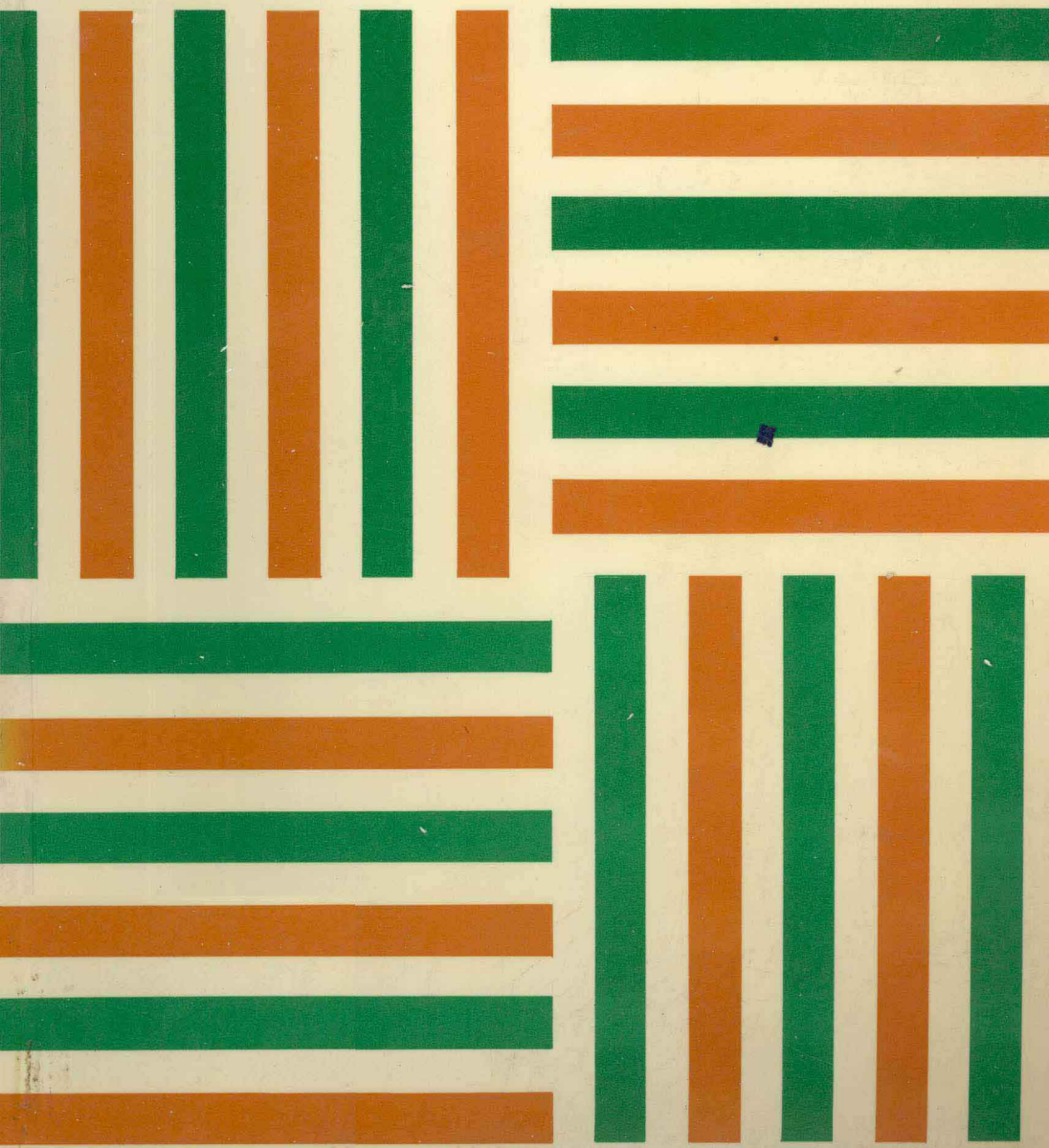


WEALTH INCOME & INEQUALITY

Second Edition
Edited by A.B. Atkinson



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A. B. ATKINSON

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FOREWORD

This is the second edition of a volume of readings first published in 1973. In the period since then, the study of economic inequality has developed considerably, and this is reflected in the substantial number of new readings included here (19 out of 25). In contrast, progress towards reducing inequality and poverty has been less marked; and the problems dealt with remain among the most pressing of any society. I hope that the collection of readings conveys an impression as to how economic analysis can be applied to help understand the extent and causes of inequality.

