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Introduction

Through this century of passing economic fashion the dominating idea has swung from 'Supply creates its own Demand' to the opposite 'Demand creates its own Supply' then back to 'Supply creates its own Demand'. The process continues; there are signs of the pendulum beginning yet another journey. This alternation of the dominant idea has arisen from a division between demand-side and supply-side theory, each enshrined in its own school of thought and each claiming to be complete in itself. These schools describe one-sided views which distort what is in reality a coherent whole. Half a loaf is said to be better than no bread, but this division of economic theory gives to each faction only, as it were, half a pair of trousers. Such an incomplete conceptual garment is worse than nothing. In the sphere of government, policy prescriptions derived from half a theory mislead both politicians and their electors. Throughout the world governments have been misled into pursuing policies which have led from a slump to an inflation and on to a combination of the two — 'slumpflation'. The toast given by Lord Keynes a few months before his death in 1946 to 'the Royal Economic Society, economics and economists who are the trustees, not of civilisation but of the possibility of civilisation',[1] offers little cheer to governments and their electors today.

The so-called Keynesian school of economic thought is more accurately described as the demand-side school, for it concentrates on aggregate demand and ignores the spirit and much of the economics of Keynes. Its policy prescriptions seek, largely by means of a high volume of public spending, to hold aggregate demand at a level sufficient to keep an economy operating at, or close to, 'full employment'. The demand-side concept of full employment, as well as the means of sustaining it, owes more to Beveridge than Keynes. In *Full Employment in a Free Society* Beveridge wrote; 'The first condition of full employment is that the total outlay should always be high enough to set up a demand for the products of industry which cannot be satisfied without using the whole manpower of the country; only so can the number of vacant jobs be always as high, or higher, than the number looking for jobs'. For Keynes the term 'full employment' did not relate to any particular rate of unemployment but was an alternative term for what he considered to be 'a condition which might be appropriately designated as one of true inflation'.[2] Again, although Keynes did argue against the then fashionable interpretation of Say's law that supply always calls forth its own demand, he did not argue the opposite — that demand will always call forth its own supply. It is this latter non-Keynes view which appears to be the assumption underlying the demand-side school's policy prescriptions. The high level of public spending necessitated by the pursuit of 'full employment' and the large tax take, topped up by an annual public borrowing requirement needed to support this spending, proved to be a sure recipe for accelerating inflation.

In *The Economic Journal* of December 1945 Colin Clark first argued his case, on the basis of pre-World War II evidence from many countries, that inflation becomes inevitable when total general government tax revenue plus borrowing requirement exceeds 25 per cent of net national product at market prices. Lord Keynes is on record as having agreed with Clark and subsequent experience in most countries of the world would seem to support their view. The level of public spending required by demand-side full employment budget results in Clark's limit being substantially exceeded. The demand-side school's solution to the inflationary consequences of their full employment policies is the imposition of central planning to include extensive and detailed public controls over such private matters as incomes, prices, external trade and capital movements. The mal-distribution of resources and the loss of personal liberty necessitated by this remedy has so far proved unacceptable to the free electorates of the western world. This being so and with inflation rampant, the demand-side school lost its domination.

With the failing fortunes of the demand-side school the Chicago, monetarist or supply-side school of economic thought rose to become the established orthodoxy. Their first objective is the eradication of inflation. Supply-side policy prescriptions include squeezing inflation out of the system by controlling the money supply, reducing the size of the public sector by privatisation or other means, and cutting public expenditure together with the tax take. Coinciding with the implementation of these policies the rate of inflation has tended to fall world-wide but the price appears to be a return to a high level of unemployment. Professor Harry Johnson, an early adherent of the Chicago school, warned of this possibility in 1971 when he wrote, '... the Keynesians are right in their view that inflation is a far less serious problem than mass unemployment. Either we will vanquish inflation at relatively little cost, or we will get used to it'.[3] Further, where active steps have been taken to reduce the size of the public sector by privatisation, in most cases Lord Stockton's castigation of Mrs Thatcher's administration for 'selling off the family silver' seems apposite. No economic principle is apparent. When the government estimate there to be a short-term financial gain by hiving off from the public sector a particular firm or industry, then that firm or industry is sold off to the private sector. There is little or no evidence to suggest supply-side policies have been effective in reducing either public spending or the tax take. Some items of public spending may be cut but spending on other items rises. Similarly while some taxes may be cut others are increased, often by more than enough to compensate in terms of total tax revenue. In the United Kingdom the new supply-side policies are presumed to have been implemented from 1979; in that year tax revenue appropriated 38.6 per cent of net national product at market prices. A decade later tax revenue was appropriating about 40 per cent of net national product at market prices.

