (assuming for the moment that the Government does not act to prevent depression).

The above result would hold only for a highly competitive industry and then only for the short run. In the longer run, firms would be forced out of the industry as a result of chronic losses (incident to saddling the industry with extra labor cost in the form of a guaranteed wage overhead) until enough firms had left to cause output to decrease and prices to rise to the level of full average cost (including overhead and taken over the whole business cycle). But such increases of the price of capital goods, as we have already seen, tends to reduce total employment.

If the industry is one characterized by considerable imperfection and by administered prices

set by the firm, we might still have short-run ruinous competition. But more likely the firms will be aware of their competitive interdependence in pricing and of their monopoly power to raise prices without losing any considerable part of their customers. Full cost considerations are likely to provide a powerful rallying ground for the firms in the industry, so that, even in the short run, prices might rise. In the long run, the same result as already indicated would follow, although we must also be prepared for the possibility that so-called monopoly profits may be made to bear part of the cost.

In the absence of effective Government full employment measures,²⁸ it would not be good policy to permit the whole scale of capacity and labor force in the capital goods sector to shrink to a point where the average price over the cycle would cover full costs including the guaranteed wage overhead. This might only make the saving and investment problem worse.

And yet, it is patently unfair to let workers (attached to the capital goods trades and who have no other place to go) receive lower earnings over the cycle than other workers. One obvious solution would be to let the Government make up the difference in relief payments or social insurance, it being manifestly undesirable to permit capital goods prices to rise over the cycle. However, if the policy of Government aid is to be followed, it becomes rather obvious that the Government might better get something for its money in the way of useful public projects. Thus we are brought to a planned program of public expenditures to fight depression; or if the people democratically feel that high priority should be given to private consumption activity, the logical policy implication is Government transfer expenditure (or tax reduction) which will increase private consumption and thereby provide job opportunities outside of the construction and capital goods industries. And just as taxes should be raised

²⁸ We deliberately refrain from discussing the problem of letting wages (and prices) fall in an attempt to reduce the surplus supply of unemployed labor. Such a discussion would be highly technical and would involve a volume by itself. Except for a small fringe, the majority of writers dealing with this problem in the last decade are of the opinion that cutting wages and prices in a hyper-deflation spiral is either undesirable or unfeasible (or both) in a modern capitalistic country. It will be clear from our emphasis that we believe that any alleged advantage of such a deflationary process could better be achieved by expansionary policies.

during inflation and Government expenditure carefully trimmed, so in lean times tax reduction is in order, while useful governmental investment and public services will need to be expanded.

CONDITIONS OF CHRONIC UNEMPLOYMENT

But what if there is no effective full employment program and the economy operates at a steady level with considerable unemployment? How does the view that the prices of unstable industries should be made to bear the costs of their instability then stand up?

It will be clear from the discussion above, that the answer must be "very poorly." In effect we are asked to place a sales tax on the capital goods industries in order to keep up the income of the unemployed. This is very nearly the worst type of financing that anyone could devise.

OPTIMAL PRICING UNDER HIGH EMPLOYMENT CONDITIONS

When we deal with a world of adequate aggregate demand and generally high employment, however, the John R. Commons reasoning comes into its own. Then any industry with great seasonal variability or with some other irregular pattern will be withdrawing the labor it hires from other productive employment.²⁹

In a high employment economy any industry that draws resources to itself and then uses them only part of a year ought properly to be charged with the cost of those resources. This industry's output must bear the responsibility of causing reductions in output elsewhere, equal in value to the productive resources taken away from all other industries.

Even if an industry is unable to stabilize its operations, it should still be charged up with its full costs, inclusive of idleness created by it. Otherwise too many resources will be going into that industry, its price will be too low, and the consumer of the goods in question will be subsidized at the expense of the group least able to afford the

²⁹ These remarks are not meant to apply to those seasonal industries which hire workers who come for limited periods into the labor market, from schools and from homes. Such industries perform a highly useful function in providing short-period employment at just the season of the year when there occurs a temporary increase in the labor force.

burden—the workers subject to intermittent income. Higher costs are more than a whip to the employer; they are a device for contracting an unstable line of activity.

If it is unavoidably necessary for a municipal fireman or an auto worker to stand by in idleness much of the time, we must redefine our concept of productive labor to include such necessary “activity.” At the same time we must tender to the auto worker what we already concede to the fireman, adequate pay for all working time that he is unable to perform elsewhere.

Undoubtedly the gradual carrying out of a program such as is implied in the above remarks would result—gradually but surely—in some drastic quantitative changes in the present pattern of prices and output. So much the better, if it is true that the present-day structure of prices is grossly distorted away from an efficient and equitable pattern of resource use.

Some people may grant that an industry should be charged with the full cost of the resources it takes away from other industries, but still argue that higher hourly wage rates rather than a longer guaranteed tenure is the proper solution to the problem. The statistical data referred to in chapter II suggest that there is no universal tendency for hourly rates to rise so as to compensate for variability of employment. However, it is undoubtedly true that in some very seasonal lines, hourly rates are very high; and variability of work is one reason offered by unions for even higher hourly rates. Often such unions are opposed to guaranteed wages, if this is to mean lower hourly rates or slower increases in future hourly rates.

In such situations, higher hourly rates may be better than no adjustment to heavy seasonal unemployment. But so long as steady work does not involve extra disutility, the longer tenure provided by guaranteed wages would be a more economically efficient arrangement because then, and only then, would there be an incentive toward regularization of employment, an incentive to put the available worker to some sort of useful work.

The only real economic drawback to guaranteed wages in such a situation arises out of the very real possibility that the workers laid off by the industry in question might possibly (had there been no guaranteed wage) been able to find fill-in productive employment elsewhere. Such possibili-

ties are no doubt limited, but to the extent that they exist, it is not proper to regard the industry in question as being responsible for totally withdrawing labor from other useful work; it is therefore incorrect to saddle the industry with their full guaranteed wages. In fact, in such situations, the guaranteed wage can have harmful effects on the mobility of labor. Our proposal of chapter VI with respect to “integration” with the unemployment insurance system may remedy this in part.³⁰

DOVETAILING AND LARGE MONOPOLIES

To the extent that the idle time of the workers hired by one industry can be dovetailed with the operations of another industry or with schooling and leisure, we need not attribute to the industry the full cost of its laid-off workers. Ideally, dovetailing of activity is one solution to the irregularity of seasonal and other short rhythms of different industries. Hence it is essential that unions relax their objections to changes in function and activity of workers.

Dovetailing is easier the larger the units, since when many intermittent lines of activity are merged, the extremes of their sums is much less than the sum of their separate extremes. Or to put this in another way, by merging activities we can cancel off the peaks of some against the troughs of others. This would seem to provide some argument in the direction of large-scale monopolies, necessarily possessed of tremendous amounts of economic power. And so it does, if the dovetailing is to take place within the firm; i. e., if the work is to be brought to the worker and not the worker to the work.

However, dovetailing tends to stabilize primarily to the extent that the components dovetailed have different cyclical rhythms and phases; in the ideal case of the coal and ice dealer, the components will have opposite phases so as to be mutually canceling. Therefore, the firm which wishes to stabilize its time-profile of production cannot do so simply by growing in scale or by adding closely duplicating lines subject to the same timing of demand. It must branch out into new territories, take on new and different lines. Con-

³⁰ Workers in some lines of activity may prefer intermittent employment. To the extent that they value occasional periods of leisure, they need not receive a full annual wage. No doubt collective bargaining in such cases will have other goals than a guaranteed wage.

sequently, the fact that it grows in size need not entail a commensurate growth in its monopoly power. Monopoly power depends primarily upon a firm's relative importance in comparison with the total demand for each of its products. If it grows by branching out into new lines the firm is also spreading itself over wider areas of demand. To revert back to the coal and ice dealer, there is no special reason to believe that his monopoly power in either of the two markets is greater than that of two separate dealers each handling one line. His over-all efficiency may be greater; but that is a good thing rather than a bad.³¹

POOLING LABOR RESERVES THROUGH A WELL ORGANIZED MARKET

If we pursue the argument concerning the desirability of pooling the labor reserves of many lines of activity in order to minimize unnecessary idleness, we are confronted with the problem of the general labor market itself. We can conceive of a vastly improved labor exchange to which workers go for placement. In the fantastically extreme case where each day every person and every firm turn anew to the central labor exchange for reassignment, idle labor reserves would be at an absolute minimum, the whole being steadier than its parts.

Common sense tells us that there are insurmountable objections to such a fantastic case. In any factory this morning's production will depend upon yesterday's activity in such a way that entirely new men coming into the plant would be at a great disadvantage, however good their general experience and training. Moreover, even if the inefficiency of such an arrangement could be overcome, we must still reckon with the intrinsic properties of human nature; the worker would find it profoundly distasteful and disorganizing to move on to a new job at frequent intervals; man requires continuity in his working as well as in his home life.

We need not prolong the discussion of what is admittedly an extreme case. There is no reason why a proposal to pool all workers together into one organized market should not be perfectly compatible with job continuity for the great majority

³¹ Those who regard "bigness" per se as an evil, without regard to its market consequences, may still object to the firm's growth.

of workers, most turn-over being confined to the "marginal" workers as is now the case. But this discussion does high light the problem of reconciling job continuity for the individual with maximum national productivity.

Thus, if guaranteed wage plans were universally adopted prior to any successful attack upon the problems of stabilizing production, the effect might be to attach workers to a given firm when there was no useful work for them to do there, even though, at the same time, there was productive employment to be found elsewhere.³² Boondoggling is boondoggling, and bad economic policy whether it is pursued by the Government or by private enterprise. Boondoggling is particularly costly during periods of high employment when productive employment opportunities are plentiful.

This illustrates that it is as necessary in this chapter, as in the last one dealing with aggregate demand, to distinguish carefully between the different conditions of economic life upon which guaranteed wage plans impinge—between high employment and depression economies. There is a danger that guaranteed wage plans, not coupled with effective stabilization planning, could immobilize men in such a way as to increase labor hoarding and the inefficient use of resources.

STABILIZATION AND DIFFERENTIAL PRICING

Thus far we have been discussing the costs of unavoidable idleness. Even if employment were not stabilized, guaranteeing steady wage income might so improve labor productivity and turn-over rates as to be, in effect, costless. This would be all to the good. Of course, it would be better still if in addition to making labor more productive while at work, it were also possible to find useful continuous work to do.

