

# Fair Wages and Just Outcomes

## Marshall and Pigou on the Labour Market and Redistribution

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Pigou's first major work in the field of labour, *Principles and Methods of Industrial Peace*, was published in 1905.<sup>1</sup> In its preface, Pigou records his debt to Marshall. It was Marshall who had suggested the topic of industrial peace as one suitable for investigation and provided detailed criticism, encouragement and general guidance. Throughout *Principles and Methods of Industrial Peace*, key arguments are developed against a Marshallian backdrop.<sup>2</sup> In particular, Pigou advances the view that the appropriate benchmark for arbitrated awards is the normal wage — that set by the free workings of supply and demand — and any artificial raising of wages adversely affects workpeople taken as a whole.

For his part, Marshall took it on himself to introduce the manuscript of *Principles of Methods of Industrial Peace* to MacMillan (Whitaker 1996, letter 810) and references the work in the later editions of *Elements of Economics of Industry*. He had earlier (1900-1901) been instrumental in securing a lectureship for Pigou (Groenewegen 1995, Whitaker 1996, letters 605, 645, 648, 649) and was unequivocal in his praise for Pigou: 'Pigou will be one of the leading economists of the world in his generation' (Marshall to the Provost, King's College, Cambridge in 1901 concerning Pigou's Fellowship dissertation, Whitaker 1996, letter 668).

We know very little about Marshall's views of Pigou's work in later periods.<sup>3</sup> But the existence of a certain tension between the Pigovian framework and that of Marshall is a theme repeated in a number of commentaries of Pigou's work. Frank Knight's 1926 review of the second edition of Pigou's *Economics of Welfare* provides an early guide to thinking. For Knight, *Economics of Welfare* 'continues and develops the "Cambridge Economics" which continues and develops English Political Economy'. He goes on to add, however, that while the 'doctrine is essentially that of Dr. Alfred Marshall; Pigou's exposition is less deliberate and more readable than that of his teacher, but lacks a certain touch of realism, the evidence of vast knowledge of detail acquired through first-hand observation'. And in later reminiscences, Joan Robinson referred to what she saw as Pigou's role in reducing Marshall's framework to a neat, consistent but essentially flawed static system (Robinson, 1966, viii, 1978 ix).<sup>4</sup>

This paper explores further the relationship between Marshall and Pigou by considering their respective approaches to the determination of wages and their views as to the appropriate characterisation of wage outcomes. In particular, I focus on the question of whether Pigou's well-known theory of exploitation and his related contribution to the living wage debate represented a significant break from the Marshallian framework.

*Principles and Methods of Industrial Peace* defined the limits above and below the normal wage within which wages could move when they were not fixed by the free workings of supply and demand (the so-called range of indeterminateness or settlement locus). But it provided a largely neutral reading as to which party, workpeople or employers, was more likely to be significantly disadvantaged in the bargaining process. Pigou's *The Economics of Welfare*

published in 1920 conveys a different image. Here, the emphasis is on the 'exploitation' of workers by employers and the likelihood of workers being exploited — i.e. being paid less than the value of their marginal product — in industries where strong trade unions did not prevail; the possibility of employers being exploited by workers is relegated to footnote status.<sup>5</sup>

Despite the obvious stronger position advanced in Pigou's *The Economics of Welfare*, there remains certain ambiguities in Pigou's presentation insofar as the question of a break with Marshall is concerned. On the one hand, the broad analytical framework adopted in *The Economics of Welfare* is clearly linked to that of *Principles and Methods of Industrial Peace* with its attendant Marshallian foundations. Moreover, the issue of exploitation is introduced by Pigou within the context of a discussion of Marshall's 'fair wages' analysis (see Marshall, 1887). On the other hand, Pigou's very use of the pejorative term 'exploitation' appears so much at odds with Marshall's balanced approach to language-use.<sup>6</sup> And despite the significance of the Marshallian foundations in *Principles and Methods of Industrial Peace*, specific features of the analytical structure developed in this work and later utilised by Pigou in his analysis of exploitation in *The Economics of Welfare* — most notably Pigou's treatment of the range of indeterminateness — must be seen as important original contributions to the field.<sup>7</sup> We are left with the question: Does the Pigouvian theory of exploitation simply represent a restatement of Marshallian wages analysis or does Pigou introduce a new critical dimension to neo-classical distribution theory?

Pigou's analysis of exploitation covers the case of 'unfair' wages. But what should be done about low wage outcomes that are considered 'fair'? For Pigou, low wages outcomes whether fair or not are unjust. But, as with Marshall, the policy of setting a 'living wage' (a mandated national minimum wage based on needs) to meet the problem of low wages, harms the very people it is designed to assist. *Wealth and Welfare*, published in 1912, replaces the demand for a living wage — made strongly at the time in policy debates — with that of the maintenance of minimum 'living conditions'.<sup>8</sup> To meet this demand, Pigou emphasised the need for major public spending programs financed through progressive income taxes and death duties. His support for a significant expansion of the state sector raises the second major question posed in this paper: To what extent did Pigou deviate from Marshall in his support for the maintenance of minimum living conditions and, more particularly, the role of the state in achieving those minima?

The paper is divided into two parts. The first deals with Pigou's theory of exploitation while the second considers his minimum standards policy.

## 1. Exploitation and unfair wages

Pigou is often credited with establishing the neo-classical theory of exploitation in *The Economics of Welfare*; Joan Robinson with extending it in *The Economics of Imperfect Competition*. Hence, the (misleading) label of the Pigou-Robinson theory of exploitation.<sup>9</sup> For Pigou, exploitation is defined in terms of workers being 'paid less than the value which their marginal net product has to firms which employ them' (Pigou 1920 p 506). This definition is both precise in form and historically linked. It is precise because whether or not a worker is exploited is determined on the basis of a single criterion: Is the wage paid above or below the value of the marginal product? And it is historically linked because it utilises a marginalist concept — the value of the marginal net product — as its evaluative benchmark. As such, Pigou locates his theory within the broad marginalist tradition. More importantly for our purposes, Pigou's analysis of exploitation in *The Economics of Welfare* is prefaced with reference to Marshall's definition of a fair rate of wages set out in Marshall (1887).<sup>10</sup>

The fact that Pigou's definition is precise and historically linked means that it is possible to directly compare, at a structural (or content) level, Marshall and Pigou on the phenomenon of

exploitation defined in terms of the payment of below normal wages. But can we leave our comparative review at this structural level?

