

# The Inflationary Prospect

*P. C. Armstrong*

THE Canadian people are as much interested in the outlook for further inflationary price rises as they are in any public question. Indeed, it is quite possible that the average citizen gives more thought to the prospect of further inflation of prices than he does to the international situation.

It is difficult to get intelligent discussion of inflation, because of the too general impression that inflation is actually the same thing as an increase in prices.

Actually, the increase in prices which has been going on in this country for twelve years is the consequence of inflation, and also a necessary if somewhat painful corrective of a condition in which the amount of money in circulation has been increasing more rapidly than the supply of goods available for the ordinary citizen to buy.

The distinction is very important. Inflation is a condition, but also a process. It is correct to describe a balloon as being inflated after a certain amount of gas at a certain pressure has puffed it out, but it would be a little difficult to think of how to prevent further inflation, unless the process by which the present inflation was created were clearly understood.

It is quite obvious that the present *condition* of inflation was created by a *process* of inflation which amounted to the Government of Canada putting into circulation vast sums of money, for pur-

poses which, however desirable or necessary, did not include an equivalent encouragement of the production of goods and services for the public to buy. It is in that way that we have ended in having a national money income, and therefore current purchasing power for the public, which has increased very much more rapidly since 1939 than has the supply of goods coming on the market. Impressive as has been the record in the increase of production of goods and services in Canada during the last twelve years, the fact is that it has been outrun by the increase in money with which to purchase them.

In such circumstances, why should anyone be surprised that prices have risen? In such circumstances, sooner or later prices must rise—unless the public are going to be satisfied to set aside their increased incomes, in some form, in which they will not enter the market at all.

That would be a very difficult plan to arrange—even if the Government had, these past twelve years, been encouraging thrift, instead of discouraging it, by holding interest rates below the level which they might have attained without Government interference, and if the Government had not been engaged in imposing taxation on a plan which means that there is a constant taking of money from those who might save it to be given to those who will spend it at once. If these policies had not been followed, then there might

have been a smaller price rise than has occurred. There still would have had to be a price rise, whenever the public felt inclined to spend increased incomes, in buying a supply of goods which has not increased at an equal rate. With the existing interest and taxation policies this tendency of prices to rise has been intensified.

Actually, if the public had saved up more of its increased incomes than has been the case, this money would sooner or later have to come in the market. Sooner or later prices would have had to rise, and, judging by what happened after price control was taken off in 1946, because it was about to break down, it seems likely that a postponed increase in prices will always be more violent than one which takes place as fast as incomes are increased more than in proportion to the increase in goods and services available on the market.

In short, immediate price rises are the quickest corrective of a dangerous condition in which price rises may get quite out of hand, when the stimulus to them becomes too strong to be withstood.

## II

**T**HE result of what has happened, the consequences of the Second World War, of welfare state experiments, and now of re-armament in order to prevent or win a Third World War, are quite visible to us all. Our incomes have, in most cases, gone up very considerably. The price of what we buy has risen at the same time.

The injustice of the situation is that, while the great majority of Canadians have had income increases which have actually gone on more rapidly than price increases, a minority have experienced and are experiencing much distress. The people who live on fixed incomes—and particularly those whose incomes are the result of past savings—have been badly hurt. The purchasing power of their incomes has fallen almost in half.

This is becoming a very serious situation. The payment of universal old age

pensions is going to be another contribution to inflation. It is going to put into circulation more money without any corresponding increase in goods and services. It is going to penalize the thrift of those who might be saving at the present time. Yet, it is necessary, or the Canadian people feel that it is necessary, because inflation to date has already reduced tens of thousands of Canadians to pauperism, who, a few years ago, felt that they had made adequate provision, out of their own savings, for their old age.

On top of that, because old age pensions used to be administered under a means test which was definitely mean, the whole means test has been abolished—so that old age pensions are now scattered, as the Baby Bonus has been scattered, to those who need them as well as to those who do not.

Particularly unfortunate is the fact that this shotgun distribution of old age pensions, as in the case of Baby Bonus, means that those who really need relief in this respect are going to get too little, in order that money may be handed out unnecessarily to those who do not need relief at all.

The injustice of this situation is evident. There are equally unjust situations in connection with earned incomes, which, for one reason or another, have not risen as prices have gone up. In some cases, as with clergymen, this is simply the result of a sort of lag. The people who contribute to religious denominations have not increased their contributions as their incomes have grown.

## III

**I**N addition to these injustices, there are also other and very serious economic effects of inflationary price rises which must be considered. Wherever any important item of prices has not gone up in proportion with the general price rise, a distortion is set up. It is now well-known that rental control has practically abolished that class of investors who used to make their living by providing rental housing to those who, for one reason or

another, are unable or unwilling to become home owners. The effect of that has been that, while housing conditions in Canada are, for most Canadians, better than they ever were, the poorer classes of tenants are being steadily reduced to the status of slum dwellers. They simply cannot obtain decent housing accommodation at any rental which they could afford to pay. The result in this case, of course, is a growing demand for more Government spending, and for the provision of housing for large numbers of fully employed Canadians at the expense of the taxpayers.