Stabilization may, however, be costly at the outset. It takes effort and planning. Under the present wage contract, which permits the laying-off of workers on short notice, there may be little,

³² Because of the considerable difficulties and costs involved in workers going from one job to another in order to utilize their special skills, there is also much to be said for mobility on the part of the employer in shifting between production lines rather than throwing the full burden of mobility upon the workers. This in no sense means that we minimize the importance of labor mobility between and within firms.

if any, counterbalancing savings of cost from steady operation.³³

But under the more optimal system of pricing discussed in earlier sections, where each employer is made to pay full wages to all workers whom he withdraws from productive employment elsewhere, the costs of stabilization will often be lower than the costs of not using the workers whose pay goes on anyway. Accordingly, stabilization plans, under this procedure, might be promoted. Being available, such workers might as well be used for whatever useful goods they could produce. Under high employment, the ingenuity exercised by an employer in financing odd jobs, or less than fully productive tasks, for his men to do in off-seasons is highly commendable.

The construction industry provides an illustrative hypothetical case to show how guaranteed wages might give rise to a different system of pricing, leading to a more efficient and equitable use of our national resources.³⁴ Let us suppose that a house requires, say, 2,000 man-hours of labor to build in the summertime and 4,000 in the winter. If labor can be hired and fired by the season at the same hourly rates, say \$2 per hour all year around, no one would ever build in the winter, because by waiting until the following season, the buyer could save 50 percent in labor cost. Construction workers would be out of jobs for, say, 6 months of the year. Houses would be sold for less than their true social cost, most of the difference coming out of the workers' loss of income.

Theoretically, it might be alleged that a way out of this situation would be for workers to accept half wages in the winter. But in view of union insistence on uniformity, and if it were assumed that similar workers on steady jobs elsewhere receive around \$1.50 per hour, we may reject this suggestion as unrealistic.

³³ One saving, mentioned earlier, results from the fact that less plant and capital equipment are necessary when loads are spread evenly over time. Against this saving in interest and depreciation (resulting from time rather than use) there is the fact that in many industries the extra capacity serves as a standby; in case of heavy sales, the busy season is lengthened. A plant operating near to capacity all the time cannot expand its production in this way, but must depend on overtime or more intensive production.

³⁴ As indicated in ch. VI, we do not think that any union should be compelled to adopt guaranteed wages except through voluntary collective bargaining. However, the present hypothetical case of the construction industry throws some light on the economic desirability of collective bargaining taking one form rather than another.

Under a system of guaranteed wages the employer would realize that his summer contracts really involved more than the wage rates paid then. Moreover, during the winter his labor force would cost him nothing extra if he kept it at work. The result: He would produce houses all year around, selling them in all seasons at about the same price (based on the hourly wage times 3,000 man-hours, the average between winter and summer labor requirement). If the old hourly wage rate were retained, the labor cost of a house at the site would now be \$6,000 summer and winter. This increase in price results from the product bearing its full economic costs.

However, if part of the \$2 hourly rate represented a premium to compensate for the winter idleness, and if similar labor elsewhere received only \$1.50 for steady jobs, then the hourly rate might now fall and workers would still be better off than under the old regime with a winter lay-off. Their annual take-home pay would be up by 50 percent. The labor cost (at the site) of houses, summer or winter, would now be about \$4,500 (or 3,000 times \$1.50), which is just where it should be.³⁵ Apart from the social desirability of subsidized low-cost housing, the price indicated would draw the right amount of resources into the building industry, and all of such resources would be efficiently used.

This is only a numerical example; it is meant to be illustrative rather than to describe an actual situation. Moreover, it assumes a condition of adequate aggregate demand and high over-all employment so that the excess labor in the unstable, seasonal industry could readily find jobs elsewhere, once the industry were stabilized.

Often a system of variable pricing may prove to be economically optimal. Such a system would mean high prices during peak demand seasons when (marginal) costs are high and output must be rationed; and lower prices during off-peak periods. In addition to price reduction, terms of sale and delivery may be made more agreeable in off periods and less agreeable in peak periods. Alternatively, a seller in peak seasons may offer a reward in terms of priority in delivery dates to

³⁵ In a moment we shall consider the possibility of seasonal variations in demand, giving rise to different prices at different seasons.

those customers who have bought steadily in off periods. To be effective, and profitable, the process of stabilization may require something more than rewards to good customers; it may also be necessary to apply penalties to bad ones. And the firms may be compelled to refuse the casual business of new customers at the peak of a sales boom. Were our markets not so imperfectly competitive and characterized during normal times by "buyers' markets," businessmen would realize more keenly

that peak-load, fair-weather customers are often very expensive customers who do not pay their way.

Most of the above patterns of price and market behavior have already been tried on a limited scale. Often they have later been abandoned because they were not economical. It might well prove to be otherwise in a world of guaranteed wages, where the penalties for unstable production would be considerably greater than at present.

VI. POLICY RECOMMENDATIONS

The analysis of previous chapters shows that there is much to be said for guaranteed wages, particularly for seasonally or otherwise unstable industries operating in an economy with relatively high and stable levels of aggregate demand. But it also suggests that guaranteed wages cannot be regarded as a cure-all for depressions. There are important limitations to the device as an anti-depression measure—especially in comparison with other economic policies such as fiscal policy and other full-employment programs. In view of these limitations, so long as our society suffers from rather wide fluctuations in business activity, guaranteed wage plans should be introduced only with proper safeguards.

This conclusion is so important that we think it worth restating in a slightly different form. We do not believe that the limitations referred to above warrant the conclusion that guaranteed wage plans are economically unsound and should be abandoned as goals. However, these reservations are sufficiently important to put us on guard against viewing the guaranteed wage as a solution for the problem of unemployment; and especially to warn us that it cannot and should not become a substitute for social security measures or a full-employment program. In this concluding chapter, we should like to put forward for discussion four policy recommendations.

Recommendation No. 1. *Guaranteed wages should be a matter for voluntary collective bargaining without legislative compulsion by the Government.*—Our analysis has not led to the conclusion that the Government should seek to intervene actively by legislation to require that industry introduce guaranteed wages. In the present state of our economy, this is a matter that should

be left to voluntary free collective bargaining between management and labor.

Recommendation No. 2. *In many lines guaranteed wage plans may properly include limitations as to the employer's liability.*—From our previous analysis, and from a factual survey of earlier depressions, it appears that unqualified guaranteed-wage plans, indiscriminately applied to industries subject to wide cyclical swings of demand, might involve such extensive financial costs as to prevent industry from undertaking such programs; or if industry had nevertheless undertaken such programs, they might have to be prematurely abandoned in order to avoid insolvency.

Some sort of limitation is therefore necessary. Existing guarantee plans provide for various kinds of limitations: coverage of less than all workers; guarantee of work for a limited number of weeks per year (for example 40 weeks); guarantee of less than full-time weekly pay for weeks covered; provision for nonrenewal of the guarantee; and so forth. What is above all needed, however, is a form of limitation which will in normal times give a maximum of security and protection to the worker, and to the employer a maximum incentive to stabilization efforts; but which, in emergency times, will come into effect to keep the firm's financial liability under the guaranteed wage within reasonable limits.

Because of the ever present danger of cyclical slumps we tend to look with favor on some sort of limitation on the percentage of the total guaranteed pay roll that the firm shall be liable for in any year or contract period. So long as production declines are not too great, workers will receive 100 percent of their full normal income. But if and

when deep depression years come along, and lay-offs from productive work involve more than, say, 10 percent (or some other suitable ratio) of the guaranteed payroll, then the workers may have to receive something less than the full guarantee.

The precise percentage liability is a matter for experimental determination over time, and would no doubt vary from industry to industry depending upon their differing degrees of cyclical variability.³⁶ For many lines of activity, 10 percent may be a reasonable percentage limitation.

With such a limitation, it should not be necessary for private industry to accumulate unduly large reserve funds. Moderate reserve accumulation may be considered necessary for prudent financial management; and, if not excessive over the whole period of the cycle, the accumulation and subsequent expenditure of the reserves may contribute to dampening the business cycle, helping to contract excessive boom-time purchasing power and to expand it during depression. But if ever the guaranteed wage should be widely adopted, and if substantial private reserve funds were accumulated in addition to the continually accumulating governmental reserves for old-age security and unemployment insurance (currently around 14 billion dollars) the problem of maintaining high employment might be made more difficult.

Momentarily, the continued growth of these social security trust funds is helpful as an anti-inflationary device. Nevertheless, over the long pull we believe these programs should be placed more nearly on a pay-as-you-go basis. Similarly, we should not like to see a long-run accumulation of large guaranteed wage reserve funds. Whether for social insurance or guaranteed wages, moderate reserves that could be drawn on in the depression phase of the cycle would, however, not only be permissible but desirable. They would help to serve as an automatic anticyclical compensatory mechanism.

Within the collective-bargaining contract itself, there would probably have to be included certain special stipulations further limiting and qualify-

ing the guarantee of work. For example, there might be a stipulation that wages would not be payable to workers out on strike. Collective-bargaining clauses might be introduced into the guarantee also limiting wages of workers in the plant, not themselves on strike but rendered unable to work by virtue of strikes outside the plant—or for that matter inside the plant but in another department or craft. Thus a transportation strike might so impair the flow of supplies as to make a continued guarantee unbearably costly. All these are matters for free collective bargaining.

The primary purposes of guaranteed wages are to insure workers more security and promote stability of production. The device is not intended to create permanent quasi-feudal rights of a worker to a given job. Thus, if a sweeping technological change makes it no longer necessary to keep the previous number of workers attached to an industry or firm, or if there is a secular change in people's tastes and demands, then the guaranteed wage should not serve to freeze workers to their old jobs and techniques and to thwart our economy's increases in efficiency and responsiveness to demand, upon which the ever-rising standard of American living fundamentally depends.

Most changes are not introduced discontinuously and suddenly. The normal attrition of the labor force of a firm, through turn-over and separation, makes it possible to reduce gradually the number of workers without undue lay-offs. Where this is not the case, the guaranteed wage, together with severance pay, may perhaps be used to soften the impact of the socially-desirable process of change upon the workers directly involved. But we feel it necessary to point out the danger that, with guaranteed wages introducing length of tenure as a new variable in the collective-bargaining negotiation, the long-term flexibility of our economic system may be impaired unless organized labor is willing to waive or limit the scope of the guarantee in situations involving permanent changes in technology and demand.