#### *The linguistic dimension*

I would argue that we must go beyond a structural critique and examine the *linguistic* dimension. How authors use language frames their discussion. The choices they make in regard to terms used will determine (often precisely so) how their analysis will be absorbed and classified. By choosing to use the word 'exploitation', highly charged with 'opprobrious' implications to use Robinson's phrase, (see Robinson 1942) to describe the phenomena of wages paid less than the value of the marginal product rather than some more neutral term, Pigou leads us to think of deep-seated ethical problems in the structure of wage payments.

While it is certainly true that Pigou's discussion of wage outcomes is transformed by his use of the term exploitation it is another matter altogether to go on to conclude that Pigou's use of language, in and of itself, is indicative of a sharp break between Pigou and Marshall. This is because there are limits on the extent to which an author's use of certain terms should be accepted without qualification as the basis for contextualising and classifying her or his theory.

The first qualification is that words have limited lives and undergo semantic shifts through those lives. A check on the etymology of key terms is, therefore, important when comparing texts over time. This is of some importance in the present case, as exploitation is a loanword from French.

The second difficulty with a face-value acceptance of language use is that the choices of terms will strongly depend on the associations that have developed around those terms for *particular* authors. Assume, for arguments sake, that Marshall associated the term exploitation with Marx's analysis of exploitation. Marshall might well believe that the exploitation of labour exists (in terms of the payment of wages below normal levels) but not accept that Marx's analysis of exploitation is correct and hence not favour the use of the term. Finally, irrespective of any links to Marx, 'exploitation' is a term, on its negative reading, rich with political and emotive appeal and hence may be eschewed by those writers arguing for a 'scientific' or 'neutral' mode of discourse in economics.

The *Oxford English Dictionary* (OED 2nd Edition) notes that the term 'exploit' was adopted into English from Old French. The first example given by the OED of the term being used in English, is from 1393 ('the sail goth up, and forth they straught. But none exploit thereof they caught'). However, the first example given of its use in a negative sense ('to utilize for one's own ends, treat selfishly as mere workable material (persons, etc.)') is from as late as 1838: 'The Humbughausens ... have exploited the obscure (to use a French phrase for which we have no equivalent) with ... profit'. Edwin Cannan's entry for *exploit* in Palgrave's *Dictionary of Political Economy* (first published in 1894) is suggestive of the absence of a full assimilation of exploitation (as a loanword) into English even as late as the 1890s.<sup>11</sup>

'The French verb *exploiter* primarily means simply to use in such a way as to make profit out of ..... There are some things which it is admittedly improper to use in such a way as to make profit out of them; it is disgraceful for instance to *exploiter* any one's credulity, ignorance, or good nature. Hence the word comes to have sometimes a bad sense ..... To *exploiter* men or labourers thus means to use them in such a way as to make profit out of them, it being implied by the use of the word that this .... is fundamentally improper .... It is almost exclusively in this bad sense that the word "exploit" has been introduced into English'.<sup>12</sup>

Against this etymological background we should not be surprised if we find few examples of the use of the term among first generation neo-classical writers (including by Marshall).

What then of Marshall's use of the term 'exploitation'? And what light can be shed on why Pigou chose to use the term 'exploitation' to define the phenomena being analysed as against some other term? In the case of Marshall, there is infrequent use of the term. Where it does appear it is used in the context of a discussion of Marx's analysis of exploitation. Marshall's first use of the term appears to be in the brief background notes on Marx that Marshall utilised for his June 1886 Lectures on Socialism and the Function of Government. Marshall's notes relate to the German edition of *Das Kapital*; the first English edition not being published until 1887.<sup>13</sup>

Marshall suggests, in his notes, that Marx's discovery is that the 'exploitation's grad' (the degree or rate of exploitation) 'is not as people have hitherto inquired to be measured' by  $S/(C+V)$  but by  $S/V$ .<sup>14</sup> Marshall then adds the following comment: 'As I can't find out what exploitation means, I am not in a position to contradict this'. In saying that he could not find out what exploitation means, Marshall is probably referring to the fact that he had been searching for but could not find the English equivalent of the word 'exploitation'. No wonder then that when we do see Marshall subsequently use the term in published work in regard to labour questions it is in the context of Marx's work.

In *Principles*, for example, the term exploitation is used but only when making reference to Marx's analysis of exploitation:

'They [Thompson, Rodbertus, and Marx] argued that labour always produces a "surplus" above its wages and the wear-and-tear of capital used in aiding it; and that the wrong done to labour lies in the exploitation of this surplus by others. But it is this assumption that the whole of this surplus is the produce of labour, already takes it for granted that they ultimately profess to prove by it; they make no attempt to prove it; and it is not true.' (Marshall, 1920, pp. 586-587, see also p.786).<sup>15</sup>

We are left to draw the following three conclusions about Marshall's use of the term exploitation. First, he was probably not familiar with the word as an English-usage term in the period of his early writings. Second, Marshall later identified the term with Marx's writings on the rate of exploitation and clearly did not accept that Marxian exploitation of labour existed because he rejected the notion explicit in the Marxian formula that labour creates *all* value. Finally, we may conjecture that even if (the later) Marshall did not identify the term exclusively with Marx's use of it, he was not prepared, in his own original contributions, to use a term which had such strong negative connotations. Marshall was particularly concerned with language use. If he shied away from using the term it would be consistent with his cautious use of language. Recall his replacement of the term 'natural' in *The Economics of Industry* with 'normal'.<sup>16</sup> Marshall and Marshall (1885 p.67): 'it has been found best to use 'Normal' because the word 'Natural' has been used loosely: men often call an arrangement 'Natural' merely because they approve it, and without taking the trouble to examine whether the Laws of Nature actually tend to bring it about.'