In selecting the readings, I have given prominence to three main aspects. The first is the clarification of essential concepts. This is particularly the subject of Part One, where the extracts deal with the meaning and measurement of inequality; but conceptual questions arise equally in later sections. What, for example, do we understand by 'poverty'? In what sense is 'heritability' relevant to socio-economic policy? In an area which can be as emotionally charged as that of economic justice, clarity concerning the use of concepts and methods is of prime importance.¹

The second aspect emphasized in the volume is the presentation of evidence about the personal distribution of income and wealth. Although Tawney (Reading 1) was right to stress that 'there are other sides of the truth about mankind and its behaviour than those [expressed in] logarithms', statistical information must provide an important foundation for any modern enquiry. Obtaining such evidence is fraught with difficulties, but considerable advances have been made in the collection and analysis of data. This is illustrated by the readings on the distribution of income (Part Two), of wealth (Part Four), and on the extent of poverty (Part Five). At the same time, despite the efforts of official statisticians and academic investigators, a great deal remains unknown, and a number of the readings point to areas where critical information is not available.

The third aspect is the analysis of the major economic factors influencing the distribution of income and wealth. Part Three presents a selection of the theories advanced to explain differences in earnings. How far, for example, can occupational differentials be attributed to differences in the training required? What is the relationship between organizational hierarchies and the distribution of earnings? In Part Four, similar questions are considered in relation to the distribution of wealth. What are the forces leading to concentration? What is the role of inheritance? The readings in Part Five examine the effects of labour market segregation and the consequences of discrimination.

In these extracts, the principal concern is with the role of *economic* factors. This should not be taken as reflecting a view on my part that these are the most important forces at work. In asking, for example, how far the earnings of doctors can be explained by their long period of training, there is no necessary presumption that this is the full explanation; and to obtain a complete

picture one certainly has to examine the social and political role of the medical profession.

The editor of any volume of readings is faced with difficult problems of selection, and inevitably some topics cannot be included. The reader will see that several important subjects have not received due weight in the present collection. Two major omissions should be noted. First, there are no readings concerned with the distribution by factor shares (labour, land, and capital). This aspect has traditionally received more attention from economists, and is covered in a number of books of readings and surveys of the field. It seemed reasonable therefore to focus here on the size distribution of income among persons. Secondly, the readings concentrate on the problem of inequality in advanced countries and do not deal explicitly with the world distribution of incomes. The subject of inequality in economic development, and of disparities between nations, warrants a volume in its own right.

In the course of preparing this revised edition, I have been greatly helped by Celia Rhodes of University College, London. I am grateful to Anil Markandya, Nicholas Rau, and Tony Shorrocks for suggestions about the revised contents. Finally, I would like to thank the authors of the readings for agreeing to the reprinting of their work in this volume.

London, 1979

A. B. ATKINSON

NOTE

¹ Such clarity can sometimes only be obtained at the expense of employing mathematical apparatus. I have however tried to avoid highly technical readings wherever possible, and in one case (Reading 3) have supplied a non-mathematical summary.

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PART ONE THE CONCEPT OF INEQUALITY

Introductory Note

The readings in this first section deal with different aspects of two fundamental questions: why are we concerned about inequality and what exactly does inequality mean?