While the supply-side school has contributed much to the advancement of economic science, its public appeal relies on little more than a reaction to the profligate proposals of the demand-side school. It offers more freedom, less government and less taxation but also, of necessity, less public spending. The first three enjoy public support but not the last. Supply-side policies can only offer a partial remedy as they do not offer an alternative to the imposition of taxation for the purpose of defraying necessary public expenditure. Its philosophy is fundamentally flawed. For example, Nozick argues that taxation is wrong, but then proceeds to admit to its necessity.[4] He rejects outright the concept of the 'Robin Hood' principle of redistributive taxation. For such purposes, he asserts, taxation cannot be justified. Against this he recognises that governments have a duty to protect private property, defend the state and uphold law and order and for these purposes concludes the imposition of taxation to be justified. This argument could be applied equally to justify a mobster's demand for protection money. If taxation is wrong then it cannot be justified by necessity. 'Necessity', said William Pitt in 1783, 'is the plea for every infringement of human freedom. It is the argument of tyrants; it is the creed of slaves'.

For the people of the industrialised trading economies it is a fact of unfortunate experience that the policy prescriptions of the succession of orthodox established schools of economic thought have offered little more than a trade-off between unemployment and inflation — both with their accompanying social evils. When, on the advice of economists, attempts have been made to reduce unemployment by increasing public spending, then inflation has become rampant with all its accompanying evils. When effective counter-inflationary policies have been pursued, then the rate of unemployment has risen with all its accompanying evils. Some economists appear to place the blame on the politicians but this is an evasion of responsibility on the part of those very economists.[5] In matters of public economic policy politicians and governments regularly seek, and usually act upon, the advice of those claiming to expertise in the sphere of economics. One has to conclude that it is the economists who have failed.

The present dispute between the demand-side and supply-side schools of economic thought is largely irrelevant to the issue of eradicating both inflation and unemployment. It is totally irrelevant to the issue of creating a just society or even a 'property owning democracy'. In this work it will be argued that a modern trading economy can provide the setting for a just society, free of home-bred inflation and unemployment; but the first requirement is for government to stop persistently flouting the principle of private property by the imposition of taxation. Adam Smith railed against public profligacy, as do contemporary supply-siders, but he endorsed the imposition of taxation. In the *Wealth of Nations* he laid down the 'Canons of Taxation', but he accepted also that, in the absence of a fund peculiarly belonging to the public authority, then the 'necessary expenses of government' must be defrayed 'from the revenue of the people'.[6] With few exceptions later writers on public finance have followed only one of Adam Smith's leads by limiting their investigations as to what necessary public spending consists of and to the most efficient or acceptable methods of raising the required tax revenue from 'the revenue of the people'.

The supply-side school, like Adam Smith, rails against public profligacy but considers for certain purposes the imposition of taxation to be justified by necessity. The demand-side school considers taxation to be an essential instrument of both fiscal and social policy. Contemporary schools of economic thought must cut loose from this traditional approach if the social and economic difficulties facing trading economies are to be remedied. Economics is required to follow up Adam Smith's other lead, to which Alfred Marshall contributes with his distinction between the public and private value of freeholds, and investigate the possibilty of a source of revenue that is peculiarly public. This investigation was begun prior to Adam Smith by the Physiocrats and has been continued by the American Henry George and his followers.[7] What governments need to know from economics is a source of public revenue that arises from the very nature of a trading economy and does not offend against the principle of private property. This public revenue must be sufficient to cover necessary public expenses after the abolition of all taxation. When economists can provide this knowledge then truly they may be considered as 'trustees ... of the possibility of civilisation'.

1. R.F. Harrod, *The Life of John Maynard Keynes.*
2. J.M. Keynes, *The General Theory of Employment Interest and Money*, Bk.V, Ch.21, p.303.
3. H.G. Johnson, *The Keynesian Revolution and the Monetarist Counter-Revolution*, p.200.
4. R. Nozick, *Anarchy, State and Utopia.*
5. Colin Clark, *Taxmanship*, Institute of Economic Affairs Hobart Paper No. 26.
6. Adam Smith, *The Wealth of Nations*, Bk. V, Ch.II.
7. Henry George, *Progress and Poverty*.