We have dealt with Marshall's use of the word exploitation at length. Pigou's use of the term is a little more easy to deal with. To understand Pigou's use of exploitation it is necessary to read carefully his discussion of Marshall's fair wages concept in *The Economics of Welfare*. This discussion precedes the main analysis of exploitation. Pigou indicates that for Marshall 'real wages in any occupation are fair .... when, allowance being made for differences in the steadiness of the demand for labour over in different industries, 'they [Pigou quotes Marshall] are about on a level with the payment made for tasks in other trades which are of equal difficulty and disagreeableness, which require equally rare natural abilities and an equally expensive

training'. From this definition, Pigou goes on to distinguish two forms of unfair wages. The first is where one group of workers in a certain firm or occupation are paid lower wages than a group of 'similar' workers located elsewhere (but both groups are paid in accordance with the value of the marginal net product). The unfair wages in this case result simply from the fact that marginal net products are lower in one place than another. The second type of unfair wages results when workers in any location are paid an amount below the marginal net products of their labour. Pigou refers to this form of unfair wage as 'exploitation'.

Pigou's distinction between two forms of unfair wages suggests a ready and obvious reason for his use of the term exploitation. To avoid verbal difficulties, Pigou used the term 'exploitation' to clearly underline the fact that it was the payment of wages below the value of labour form of 'unfair wages' which was of major ethical and policy concern. Having already reduced his degrees of freedom by one with his use of the word 'unfair' Pigou needed to find a harsher term to describe this type of wage outcome.<sup>17</sup> Nevertheless, the fact that Pigou was prepared to override Marshallian linguistic sensitivities and use the opprobrious term 'exploitation' is suggestive of a shift in emphasis — either in terms of Pigou's thinking about the seriousness of the phenomena of wages being paid below the value of the marginal net product or in terms of his view of the likely incidence of this sort of outcome.

#### *The structural argument*

We now turn to the structural argument concerning Pigou and Marshall on exploitation. Here we seek an answer to the following question: Leaving aside linguistic concerns do we find an analysis of below-normal wages in Marshall similar to that developed in Pigou's *The Economics of Welfare*?

For Pigou, free competition is incompatible with exploitation. To the extent that there is immobility of labour for one reason or another then a 'monopolistic' element is introduced. Perfect competition results in a determinate wage. With monopolistic elements introduced, a 'range of indeterminateness' arises within which wages will be affected by individual 'higgling and bargaining'. The upper limit of the range is given by a wage equal to the value of the marginal net product. The lower limit wage is the best alternative wage of the worker less the transaction costs involved in moving to the new place of employment. Given a gap between the upper and lower limits, the degree of exploitation is determined by the bargaining power of employers and workers and the willingness of the stronger party to exercise their power. (Pigou's discussion here is simply a transformation of that contained in *Principles and Methods of Industrial Peace* in regard to the settlement locus.)<sup>18</sup> The role of trade unions is critical. When workers are organised into trade unions exploitation is improbable. Where they are not, Pigou suggests, there are 'grounds for fearing that exploitation will often occur' (Pigou, 1920 p.514). Employers in these situations have much greater bargaining power than workpeople. This leads Pigou to suggest that the incidence of exploitation will be greater among women than men because women were less likely to be organised than men.

Pigou provides support for intervention by Conciliation and Arbitration Boards to remove or offset exploitative practices.<sup>19</sup> However, he suggests that intervention has to be assessed on a case-by-case basis where prima facie evidence for exploitation exists. Because of the difficulties involved in diagnosing cases of exploitation, it is difficult for the State to enact legislation to remove exploitation and as between no intervention or legislation designed to implement a national uniform wage standard it can be better not to interfere at all. Furthermore, removal of exploitation while benefiting 'economic welfare' (from a distributional point of view) generally makes no difference to the magnitude of the 'national dividend'. There are three exceptions: (1) when the elimination of exploitation results in an increase in labour supply; (2) when the elimination of exploitation forces employers to use existing resources more efficiently;

and, (3) when the elimination of exploitation removes inefficient employers who tend to be also the worst exploiters.

One final comment regarding Pigou's analysis of exploitation is worth making. That is his emphasis on efficiency wage influences. Pigou suggests that low wages reduce productivity. A fall in productivity ratchets down a worker's value to the employer. Hence, a worker who is exploited (and receives low wages) in one period will be in a worse off position in the following period; irrespective of any actions by exploitative employers.

Let us now consider Marshall's approach to unfair wages. Marshall's early theory of the determination of wages is based on an amalgam of wages-fund and demand and supply frameworks (see Whitaker, 1975, and Marshall, 1873a, 1873b, 1874).<sup>20</sup> Of particular interest for our purposes are two unpublished papers 'Essay on Wages' and 'Allotments' (dated by Whitaker to the early 1870s). Here Marshall refers to the wage outcomes which prevail in a variety of bargaining regimes. When an individual labourer faces an employer, or labour markets are separate from each other as a result of mobility frictions, the employer has 'the advantage of the initiative'. In these circumstances, the new hand who produces more (in value terms) than the current wage prevailing will not receive payment above the wage paid in the market but be forced down to that market wage. Pressure from other employers and the fear that all additional labourers would need to be paid the higher wage would ensure that the employer did not stray from the common position.

By the late-1880s we have a variety of sources to draw on. In particular, the later editions of the *Economics of Industry*, Marshall's lectures on poverty in 1883, his paper read before the Industrial Remuneration Conference in 1885, and the essay on 'A Fair Rate of Wages' (written as a preface to Price's *Industrial Peace* published in 1887 and partially reproduced in Pigou, 1925). These works form the essential link to the *Principles* and to the familiar Marshallian demand and supply framework used to examine issues of wage determination.