These are controversial questions. Some people argue that inequality is not a matter for concern and that intervention by the state to reduce inequality cannot be justified on moral grounds. A recent example is the entitlement theory of justice of Nozick (1974). This approach, which draws on a long tradition, can basically be summarized as asserting that moral judgements must be based on the *process* by which a distribution is attained rather than on the final distribution itself. It is a theory based on 'historical' rather than 'end-state' principles. The justice of a distribution of income depends, in this view, on how it came about and not on any difference between Messrs. A and B. If we start from a position in which everyone is entitled to the rights and assets which they hold (justice of original holdings), and proceed from it by a series of moves (exchanges, gifts, etc.) which are considered to be just, then the distribution is morally legitimate. The key issue is of course the determination of just initial entitlements, and here the theory is less fully developed.¹

Nozick argues by defining a just state of entitlements and then considering legitimate processes for departing from it; in contrast, the traditional egalitarian argument starts from an ideal end-state — equality of outcome — and then considers the justification for departures from it. Reading 1 is an extract from Tawney's classic essay on *Equality*. Although it does not cover all modern arguments for lesser inequality — for example, the recent work of Rawls (1971) — it provides a powerful statement of the case. (A further reason for retaining this reading is that Tawney's vigorous style contrasts well with the anaemic prose which characterizes much modern economics.)

For Tawney the case for equality rests principally on the grounds that:

What a community requires . . . is a common culture, because without it, it is not a community at all . . . But a common culture cannot be created merely by desiring it. It must rest upon practical foundations of social organisation. It is incompatible with the existence of sharp contrasts between the economic standards and educational opportunities of different classes . . . It involves, in short, a large measure of economic equality (Reading 1, pp. 7–8).

He emphasizes that the case for equality rests in no sense on the assumption that people are identical in their natural endowments of character or intelligence.

2 *Wealth, Income, and Inequality*

Similarly, economic equality does not necessarily involve an identical level of money incomes or provision of public services, rather it requires 'equality of consideration'.

The translation of the concept of 'consideration' into an actual measure of how far we are from equality raises many methodological questions. The mere existence of differences between people certainly does not imply the existence of injustice — on any principle. As Bauer and Prest (1973) have noted, it is unfortunate that the term 'inequality' is applied both to situations where incomes are different (just as we might say that Mr. A is taller than Mr. B) and to cases where there is a moral content (i.e. a presumption that equality would be desirable).

One reason why differences in income do not inevitably imply the existence of injustice is that there may be offsetting non-monetary differences. This is one of the points made in Reading 2 by Okun: 'the box-score numbers on family incomes cannot tell the whole story of the distribution of economic welfare' (Reading 2, p. 18). As he notes, 'extra earnings that reflect a premium for being a steeplejack or an embalmer or working on the night shift do not constitute a fundamental inequality in economic welfare' (Reading 2, p. 19). To this extent differences in income may simply reflect differences in preferences or choices. At the same time, it would be quite misleading to suggest that this is the only, or primary, source of dispersion in incomes: 'the labor market is not, in fact, a cafeteria line, and what people get on their trays bears only a slight relationship to their preferences' (Reading 2, p. 20).

The genuine inequality which does arise may cause concern for two reasons. The first is that, even if individuals start equally placed, there may be differences of outcome — Okun's 'casino'. Secondly, individuals have differing initial advantages, arising from natural abilities, family background, or other factors. As it is commonly put, there is inequality of 'opportunity'.

The weight placed on these sources of inequality depends on one's view of social justice. Okun refers to a widespread conviction that inequality of opportunity is more objectionable. At the same time, he recognizes that the concept of equality of opportunity is highly elusive. The casual use of the term in political and popular debate takes little account of the problems in making precise what is entailed (see the discussion by, among others, Plamenatz, 1957; Williams, 1962; and Klappholz, 1972).

The concept of inequality of outcome is more readily defined, but it remains to translate this into a concrete measure. There are, for example, the formidable problems of defining income (or wealth) and the unit of analysis. As Titmuss (1962) and others have argued, the measure of income commonly used in studies of inequality, particularly those based on income tax statistics, falls a long way short of a comprehensive definition such as that advanced by Simons (1938). That definition in turn needs to be extended to allow for differences over the individual life-cycle, for the benefits derived from government expenditure, for the impact of inflation, etc. We need to consider the choice of the unit of analysis. Are we interested in the position of individuals, of families or of households?

What allowance should be made for differences in needs? (These issues are discussed more fully in Atkinson, 1975.)

Even when a definition of income has been selected, there is still the question as to how the extent of inequality should be measured. The distribution of income could be presented in its entirety. However, many people seek to attach a single number to the degree of inequality. Politicians, for example, like to be able to say that 'inequality' has gone up or gone down, or that it is greater, or less, in the United States than in France.

