THE INTER-WAR ECONOMY IN THE WRITINGS OF CONTEMPORARY ECONOMISTS

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CONTENTS

ABSTRACT

This dissertation takes as its starting point the view that although scholarly research dealing with the inter-war British economy produces transparent assessments of the available evidence, an emphasis on modern economic theory may stifle an understanding of the prevailing economic and social environment. The work focuses on a variety of popular and academic inter-war economic texts in order to gain an impression of contemporary interpretations of the inter-war British economy. Although appearing to fall between the disciplines of economic history and the history of economic thought, the work is firmly intended as a contribution to the former.

The work concentrates on the psychological and emotional interpretations presented by inter-war economists. The first theme of the study deals with contemporary opinion regarding impediments that appeared to be preventing the British economy from responding to post-war economic conditions. A variety of topics are examined including the trade cycle, unemployment, economic development, government expenditure, free trade, protectionism, and economic integration. The second theme deals with contemporary interpretations of the vicissitudes of the sterling-dollar exchange and the events surrounding the financial crisis of 1931.

It is suggested that the study of such economic texts contributes to a more heterogeneous methodology, and provides a fresh perspective on several topics of modern historiography.

DECLARATION AND COPYRIGHT STATEMENT

No portion of the work referred to in the thesis has been submitted in support of an application for another degree or qualification of this or any other university or institute of learning.

For Mum, Dad and Paul

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THE AUTHOR

Christopher Godden was born in 1978 and graduated from the University of Manchester with a BA in Economic History and Economics in 2000, and an MA in Economic and Social History in 2001. His primary research interests are concerned with the relationship between British inter-war economic history and the history of inter-war economic analysis.

CHAPTER 1

INTRODUCTION

> "You will find lots of people ready with explanations. 'This is the breakdown of capitalism', some will say. 'This is the wickedness of trade unions in holding up wages', others will say. 'No, it is the wickedness of the banks in refusing credit'. 'It is the wickedness of foreigners in stopping trade by tariffs and quotas'. 'No, it is our own absurdity in following their example'. Or, finally: 'This is the result of an over-generous system of relief for the unemployed'. You can have your fill of explanations."
>
> William Beveridge[1]

> "The authors of books, editors of journals, leaders of schools of opinion, furnish their services in quite un-rationalized competition with each other."[2]
>
> D. H. Macgregor

> "I write as an observer, not from experience!"
>
> J. H. Jones[3]

Introduction

This thesis examines contemporary economic impressions of, and reactions to, the changing contours of the British inter-war economic landscape, and offers some account of their potential relevance to the study of inter-war economic history. Whilst it may be argued that the topic falls between the disciplines of economic history and the history of economic thought, this work is firmly intended as a contribution to the former.

[1] Beveridge, W. (1935) 'Rake's Progress in Unemployment', *The Listener*, 13 (27 February), p. 259
[2] Macgregor, D.H. (1934) *Enterprise, Purpose & Profit*, Oxford: Clarendon Press, p. 42
[3] Jones, J.H. (1930) 'Changes in World Demand', *The Accountant*, 83 (29 November), p. 731

In this introductory chapter, we shall explore some of the established methodological problems associated with the study of economic history, suggest how these may be overcome through a study of contemporary economic texts, and examine the character of the source material. We shall also outline some of the limitations associated with this material. A chapter breakdown of the thesis is also provided.

In addition to purely theoretical texts, many respected inter-war economic commentators regularly contributed letters, articles and reviews[4] to a variety of newspapers and journals. Such material cannot be classified as contributions to economic theory, but rather as social documents that reflected thoughts and observations upon contemporary issues. As will be demonstrated below, it was through this literature that economists sought to expound their views on the structural and psychological forces hindering Britain's post-war economic reconstruction, explain the ways in which they believed government policy could be utilised to influence the activity of economic agents, as well as discussing events surrounding the restoration of the gold standard and the financial crisis of 1931.

The unprecedented economic instability of the British inter-war economy, represented by the dislocation of once prominent export industries and the persistent burden of unemployment, has long provided a fertile ground for historical research. Yet the economic histories of this period, including works by Richardson[5], Buxton

[4] The importance of book reviews should not be underestimated in this context should not be ignored. For an interesting discussion of the relationship between economics and book reviews, see Newman, P. (1990) 'Reviews by Edgeworth' in Hey, J.D & Winch, D. (eds.) *A Century of Economics: 100 Years of the Royal Economic Society and the Economic Journal*, Oxford: Basil Blackwell, pp. 109 – 142

[5] Richardson, H.W. (1967) *Economic Recovery in Britain, 1932 – 1939*, London: Weidenfeld & Nicolson

and Aldcroft[6], Capie and Collins[7], Broadberry[8], Matthew,[9] and Solomou[10], do not employ the views of contemporary economic writers. Other areas of the modern literature have focused on the output of a select group of high theorists[11], the delayed official reaction to the Keynesian policy prescription,[12] and the relationship between the professionalisation of twentieth century economists, economic policy and Britain's relative economic decline.[13] Put simply, modern historiography is devoid of any systematic examination of the popular aspects of the inter-war economic literature.