In the preface to the second edition of the *Economics of Industry* (1885), Marshall suggests that there is unity in terms of the various branches of economic theory so that the same law of competition applies to the determination of wages as it does to profits and prices. That law in terms of distribution ensures that under 'free competition' and in the 'long-run' workers receive wages which reflect two forces: the 'net return' of labour and its scarcity (Marshall, 1883 pp.193-4, 1885 pp.194-199; 1887 p.224; and, Marshall and Marshall 1885 ch. XI).<sup>21</sup>

To fix our ideas on an (implicit) theory of exploitation in this early work we need to examine Marshall's position on fairness in the payment of wages and references to the role of trade unions in determining wage outcomes. Marshall equates a fair wage (or more precisely the wages a 'fair' employer would pay) with the payment of a normal wage — the long run competitive wage (Marshall and Marshall 1885 p.216, Marshall 1887 p.xii). If we ignore the linguistic dimension and equate fairness in the payment of wages to non-exploitative wage outcomes, then two key Marshallian propositions on the exploitation of labour follow.

1. Employers are acting exploitatively when they pay workers less than their competitors as a result of taking direct or indirect advantage of employees who are ignorant of trends in wages in other areas or who are in a vulnerable position (particularly if they were taken on from the ranks of the unemployed).<sup>22</sup>
2. The payment of unfair (or exploitative) wages 'makes trade unions necessary and gives them their chief force' (Marshall 1887, p.xii). It is not possible for labour to manage properly without trade unions when they face a 'powerful and unscrupulous master' (Marshall 1883, p.199 see also Marshall and Marshall 1885).

*Principles of Economics* contains a more detailed account of a marginal productivity theory of factor remuneration than that presented in his earlier work (see Marshall, 1920, 334-

339, 427-450, 554-555, 587-589). Again, in general, wages in the long-run tend to their normal values and exploitation (in terms of unfair wages) does not persist over time. As discussed previously, the *Principles* also contains a direct reference to the issue of the exploitation of labour but only in terms of a critique of Marx's theory of exploitation. Here Marshall presents the position common to all marginal productivity theorists of the time: the output produced by firms results from the *co-ordinated* input of all factors of production (finished goods are the product of 'labour, together with that of the employer and subordinate managers, and of the capital employed' Marshall, 1920, p.587). But Marx's theory of exploitation presupposes that all surplus arises from labour and in that view he is wrong. Labour is not to be given privileged status over other factors.

Marshall also returns, in the *Principles*, to the theme of 'free competition' and the role of unions. Under free competition, isolated workers are at a bargaining disadvantage as compared with the employer (Marshall, 1920, pp.567-569). Bargaining disadvantage results from the fact that labour is 'perishable' (skills decay when workers are unemployed) and because workers are often poor and so have no reserve fund. As a consequence, workers cannot withhold labour from the market. Marshall also notes that the disadvantage of labour is 'likely to be cumulative in its effects' (Marshall 1920 p.569). A lower wage reduces a worker's efficiency and thereby reduces the 'normal value of his labour' but also 'diminishes his efficiency as a bargainer'. Pigou's discussion of the efficiency-exploitation link in *The Economics of Welfare* can be seen as a clear extension of these Marshallian themes.

For Marshall, trade unions have played a beneficial role in reducing the significance of the under-payment of workers. But at the same time Marshall reports a range of examples where trade unions interfere with the achievement of the appropriate standard of wages. One interesting case is that of a depression where Marshall suggests that trade unions may enforce a downward stickiness in nominal wages at the time of price falls thus leading to the over-payment of labour and a decline in employment. In *Elements of Economics of Industry*, the work in which Marshall attempted to summarise *Principles* to meet the 'needs of junior students', he considerably extends the discussion with the inclusion of a chapter on the role of trade unions. Returning to earlier themes (see 'The Essay on Wages'), Marshall suggests that a resolute employer has a stronger bargaining position than his or her workers. He goes on to suggest that 'in such cases as these the special disadvantages of the workman in bargaining certainly put his wages for a time below the position at which they would find their level under the free action of demand and supply — the force of economic fiction is exerted against the workman' (Marshall, 1958 pp. 370-371). In these circumstances, the strategy of working people to form trade unions and press for wage increases using reasonable methods will make for 'social well-being' (Marshall, 1958 p.399). Again, Marshall provides a balance: 'the case is different with applications of the Common Rule which make for a false standardisation; which tend to force employers to put relatively inefficient workers in the same class for payment as more efficient workers' (Marshall, 1958 p.399).

In reviewing Marshall's discussion of wage outcomes, it is hard not to be struck by the many similarities with Pigou's treatment of exploitation. In both analyses there is an emphasis on the disadvantage of labour, on the greater incidence of unfair (or exploitative) wages in industries with poor trade union coverage, on the importance of cumulative causation, and on the benchmark norm of long-run competitive wages. In short, Pigou's reads as a restatement of Marshallian unfair wages analysis.

This is not to deny that Pigou's treatment of exploitation is bereft of interesting new features. His linkage of the degree of exploitation with the settlement locus apparatus is an important extension. Nor that Pigou was more likely than Marshall to accept that exploitation was an important phenomenon. But what we can say is that Pigou's exploitation analysis does

not represent a sharp break from first-generation neoclassical wage theory.<sup>23</sup> Why? Because a prototype model of labour market exploitation already existed in neoclassical wage theory. (It is important to emphasise this point given the common *representation* of nascent neo-classical wage theory as a 'non-exploitation' theory of wages.)<sup>24</sup>

## 2. Minimum conditions and just outcomes

In *Principles and Methods of Industrial Peace*, Pigou asks the question: 'Is it desirable that arbitrators should take the general trend of economic forces for granted, or that they should introduce a bias into their awards with a view to improving the distribution of wealth? Ought they in short to try to modify long-period competitive results' (Pigou 1905, p.41). A similar question is put in Pigou's 'A Minimum Wage for Agriculture', published in 1913 '... is it desirable, in these circumstances, that the machinery of Wages Boards should be employed to force the rate of wages, which has already, *ex hypothesi*, attained to the ideal of fairness, towards the different and more elevated ideal of a 'living minimum'?'