The conventional approach to the measurement of inequality is to adopt one of a variety of summary statistics, of which the most popular is the Gini coefficient. In Reading 3, I examine these summary measures. I argue that implicit in their use are values about a desirable distribution of income and that there is no *a priori* reason to believe that the values embodied in, say, the Gini coefficient would be widely acceptable. (Since the argument is set out mathematically, a summary for non-mathematical readers is appended.) In the article it is shown that, if one adopts a social welfare function approach, and if we rank distributions independently of the mean levels of income, then an unambiguous conclusion can only be reached where the Lorenz curves do not intersect. (The Lorenz curve shows the proportion of total income accruing to different percentage groups of the population, ranked in order of increasing income.)

This suggests that the first stage in any comparison should be to draw the Lorenz curves. If they do not intersect (as in Figure 3.8), then the position is relatively straightforward; if however they intersect (as in Figure 3.9), the conclusion depends on the relative weight attached to the different points of the income distribution. For example, on the Rawlsian difference principle, where inequality is assessed in terms of the position of the least advantaged (Rawls, 1971), we would rank the distribution in terms of the share of the lowest income group.

In the latter part of Reading 3, it is argued that social values should be introduced explicitly, and for this purpose a parameter (ϵ) is defined to capture attitudes towards inequality. The way in which this can be calibrated is described in the Non-Mathematical Summary. This calibration, dubbed by Okun (1975) 'the leaky-bucket experiment', considers the trade-off between transfers to the poor and the cost to the rich. Suppose £1 is taken from the rich, and £ x given to the poor, where x is less than 1 (the remainder 'leaking' out of the bucket). How small can x become before we regard the transfer as undesirable? Okun interprets the position of Friedman (1962) as being opposed to any loss, and contrasts it with that of Rawls, who would accept any leak up to 100 per cent.²

The argument of Reading 3 treats inequality as synonymous with loss of social welfare. Since writing it, I have come to believe that it may be more useful to keep the two concepts distinct, that is to distinguish between the objective of maximizing social welfare and the egalitarian principle. According to the latter, it is differences between people that is the crucial feature, and the reduction of inequality is desired for its own sake, not as a means to achieve another goal.

4 Wealth, Income, and Inequality

The implications may be illustrated by a comparison with the Rawlsian difference principle. Some writers treat this Rawlsian principle as equivalent to egalitarianism: for example, Okun states that ‘Rawls has a clear, crisp answer: Give priority to equality’ (1975, p. 92). However, this is not correct. Consider, for example, two societies each consisting of two people. In society A, the distribution is (3, 4); in B it is (2, 2). Society A has greater inequality, but would be preferred according to the Rawlsian principle of justice. Egalitarianism is an independent principle in its own right (a point which is clearly recognized by Nozick 1974, pp. 210–13), and may lead to different conclusions.

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NOTES

¹ For an interesting review of Nozick (and Rawls, 1971) from the perspective of economics, see Gordon (1976).

² For further discussion of the measurement of inequality, see Sen (1973) and Cowell (1977).

1. The Religion of Inequality*

Discoursing some sixty years ago on the text, ‘Choose equality and flee greed’, Matthew Arnold observed that in England inequality is almost a religion. He remarked on the incompatibility of that attitude with the spirit of humanity, and sense of the dignity of man as man, which are the marks of a truly civilized

*Extracts from R. H. Tawney, *Equality*, Unwin Books, 1965. Reprinted by permission of Allen & Unwin Ltd.

society. 'On the one side, in fact, inequality harms by pampering; on the other by vulgarizing and depressing. A system founded on it is against nature, and, in the long run, breaks down.' [Arnold, 1903.]

