

G. Criticism of Kuznets criteria

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Dear Simon:

As far as I can make out, your criteria for identifying the final product of government (other than capital formation) are four in number: (1) you first distinguish between (a) services provided at a price that is not merely a token price and (b) those given gratis or at a token price; (2) to group (a) you apply the usual test for distinguishing between (a1) finished and (a2) unfinished goods (as stated by you, the test is purchase or use by individuals in their capacity as ultimate consumers or in their capacity as members of business firms); (3) group (b) is broken down between (b1) services available only upon an individual's overt initiative and (b2) all other services, the latter being considered entirely "unfinished"; (4) to group (b1) you apply the criterion of similarity to "widespread" private services commanding a price, thus distinguishing between (blx), which includes those items in (b1) which are so similar, and (bly), which includes all other items in (b1), which are considered entirely unfinished; and finally, (5), you apply to items in (blx) the same criterion used in step (2) above, distinguishing between (blxI) finished and (blxII) unfinished. The final product of government is, then, group (a1) plus (blxI).

Questions may be raised concerning each of these steps. To many of them you yourself have pointed. When is a price a token price will raise some trouble in connection, for example, with the N. Y. City subway system and similarly subsidized government utilities, but I presume this question is not very important.

More significant is the ^{basic} question, what is finished and what is unfinished? The usual test seems arbitrary, at least in the sense that no really satisfactory rationale for it has yet been stated. Even if one may admit that business concerns buy few, if any, consumers' goods and services for "free" transfer to employees, owners or customers, it does not seem

which runs all through - incl. the non profit sectors.

admissible that all goods purchased by consumers are strictly "finished". You imply as much in discussing the "paid bodyguard" problem. If you are going to consider police services unfinished, don't you have to do the same with locks, safes, and theft insurance purchased by consumers? If you're going to consider the latter to be final goods, don't you have to do the same with all police services in suburban communities in which no industry is situated? How can you draw a line between police protection of life and limb and medical protection of life and limb?

This leads me to the "overt initiative" criterion. I see no real difference between the protection purchased by a father for his innocent children and the protection purchased by a large group -- whether a fraternal group, philanthropic association, or government -- for its members or subjects. The government -- even in a democratic society -- is a pater familias too. A good deal even of government medical and health service is forced on individuals in one way or another. *Even education is forced.*

As for the similarity to "widespread private services" criterion: I suspect that your "eventually free government medicine" paradox undermines this criterion. If the paradox is resolved as you suggest will you not violate an important principle of invariance? Suppose, for example, that business men decide that it is essential to provide their men with free hot lunches of a superior type and to prohibit the sale of hot dogs on their premises. Will this turn the lunch into an unfinished good? One might also argue, in connection with the paradox, that a change in taste (opinion) has occurred; and that the two situations can not be compared at all. This particular line of argument is sympathetic to yours, but does not reach the same conclusion.

Some details: I am unhappy about your putting the legislative function into your group (iii), p. 74. This function belongs under (v), because it involves decisions to perform functions falling into all other groups. The same goes for the "higher judiciary", which serves largely to interpret decisions of the legislature; and such executive departments as "public buildings", which cover various functions. And why do you put highways under (v)? What is the private analogue of highways?

Where does this leave us? Speaking for myself, I would suggest merely that we follow the usual criterion of finished and unfinished: services rendered to consumers, whether or not they use initiative in obtaining them and whether or not there is a private analogue, should be treated as finished. This would involve a classification similar to yours on p. 74, except that I would probably put police and such functions into group (v); and I would confine group (v) to services for which there is some obviously reasonable basis for division between finished and unfinished. Group (iii) would then include services for which no such obvious basis can be found -- but it would not be defined as unfinished. It would be treated as a peripheral group, at the margin of uncertainty, and I would prepare totals of finished goods both including and excluding it.

I would prefer to handle this problem in the way we handle the house-wife paradox today: we leave it as a paradox, note it to be a possible source of bias, and "watch" the magnitude of the bias. An even better course is to treat free government medicine as a final product even if there is no longer any private medicine; just as the better way of handling the housewife paradox is to include the value of wives' services in the national income. We certainly do not say that "one could argue" that when housekeepers get married there is a real decline in national

But I wouldn't stop there. I would go on to point to two significant qualifications of the totals: (1) The decision to treat all goods and services purchased and/or consumed by consumers as final products, and all goods and services purchased and/or consumed by business houses as intermediate products (except for capital formation), is in some respects an arbitrary one. It can lead to a serious bias in national product as a measure of welfare. I would discuss the elements tending to strengthen or offset this bias. (2) In comparing two situations or periods, two troublesome problems arise. One is the problem of differences in tastes. Another is the problem of differences in the environment; e.g., the North-South differential in fuel needed to maintain a given degree of comfort. These environmental differences may be natural or social. Climatic differences are natural. The need for certain services in highly urbanized communities, services which are not needed in rural or less urbanized areas, leads to a social difference. Another example of a social difference may be found in the international field. An increase in military measures in Country A will heighten its social security and therefore its welfare (if that act does not lead to "reprisals"). But to Country B there will appear a change in the environment.

I realize that my solution is really no solution. It does not get rid of the peripheral group; nor does it obviate the need for qualifications along the line of the preceding paragraph. But I don't think that we can ever get closer to a solution than that; production and consumption are too closely integrated.

Whatever you decide on your criteria, I hope you will apply them to the U. S. data for the period 1900-1946. I'd like to use the results in one section of my study of government employment -- though I do not promise to stick to your categories.

I shall try to read your criticism of Hicks soon. I must admit, however, that I take so little stock in his position that I can't get very excited about a criticism of it.

Sincerely yours,

Solomon Fabricant

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