After all, the man who is forced to look to the Government to subsidize his housing has become a pauper in an almshouse.

Another very serious distortion is in connection with dairy production. Under the system by which the price of milk is fixed by public authorities, the total production of milk in Canada is decreasing, while the consumption of milk and cream in fluid form is increasing.

This situation is temporarily relieved by the diversion of more milk from the production of cheese for export, by the importation of fats to make margarine, and by imports of butter. It is now evident that it will not be long before all these sources of supply at present prices are exhausted, and then the price of milk will have to rise very steeply indeed, if the balance between production and consumption in Canada is to be restored.

Another very great lag is in connection with railway freight rates. Owing to a general but erroneous belief that it is always desirable to keep freight rates low, political pressure has produced a lag in granting the railways the right to raise their prices as other prices have risen.

The effect in this case is to keep railway services unduly low in price. That results in the uneconomic use of railway transportation, and, in particular, in an increasing tendency to the centralization of industry of Canada in those older areas which have had a start over new areas in this type of enterprise.

It would be amusing if it were not so tragic to note that it is exactly those

areas—the Maritime Provinces and the Prairies—where industrial development is lagging where local politicians exercise every effort to keep freight rates unduly low, and thus perpetuate the disadvantages of their sections of the country.

Summing up the situation, while it is a fact that most individual Canadians have had income increases at least in proportion to price increases, and in greater proportion in the case of the majority of organized workers, the injustices imposed on those whose incomes have not risen in this proportion, and the economic distortions set up in the country by lags in price increases—chiefly due to political interference—mean that inflation, over all, has been a grave disadvantage to the economy.

#### IV

**I**NFLATION produces a dangerous illusion in the minds of most individuals. They believe that a dollar still remains a dollar. Thus, as their dollar income increases, they fail to realize that money is losing its purchasing power. Thus, they become indifferent to the rules of thrift. They save as many dollars as they used to save, but not as large a proportion of the dollars which they receive as they used to save. That means that consumption is encouraged and thrift is discouraged, at a time when exactly the reverse is desirable.

In the end, experience in other countries in time of inflation would indicate that there will be sudden appreciation of the decreased purchasing power of money, and that has often produced a wave of panic exchange of money for goods, which has frequently caused economic disaster.

The point has been made that it is Government spending for unproductive purposes which is the basic cause of inflation. It has been inevitable that the danger would be intensified by secondary effects. The very existence of inflationary pressures encourages rash investment. It leads organized workers to seek increases in wages unjustified by any corresponding increase in productivity. It encourages

employers to be too readily willing to concede these increases. Inflationary pressure, in short, tends to increase, automatically and cumulatively.

Basically, however, inflation results from Government spending for non-productive purposes, on a scale which outruns the increase in national production. Thus, the first consideration, when we examine the prospect for further inflation, is that of whether Government spending for non-productive purposes will still expand.

To some extent, expansion in this direction is inevitable. It is by no choice of the Government of Canada that enormous expenditures have to be made for preparations to prevent war. Yet, those preparations must go on, so that there is one source of added inflationary pressure which cannot be shut off.

It has already been pointed out that, as inflation reduces an increasing number of the people of Canada to pauperism, there will be louder demands than have yet been heard for further Government distribution of charity out of taxes.

The secondary effect of inflation, in encouraging organized workers to seek ever higher wages, can scarcely be regarded as otherwise than inevitable in the present state of public understanding of the problems involved.

On top of all this, the Government of Canada is now constantly increasing expenditures in many directions, where this must end in increasing inflationary pressure. Take, for example, the new St. Lawrence waterway and power development. Even the construction of the power plant, which will very quickly begin to add to the productive capacity of the nation, must be temporarily inflationary. The waterway works, which are most unlikely to be of any value in increasing national productivity for years to come, if ever, will be directly and seriously inflationary.

## V

**I**T must be evident then that the inflationary dangers which alarm sober observers still continue. What prospects

are there of any corrective forces coming into play?

It is a fact that the public may, at any time, stop price increases in any particular field of production, by simply refusing to buy. Some basic foods must be purchased every day. A minimum standard of housing must be maintained. Fuel must be consumed. A certain amount of clothing is necessary. Beyond these bare necessities, there is nothing which the public must buy. There are already signs that the public, resentful at present price levels, are withdrawing from the market in the case of many of the less necessary commodities.

That will not stop inflation. It will merely postpone and intensify it. In the present mood of organized labour in Canada, there is but a negligible chance that manufacturers can reduce costs, and thus prices, to satisfy the desires of buyers to purchase more cheaply. All that could come out of a buyer's strike at present would be a temporary reduction of production, and that is certainly no contribution to the solution of inflationary problems.

There is a theory, of course, that if the public stay out of the market long enough prices must come down, but that simply assumes that the fear of unemployment might force organized labour to take less wages—for wages are, of course, the major component of all costs, and therefore of all prices. At the present moment, there cannot be the least doubt that any signs of serious unemployment in Canada would not produce general wage decreases, but would be met by further Government spending, deliberately undertaken for the purpose of preventing unemployment from exercising a deflationary effect.