Much has changed since Arnold wrote, and not least what he called the Religion of Inequality. The temper which evoked his criticism, the temper which regarded violent contrasts between the circumstances and opportunities of different classes with respectful enthusiasm, as a phenomenon, not merely inevitable, but admirable and exhilarating, if by no means extinct, is no longer vociferous. Few politicians today would dwell, with Mr Lowe, on the English tradition of inequality as a pearl beyond price, to be jealously guarded against the profane. Few educationalists would seek, with Thring, the founder of the Headmasters' Conference and one of the most influential figures in the educational world of his day, to assuage the apprehension felt by the rich at the extension of education by arguing that 'the law of labour' compels the majority of children to work for wages at the age of ten, and that 'it is not possible that a class which is compelled to leave off training at ten years of age can oust, by superior intelligence, a class which is able to spend four years more in acquiring skill'. Few political thinkers would find, with Bagehot, the secret of English political institutions in the fact that they have been created by a 'deferential people'; or write, as Erskine May wrote in his *Democracy in Europe*, of the demoralization of French society, and the paralysis of the French intellect, by the attachment of France to the bloodstained chimera of social equality; or declare, with the melancholy assurance of Lecky, that liberty and equality are irreconcilable enemies, of which the latter can triumph only at the expense of the former. When Taine published his *Notes sur l'Angleterre* in 1872, he could describe it, by contrast with France, as still haunted by the ghost of the feudal spirit, a country governed by 100,000 to 120,000 families with an income of £1,000 a year and upwards, in which the lord provides for the needs of his dependent, and the dependent is proud of his lord'. It is improbable that, if he analysed the English scene today, even the relentless exigencies of historical antithesis would lead him to regard it as gilded with quite the same halo of haughty benevolence and submissive gratitude. [Thring, 1864; Bagehot, 1867; Erskine May, 1877; Lecky, 1899; Taine, 1863.]

Institutions which have died as creeds sometimes continue, nevertheless, to survive as habits. If the cult of inequality as a principle and an ideal has declined with the decline of the aristocratic society of which it was the accompaniment, it is less certain, perhaps that the loss of its sentimental credentials has so far impaired its practical influence as to empty Arnold's words of all their significance. It is true, no doubt, that, were he writing today, his emphasis and illustrations would be different. No doubt he would be less impressed by inequality as a source of torpor and stagnation, and more by inequality as a cause of active irritation, inefficiency and confusion. No doubt he would say less of great landed estates, and more of finance; less of the territorial aristocracy and the social system represented by it, and more of fortunes which, however interesting

their origin, are not associated with historic names; less of the effects of entail and settlement in preventing the wider distribution of property in land, and more of the economic forces, in his day unforseen, which have led to a progressive concentration of the control of capital; less of the English reverence for birth, and more of the English worship of money and economic power. But, if he could be induced to study the statistical evidence accumulated since he wrote, it is probable that he would hail it as an unanticipated confirmation of conclusions to which, unaided by the apparatus of science, he had found his way, and, while noting with interest the inequalities which had fallen, would feel even greater astonishment at those which had survived. Observing the heightened tension between political democracy and a social system marked by sharp disparities of circumstance and education, and of the opportunities which circumstance and education confer, he would find, it may be suspected, in the history of the two generations since his essay appeared a more impressive proof of the justice of his diagnosis than it falls to the lot of most prophets to receive. 'A system founded on inequality is against nature, and, in the long run, breaks down.' . . .

The truth is that, in this matter, judged by Arnold's standard, we are all barbarians, and that no section or class is in a position to throw stones at another. Certainly a professional man, like the writer of these pages, is not.

High Heaven rejects the lore
Of nicely calculated less and more:

and how, when he accepts an income five times as large as that of the average working-class family, can he cavil at his neighbours merely because their consciences allow them to accept one twenty, or thirty, or fifty times as large? Certainly the mass of the wage-earners themselves, in spite of the immense advance which they have achieved since Arnold wrote, are but little better entitled to adopt a pose of righteous indignation.

What the working-class movement stands for is obviously the ideal of social justice and solidarity, as a corrective to the exaggerated emphasis on individual advancement through the acquisition of wealth. It is a faith in the possibility of a society in which a higher value will be set on human beings, and a lower value on money and economic power, when money and power do not serve human ends. But that movement is liable, like all of us, to fall at times below itself, and to forget its mission. When it does so, what it is apt to desire is not a social order of a different kind, in which money and economic power will no longer be the criterion of achievement, but a social order of the same kind, in which money and economic power will be somewhat differently distributed.