Recommendation No. 3. *Corporate income tax law and practice should be changed so as to encourage guaranteed wage programs.*—Under present tax law and practice, corporations may for tax purposes deduct as an expense all payments made to workers under guaranteed wage programs, during the year when such payments are

³⁶ The Latimer Report on guaranteed wages presents data showing what the costs to a number of industries of an unqualified guarantee would have been in earlier years. See ch. VIII, pp. 70-100. The report discusses the rather intricate problem of how the guaranteed wage funds are to be allocated among the laid-off workers whenever the drop in production turns out to be great enough to bring the percentage limitation into effect.

made. Suppose, however, that a corporation wishes in good times to set aside a reserve fund in anticipation of the time when it will have to pay out guaranteed wages to the workers it is currently hiring. Such appropriations to guaranteed wage reserve funds—unlike retirement pension and profit-sharing programs—cannot now be treated as an expense to be deducted from taxable earnings in good times; only later, when actually paid out, can they be so treated.

The present tax situation is, therefore, in a sense discouraging to guaranteed wage plans. It is, however, easy to exaggerate the quantitative importance of this whole matter. A few years' delay in receiving a tax reduction or credit means primarily the loss of interest on the sums involved. This is all the more true to the extent that corporate income tax rates remain stable, and to the extent that a system of carry-forward (and carry-back) is in force so that the accounting period for tax purposes becomes longer than a year and variations in income are averaged over a longer period.

There seems to be no question that any change in existing practice would require new legislation by Congress. This might take at least two possible forms. First, Congress might specifically provide that any guaranteed-wage payments might be carried back over previous years as deductible expenses. In effect, the company would be reimbursed for its previously overpaid taxes, resulting from its previously overstated earnings—overstated because the accruing liability for guaranteed-wage payments had not been recognized as an expense of production at that time.

A second method of handling this problem would be to permit appropriations to the reserve fund to be deductible as expenses during the year when they are being set aside. Then, later when the reserve is being used to finance guaranteed wages, such outlays would not again be chargeable as an expense and as a tax deduction—for, otherwise, there would be an unwarranted tax loss to the Treasury and an unfair subsidy to the guaranteed-wage plan. So far this second plan seems simple enough; but under some circumstances difficulties may arise. What if more is appropriated to the reserve than is ever necessary to meet guaranteed wages, either because of good luck, or because of good stabilization planning by the employer, or because the employer deliberately

builds up an excessive reserve? Certainly under these circumstances it would be wrong to permit the employer to recover the excess reserves, and to escape corporate income taxation completely on the sums involved. For this reason, it would be necessary to insist that the reserve be a "trust," created to provide guaranteed wages or other benefits for the workers. The trust would necessarily have to be irrevocable as far as the corporation was concerned.³⁷

Our previous economic analysis and the specific accounting aspects of guaranteed wages justify, we believe, the recommendation that the present tax deterrents to guaranteed wages be removed by one or another of the above described methods: that is by a specific carry-back on guaranteed wage costs, or by tax deductibility (with safeguards) of appropriations to guaranteed wage reserve funds.

Recommendation No. 4. *Social security legislation should be altered so that guaranteed wage plans can be integrated with the unemployment compensation system to the mutual advantage of each.*—Guaranteed wages should never be looked upon as a substitute for our existing unemployment-insurance system. This system admittedly needs substantial improvement and strengthening. And we believe that guaranteed-wage plans if integrated with social security could operate in this direction. Such integration would serve to strengthen rather than weaken the system of unemployment insurance.

The workers of employers who maintain wage payments under guarantee plans should be permitted to draw unemployment benefits, provided that they are unemployed in the sense that would qualify them for unemployment compensation in the absence of a guarantee.³⁸ If the employer had to pay only the difference between the full guaranteed wage and the amount paid by the unemployment insurance system, then he might be more willing to undertake such wage guarantees and more willing to broaden the coverage and extend the duration of the guarantee.

³⁷ Any excess reserve funds might be finally used up if all further appropriations to the reserve fund were curtailed. If even this does not meet the problem, the terms of the trust should stipulate that any remaining excess funds be used for the benefit of the workers through providing old-age pensions or for some other welfare provision now permissible from the tax standpoint.

³⁸ Some important technical and administrative problems have to be faced. These are discussed in Mr. Latimer's report.

Moreover, the employer would then be in the position of wishing to support the extension of Social Security instead of—as under the present system of merit rating—having a financial interest in keeping its benefits limited. The only alternative to the method of “integration” here proposed, that would tend to remedy the present discrimination against the employer who voluntarily agrees to guarantee full incomes to his idle workers, would be the method of further extending merit rating—perhaps to the point where all employers with effective guaranteed-wage plans would be excluded completely from all unemployment insurance taxation. We should consider the adoption of such an alternative as something of a calamity, designed to divide and weaken the forces making for an effective social security system.

The method of integrating social-insurance benefits with guaranteed-wage plans would have just the opposite effect, as we have already indicated. It would serve to strengthen rather than weaken our social-insurance system. In addition, the integration with present unemployment compensation would have the further advantage of reducing the tendency for guaranteed wages to freeze workers to a given employment when it may be socially desirable for them to transfer to other

occupations. Under the integrated plan, in order to draw unemployment benefits, workers would have to be registered with the central employment exchange, and would be obliged to accept suitable alternative employment. This would lessen but not obliterate the tendency for 100 percent income maintenance to have deleterious effects upon the mobility of labor.

Important as these legislative changes are, we do not mean to imply that the growth of guaranteed-wage plans should wait upon the reforms here suggested. On the contrary, in some lines of industry the guaranteed wage can be economically introduced under present conditions to the advantage of all parties. As the number of such industries grows, both employers and employees would have an increasing incentive to press for the needed legislation.

These legislative reforms, especially the integration with social security, would make it possible to strengthen such guaranteed-wage plans as may in any event be developed without waiting for new legislation; and they would encourage the spread of plans to other industries which (even with some kind of limitation of employer liability) might otherwise find it difficult to set up adequate and satisfactory programs.

ADDENDUM—DEPRESSION POLICY AND THE GUARANTEED WAGE

NOTE: This Addendum is presented as a basis for further discussion. It does not constitute a part of our Recommendations.

The analysis of previous chapters points to the conclusion that the guaranteed wage would be a weak rod to lean upon, by itself alone, as an anti-depression measure. Taken in conjunction with other measures—especially fiscal policy and social security—it can serve a useful purpose as a supplementary device. The guaranteed wage is not a cure for depressions. However, as we have seen in chapter V, it could perhaps serve its most useful purpose by overcoming seasonal or other irregularities of employment in industries operating in an economy with relatively high and stable aggregate demand.

THE FEAR OF DEPRESSION

But industry cannot safely assume that we shall in fact achieve in future a continuing high and stable level of demand for goods and services. It is precisely the fear of recurring major depressions that makes management reluctant to undertake commitments under the guaranteed wage. So long as the prospect of serious depressions remains as a major but incalculable risk, guaranteed-wage commitments must be rather severely restricted with respect to the liability involved. Such restrictions could be eased somewhat by building up in good times guaranteed-wage reserve funds.

Guaranteed-wage plans, privately financed, could reasonably be regarded as a manageable risk in a society freed from the fear of major depression. And even though this danger of recurring depressions must be faced, plans can, we believe, be devised along the lines discussed in chapter VI, which are made as "cyclone-proof" as possible. It now remains to consider whether some direct Government financial support of guaranteed wages might not be justified from two standpoints: (1) as a means of encouraging, in

an unstable world, more widespread adoption by private industry of guaranteed wage plans; and (2) as a part of a rounded governmental anti-depression program.

ECONOMIC ASPECTS OF GOVERNMENT AID

The purely economic aspects of such Government support deserves to be considered on its own merits. In terms of political realism, so long as we are not prepared to accept direct Government contributions to social insurance programs (a policy adopted at the very inception of social insurance in England a generation ago), there is no likelihood that governmental grants-in-aid to guaranteed-wage plans will be acceptable. Social insurance should be first in line for governmental contributions from general revenues. This is true, among many reasons, partly because social insurance is of universal application (within limits legally established) and does not apply only to such individual firms as may voluntarily choose to take advantage of Government aid; and partly because social insurance provides a lower minimum income than is contemplated in most guaranteed-wage plans. Virtual universal coverage, taken in conjunction with the principle of a national minimum, commends social insurance as a program deserving direct Government financial aid and support. The case is less strong for the guaranteed wage. Until direct Government contributions to social insurance become a reality, it is probably somewhat utopian to discuss such aid for guaranteed wages. We should ourselves wish first to see direct Federal contributions to social insurance, thereby diminishing the deflationary effect of the regressive pay-roll taxes.

Nevertheless, the economics (apart from the politics) of support for the guaranteed wage deserves study. In terms of employment and anti-depression policy, there is much to be said for governmental grants-in-aid to guaranteed-wage

programs. Indeed, even with respect to social insurance, Government contributions commend themselves in large part by reason of their implications with respect to full employment policy. The more social insurance is financed from progressive income taxation, the more expansionist will the program be.

Our exploratory discussion, in this addendum, of partial governmental aid to the guaranteed wage, contingent upon emergency depression conditions, is very much in the spirit of many of the less controversial Government programs in other spheres. Federal insurance of bank deposits and the capital salvage activities of the Reconstruction Finance Corporation are more or less analogous instances. A third and more venerable precedent is that of central banking (Bank of England, the Federal Reserve System, etc.) whose function has long been recognized as that of providing succor of "last resort" in times of crisis and depression.

Accordingly, we wish to raise the question whether the program of financing guaranteed-wage plans might not, to a degree, be incorporated in a comprehensive antidepression program, such as the Government may find itself called upon to undertake in periods of substantial unemployment. We believe that there are few, if any, who doubt that we shall in fact encounter more or less violent fluctuations in business activity. A slump once started can cumulate, under modern conditions, with incredible speed. The Federal Government will not be able to stand by without undertaking some positive program of action. In such periods, governmental intervention in various directions will be required in any event. In such periods of crisis, therefore, governmental support for existing guaranteed-wage plans might provide one additional compensatory mechanism, thereby reducing somewhat the danger of unplanned and makeshift depression projects which otherwise are likely to be undertaken.