In both cases, Pigou makes the distinction between fair wages and what might be referred to as just outcomes. While fair wages are clearly desirable they do not represent the end-point in terms of a just distribution of resources. A fair wage is a necessary but not sufficient condition for a just distribution of income and material resources.<sup>25</sup>

Pigou's answer to the question posed in *Principles and Methods of Industrial Peace* is that, efficiency wage considerations apart, workpeople will generally be adversely affected by an 'artificially elevated wage'. This is despite the fact that if a higher wage is paid, the low income worker will receive greater utility from the additional dollar than the (relatively better off) consumer will lose. Three arguments are advanced against the 'artificially elevated wage' or 'living wage'. Summarised in the Aneurin Williams Memorial Lecture given at the Copartnership Congress in 1926 (Pigou, 1926), these are: (1) a living wage policy 'threatens heavy unemployment' and loss of output; (2) the living wage is an 'ineffective means of social advance' as it does not take into account differences in needs between families of different sizes; and, (3) it is entirely ineffective in dealing with the case of workpeople who lose their jobs or become sick.

In arguing against a living wage, Pigou was at odds with Fabian policy on a national minimum wage advanced in the Webbs' *Industrial Democracy* and in various tracts such as *State Arbitration and the Living Wage* (1898) and *The Case for a Legal Minimum Wage* (1906). Fabian policy on the living wage received significant public support in Edwardian Britain particularly following the Sweated Industries Exhibition in 1906 and was a central point of debate during the miners' strike of 1912.<sup>26</sup> Interestingly, both Marshall and Pigou engaged in the public debate surrounding the miners' strike. Marshall, in a letter to the *Daily Chronicle*, 25 March 1912, notes that a uniform national minimum wage 'would very greatly increase the evils without materially increasing the benefits of collective bargaining as to wages' (Whitaker, 1996 letter 1010). But he then goes on to note the benefits that *local minima* may provide in coal mining.<sup>27</sup> Pigou in his letter to *The Times* (5 March 1912) provides support for the miners in the deadlock that had developed during the miners' strike. He argues that the miners should not be forced to arbitration before a set of principles on which arbitrated awards are to be made, had been agreed to by the miners, the employers, and the government. To do so would be to give a 'blank cheque' to an arbitrator. And while not directly suggesting that the principle should be minimum wages in each district set at the 'fair average' of the district, it is clear from his letter that that would be one plausible principle.<sup>28</sup>

Rather than support a national uniform living wage, Pigou argues instead for the establishment of a 'national minimum of conditions' 'at a level high enough to make impossible the occurrence to anybody of extreme want'. Two features of Pigou's minimum standard policy



should be noted. The first is that the minimum standard represents an equality of resources rather than an equality of welfare or utility approach. The second is that the minimum standard should rise in line with movements in per capita real income. Pigou suggests that 'wealthy States of the modern world can afford, and, indeed, are in public duty bound, to do much more than this' (Pigou 1912, p.397). As set out in *Wealth and Welfare* and developed in The Warburton Lecture of 1914 'Some Aspects of the Housing Problem', minimum conditions are to be set in a large range of areas: health and safety, hours of work, dwelling accommodation, education, health care, and food and clothing. Moreover, each standard was to be enforced separately.

As compared to the case of the artificially elevated living wage, Pigou argues that the direct transfer of resources from the relatively well-off to the needy to ensure maintenance of the minimum set of conditions would not necessarily harm the national dividend and therefore lower economic welfare. As stated in *Wealth and Welfare*, the national dividend would sometimes rise and at other times fall with such a transfer. Even in the latter case, Pigou was prepared to enforce the minimum: 'it is no more than an acceptance in concrete form of the compelling obligation of humanity' (Pigou, 1914 p.113).<sup>29</sup>

In Pigou's various discussions on the subject, three methods for transferring resources from the relatively rich to the relatively poor are noted. These are: (1) philanthropic actions; (2) employer chivalry; and, (3) State redistribution. The role of philanthropic actions and employer chivalry are examined in *Wealth and Welfare* together with Pigou's paper 'Employers and Economic Chivalry' written in 1913 but only published in 1923 in a collected set of essays. This latter paper was directly influenced by Marshall's last public lecture in which he introduced the notion of economic chivalry (see Marshall, 1907). In 'Employers and Economic Chivalry', Pigou urges employers not to restrict themselves to doing what is 'right'. Rather they are encouraged to undertake 'praiseworthy' actions. In other words, not only are employers required to meet legislative standards in areas such as health and safety but they are also encouraged to invest in the human capital of their workforce through expenditures on education. Moreover, Pigou encourages employers to provide, on a voluntary basis, wage payments in excess of normal levels and to support their employees during periods of temporary slackness in demand.

While 'Employers and Economic Chivalry' accords a role for employer chivalry and *Wealth and Welfare*, for private philanthropic actions (outside the domain of work), the channel stressed increasingly by Pigou is that of direct transfers through State intermediation. This is so in *Wealth and Welfare* and becomes ever more the case in Pigou's work in the post-war period. In this context, graduated (or progressive) income tax and death duties are accorded a central role in financing public expenditures designed to achieve minimum standards.