Its characteristic fault is not, as is sometimes alleged, that the spirit behind it is one of querulous discontent. It is, on the contrary, that a considerable number among those to whom it appeals are too easily contented — too ready to forget fundamental issues and to allow themselves to be bought off with an advance in wages, too willing to accept the moral premises of their masters, even when they

dispute the economic conclusions which their masters draw from them, too distrustful of themselves and too much disposed to believe that the minority which has exercised authority in the past possesses a *mana*, a mysterious wisdom, and can wield a *karakia*, a magical influence bringing prosperity or misfortune. [De Man, 1927.] Their sentiment is just, but their action is timid, because it lacks a strong root of independent conviction to nourish and sustain it. If leaders, their bearing not infrequently recalls, less the tribune, than the courtier: they pay salaams of exaggerated amplitude to established proprieties, as though delighted and overawed by the privilege of saluting them. If followers, they are liable, with more excuse, to behave on occasion in a manner at once docile and irritable, as men who alternately touch their hats and grumble at the wickedness of those to whom they touch them.

Heaven takes, to paraphrase Homer, half the virtue from a man, when, if he behaves like a man, he may lose his job; and it is not for one who has not experienced the wage-earners' insecurity to be critical of the wage-earners' patience. But it would be better, nevertheless, both for them and for the nation as a whole, if they were more continuously alive, not only to their economic interests, but to their dignity as human beings. As it is, though they resent poverty and unemployment, and the physical miseries of a proletariat, they do not always resent, as they should, the moral humiliation which gross contrasts of wealth and economic power necessarily produce. While they will starve for a year to resist a reduction in wages, they still often accept quite tamely an organization of industry under which a dozen gentlemen, who are not conspicuously wiser than their neighbours, determine the conditions of life and work for several thousand families; and an organization of finance which enables a handful of bankers to raise and lower the economic temperature of a whole community; and an organization of justice which makes it difficult, as Sir Edward Parry has shown [1914], for a poor man to face the cost of obtaining it; and an organization of education which still makes higher education inaccessible to the great majority of working-class children, as though such children had, like anthropoid apes, fewer convolutions in their brains than the children of the well-to-do.

They denounce, and rightly, the injustices of capitalism; but they do not always realize that capitalism is maintained, not only by capitalists, but by those who, like some of themselves, would be capitalists if they could, and that the injustices survive, not merely because the rich exploit the poor, but because, in their hearts, too many of the poor admire the rich. They know and complain that they are tyrannized over by the power of money. But they do not yet see that what makes money the tyrant of society is largely their own reverence for it. They do not sufficiently realize that, if they were as determined to maintain their dignity as they are, quite rightly, to maintain their wage, they would produce a world in which their material miseries would become less unmanageable, since they would no longer be under a kind of nervous tutelage on the part of the minority, and the determination of their economic destinies would rest in their own hands. . . . What a community requires, as the word itself suggests, is a

common culture, because, without it, it is not a community at all. And evidently it requires it in a special degree at a moment like the present, when circumstances confront it with the necessity of giving a new orientation to its economic life, because it is in such circumstances that the need for co-operation, and for the mutual confidence and tolerance upon which co-operation depends, is particularly pressing. But a common culture cannot be created merely by desiring it. It must rest upon practical foundations of social organization. It is incompatible with the existence of sharp contrasts between the economic standards and educational opportunities of different classes, for such contrasts have as their result, not a common culture, but servility or resentment, on the one hand, and patronage or arrogance, on the other. It involves, in short, a large measure of economic equality — not necessarily in the sense of an identical level of pecuniary incomes, but of equality of environment, of access to education and the means of civilization, of security and independence, and of the social consideration which equality in these matters usually carries with it.