Methodological Questions

How does an appreciation of "popular" contemporary economic material assist historical inquiry? To simply seek to rescue forgotten economic opinions from the condescension of posterity can hardly be considered a sufficient motive. As Keith Tribe has observed, a "better acquaintance" with a neglected area of economic

[6] Buxton, N.K. & Aldcroft, D.H. (1979) *British Industry Between The Wars: Instability and Industrial Development, 1919 – 1939*, London: Scolar Press

[7] Capie, F. & Collins, M. (1983) *The Inter-War British Economy: A Statistical Abstract*, Manchester: Manchester University Press

[8] Broadberry, S. (1986) *The British Economy Between the Wars: A Macroeconomic Survey*, Oxford: Basil Blackwell

[9] Matthews, K.G.P. (1986) *The Inter-War Economy: An Equilibrium Approach*, Aldershot: Gower Publishing Co. Ltd

[10] Solomou, S. (1996) *Themes In Macroeconomic History: The UK Economy, 1919 – 1939*, Cambridge: Cambridge University Press

[11] See, for example, Shackle, G.L.S. (1967) *The Years of High Theory: Invention and Tradition in Economic Thought, 1926 – 1939*, Cambridge: Cambridge University Press; Laidler, D. (1999) *Fabricating the Keynesian Revolution: Studies of the Inter-war Literature on Money, the Cycle and Unemployment*, Cambridge University Press, Cambridge; and Dimand, R.W. (2003) 'Inter-war Monetary and Business Cycle Theory: Macroeconomic Before Keynes' in Samuels, W.J, Biddle, J. & Davis, J.B. (2003) *A Companion to the History of Economic Thought*, Oxford: Blackwell Publishing Ltd, pp. 325 – 342

[12] See, for example, Peden, G.C. (1980) 'Keynes, the Treasury and Unemployment in the Late Nineteen-Thirties', *Oxford Economic Papers*, 32, pp. 1 – 18; Booth, A. (1989) *British Economic Policy, 1931 – 1949: Was There A Keynesian Revolution?*, London: Harvester Wheatsheaf and Middleton, R. (1985) *Towards The Managed Economy: Keynes, the Treasury and the Fiscal Policy Debate of the 1930s*, London: Methuen.

[13] Middleton, R. (1998) *Charlatans or Saviours? Economists and the British Economy from Marshall to Meade*, Cheltenham: Edward Elgar

analysis, although in it self intellectually rewarding, may ultimately teach us nothing "apart from its difference and limitations." The associated opportunity costs imply that there must be something "more compelling than personal curiosity and perversity" to motivate such research.[14] Given that the potential benefits of examining contemporary economic texts are far from self-evident, I shall briefly outline two methodological problems, both of which support the intellectual legitimacy of the research topic.

The first methodological problem relates to the supposed efficiency of research markets. It is widely accepted that continuous, academic investigation guarantees research market efficiency, so leading to the belief that knowledge advances by accumulation. The methodological implications of this argument are (a) that antiquated and inadequate arguments, having been constructed without proper theoretical foundations or knowledge of events, are consigned to the flames, (the so-called "wrong opinions of dead men" argument[15]), but also (b) that any significant information developed by past research will be integrated into the modern literature. The theme that past analysis is of negligible value to modern practitioners is one that permeates many areas of scholarly research. Unless a chemist is specifically interested in the history of his subject, for example, it is assumed he will gain nothing from an examination of the works of Lavoisier, Cavendish or Priestley; unless a mathematician is interested in the history of his subject, he will gain nothing from the work of Lagrange, Euler or Gauss. Through the evolution of human knowledge, it is assumed that there can be no material benefit from raking among the embers of a fire that has long since burnt itself out. In slightly more prosaic terms, neo-classical

[14]Tribe, K. (1988) *Governing Economy: The Reformation of German Economic Discourse, 1750 – 1840*, Cambridge: Cambridge University Press, p. 4

[15]Commonly attributed to Pigou, the phrase is of doubtful origin, and has been variously ascribed to John Maynard Keynes, Frank Knight, and Jean-Baptiste Say.

economics would suggest that, through the efficiency of research markets, the expected marginal product of studying archaic economic texts is zero.[16] However, forces that impede market efficiency are a recognised element of microeconomic theory. This leads us to question whether widespread belief in research market efficiency is fully justified. A possible cause of such inefficiency arises from the tendency of economists and economic historians to employ a select group of academic writers or texts to buttress their arguments. The most famous example of this is John Maynard Keynes, for although the Keynesian hegemony has declined, the position of Keynes as a figure of intense historical and intellectual interest persists. Further more, if researchers conform to the prevailing ideas of the wider academic community, a particular methodological approach may establish an advantage across a range of research programs, thereby imposing unexpected constraints on subsequent research. Research market inefficiency therefore arises from the inability of research programs to deviate from their established "path". In a more formal sense, such inefficiency arises once research programs become set on a non-ergodic path.[17]