It must be evident that a buyer's strike, the unwillingness of the public to purchase at present price level, would not bring prices down. It would merely create unemployment, and lead to further inflation. Meanwhile, the public, as is at present very visibly the case, would store up the money which the buyer's strike removed from circulation, to be spent later on, and probably at the very moment

when Governmental attempts to correct any temporary deflation were already renewing and intensifying inflationary pressures.

Actually, there could be no more certain prelude in present circumstances to renewed and intensified inflationary pressures than any signs of temporary deflation produced by a buyer's strike.

The theory is still rather generally accepted that the Government can limit inflationary pressures by the two methods of severe taxation and limitation of credit. It is now becoming increasingly realized by economists that taxation is not, in a country which does not use a metallic currency base, a practical method of reducing the disposable income of the community. In theory, taxation can reduce the disposable income of the nation, if the money so taken out of circulation is in some way sterilized, but no one has really suggested any practical program in this direction. The money taken out of circulation by taxation is restored to circulation by new types of Government spending, so that, while there are temporary decreases in the disposable incomes of individuals as taxation is imposed, the disposable income of the community does not get decreased.

**T**O put this in other terms. If, the Government cuts down the spending power of Canadian workers by taxation, all that happens is that workers at once demand increased wages in order to maintain their take-home pay. In the present attitude of public authorities and private business, these increases are conceded unhesitatingly. The result is that the taking of money out of circulation by taxation proves entirely ineffective as a method of reducing the total disposable income of the nation.

The limitation of credit has temporary value as a method of reducing inflationary pressures, but the effect is very much like that of a buyer's strike. The cure of a condition in which too much money is chasing too few goods cannot be found by reducing the production and distri-

bution of goods as fast as the amount of money in circulation is reduced.

It would be possible, as was the case at the beginning of the great pre-war depression, for there to be such rigid limitation of credit as to produce actual deflation. Banks, for example, by rigid refusal to grant credit, might easily bring many forms of business to a standstill, but there are going to be no more cases of the sort of deflation which ushered in the great depression. No democratic Government in existence today would accept such a situation. The only effect of throwing men out of work by limitation of credit would be to lead to the Government increasing its inflationary expenditures, so as to put these men back at work.

## VI

**I**S it then to be assumed that there is no method of reducing inflationary pressures? No plan by which they can be kept from increasing? No better method of dealing with them than the present one of trying by buyer's strikes and credit limitation, to create deflation here and there in the economy, only to have this deflation more than corrected by new inflationary effects deliberately created by the public authorities?

The fact is that there is no real method of reducing the existing inflationary pressures, except to increase the supply of goods available for consumers, by more production per man per hour, and even by more hours work per man.

Comparatively small increases in this way, added to the regular annual increase in production as new and better equipment is provided for the worker, would lead, in the not too distant future, to a condition in which there was no longer any need for inflationary pressures to be discharged in higher prices.

Inevitably, such a condition, as fast as it develops, will produce special and temporary deflationary problems here and there in the economy. The supply of some types of goods will expand even beyond market needs, while others will

lag, but, in a free country, that sort of mal-adjustment soon irons itself out.

There are only two obstacles in the way of this, the only reasonable method of curing inflation. One is that a democratic Government may at any time be frightened into applying price control. The minute that occurs, it is made certain that inflationary pressures will once again begin to build up, to be discharged later on when the price control system breaks down. The other danger is that, as the balance between the supply of goods and the money available to purchase goods begins to be restored, every minor case of temporary or local deflation which occurs will at once stampede the Government into new forms of inflationary spending.

**I**F the Government shows a consistent courage in refusing to be stampeded into price control, or into spending on a great scale for the relief of temporary or local distresses caused in the process of readjustment, then it is possible to foresee, over a period, this readjustment actually taking place, and prices stabilizing.

Those major groups of prices which have not yet risen in accordance with the general increase in price levels will have

to be permitted to rise normally. There will have to be an end to all this political pressure to keep rentals, freight rates and some other groups of prices unduly low. As long as this continues, distortions are being set up which will have very evil effects in the future.

Of course, it is scarcely necessary to say that plans undertaken for great increases in Government spending for non-productive purposes, where these can possibly be avoided at a time when employment is full, make it impossible to hope for any end of inflationary pressures, and quite reasonable to fear that they may get out of hand in an inflationary panic.

The important thing is not to be deceived by minor signs which seem to indicate that inflation is over. It is still a very serious danger. Even more important is the necessity for all those who understand the situation watching the conduct of public authorities very closely, and doing everything possible to convince them that at least some voters do understand what this is all about, and are not to be tempted into accepting further inflation by great promises that the public will be furnished with more and more benefits out of the taxes which they pay.

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## *Unexperienced Preferred*

Evidently politics is the only profession in which the absence of experience and of adequate training is by popular opinion considered rather an asset than a handicap . . . The same man who would not think of having a tooth pulled by his barber, will gladly entrust the political future of his country, and so his own and his children's fate, perhaps to the same barber, by electing him as his representative.

FRANZ SCHOENBERNER