We believe, as we have repeatedly stated, that worker income security can best be promoted by strengthening our already established system of social security and by a comprehensive full employment program designed to maintain a high and stable level of demand, production and employment. Within this pattern, the guaranteed wage can be made a useful supplementary device. It is not something upon which we should embark

with a view to making it carry the whole load. It is not and cannot, we believe, be made the basic foundation of worker income security. But it can be made a significant part of a larger program.

To this end we explore below two highly tentative suggestions. We present them, not because we believe them currently to be within the range of practical politics, but to round out our economic analysis of the guaranteed wage, and to provide a starting point for further discussion. We suggest, in line with the discussion in Chapter V, that guaranteed-wage programs shall be wholly privately financed except in abnormal emergency periods of serious depression. We consider governmental aid to such plans only as a last resort measure, and as a part of a comprehensive attack on depression. We therefore explore two criteria indicating at what point in the depression phase of the cycle governmental aid might be invoked. The first is based on the level of profits of the firm in question; the second is based on the broad general level of business activity in the nation as a whole.

GOVERNMENTAL GRANT-IN-AID BASED ON PROFIT LEVELS OF FIRMS

Precisely in a condition of serious mass unemployment, government support for the continuation of guaranteed wage plans may be far more sensible than ill-designed antidepression measures, which in the absence of adequate planning are likely to be improvised. If a firm were assured that, upon a fall in the annual profits of the company to a small fraction of, say, the previous 5-year average, the Government would come to its support, the guaranteed wage plan might be saved from extinction; and what is more, many firms might be induced to establish guaranteed wages in good times, if they were assured that the Government would bear part of the costs contingent upon a deep depression when profits are low and losses are likely to be sustained. While it is true that special conditions may cause low profits for an individual firm even though general business activity is high, nevertheless experience shows that the profits of most firms fluctuate in close correlation with the cycle. A more complicated formula than the one we suggest below might be designed so as to combine both the criteria of (a) the firm's profits and (b) the general state of business.

Using the more simplified formula, however, let us suppose that the firm's profits have fallen to 30 percent (or some other appropriate figure) of the previous 5-year average. The Government might now undertake to contribute a grant-in-aid on a sliding scale basis, and increasing at a specified rate as profits continue to fall. The scale might, by way of illustration, be somewhat as follows:

Percent profits of previous 5-year average:	Government share of guaranteed wage cost
30 -----	10
25 -----	20
20 -----	30
15 -----	40
10 -----	50

According to this formula, the Government would make an outright grant-in-aid to the current cost of the guaranteed wage plan (that is, to the guaranteed wage payments for workers declared by the company to be totally unemployed) beginning at 10 percent of the cost when profits fall to 30 percent of the previous 5-year average. The grant-in-aid might rise on a step-up basis as profits fall, finally reaching a maximum of 50 percent of the cost when profits fall to 10 percent or less. (A more precise formula is given below.)

In the next section we wish to discuss an alternative grant-in-aid procedure, based not on the profits of the particular firm, but on more general employment and business conditions in the Nation as a whole.²⁹

GOVERNMENTAL FINANCIAL AID BASED ON LEVEL OF GROSS NATIONAL PRODUCT

The feasibility of a guaranteed wage, financed by private business, depends in large measure upon the kind of economy we shall have in the future—how violent will the fluctuations in the gross national product (GNP), employment and business activity be? To the extent that we succeed in narrowing the over-all range of fluctuation in the gross national product, the guaranteed wage becomes more feasible as a practical proposition. It is not feasible for guaranteed wage plans to include any substantial proportion of the total

²⁹ Again it may be noted that a more complicated formula might be constructed which combines both criteria. On this basis, the governmental grant-in-aid would apply only when both general business conditions and the firm's profits had fallen to a certain level.

labor force in a society in which the gross national product fluctuates from 100 billion dollars to 50 billion dollars and then up to 200 billion dollars, as it actually did from 1929 to 1944. If, however, we could narrow the range of fluctuations in the gross national product to within 15 to 20 percent, it would become feasible to include in guaranteed wage plans a substantial percentage of the total labor force.

Grants-in-aid to guaranteed wage plans, once the gross national product had fallen to a certain level—for example, to 85 percent of a full-employment level—might well be included as a part, however modest, of a general antidepression program. There would indeed be no guarantee that the gross national product might not fall far below the level at which grants-in-aid would begin. The program would amount to no commitment with respect to full employment. It presumably would mean that the Federal Government would seek to promote full employment by such politically acceptable measures as were available. If these were reasonably successful, the gross national product might not fall to the level at which the grants-in-aid program would begin. Up to this point, private business would be exclusively responsible for the financing of such guaranteed wage plans as had voluntarily been put in operation.

The grant-in-aid could be stepped up if the GNP should continue to fall to lower levels. It is here suggested, by way of illustration, that at 85 percent of a full employment GNP the grant-in-aid might equal 25 percent of the current cost of any guaranteed wage plan, i. e., 25 percent of the amount actually paid out in wages to workers covered by the plans over and above the wages received by workers for productive employment together with unemployment compensation, during the year or period covered. If the GNP should fall to 80 percent of the full employment level, or below, the grant-in-aid might be raised to 50 percent of the cost. (A more precise formula is given below.)

The criterion has been stated in terms of the gross national product (GNP). In point of fact, the statistical calculation of the GNP is neither sufficiently current nor sufficiently precise to provide the basis for a legal determination of the point at which a grant-in-aid would be made.

Some other statistical index which is precise and unequivocal, but which reflects fairly accurately the fluctuations in the gross national product, would have to be found. This is a matter which will require much careful study. Possibly the ratio of the number of workers receiving benefit payments under the unemployment insurance system to the total number of workers covered by the system might serve as an appropriate index. But the ratio should be applied so as to permit the entry of grants-in-aid (together with the step-up) as nearly as may be at some such points in the level of the gross national product as were indicated above.

It may be appropriate to note that the system of "compensatory payments" to farmers, advocated by some leading agricultural economists, offers an interesting analogy to the suggestion to support guaranteed wage plans at say 80 or 85 percent of a "full employment" GNP or below. The agricultural "compensatory payments" plan, very briefly, may be explained as follows:⁴⁰ The plan does not envisage any price controls or market price supports. Assume that, as a result of a depression, the market price of a given farm commodity falls below 85 percent, say, of the predepression base. Assume the predepression price was \$1 and it now falls to 60 cents. The Government then undertakes to make compensatory payments to all farmers covering the difference between the price actually received (60 cents) and 85 cents, the guaranteed 85 percent of the predepression base. Such payments would provide minimum income security to farmers without interfering with market forces. Prices would not be raised. The commodity would not be "priced out of the market." But the farmer would be protected. And the compensatory payments would be made by the Government at just the phase of the cycle when it is important for the Government to find sensible, useful and justifiable outlets for public expenditures—expenditures needed to swell the diminishing income stream and stop the cumulative collapse. As soon as recovery had proceeded to a point at which the price of the commodity had again reached 85 percent of the pre-

⁴⁰ See Theodore W. Schultz, *Agriculture in an Unstable Economy* (McGraw-Hill, 1945), pp. 220-235. This is a research study for the Committee for Economic Development.

depression base, the Government support would cease.

So also in the Government's support of the guaranteed wage; as soon as the GNP had recovered to 85 percent, say of the "full employment level," or the more specific and definitive index indicative of the degree of full employment (such as the ratio of current beneficiaries to the number of covered employees), the Government's support of established guaranteed wage plans would cease.

Our two suggestions involve one possible technical difficulty from which the agricultural compensatory payments plan is free. According to that plan, as farm prices drop from 86 percent of the predepression base down to 84 percent, nothing very drastic or discontinuous happens. Such a small change is accompanied by a commensurately small change in Government payments. All trouble of "discontinuous brackets" is avoided.

A MORE PRECISE FORMULA FOR EACH PROPOSAL

Our two suggestions seem to involve this technical difficulty. As a firm's profits suddenly fall to below the critical 30 percent level, or as GNP falls below the critical 85 percent level, suddenly and discontinuously the payments of the Federal Government go from nothing to the first bracket rates. This might give rise to troublesome litigation concerning the last decimal point of profits and GNP, and might even occasion deliberate efforts on the part of firms to cause their profits to fall!

These bracket difficulties can be avoided by making our grants-in-aid formula or table slightly more complex.

Thus, just as the Government financial share grows from 10 to 20 percent as profits fall from a 30 percent level to a 25 percent level, so we might arrange for the Government's share to rise gradually to the first 10 percent level, corresponding to the gradual fall in profits from 35 to 30 percent. Our exact formula might be something like the following:

(a) When percent of corporate profits to normal are above 35 percent—no Government aid.

(b) When percent of corporate profits to normal are less than 10 percent—Government aid equal to 50 percent of cost.

(c) Anywhere in between these two extremes we suggest the formula :

Percent of Government aid equals 70 minus (2 times the percent profits are of normal). This could be written as an equation as follows: $G=70-2P$, in which G is the percent of government aid and P is the percent which current profits are of normal profits.

This will be found to agree with the earlier table, and to avoid all bracket difficulty.

Similarly, our second formula based on GNP too might be as follows :

(a) Percent of GNP to full employment GNP above 90 percent—no Government aid.

(b) Percent of GNP to full employment GNP below 80 percent—Government aid equal to 50 percent of cost.

(c) Anywhere in between, the formula :

Percent of Government aid equals 450 minus (5 times the percent of GNP to full employment GNP). This could be written as an equation as follows: $G'=450-5P'$, in which G' is the percent of Government aid, and P' is the percent which the current GNP is of a full employment GNP.

VARIOUS ASPECTS OF THE GOVERNMENT AID PROGRAM

The two alternative grant-in-aid procedures which we have outlined would have a number of advantages. They would leave to collective bargaining, or to the employer alone in the absence of collective bargaining, the choice of whether or not to set up a guaranteed wage. Under the procedures here suggested, if a guaranteed wage plan is set up, the responsibility would devolve wholly upon private enterprise so long as (a) profits equalled 35 percent of the preceding 5 years, or (b) alternatively the gross national product did not fall below 90 (85 in the cruder formula) percent of a full employment product. The responsibility of the Government, up to this point, would not relate to the guaranteed wage, but rather to policies and programs that promote high business activity and high employment. Thus up to the point indicated the Government would not enter the picture at all with respect to the guaranteed wage programs so far as direct grants-in-aid are concerned.