A significant extension of the tax base raises the issue of negative incentive effects and the possibility of a net fall in the national dividend. This possibility is recognised by Pigou. A comparison of Pigou's earlier work on the minimum standard with his later analysis reveals, however, an increasingly positive stance on this issue. In his well-known *Socialism versus Capitalism* 'lectures' of 1937, Pigou examined the arguments for and against significantly expanding the tax base for redistributive purposes. He suggests that 'heavy taxes on large incomes may [italics in the original] to some extent check the accumulation of capital home use'. In other words, the redistributive program could have little or even no negative effect on private capital accumulation. But Pigou goes much further:

'but once establish socialism, and the whole argument [of possible negative incentive effects] disappears. The accumulation of capital is cared for directly by the State. There is no longer need to rely on the ability and the willingness of private persons to provide it....The State has the power to take whatever it pleases for capital development before any income at all is distributed to individuals' (Pigou 1937 p.29).

In other words, linking redistribution to 'general socialism' or Pigou's limited form of 'collectivism' significantly increases the possibility of achieving just outcomes. One further feature of Pigou's *Socialism versus Capitalism* should be noted. While Pigou continues to adhere to the gradualist approach to public policy evident in *Principles and Methods of Industrial Peace*, there is a stridency in his tone. Referring to his own broad program of political and social reform, Pigou suggests:

'In his political testament he would recommend his successor also to follow the path of gradualness—to mould and transform, not violently uproot; but he would add in large capitals, a final sentence, that gradualness implies action, and is not a polite name for standing still' (Pigou 1937 p.139).

Having set out Pigou's program to achieve just outcomes for workers receiving low wages we can briefly state the main areas where Pigou and Marshall differ. Three differences with Marshall can be identified. (But it must be admitted that these differences are not great.) These areas are: (1) Marshall's greater emphasis on the role of education in gradually alleviating the problem of poverty as compared with Pigou's more generalist and immediate program developed around the minimum standard; (2) Marshall's support for a strong role for co-operation and economic chivalry in achieving just outcomes (compared with Pigou's apparent waning interest in this approach); and (3) Marshall's less enthusiastic embrace of redistributive taxes and more particularly of a significantly expanded program of public spending.

Marshall's Lectures on Poverty in 1883 provide a useful point of comparison between Pigou and Marshall on the role of remedial state action in regard to poverty. As mentioned previously, these lectures can be interpreted as providing a clear confirmation of the movement to a marginal productivity theory of wage determination in Marshall's work.<sup>30</sup> But they are also important in setting out an agenda for reform in terms of poverty. To overcome the problem of low wages, Marshall emphasises the role of education. The provision of a 'first-rate education, general and technical' to every child would result in a decline in the number of unskilled labourers (consequently increasing the wages of the unskilled through 'mechanical effects') but more importantly, the resulting rise in efficiency would increase production and the 'earnings-and-interest fund'. Importantly, an increase in levels of education could not be expected to have immediate effects. It may take one, or more probably, two generations for poverty to be significantly reduced.<sup>31</sup>

The theme of a significant role for education is developed in Marshall's presentation to the Industrial Remuneration Conference in 1885.<sup>32</sup> As he suggests, the 'chief remedy, then, for low wages is better education'. He goes on to add: 'School education ought to be good and cheap, if not free.' His presentation also affords an insight into Marshall's thoughts on the effects of a good education. The emphasis is not on specific but rather general skills. The chief virtue of 'book-learning' is that it helps to form a 'rigorous, straightforward character' and makes 'the mind elastic, ready to take in new ideas, and able to communicate freely with others'. Although education dominates Marshall's discussion on poverty alleviation in his presentation to the Industrial Remuneration Conference (Marshall 1885), it is important to recognise that this was not the only target area of concern. In reference to the particular problems of workers in London unable to rent adequate housing, Marshall suggests that sanitary regulations need to be enforced with 'rapidly-increasing stringency' and 'liberal' action be taken to encourage movement from those in London to 'industrial villages'.<sup>33</sup>

Marshall's *Principles* bring together the array of arguments developed in earlier works in terms of poverty alleviation. In his final chapter on 'Progress in Relation to Standards of Life' Marshall suggests that there is no 'moral justification for extreme poverty side by side with great

wealth' but significant progress has already been made and a 'gradualist approach to reform must be adopted' (Marshall 1920). The positive virtues of education are again promoted. Something of a shift in the language used is apparent. The education of the people is 'a national duty and national economy'. In terms of public expenditures, Marshall is explicit in suggesting that 'public money must flow freely'. Moreover it [public money] 'must flow freely to provide fresh air and space for the children in all working class quarters'. Likewise, public aid is required in terms of health care and sanitation.

Education for Pigou was also an important critical component of his minimum standard. However, it does not assume the paramount importance that it does for Marshall nor does Pigou give the impression of being prepared to accept the generational wait that is apparent in Marshall.

The second difference between Marshall and Pigou can be dealt with easily. As discussed previously Pigou had, following Marshall, supported a focus on economic chivalry. However, his interest in the positive virtues of co-operation and economic chivalry appears to vanish by the 1930s — perhaps in response to the extremes of the depression — to be replaced by an emphasis on State regulation and planning and the expansion of public enterprises in the 1930s (see Pigou 1935, 1937).

The final difference between Pigou and Marshall relates to Pigou's position, advanced increasingly forcefully over time, of a significant expansion of public spending financed by graduated income tax and death duties. The differences between Pigou and the *later* Marshall in this area are not as great as might be imagined for as noted by Groenewegen (1995), Marshall performed a 'volte face' on the issue of graduated taxes and death duties. In his letter to Lord Reay (12 November 1909), concerning Lloyd George's 1909 Budget, Marshall suggests: 'For about fifteen years I taught somewhat eagerly that 'Death Duties' were a grievous evil because they checked the growth of capital. For the next few years I hesitated. Now I think they are on the whole a good method of raising a rather large part of the national revenue; because they do not check accumulation as much as had been expected, and a small check does not seem to me as great an evil as it did then.'<sup>34</sup> While the later Marshall held a position close to that of Pigou in regard to effects of increased tax levies on capital accumulation, it is probable that Marshall would have balked at the second prong of Pigou's argument previously noted in the paper regarding the incentive effects of redistributive taxes on private production; namely, that with a significant expansion of public ownership the argument was irrelevant. As set out in his paper 'Social Possibilities of Economic Chivalry' Marshall defended a role for free enterprise: 'The world under free enterprise will fall short of the finest ideals until economic chivalry is developed. But until it is developed, every great step in the direction of collectivism is a grave menace to the maintenance of even our present moderate rate of progress'.<sup>35</sup>