And who does not know that to approach the question of economic equality is to enter a region haunted, not, indeed, 'by hobgoblins, satyrs, and dragons of the pit', yet by a host of hardly less formidable terrors — 'doleful voices and rushings to and fro', and the giant with a grim and surly voice, who shows pilgrims the skulls of those whom he has already despatched, and threatens to tear them also in pieces, and who, unlike Bunyan's giant, does not even fall into fits on sunshiny days, since in his territory the sun does not shine, and, even if it did, he would be protected against the weaknesses that beset mere theological ogres by the inflexible iron of his economic principles? Who does not recognize, when the words are mentioned, that there is an immediate stiffening against them in the minds of the great mass of his fellow-countrymen, and that, while in France and Scandinavia, and even in parts of the United States, there is, at least, an initial sympathy for the conception, and a disposition to be proud of such economic equality as exists, in England the instinctive feeling is one, not of sympathy, but of apprehension and repulsion, as though economic equality were a matter upon which it were not in good taste to touch? And who does not feel that, as a consequence of this attitude, Englishmen approach the subject with minds that are rarely more than half open? They do not welcome the idea, and then consider whether, and by what means, the difficulties in the way of its realization, which are serious enough, can be overcome. They recite the difficulties with melancholy, and sometimes with exultant, satisfaction, because on quite other grounds — grounds of history, and social nervousness, and a traditional belief that advantages which are shared cease to be advantages at all, as though, when everybody is somebody, nobody will be anybody — they are determined to reject the idea.

So, when the question is raised whether some attempt to establish greater economic equality may not be desirable, there is a sound of what Bunyan called 'doleful voices and rushings to and fro'. They rear, and snort, and paw the air, and affirm with one accord that the suggestion is at once wicked and impracticable.

Lord Birkenhead, for example, declared that the idea that men are equal is 'a poisonous doctrine', and wrung his hands at the thought of the 'glittering prizes' of life being diminished in value; and Mr Garvin, with his eye for the dangers of the moment, and the temptations to which his fellow-countrymen are most prone to succumb, warns us against the spirit that seeks the dead level and ignores the inequality of human endowments; and Sir Ernest Benn writes that economic equality is 'a scientific impossibility', because Professor Pareto has shown, he says, that 'if the logarithms of income sizes be charted on a horizontal scale, and the logarithms of the number of persons having an income of a particular size or over be charted on a vertical scale, then the resulting observational points will lie approximately along a straight line', and that, if only this were more generally known, the poor, like the wicked, would cease from troubling. A great industrialist, like Sir Herbert Austin, and a distinguished minister of religion, like Dean Inge, rehearse, in their different ways, the same lesson. The former implores us to 'cease teaching that all men are equal and entitled to an equal share of the common wealth', and 'enrich the men who make sacrifices justifying enrichment', and 'leave the others in their contentment, rather than try to mould material that was never intended to withstand the fires of refinement'. The latter complains, in an address at Oxford — with a view, perhaps, to mitigating the class feeling which he rightly deplures — that 'the Government is taking the pick of the working classes and educating them at the expense of the rate-payers to enable them to take the bread out of the mouths of the sons of professional men'. This deplorable procedure, he argues, cannot fail to be injurious to the nation as a whole, since it injures 'the upper middle classes', who are 'the cream of the community'.¹

When he hears this comminatory chorus directed against the idea of equality by men of such eminence, the first impulse of the layman is to exclaim with Moses, 'Would God that all the Lord's people were prophets!' He wishes that he himself, and all his fellow-countrymen, were capable of charting logarithms on horizontal and vertical scales in the manner of Sir Ernest Benn, and of escaping with confidence the dead-level of mediocrity so justly deprecated by Mr Garvin, and of being moved by the righteous indignation which fills Dean Inge when he contemplates those vessels of wrath, the working classes. But he knows, to his dismay, that these gifts have been denied to ordinary men, and that it would, indeed, be a kind of presumption for ordinary men to desire them, for to do so would be to aspire to an impious and unattainable equality with their betters. So he is bewildered and confounded by the perversity of the universe; he is oppressed by the weight of all this unintelligible world. If only the mass of mankind were more intelligent, they would realize how unintelligent their pretensions are. But they are condemned, it seems, to be unaware of their inferiority by the very fact of their inferiority itself.

When an argument leads to an *impasse*, it is advisable to re-examine the premises from which it started. It is possible that the dilemma is not, after all, quite so