Should, however, the situation with respect to individual businesses, or alternatively with respect

to the economy as a whole, become serious, Government support in a variety of directions would sooner or later become necessary. Grants-in-aid for established guaranteed wage plans might well prove, in such circumstances, to be one measure which along with others might stop a deflationary spiral. There is increasingly general support for the thesis that early and vigorous support in many directions is less dangerous than delay, and is much to be preferred to risking all on any one policy. Reasonably early action may prevent a bad situation from getting worse.

Along with other antidepression measures, grants-in-aid to established guaranteed wage plans could help to put a cushion under a recession and prevent a further downward cumulative movement. The governmental grant-in-aid would involve the payment of funds into the income stream at a time when a Nation-wide depression is becoming really serious and needs to be stopped quickly and effectively. Planned public works and public development projects can play an important role, but many such projects cannot be timed quickly nor can they be adequate to check, without the aid of other measures, a cumulative downturn. What other programs may be necessary or desirable (including tax adjustment) is not a matter which properly comes under discussion here.

The plans discussed above would be automatically self-disciplinary. If the particular guaranteed wage plan introduced by an individual firm were overly cautious, it would be relatively ineffective. It would cost the firm very little, and by the same token, it would cost the Government very little; and it would not satisfy labor. If the plan were overly ambitious, it would be costly to the firm up to the point at which the governmental grant-in-aid would begin. This fact could be counted upon to deter the company from setting up too ambitious a plan. If the firm had failed to make good on its financial responsibilities under the plan, having dropped it entirely either in accordance with the terms of the plan or in violation of these terms, the Government would have no responsibility to undertake the grant-in-aid. Government support would be accorded only such plans as were actually in full operation at the point where grants-in-aid were scheduled to begin. As soon as the GNP again rose to a level above the

point indicated (or alternately profits rose) the Government support would cease.

On this basis every firm would know that any plan it might inaugurate would entail financial obligations to cover the entire cost of the guaranteed wage for its covered employees only under reasonably favorable conditions. In the event of a nation-wide depression, it could rely upon Government support. The business firm must indeed prepare a plan which could reasonably be expected to weather the storm up to the point at which governmental aid enters. And even then it must be prepared to carry its share of the load. With such guaranteed support, a firm could at least go farther both with respect to the proportion of its workers covered under the plan, and the percent of the full-time wage guaranteed under the plan, than would be the case without such support. How far each firm is willing and able to go, under these conditions, is for it to determine for itself, either on its own volition or on the basis of collective bargaining with the union representing its employees. There is no governmental compulsion. Any firm which objects to a guaranteed wage is quite free to go on without any plan. The governmental aid, available when conditions become difficult, is indeed an inducement, but it represents no compulsion whatever to set up a guaranteed wage plan.

It will be noted that both of the suggested plans are free of any element of unfair government wage subsidization of one producer as compared to his competitor. The Government contributes not a cent toward the wage of any worker who is to any degree productively employed.⁴¹ Only after the employer has declared a man completely unemployed would the Government's aid be forthcoming. We do not wish to spell out the details, but presumably such workers would be required to be registered with the unemployment insurance labor exchange, and would be required to accept suitable alternative employment. Also, as discussed in chapter VI, we suggest that unemployed workers should be eligible for regular unemployment compensation benefits, with the employer and govern-

⁴¹ It might be objected that an element of discrimination and inequity is involved in the respect that government aid to the maintenance of wage income is applied only to workers who happen to be employed by firms with a guaranteed wage. This, however, we should not regard as decisive. What is important is that firms be encouraged to introduce the guaranteed wage, and that all firms doing so shall be accorded equal treatment.

ment (under the guaranteed wage plan) making up the difference as specified in the guarantee.

To some extent these suggestions avoid the criticism that worker mobility will be adversely affected. The employer is still always left with an incentive—perhaps greater than that now existing under experience rating—to see that his laid-off workers accept suitable other employment. Nonetheless, we must expect that any system of almost 100-percent out-of-work compensation will weaken the employee's exertions to find another job and will make him more particular in accepting proffered alternative offers. This, however, is a basic difficulty of all guaranteed wages, whether completely privately financed or financed in part by the Government. Moreover, the loss of workers' incentives toward mobility is a much less serious economic problem at a time when there is widespread unemployment in all fields.

Since the Government comes in with financial aid when guaranteed workers are declared completely idle, there will always be some tendency for firms with guaranteed-wage plans to relax in their efforts to find low-productivity "fill-in" jobs for the workers to do in their own plants. As soon as the Government support came into operation, the costs incident to the guaranteed-wage plan in any firm would be carried in part by the Government and increasingly so as the depression deepened. There would thus be less incentive left for the firm to hold down costs by putting the largest possible number of covered employees to productive work or by securing work for them elsewhere. Nevertheless, there would always be some considerable incentive left, since the firm would cover at first all, then most, and finally at least 50 percent of, the cost.

The suggestion here made has the great merit that it could reasonably be expected that active full employment policies may be sufficiently successful so that the GNP would fall below 85 to 80 percent of the calculated "full employment" level only under relatively unusual circumstances, when the underlying factors were such as to threaten a really serious major depression. Under this suggestion one may hope that the Government guarantee would be invoked on any substantial scale only in periods of serious depression when vigorous measures to combat the downswing would, in any event, be necessary.

If the GNP has fallen below 80 percent of the "full employment level," the labor market would already be flooded with a large excess of applicants. Accordingly, from the social viewpoint, it would relieve the situation somewhat if the employees covered in guaranteed wage plans did not come on the market at all. Moreover, it might not help the general situation, under conditions of falling and low aggregate demand, for firms having guaranteed wage plans to enter the market with competing sidelines to give productive employment to some of their covered workers. Such action, in a period when total demand was sharply restricted, would contribute little, if at all, toward an expansion of aggregate demand. In such periods, taking on new lines by one firm probably supplants jobs elsewhere rather than adding to the total. In contrast, in periods of brisk demand and full employment, the elimination of seasonal and frictional unemployment would represent a net gain in social efficiency and total real income. If all workers were given steadier employment throughout the year, there would be a net gain in total output and total real income.

Neither the payment of compensatory supplements to farmers nor the payment of wages to idle workers covered by guaranteed wage plans represent the ideal situation. The ideal situation is one of sustained aggregate demand and full or high employment. But if, in fact, full employment policies prove to be only partially effective; or if wholly abnormal and unexpected factors emerge which cannot, in the short run, be coped with adequately, then compensatory payments to farmers and wage payments to covered workers under guaranteed wage plans may be valid, justifiable and helpful under the circumstances. The situation is a temporary one in which unusual and rather drastic measures may become necessary.

Financial aid to guaranteed wage plans is one channel of depression Government spending. In terms of the encroachment of Government activity on the private sector of the economy, it is a relatively conservative measure, since it involves only "transfer payments" to individuals, who in turn spend this money as they wish on the products of private industry. Thus, it is neither competitive with private industry nor "socialistic" in the

sense of expanding the productive or collective consumption role of Government.

The problem is one of spending wisely, effectively, and equitably. Giving one favored group of workers 100-percent unemployment insurance while others receive limited partial benefits for a limited time, or no insurance benefits at all but only relief, cannot be defended as equity. From this point of view it might well be desirable to confine Government aid to plans with some sort of time limitation with respect to the period in which any one worker could continue to draw guaranteed wage payments. As a first line of defense against depression, relatively generous treatment of certain workers for a limited period can be defended. But it would be more important still to strengthen our general social security, relief, and public works and development programs during the next serious depression. In the final analysis, productive and useful employment should be the goal.

The primary purpose of the suggestions described is to contribute in some measure to the general insurance against the social plague of deep depression. These suggestions, like all insurance measures, would serve their purpose best if it never became necessary to invoke them—if the system always remained at high levels of employment and general profits did not decline to low levels as a result of adverse business conditions.

To conclude: An adequate full employment program would make governmental grants-in-aid to guaranteed wages quite irrelevant as an anti-depression device. But in the event, as is not improbable, that we shall at times face rather serious unemployment, such grants-in-aid could be a useful "last resort" instrument, to be applied along with other measures as one part of a many-sided antidepression program. But while it is necessary to be prepared with antidepression policies, we must never lose sight of the positive program designed to provide continuing and high levels of useful and productive employment. Guaranteed wage plans are not adequate substitutes for other public and private economic policies, even though they may provide supplementary protection against instability of production, employment and income.

SUBADDENDUM—COMMENTS ON THE HANSEN-SAMUELSON REPORT

By Prof. J. M. CLARK, Columbia University; Prof. EDWARD S. MASON, Harvard University; Prof. SUMNER H. SLICHTER, Harvard University, together with Final Comments by Professors HANSEN and SAMUELSON

1. COMMENTS BY J. M. CLARK

In general, the writer is in hearty agreement with the actual recommendations of the report, and approves of their cautious and realistic character. He has, however, a feeling that in the body of the discussion this caution is not always fully maintained; and here and there, by tone and implication, an impression is conveyed of promise of greater results, both in extent of voluntary adoption and in effect on stabilization of employment, than are wholly consistent with the cautious character of the actual recommendations. The frequent qualifications which are introduced do not entirely offset this optimistic impression. A few major and minor comments follow.

Perhaps the chief aspect which seems insufficiently recognized is the probability that if a guaranteed-wage plan were installed, covering all or most of the employees in an industry, the hiring of additional workers might involve such a heavy commitment on the part of the employer that he would go slow about such hiring in times of active demand, with the result that employment might not simply be stabilized, but the total reduced. This would place a heavier burden on the high-employment program which, it is assumed, goes with the wage program. It might be replied that, since the wage program is voluntary, employers would not be likely to undertake commitments so heavy as to have this effect. This seems not fully convincing, since the pressure of organized labor toward such programs may be very strong, and may even develop quasicompulsory effects, impelling employers toward assuming heavier commitments than caution would dictate, in the light of the possibility here considered.