### 3. Conclusion

Three propositions on the labour market are accepted by both Pigou and Marshall. Firstly, the payment of wages below the value of the marginal product is unfair. Moreover, unorganised workers faced by non-chivalrous employers are likely to be paid a wage below the value of their marginal product to the firm. Secondly, a principal goal of policy must be to raise the standard of living of those workers receiving low wages irrespective of whether they are receiving fair wages or not. That is, justice in the labour market is not achieved simply when the fair wage is paid. Thirdly, uniform national minimum wage legislation is an inefficient policy to adopt to meet the problem of the working poor.

Where Pigou and Marshall appear to differ is in terms of Pigou's greater insistence on the incidence and severity of exploitation (reflected in some degree in the language used) but more importantly in the program required to raise the standard of living of poor workers. The

early Pigou retains much of Marshall's broad program emphasising both State and non-State actions in redistributing income. However, Pigou increasingly focussed on the single channel of State spending to meet the minimum standard.

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## Notes

1. Pigou had previously published several short papers and in 1903, *The Riddle of the Tariff*.
2. Pigou draws on a long list of Marshall references including *Economics of Industry*, Marshall's Preface to Price's *Industrial Peace*, 'Co-operation', 'Some Aspects of Competition', *Principles of Economics*, and *Elements of Economics of Industry*.
3. Bharadwaj (1972), however, reveals in her study of Marshall's marginal notes to Pigou's *Wealth and Welfare* (1912) that Marshall had difficulties with Pigou's construction of the marginal supply relationship and his treatment of increasing and decreasing returns. A referee highlighted a further recorded instance of Marshall's concerns with Pigou's work. On reading Pigou's *The Economy and Finance of the War* published in 1916, Marshall wrote to Pigou commending him for his book but noting that he was 'a little frightened' at the possibility that some of what Pigou says in the book is likely to mislead 'people who do not know the ropes of economic complex interactions' (Whitaker 1996, letter 1058).
4. See Collard (1981, 1990) and Groenewegen (1995) for general assessments of the Marshall-Pigou link; Fry (1976) compares Marshall and Pigou on the role of the State.
5. Despite the close links between Pigou's *Wealth and Welfare* published in 1912 and *The Economics of Welfare*, the former work contains no direct treatment of 'exploitation'.
6. On Marshall's use of language, recall Marshall's replacement of the term 'natural' with 'normal' in *The Economics of Industry*. The issue of Marshall's and Pigou's use of language is discussed further below.
7. Pigou set out his technical analysis on the range of indeterminateness in Appendix A to *Principles and Methods of Industrial Peace*. It is of some interest that the young J.M. Keynes had assisted with the diagrams in the Appendix. As acknowledged by Pigou, Edgeworth's *Mathematical Psychics* had some influence on the development of his range of indeterminateness analysis. See Creedy (1990) for a discussion of Edgeworth and Marshall on wage bargaining models.
8. The demand for a living wage was made in the parliamentary debates surrounding the introduction of Trades Boards legislation in 1909 and again at various points thereafter including the crisis debates surrounding the coal miners strike of 1912, the introduction of Agricultural Wages Boards in 1917 and the introduction of the Trades Boards Act of 1918. The Fabians had, of course, advanced the National Minimum policy from the 1890s (see McBriar 1962). Despite Pigou's rejection of the living wage policy, he was clearly influenced by the broader contours of the Fabian national minimum framework. It may be noted in this context that Pigou makes relatively frequent reference to the Webb's work in his books and articles.
9. The 'Pigou-Robinson' theory of exploitation is misleading because of the radically different frameworks utilised by Pigou and Robinson in their respective analyses of exploitation, see Flatau 1997.
10. In the first edition of *The Economics of Welfare* published in 1920, the allusion to Marshall's 'fair wages' is prominent being placed at the beginning of the relevant chapter. In subsequent editions, the reference to Marshall becomes more submerged in the text.
11. A referee pointed out that 'exploitation' was one of the words examined by Raymond Williams in *Keywords* (Williams 1988). Williams' entry for exploitation provides further examples of early usages of the word exploitation. It is instructive to read Williams' entry in conjunction with the introduction to *Keywords* which explores the development of the meaning of words within a cultural context.

