

power. This increase is not accompanied by a parallel development in the consuming power of the masses, since their share of the general income is too small. Consequently this process inevitably leads to a crisis, market stagnation, unemployment, the ruin of numbers of undertakings, and general poverty. Every great depression shows this tragic economic contradiction of excessive production and unsatisfied needs. There is a plethora of clothing and food, and yet the people are starving and in tatters. In short, under-consumption is the fundamental disequilibrium between productive capacity and purchasing power that results from maldistribution of the income of any community. Excessive saving is none the less real for being purely relative: there is too much capital because there is too little consumption, and *vice versa*. This is the essential part of the theory, which has remained unchanged since it was first enunciated.

It should be noted here that the theory of under-consumption is not the same as the theory of over-production, which at first sight might appear to be another aspect of the same thing. The latter is a complex conception differing from the former; over-production is taken to mean the inability of undertakings to sell their products at prices which will cover the cost of production. The theory under consideration in this article is both wider in its scope and less clearly defined in its outlines; it embraces the whole economic and social structure of society. It is true that it would be possible to find very limited cases of under-consumption. For instance, there is under-consumption when demand falls and supply remains constant, or at least when demand falls more than supply. There would be over-production in the strict sense of the term if supply increased and demand remained constant, or if the rise in supply were more rapid than the rise in demand. From this point of view cyclical depressions offer numerous examples of under-consumption of particular commodities, due to fluctuations in profits and wages which lead to a drop in the demand for certain products.

The general theory of under-consumption has been severely criticised. A frequent point of attack has been the disagreement between the theory and the facts of the economic cycle, at least during the periods of recovery and boom which make up the prosperity phase of the cycle. More than one economist holds that during these periods consumption outstrips and exceeds production, so that there would be not a constant deficiency of purchasing power as compared with

productive capacity, but alternate deficiency and excess. This alternation could be explained by the very natural difficulty of establishing an exact and constant balance between supply and demand, in view of the roundabout nature of production under the capitalist system and the consequent importance of forecasting, which is always open to error. In that view there is really no social question involved. The inequality in incomes—corresponding to an inequality in services rendered—could not really be held responsible for the sufferings caused by the crisis and the depression, which should rather be considered as an inevitable consequence of the extreme complexity of modern economic life. This controversy cannot be settled without a consideration of the facts, or, to speak more precisely, without a study of the whole course of the economic cycle.

The cycle begins with an increase in business activity of varying magnitude, intensity, and duration. This movement is possible only when several conditions are simultaneously fulfilled. One of these is a certain abundance of available capital. This actually exists and is shown to exist by the low interest rates. The available capital is generally in the form of fiduciary currency: notes or sight deposits, both of which constitute credits payable on demand by the banks. The cover for this available capital must also be very considerable, so as to permit a possible simultaneous extension of bank credits.⁴ It has been argued that at the beginning of the period of increasing activity there is no very large amount of savings available in liquid form. The fact, however, is certain. What happens is that notes are hoarded, and above all that relatively large sums are invested temporarily in the form of deposit accounts subject to cheque. The revival of trade gradually brings these sums into circulation. This does not mean that the deposits are withdrawn altogether from the banks, but that they will be used more and more rapidly for payments by way of transfers to other accounts. The hoarding of cash or of notes, and more especially deposit currency, are the two forms in which liquid capital is accumulated. The reasons that lead capitalists to keep these

⁴With reference to money available on demand from the banks which might be termed deposit currency, the reader is referred to the present writer's *Traité d'économie politique*, 2nd edition (Paris, 1926), Vol. II, Ch. XVII, and his article on the accumulation and investment of savings during booms and depressions in the *Bulletin d'information et de documentation de la Banque Nationale de Belgique*, Sixth Year, Vol. I, No. 7, 10 April 1931.

sums available until there is an increase in business activity will be discussed later.

As soon as trade begins to revive, inducements to invest multiply. The Far East is to be inundated with cotton goods; railways and ships are to be built; housing schemes are to be carried out in large towns; water-power is to be harnessed and electrical appliances manufactured; factories and plant are to be rationalised, that is, renewed and transformed.⁵ Inaction gives place to business activity, hesitation to confidence. Rightly or wrongly, there is a flood of capital investment. The flood would soon run dry if it were not fed by new savings drawn from evergrowing profits. At the same time, even those savings are not enough. Bank credits, with their power of creating money, must come to the rescue. The rise in prices which has taken place is sustained by the extension of credit. In this manner funds are provided for the purposes of production, partly by restricting the purchasing power of fixed incomes and partly by preventing, at least theoretically, the scarcity of the means of payment which would otherwise follow from an increase in the volume of commodity transactions.

This brings us to the point which is of interest in the present connection. All this burst of construction activity is not necessarily due to any actual immediate increase in the demand from the consumer, but to an expectation of such an increase in the more or less immediate future. When, in the middle forties of last century, England began feverishly to build a network of railways no one could have demonstrated satisfactorily that these railways would pay; it would at least have been impossible to determine the date at which the consumption hoped for would become a commercial reality. Similarly, in recent years, when so many motor or artificial silk factories were being built or extended, and when the output of rubber, wheat, oil, and sugar was being steadily increased, there lay behind that movement merely calculations, or perhaps only a vague belief: it was thought that the volume of consumption would continue to increase at a more and more rapid rate. We know to-day what a huge margin of error there was in these estimates. In any case, under our present system of competition,

⁵The case of the reconstruction of devastated areas is somewhat different. From the point of view of the present article, the devastation of certain areas means a loss of capital which may lead to a temporary change in the ratio of saving to consumption. The productive equipment which has been destroyed will have to be replaced by using the available liquid capital to finance purchases of materials and the employment of labour.

the over-estimating of future market possibilities has become almost a chronic disease. As there is no general plan and no co-ordination, each undertaking expands the scale of its operations in isolation and ignores what is being done by its competitors. And it must be remembered that for purely technical reasons time is required for the construction of plant and equipment. As has been shown, during the whole of this period of increasing activity prices remain high, and provide a constant stimulus to further expansion.

The fact that a shortage of capital is found to exist towards the end of the period of increasing activity which culminates in a boom is no argument against the theory of under-consumption. This shortage is not relative to real needs; it is a shortage merely as compared with the megalomania of producers who over-estimate future demand. There is thus, first, a lack of sufficient capital to satisfy the desires of producers, and secondly, a volume of consumption inadequate to the actual volume of production, which, while it has been limited by the amounts of capital available, and also, be it said, by the supply of bank credit, is yet disproportionately great in comparison with the actual or prospective requirements of consumers. Thus the alternation of periods of prosperity and of depression is based entirely on the fluctuations from illusion to disillusion; it is not a swing of the pendulum from under-production to under-consumption and back again.⁶

This will be confirmed by a study of the distinctive features of the crisis which succeeds the boom and the depression which results from the crisis.

As a rule, the source of the crisis is the over-hasty investment of capital. Producing and financial undertakings have been reckoning on a very early expansion of consumption on a scale which will not be realised until considerably later, perhaps ten or twenty years hence. In order to adapt their productive capacity immediately to this future market, they have been compelled literally to over-work all the factors of production, to strain all the resources of credit, to exhaust the available savings, to force on unduly the mining of coal, iron, and copper and the manufacture of steel, to utilise all the available labour, even of poor quality,

⁶It is well to remember that the first part of the increase in activity is generally on a sound basis, as, for example, when some technical innovation such as the construction of railways is first introduced. Conversely it should be noted that the last part of the depression is generally fundamentally unsound, as disillusionment degenerates into excessive pessimism and morbid lack of confidence.