A second point is that, in view of the voluntary nature of the proposals, more attention might be given to modified plans, even if they may not so far have been proposed by interested parties. For example, it might be regarded as a defect of a simple guarantee from the standpoint of workers' incentives, that under it the worker would get paid no more for working the guaranteed amount of time than for working less. This could be avoided, and the employer's commitment be at the same time lightened, by a plan under which the worker would be paid full wages for full-time work, and something less though presumably more than half wages for idle time, down to some absolute minimum. The guarantee should properly be so figured as to give the worker something more than his unemployment benefits under social security, but less than full pay for idle time. This would avoid asking him, in effect, to work part of the time for nothing.

Methods of financing reserves deserve more discussion than is given them. In voluntary private plans, the employer would be under strong pressure to invest them productively, in private securities. Then when they had to be drawn on, in bad times, if these securities were thrown on the market in order to realize funds, the effect might be to accentuate depression, offsetting the alleviating effects of the distribution of the proceeds to the workers. This dilemma seems to deserve consideration; it might be avoided by some credit arrangement.

A fourth point concerns the effect of stabilization on the productivity of workers. Here I agree with the general conclusion that the net effect is likely to be favorable, and my reservation is largely concerned with the timing of the effect. Experience seems to show that when bad times threaten, workers work harder, and increase their output. It is when a lay-off does not immediately impend

that workers are urged to make their jobs last as long as possible, by restraining output. This is complicated by the effect of reduced output in increasing indirect costs per unit produced, so that total labor cost per unit of product may rise, or output per man-hour fall, on account of this latter factor, which has nothing to do with the attitude of the workers, or how well they work. Dr. Julius Hirsch, in a paper delivered before the American Economic Association, January 25, 1947, attempted to separate these two effects on productivity, and found that the kind that registers the efficiency of the workers behaved in the way I have indicated.

A fifth point concerns the incentive the employer has to make capital outlays in slack times, because of the lower prices then available. This is an incentive which must, in the nature of the case, stop far short of full stabilization, since it is only if demand is slack that prices are likely to come down. A single industry could get this gain, in an economy where the rest were still following the usual practice and concentrating their capital outlays in active times. But if capital-expansion in dull times became the standard practice, the price-incentive would be destroyed. Further, it is still true that, the longer the employer waits, before a revival is expected, the shorter is the time during which his capital is tied up, idle, and the risk he runs of installing equipment that does not embody the latest improvements. Therefore, this incentive seems to be subject to a much heavier discount than is indicated in the report.

The incentives of the employer, arising from the combination of a guaranteed wage with social security, seem to deserve some analysis. It seems to be implied that the employer could, at his option, limit his liability to the excess of the guaranteed wage above the regular unemployment-benefits, by declaring his worker unemployed, and leaving him to find another job if one is offered. It appears that this would, in practice, involve him in little likelihood of losing a worker through the worker's getting another job, because it seems only natural that the employment office would give priority to job-seekers who were not covered by guaranteed-wage plans—this on the assumption that such plans are voluntary, and have not become universal. Then if social security pays the worker, for example, 55 percent of his regular

wages, it would pay the employer to let his worker go onto social security if the only work the employer could find for him to do were worth less than 55 percent of full wages. If it were worth more, it would pay the employer to keep him.

In this connection, the discussion of the loss, or cost, of unemployment, gives the impression that it is the worker's full wage, or its equivalent, that is lost, though elsewhere it is noted that the best employment that is available in depressed times is likely to be something that is not worth the full amount of the standard wage.

Other minor points might be mentioned. The report suggests the maintenance of adequate total demand as a goal, and takes the position that a fair approach to attainment of this goal is a prerequisite to any general successful adoption of guaranteed-wage plans. But no ways and means are suggested for a full employment program nor is any estimate made of the probable degree of success of any measures of the sort which might be adopted. This is perhaps a matter in the purview of the President's committee of advisers, set up under the Full Employment Act; but this committee does not seem as yet to have filled this gap.

In chapter II, section 1, the report states: "It is perhaps not too hard to imagine an economic system in which the wage contract with all employees was more nearly like that with executives and white-collar workers than like the present prevailing mode of wage payment and tenure." I agree that present modes of wage payment show a remarkable lack of imaginative adaptation to the facts of modern industry. But if this means that all workers could be put on a basis of fixed salary, it is hard for me to imagine this under a system of private enterprise, in view of what seems to be the admitted fact that private enterprise is inescapably subject to some degree of fluctuation, and probably a fairly substantial degree, even with the best that can be done toward stabilization. It is easier for me to imagine a system of cooperatives in which the workers are their own employers, and hire capital for a fixed return; but in that case they would necessarily take the risks that now fall on equity capital. Their salaries might be fixed, but they would be combined with sharing of profits and losses.

In conclusion, let me repeat that the actual recommendations of the report appear to deserve approval.

2. COMMENTS BY EDWARD S. MASON

Messrs. Hansen and Samuelson rightly emphasize the wide range of variation in types of guaranteed wage plans, and in employee coverage and employer commitments involved. Taking this range into account it is possible to conceive a situation in which guaranteed wage plans would be widely used without any appreciable effect on worker security or on the functioning of the economy. This would be so if the only workers covered were those the employer could reasonably expect to retain at the lowest expected rate of operations, and if his commitment were subject to frequent revision. Under these circumstances the acceptance of the plan would offer no special inducement to the employer to explore ways and means of stabilizing employment; it would offer no appreciable increase in the employees' security of tenure; and it is difficult to see how it would in any way significantly alter work incentives, income distribution, or, in general, the functioning of the economy. Even a wide acceptance of such guaranteed wage plans would have the same negligible effect as minimum-wage-rate legislation setting rates substantially below the market minimum.

The problem becomes interesting and important only if plans are adopted committing the employer to wage payments he would not otherwise assume and offering a greater measure of security to employees than they would otherwise enjoy. Under what circumstances would the employer be likely voluntarily to accept such a commitment? A guaranteed wage plan might be adopted if it promised to give the employer the pick of the labor market, if it were judged to offer new and important work incentives, and if possibilities existed for lessening the disadvantages of a new overhead commitment by stabilizing operations through diversification or otherwise.

These are all real possibilities. But it must be recognized (*a*) that the advantages of the plan depend largely on its not being extensively adopted by competitors in the labor market, and (*b*) that the stabilization effects are mainly limited to the firm and have no appreciable ad-

vantages for business cycle stability in the whole economy. If all—or even a large number of—employers accepted additional commitments under guaranteed wage plans in the expectation that their selection of employees would be improved or that their operations could be stabilized by diversification, the expectations of a large percentage would be unavoidably disappointed. It must also be recognized that the advantages of a guaranteed wage plan, which may be real enough as long as the number of such plans is small, may create additional disadvantages for the firms not adapting to the scheme.

Some possibilities for improving efficiency or stabilizing employment, which are net for the economy as a whole, may exist, but these possibilities would seem to be slight. It is possible that the productivity of workers already employed may be increased by the additional security offered by a guaranteed wage plan. Hansen and Samuelson consider this possibility and, in my view, rightly discount its certainty or quantitative importance. There is also the possibility that the adoption of guaranteed wage plans might lead to the merging of operations which are complementary over time (e. g., coal and ice). Although this would make no contribution to over-all business cycle stability, it might lessen the number of necessary changes in employment. Again, however, the main effects of diversification by particular firms might often be to increase the instability of operations of other firms. All this is simply an elaboration of the point that the main influences on stability for the whole economy lie outside the control of single firms.

Recognizing this fact, the authors raise the question whether it is possible for employers in unstable industries by acting together to contribute to stability. Although this might be done independently of guaranteed wage plans, it is possible that the common introduction of such plans in an industry could provide an incentive for stabilization otherwise lacking. The question is whether the causes of instability lying outside the control of individual firms may be to some extent within the control of an industry acting as a unit. Commenting on the notorious instability of employment and output in the automobile industry, Hansen and Samuelson emphasize that, to the extent that this instability is cyclical, the search for

remedies must look in other directions than toward guaranteed wage plans. "But," they say, "it is not too much to hope for, and to ask of management and labor, that measures be taken and practices be altered to moderate the incidence of irregular and seasonal employment and of economic idleness. This may require many far-sweeping changes in the organization of the industry; increases in inventories and storage facilities, limitations on undue coddling of consumers' desires with respect to modification of style and model changes, perhaps acceptance of lower hourly wage rates in exchange for higher annual earnings."

It is possible that action of this sort might make a substantial contribution to stability of employment in automobile production. It is probable that the suggested changes would increase costs and prices to consumers. It seems to me unlikely that standardization, for example, could be brought about without collusive action or a degree of cooperation among competitors beyond the limits permitted by present public policy. Perhaps existing policy should be changed. But this question raises issues of considerably greater importance than those involved in guaranteed wage plans. It seems doubtful whether the stabilization possibilities lying outside the control of individual firms, but within the control of the industry, are of sufficient importance, in themselves, to justify the degree of industry planning—with the concomitant necessity of Government supervision—it would be necessary to achieve in order to realize these possibilities. In any case the question opens vistas too broad for adequate consideration here.

If the scope of guaranteed wage plans is primarily determined by profit considerations and if industry-wide stabilization operations (which might broaden the opportunities for such plans) are excluded, it does not seem probable that a system of wage guarantees will be widely adopted, at least in an economy as unstable as the American economy has historically been. Yet the most important and interesting questions that Hansen and Samuelson discuss assume a substantial coverage of the economy by guaranteed wage plans. It is possible that, if accompanied by effective counter-cyclical stabilization measures, the cover-

age of wage guarantees would in fact be substantially increased. This will be discussed presently. The important questions referred to above have to do with the changes in aggregate demand and its stabilization over the cycle and with the effect of the increase in overhead costs involved in guaranteed wage plans on pricing policy.

With respect to the first question, the authors point out that the level of aggregate demand is not likely to be raised by guarantee of wages unless such guarantees transfer incomes from profits to wages and unless these transfers increase marginal propensities to consume. They are properly dubious about such effects. Even if wage guarantees clearly worked in this direction, it would still be difficult to see why employers would voluntarily accede to them unless we suppose a general understanding and agreement among businessmen that their own long-run best interests are served by the higher and more stable level of employment that the acceptance of a lower rate of profit might be supposed to entail. It seems probable that the "Keynesian revolution" has not yet been this successful.