12. That Cannan was the author of the entry on 'exploit' for the Palgrave is not surprising given his interest in distribution theory and his prior analysis of the issue of exploitation. In a paper read to the Fabian Society on July 5 1889 (see Cannan 1889), he makes reference to the phrase the 'subjection of labour to capital'. Cannan goes on to remark that possibly the phrase 'means that owners of capital 'exploit' labourers. A person who says that labourers are exploited cannot very well be contradicted unless he is rash enough to give an explanation of the word, which he very seldom is. If exploit means anything, I suppose it means to employ at competition wages' (Cannan, 1889 p.82). See also Cannan (1914 p.73).
13. But note that Engels wrote a synopsis (in English) of *Das Kapital* for the *Formightly Review* in 1868 in which the term 'exploitation' was frequently used. A referee pointed out that Marshall was an avid reader of the *Formightly*. (It should be noted that Marshall was fluent in German and would not have required the assistance of Engel's English synopsis.) Marshall's notes are held in the Marshall Archive at the Faculty of Economics and Politics, University of Cambridge, Marshall 3/11 (formerly Box 5/1E).
14. S is surplus labour, C is constant capital, and V is variable capital.
15. This extract so since the second edition of the *Principles* (see Guillebaud, 1961, vol 2, p633). In the first edition the corresponding section read: 'They have argued that the value of a thing consists exclusively of the labour that has been spent in making it; and that therefore the payment of interest is a robbery of labour.' While the term 'exploitation' was not used in this passage, it was adopted in the Historical Note on Definitions of the Term 'Capital' appended to Book II, Ch. V (p.138) in the first edition of the *Principles*: 'Karl Marx and his followers lay down the doctrine that only that is capital, which is a means of production owned by one person (or group of persons) and used to produce things for benefit for another, generally by means of the hired labour of a third; in such a wise that the first has the opportunity of plundering or exploiting the others.' For a later reference to Marx's analysis of exploitation see Marshall (1919, pp.71-72). A reference to 'exploitation' is also made in Marshall (1890).
16. Marshall returns to the distinction between 'normal' and 'natural' in the *Principles* when referring to Adam Smith's use of the term 'natural'. See Marshall (1920, p.758).
17. The earliest use by Pigou of the word 'exploitation' the author could find is in his paper 'A Minimum Wage for Agriculture' published in *The Nineteenth Century* in 1913. Here Pigou suggests that the establishment of a minimum wage in cases involving payments below the normal level will have the following effect: 'Labourers upon whom formerly exploitation was practised would now be exploited no longer. Their employment would be as extensive as before their wages would be rather larger; and there would be no compensating evil to be set against this gain' (Pigou, 1913 p.1175). Moreover he notes that the explanation for the exploitative wages is 'a species of monopolistic action on the part of a group of local farmers' which restricts the economic forces which would tend to raise wages to their normal level.
18. Pigou's *Economics of Welfare* also includes a discussion of the arbitration locus — the range of 'practicable bargains' — which also follows *Principles and Methods of Industrial Peace*.
19. Saltmarsh and Wilkinson (1960) note that Pigou held a part-time appointment on the Board of Trade.
20. See Guillebaud (1961), Petridis (1973, 1990), Whitaker (1974, 1975), Matthews (1990), and Groenewegen (1995) for an outline of the development of Marshall's theory of wages and the role of trade unions.
21. The net return of labour equals the 'value of the produce which he [the worker] takes part in producing after deducting all other expenses of producing it' (Marshall and Marshall 1885 p.133). The definition adopted of free competition in this early work is revealing as it revolves around both the attitudes adopted by participants in the market together with the industrial structure of the market rather than simply the industrial structure of the market itself (Marshall and Marshall 1885 p.vi). Individuals compete freely when they do not act in combination and pursue their own (and children's) material advantage (the so-called *active principle*). The long-run is that time period when the so-called *passive* elements such as custom, inertness, and ignorance have been overcome by active forces. Long-run forces dominate and are, therefore, taken as the 'normal' outcome. Long-run competitive wages are designated as normal wages.
22. See Matthews 1990 for a further discussion of Marshall's views on the employer's advantage.
23. In this context it is worthwhile noting that even J.B. Clark adhered to the bargaining disadvantage of labour model, see Clark 1902. At various points in *Principles and Methods of Industrial Peace*, Pigou referenced Clark's work including the above mentioned work.
24. The phrase the 'non-exploitation' theory of wages comes from Hamilton's 1922 survey of wage theories. Hamilton (1922) describes the 'productivity' theory of wages as a 'non-exploitation' theory of wages because 'under analysis it becomes an argument that, in buying labour and selling its products, the employer cannot appropriate an 'unearned' surplus produced by labour'. He contrasts the productivity theory with the exploitation theory of wages presumably derived from Marx.
25. Consider also Marshall's views on just outcomes and fair wages contained in his discussion of fair wages in the preface to Price's *Industrial Peace*. In making judgements about fair wages, Marshall was not 'trying to settle according to any absolute standard of justness' how much workers should receive. Indeed the normal

rate has no claim to be an absolutely just rate; it is relative to the existing state of things here and now' (Marshall 1883 p.198, 1887 p.xi). A point of curiosity: a close inspection of Pigou's reproduction of selections of Marshall's original *Preface* in the *Memorials* reveals that Pigou did not follow precisely the original text. The above phrase is reproduced as '... it is relative to the existing state of things at a particular place and time.'

26. See Snowden (1912) for the presentation of the case for a living wage from the parliamentary wing of the labour movement.
27. As pointed out by a referee, Marshall's general opposition to minimum wages was forcibly expressed in the Labour Commission (see Groenewegen, 1996).
28. Pigou submitted letters to the *Times* at regular intervals concerning policy issues. While not as engaged in government committee work as Marshall, Pigou did serve on Cunliffe Committee on the Foreign Exchanges, the Chamberlain Committee on the Currency and the Bank of England and was involved in the Royal Commission on the Income Tax (see Saltmarsh and Wilkinson, 1960).
29. It is interesting to note that Wicksteed advanced a program of support for minimum conditions and rejection of a national minimum wage at roughly the same time and in the same form as Pigou. See his little known paper 'The Distinction Between Earnings and Income, and Between a Minimum Wage and a Decent Maintenance: A Challenge' read at the Inter-Denominational Summer School at Swanwick, Derbyshire in 1913.
30. As pointed out by a referee, a marginal productivity theory of wages was visible in *Economics of Industry*.
31. Marshall: 'It may be too late to get rid of poverty in our generation; let us resolve that our children, or at all events our children's children, shall be free from it'.
32. For an earlier indication of his views, see Marshall's 1873 paper on the Future of the Working Classes and his Lectures to Women.
33. See also his 'Where to House the London Poor' of a year earlier (1884).
34. See also Marshall's 1917 paper 'The Equitable Distribution of Taxation'. For a further discussion on Marshall's change of mind on the consequences of graduated taxes on capital accumulation see Groenewegen (1990).
35. For a similar viewpoint see Marshall (1919 p.viii). As outlined in detail in Groenewegen (1995), Marshall's position on 'socialism' changed considerably over his lifetime. See McWilliams Tullberg (1975), Elliott (1990) and Groenewegen (1995) for a discussion on Marshall's tendency to socialism.

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