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The wage - employment relationship in Keynes in Light of the Great Depression

Abstract:

The wage-employment relationship is one of the central and most controversial issues in the *General Theory*. At the beginning Keynes makes the assumption of a given money wage as a preliminary working hypothesis. “But this simplification, with which we shall dispense later, is introduced solely to facilitate the exposition. The essential character of the argument is precisely the same whether or not money-wages, etc., are liable to change” (JMK, CW VII, p.27). Despite this clear statement Keynes has often been interpreted that he assumes rigid wages. Due to the complex interdependencies between the different markets in the economy it takes until chapter 19 that Keynes dispenses with his preliminary assumption. Here Keynes argues against the ‘classical doctrine’ that a downward flexibility of money wages will systematicallylead to full employment. On the contrary, lower nominal wages would nurture deflation, lead to higher bankruptcies and thereby would make things worse.

The British wage debate arose after the return to the gold standard in 1925 at the prewar parity of the pound sterling, which had been heavily opposed by Keynes, and the resulting difficulties of British industry due to the increase in export prices. After the outbreak of the Depression Keynes contributed an important but widely overlooked article ‘The question of high wages’ (1930) in which he challenged the purchasing power theory, which in England, for example, was represented by Maurice Dobb, and confronted the ‘high-wage party’ with the competitive argument. Interestingly, Keynes advocated “squeezing the higher wages out of increased efficiency” (p. 11), i.e. he favored*relative* instead of *absolute* wage reductions to regain international price competitiveness, a proposal which is topical also for today.

Finally, the paper deals with the more recent controversies which have arisen on the Preface of the German language edition of the *General Theory*, which are based on only one passage which was added in the German translation to Keynes’s original English text. The additional text appears reasonable if one links it to an important distinction Keynes makes in Chapter 19 “Changes in Money-Wages” between democratic systems with de-centralized wage bargaining and “highly authoritarian” systems for which the problem of destabilizing elastic price expectations in the process of deflationary wage policies does not exist (p.269).