The effect of guaranteed wages as a stabilizer of aggregate demand over the cycle depends primarily on the method of financing. If reserves accumulated in good times are paid out in bad, some stabilizing effect will be produced. But unless firms can be supposed to undertake commitments of a character and magnitude that would substantially increase business risks this effect is bound to be small. The authors recognize this fully and their tentative support, in the appendix, of Government grants-in-aid to guaranteed wage plans, stems from this recognition. In part the case for grants-in-aid depends on the expanded coverage by guaranteed wage plans that might be expected to follow from the adoption of grants; in part, the case rests in the familiar argument for deficit spending in depression. To the extent that deficit spending is the remedy, this type of spending has to be justified as against other claimants. The main advantage, stressed by Hansen and Samuelson—though not in these words—is that it can be "built in" to a functioning economic system rather than being hastily improvised as so many kinds of Government depression spending are. Although a number of practical difficulties (having to do mainly with inequality of treatment of

different firms and industries) are obvious, the suggestion merits careful attention.

With respect to the consequences of guaranteed wage plans for price behavior, the conclusion of the authors appears to be that the conversion of variable into overhead costs would probably have only a slight effect. While this conversion might, under competitive pricing conditions, be expected to lead to greater variation in prices over the cycle, they think that, in industries likely to adopt guaranteed wage plans, market structures are such as to favor the use of "full cost" pricing policies. If, therefore, it can be shown that such plans increase the "full cost" per unit of operations over the cycle, the effect on prices might be considerable. Regardless of the extent to which firms may or may not undertake full cost pricing, it is clear that any substantial increase in the relative importance of overhead costs will accentuate the danger to profits to be expected from competitive price cutting. The tendency to stabilize prices, by agreement or otherwise, will thereby be encouraged. Insofar as the effects are limited to an increased resistance to price declines in depression, the writer would agree with Hansen and Samuelson that the weight of modern opinion considers such effects to be contributory to stability in the whole economy. If "cooperation" among competitors is seriously promoted through a widespread adoption of guaranteed wage plans, it is improbable, however, that joint action would be limited to resistance against depression price declines. It is clearly possible that the substantial conversion of variable into overhead cost inherent in these plans might, through the increased incentives it offers to industry-wide planning, considerably reduce the scope of desirable competitive adjustment in the economy. It must be admitted, however, that this question is highly speculative.

It is the view of the authors of this report that guaranteed wage plans are unlikely to play a significant role except within the framework of an effective national policy directed toward the maintenance of a high level of employment. In the unstable American economy of the recent past, the advantages to the employer of lay-offs on short notice are of such importance as to make it improbable that more than a small number of firms will adopt such plans. Furthermore, as already emphasized, the advantage of these plans to the firms

adopting them are likely to be substantial only if the number remains small.

If an effective national employment policy can be assumed, the situation is different. Even under these circumstances, however, the authors caution against exaggerating the merits of a guaranteed wage program. They state explicitly that "if it ever had to come to a choice between guaranteed wages and other important depression and anti-cyclical public and private policies, * * * then it would be guaranteed wages that would have to be rejected." It is a great strength of the report, in the eyes of this reviewer, that the relative merits of guaranteed wages as against other reform programs are carefully weighed. In a situation in which the stimulus to reform is strictly limited it is important to establish a carefully considered priority of objectives.

If a high level of employment were expected to be maintained the coverage of voluntarily initiated guaranteed wage plans might, for a number of reasons, be very substantial. A much larger number of firms could apply such plans to a much larger percentage of their employees without an appreciable increase in business risk. Employers, faced with a continually serious problem of recruiting and maintaining a labor force would find that the relative merit of guaranteed wage plans as compared with the privilege of lay-off at short notice had measurably increased. Although the authors find, even in the recent past, little evidence that instability of employment is compensated by higher hourly earnings in unstable industries, it might be expected that with a high and sustained level of employment this condition would be rectified by competitive forces. If this were so, firms, even in unstable industries, would probably find it possible to adopt guaranteed wage plans without incurring a large increase in labor costs.

On the other hand, although the coverage might be much larger, the importance of worker insecurity under such circumstances would be much less. The authors, nevertheless, believe that guaranteed wages might make an important contribution to stabilizing "seasonal and other short rhythms in production and by equitably allocating the economic burden of the residual amount of unavoidable idleness and unemployment." By shifting the burden of seasonal and short-term unemployment to the shoulders of employers, the

incentive to integrate operations having complementary time periods and to undertake industry-wide planning to increase stability of output would certainly be increased.

As we have seen, there are real disadvantages involved in this process that must be set off against the advantages. In addition the substantial lessening or disappearance of worker incentives to seek other employment during slack periods would handicap short-term adjustment. As so often is the case in the area of economic policy, there seems to be a real conflict between security and efficiency involved in this question of guaranteed wages. It is not obvious to the writer that, even if the maintenance of a high level of employment could be assumed, the probable disadvantages of a large-scale acceptance of guaranteed wages would not outweigh the advantages.

3. COMMENTS BY SUMNER H. SLICHTER

The guaranteed wage is a proposal to impose an additional liability upon business owners. Although the proposals vary substantially, they have one common characteristic—the liability to pay for labor which would not otherwise be used is one which would have to be met in the main, not in periods of expansion and optimism, but in periods of contraction and pessimism. Furthermore, the amount of the liability in most industries would be conjectural in the extreme because the severity of business cycles cannot be foreseen. This second characteristic could be altered somewhat by modifications in the plans. In fact some existing wage or employment guarantee plans provide ways for reducing the employer's liability in the event of severe depression. Finally, the liability is of such nature that it is increased in amount by the very conditions which decrease the business enterprise's ability to meet it out of current income.

Hansen and Samuelson consider two types of plans: (1) Pay-as-you-go plans, and (2) reserve plans in which, however, the liability is not limited to the amount in the reserve funds. I believe that a third type of plan should be examined, namely reserve plans with liability limited to the amount in the reserve fund. Hansen and Samuelson make a suggestion closely akin to this in their recommendations. They suggest that the liability of employers be limited. They do not, however, sug-

gest that it be limited to the amount in the reserve funds.

Three basic questions are raised by wage guarantee plans: (1) Their effect upon the distribution of income; (2) their effect upon the utilization of resources; and (3) their effect upon the business cycle and the growth of industry. In general I agree with Hansen and Samuelson with respect to the effect of wage guarantees upon the distribution of income and the utilization of resources. With much of their analysis of the cyclical effects of wage guarantees I am in agreement. There are, however, some points of difference. Consequently, I have confined these notes to a discussion of the cyclical effects of wage guarantee plans.

Before I start this discussion I wish to call attention to the fact that wage guarantee plans would require during boom times a larger spread than would otherwise exist between the price of labor and the prices of goods. This would be necessary because of the risk that employers would be compelled during slack periods to make wage payments which are not covered by the value of the services rendered. The greater spread between wages and prices during boom times might be accomplished either by a rise in prices or by a slower rise in wages. It is uncertain which of these ways would be more important in bringing about the greater spread between wages and prices. If one assumes that the amplitude of boom and depression is unchanged, the distribution of income over the period of the whole cycle would not be significantly changed. Wage earners and consumers would fare worse than now during boom periods and better than now during depressions; business owners would fare better than now during booms and worse during depressions.

Pay-as-you-go wage guarantees

Pay-as-you-go wage guarantees would accentuate business recessions. This result would occur for several reasons. One effect of pay-as-you-go plans would be to stimulate managements to strengthen the liquid position of their enterprises at the first signs of contraction in business. Business concerns, of course, now do the same thing—especially enterprises which have short-term debts or other important liabilities to meet. The very efforts of business concerns to protect themselves against the drop in business aggravate the decline.

The pursuit of liquidity by enterprises during periods of contraction ought to be discouraged rather than encouraged. Pay-as-you-go wage guarantee plans, however, would encourage it. All of this amounts to saying that most pay-as-you-go plans could not be kept strictly on a pay-as-you-go basis. Even if assets were not earmarked and called "reserve funds," they would be accumulated against the liability imposed by the wage guarantee plans. Furthermore, under the so-called "pay-as-you-go plan," the accumulation would occur just when it would do the most harm.

A second effect of wage guarantees (whether pay-as-you-go or not) would be to make cost-price relationships during depressions more unfavorable than they would be in the absence of guaranteed wages. Since workers would have to be paid whether they produced or not, managements would be willing to produce goods which have to be sold at prices which would not cover cost of production computed by conventional methods. Hence wage guarantees would depress prices and make prices even lower relative to costs than they would otherwise be. The effects of wage guarantees upon production would not probably be very great in oligopolistic industries. It would, however, be an important influence in industries where there are many small competitors, particularly the "soft goods" industries.

The unfavorable cost-price relationships thus produced by wage guarantees and the resulting drain on liquid assets would put managements under greater pressure than ever to cut expenditures for maintenance, replacement, research, and product development. It would also discourage the starting of new enterprises. Even in severe depressions there are many thousands of business births each year and substantial expenditures on capital goods for replacement, reduction of costs, and expansion by established enterprises.

Special mention should be made of the effect of pay-as-you-go plans upon the operation of the credit system during depressions. The liabilities imposed by these plans would make banks more eager to reduce outstanding credits to enterprises subject to the liability and less inclined to extend new credits. Thus, pay-as-you-go plans would be a powerful influence in enforcing a contraction in demand deposits.

The effect of pay-as-you-go plans upon the demand for labor and upon wages would be unfavorable. Naturally enterprises which had wage guarantee plans that were about to expire would seek to anticipate their orders for goods after the expiration of the plans by making large quantities of goods before the expiration of the plans. Thus plans which were about to expire would build up inventories of partly manufactured and manufactured goods that would prove troublesome. Certainly the fact that this process was going on and that inventories were overhanging the market would discourage both the starting of new enterprises and the execution of many projects by existing concerns. The fact that employers who had built up large inventories under the stimulus of wage guarantees would be in an unusually strong bargaining position in negotiating renewals of their contracts with unions would introduce uncertainty into the whole wage structure of the industries affected.

These several difficulties might not be serious if the depression were mild, but the existence of a large number of pay-as-you-go plans would increase the difficulty of keeping depressions mild. If the depression were severe, pay-as-you-go wage guarantee plans would appear to be well designed to make it more severe and to weaken the bargaining position of unions in renewing contracts which expire during the depression.

Wage guarantee plans with liability not limited to the amount in the reserve funds

Wage guarantee plans financed out of reserve funds but with the liability not limited to the amounts in the reserve might mitigate depressions provided business managers felt quite confident that the depression would be mild and that the reserve funds would be more than adequate. The disbursement of the reserve funds by raising the propensity to consume would limit the effect of a given drop in investment upon incomes and upon employment. Furthermore, if businessmen were quite sure that reserve funds would be more than adequate, the disbursement of the funds would make managements less inclined to cut postponable expenditures, such as outlays for maintenance and replacements and some expenditures for expansion.

All of the above assumes that managements are governed by the belief that reserve funds would

be ample. This would certainly not be true in severe or even moderately severe depressions. As it became apparent that the depression was going to be deeper than businessmen had anticipated, wage guarantee plans financed out of reserve funds would produce more and more the same unfortunate effects as pay-as-you-go plans. Furthermore, even in mild depressions wage guarantee plans with the liability of employers not limited to the amount in the reserve funds would produce some unfavorable effects. Some firms would be new and would have had no opportunity to accumulate reserve funds; some would have had a bad employment record. Hence, at least a few firms would be led by their liabilities under wage guarantees to strive for greater liquidity than they would otherwise have sought. Many more firms, as a result of their liabilities, would be viewed as unattractive credit risks by banks and would be forced by the reduction of their lines of credit to curtail expenditures on maintenance and replacements and possibly to liquidate inventories at distress prices.

Reserves with liability limited to the amount in the reserves

Guaranteed wage plans financed by reserves and with the employer's liability limited to the amount in the reserves would make a moderate, but nevertheless important, contribution to the stabilization of employment. The limitation of the employer's liability to the amount in the reserve fund would prevent the wage guarantee from stimulating employers to attempt to increase their liquid assets during periods of contraction. Thus wage guarantee plans of this third type would not have unfavorable effects upon the expenditures of business concerns for maintenance, replacements, and expansion. On the contrary, the reserves would have two favorable effects upon the level of employment. First, by increasing the propensity to consume it would diminish the unfavorable effect of a given drop in investment upon income and hence upon employment. Second, by limiting the losses of business enterprises and improving the terms on which they could liquidate their inventories, the disbursement of the reserve funds would make managements less inclined to cut expenditures on maintenance and replacements and to suspend the execution of plans for expansion.

Would not the favorable effects of the disbursement of reserves during periods of contraction be offset by deflationary effects from the accumulation of reserves during periods of expansion? I do not think so. In the first place, favorable effects of the disbursements of reserves during periods of depression would cause prospective investors to take a slightly more favorable view of investment opportunities. In the second place, the accumulation of reserves would make investment-seeking funds available on slightly more favorable terms.

Would not the accumulation of reserves during periods of expansion limit expansion by raising the propensity to save? There are some major uncertainties in the effect of the accumulation of reserves during periods of expansion. It is quite conceivable, as I shall point out presently, that the accumulation of reserves would have inflationary repercussions on the credit system. More likely is the possibility that the accumulation of reserves would modify the character of booms by limiting the expansion of credit and the rise in prices. Booms are periods when incomes rise because the planned savings of individuals and business enterprises fail to meet the demand for investment-seeking funds. The impatient demand for investment-seeking funds causes the rise of income to be accelerated by the expansion of credit and usually by a rise in prices and often by speculation in inventories. The rise in prices limits the favorable effect upon employment from a given rise in expenditures. Furthermore, after this type of expansion has gone on for some time, it creates market conditions which discourage business enterprises from immediately executing long-term investment plans. Hence the nature of booms under the modern credit system limits the capacity of the economy to utilize investment opportunities created by technological change. Were expansions financed to some extent out of reserve funds rather than by the expansion of credit, the expansion would probably go farther and the expansion would consist to a greater extent in a rise in employment and to a lesser extent in a rise in prices. Hence, although the effect of the accumulation of reserve funds would be deflationary in terms of prices, it would not necessarily be deflationary in terms of employment.

There is a real possibility, however, that the accumulation of reserve funds will stimulate the expansion of credit. The reserve funds would undoubtedly be invested largely in the short-term obligations of the Government. The buying of these obligations by the reserve funds would interfere with the ability of the banks to maintain the volume of their investments in short-term governments. At times when the business outlook is regarded as favorable, banks are averse to permitting a drop in their earning assets. Hence, failure of banks to replace their short-term governments would undoubtedly lead them to be more enterprising and aggressive in putting money to work in commercial loans and term loans. As an aftermath to the unfortunate inflationary effects of the expansion of bank credit during the boom, would be the even more unfortunate deflationary effects produced by the repayment of these loans in periods of contraction.

This analysis of the probable effects of different types of wage guarantees should not be concluded without pointing out that the judgment of the probable effects of the plan must be predicated upon estimates of the number of workers whom such plans may cover and to whom they might make an important difference. About one-fourth of the workforce would not be included because they are self-employed rather than employees. A substantial proportion of the workforce, even if covered, would get no appreciable benefit from guaranteed wage plans because they are virtually assured of indefinite tenure under present conditions. These include nearly all employees in the public service, a substantial number of employees in the industries and occupations with little seasonal or cyclical fluctuations, and a substantial number of additional employees who are protected from seasonal or cyclical lay-offs because of seniority rules. A third large group of employees work under conditions which would make a 12 months' guarantee (or even a 6 months' and, in many cases, a 3 months' guarantee) impractical. These include people in intermittent employments such as most people in the construction industry, the amusement industry, the vacation industry, and the large number of people who enter the labor market for a few weeks only during each year. As a very rough guess I

would estimate that about one-fifth or one-fourth of the entire workforce are employed under such conditions that a guarantee would appreciably affect their annual income. This does not mean a guarantee might not be a useful device in the case of this fraction of the workforce. Nevertheless, it does indicate, however, that the possible favorable effects upon the total volume of consumer income from all sources would be quite limited. At the best, the incomes of people receiving only about one-sixth of all consumer incomes would be directly augmented to an appreciable extent by an annual wage guarantee.

4. FINAL COMMENTS

By ALVIN H. HANSEN and PAUL A. SAMUELSON

The comments of Professors Clark, Mason, and Slichter are particularly welcome and valuable because the complex imponderable factors involved in an economic evaluation of guaranteed wages cannot definitively be appraised by one team of investigators. Accordingly, we wish to confine our reaction to their comments to a few of the more important points where there still remain some substantive difference in analysis and emphasis.

1. *Depressant effects upon investment due to higher wage costs.*—All three writers emphasize—as we do too (pp. 29–31)—that guaranteed wage commitments may act as an appreciable deterrent to business investment. Taken by itself, this is a damning consideration. But it should not be taken by itself, since there may also be a favorable effect upon income when wages are maintained.

There is a universal dilemma to be faced here, which goes far beyond the guaranteed wage. Compulsory workmen's compensation legislation, minimum wages and conditions of work, collective bargaining and pressure for higher wages, social security legislation—all of these can be thought of simply as a hampering drag upon "venture capital." But they each also have favorable aspects from the standpoint of social and individual welfare, equity, and income maintenance. Realistically, they are probably here to stay; our private enterprise system cannot shirk their challenge. Nor, taking the long view, is it likely that it can hold the line against their further extension over future decades.

Fortunately, the trend of economists' opinions over the last two decades does not appear to be definitely toward the view that the favorable income and purchasing power side of the wage question is overbalanced by the unfavorable investment effects. But to discuss this further would take us far afield.

2. *Anticyclical effects of reserve financing.*—Because of our stated belief that all reserve funds should be invested in Government bonds or equivalents, and because it is now definitely unfashionable to invest pension funds in the private securities of the employing company, we did not feel it necessary to discuss the problems raised by such private modes of financing. High-grade Government bonds tend to go to a premium in bad times. For this reason, and because the Federal Reserve authorities have ample powers to stabilize their marketability, such securities offer the ideal medium for reserve financing.

Professor Slichter expresses concern that guaranteed wage reserve funds will purchase Government securities at the expense of the banking system; in the process excess reserves would be created; thereby private loan expansion would be encouraged. This represents an instance of our statement (p. 33) that the deflationary impact of boom-time reserve accumulation may be partially offset by an easing of interest rates and capital availability. At worst, this could only be a partial offset: Partial because interest rates weaken only in consequence of a final decline in total income. Even this partial perversity can be easily offset by having the Federal Reserve authorities do what they always should do with respect to actual or potential excess reserves during inflationary boom times.

We cannot wholly acquiesce in Professor Slichter's appraisal of the absence of deflationary influences resulting from boom-time reserve accumulations. The reasoning of his preceding paragraph seems to hold that an increase of cor-

porate saving—for that is precisely what reserve financing means—is, by itself, an “expansionary” factor. In our view it could be so only in the following inverted sense: A deliberate deflationary policy which successfully offsets an inflationary boom-time situation may prolong the duration of prosperity and full employment. Only in this sense, could a “deflationary” policy be “expansionary”; and this does not deny its deflationary character or differ with the accepted view that reserve financing is anticyclical. Moreover, only in those special boom periods where employment and purchasing power tend to be “more than full,” would such a deflationary policy be desirable.

During depressions, replacement expenditures of corporations often fall below depreciation charges; they often fall by more than the total of corporation losses. Consequently, there is a “run-off” on fixed assets which will to some degree moderate the need of the corporation to rely completely upon previously funded reserves. Guaranteed wages may also be paid at the expense of depression dividends. But as we pointed out (on p. 29), in the absence of funded reserves, there may still be some harmful effects of guaranteed wage payments upon the ability of the firm to maintain some of its depression gross investment, and this is in line with Professor Slichter's discussion.

3. *Guaranteed wage plans with alternative limitations.*—Professor Clark (p. 53) and Professor Slichter (p. 60) have each suggested a modified guaranteed wage plan. There are an infinite range of such programs and it is useful to explore a variety of possibilities. In our Report we have suggested the need in many fields of some limitation upon employers' guaranteed wage liabilities. In particular our recommendation No. 2 in chapter VI suggested the advisability of the type of limitation of liability developed in Mr. Latimer's final report (whereby the liability of any employer in a given period is limited to some agreed-upon percentage of his total guaranteed pay roll).