A second problem, directly related to the first, arises from the increased application of modern economic theory to the study of economic history. This may be taken as a restatement of the "Ricardo-Malthus" problem. On one side, Ricardo wielded the classic principle of Ockham's razor[18], arguing that the ability to reduce phenomenon to a select number of variables enabled the central features to be identified. On the other side, Malthus argued that abstraction from the complexities

[16]Anderson, G.M. & Tollison, R.D. (1991) 'Dead Men Tell No Tales', in Blaug, M. (ed.) *The Historiography of Economics*, Aldershot: Edward Elgar, pp. 171 – 173

[17]Khalil, E.L. (1995) 'Has Economics Progressed? Rectilinear, Historicist, Universalist, and Evolutionary Historiographies', *History of Political Economy*, 27, p.79

[18]*entia non sunt multiplicanda praeter necessitatem* ("entities are not to be multiplied beyond necessity")

of the real world signalled an intellectual unwillingness to acknowledge other forces that could be in operation.

We cannot lightly dismiss the phenomenal analytical and technical developments of economics over the past fifty-years. Yet since the methodology of economic history is firmly rooted in the methods of economic science, the changing structure of economics has inevitably influenced the research programs of economic historians.[19] As Douglas C. North once observed:

> "Economic historians are predominantly economists rather than historians and systematically use the tools of economics."[20]

The intensity of the modern dialogue between economics and mathematics has led economic theory to move away from depicting the real world, to creating its own idealised form. By attempting to emulate the principles of the physical sciences, and so develop universal truths regarding economic activity, modern economics has forced our perception of economic activity, in any period, to conform to the supposed formal relationships between economic variables. This raises serious questions regarding the use of modern economic laws to understand historical settings distant from our own. In the real world, individuals are forced to exist in a constantly changing climate of risk and uncertainty. It need hardly be said that history is never neat. Yet *ex post*, everything can be justified; risk and uncertainty vanishes, and history is reconstructed as a logical and unavoidable course of events. There is therefore solid ground to argue that the methodology of modern economic history, although clearly dazzling in its boldness and composition, acts to exclude forces that

[19]Marwick, A. (2001) *The New Nature of History: Knowledge, Evidence, Language*, Hampshire: Palgrave, p. 126
[20]North, D.C (1976) 'The Place of Economic History in the Discipline of Economics', *Economic Inquiry*, 14, p. 461

reflect the intellectual, emotional, political and/or social conditions of a particular historical period.

It should be made clear that this methodological critique is by no means original. For example, Salvati has argued that the economic model "redefines history with dangerous convenient assumptions", while Cipolla has denounced the use of sophisticated economic models as "a kind of research fetish."[21] In a similar vein, McCloskey has suggested that the modern desire for statistical precision – that is to say, the attempt to view economic activity through the prism of statistics – only serves to marginalise important questions relating to the human character and judgements of economic agents.[22]

How does the modern academic situation contrast with the approach of economists writing during the late nineteenth and early twentieth century? For these economists, the desire to appreciate the broad canvas of economic existence required some understanding of the prevailing psychological and spiritual environment.[23] In attempting to identify and document the qualities of modern life, inter-war economists sought to ground their impressions in economic and social reality. It is therefore suggested that, similar to a photograph, academic and, more importantly, popular economic literature from the inter-war period captured some of the energy and immediacy of contemporary economic forces. While reflecting issues in the history of political thought, Robert Wokler's comments on the authority of political manuscripts is equally applicable to the defining qualities of ephemeral economic texts:

[21]Cipolla, C.M. (1991) (trans: C. Woodall) *Beyond History and Economics: An Introduction to Economic History*, Oxford: Basil Blackwell, p. 69

[22]McCloskey, D.N. (1999) *The Rhetoric of Economics*, Wisconsin: University of Wisconsin Press (2nd edition), p. 112.

[23]As examples of this, see Ashley, W.J. (1899) 'American Trusts', *Economic Journal*, 9 (June), p. 162; Foxwell, H.S. (1914) 'Review – 'Money-Changing: An Introduction to Foreign Exchange' by H. Withers', *Economic Journal*, 24, p. 256; Jones, J.H. (1935) 'Materialism', *Accountant*, 93 (9 November), p. 621

> "They may articulate a free association of ideas and give expressions to dreams that wend across disciplines...[T]hey are genuine *pièces fugitives*, not to be confined to quarters, bursting from their contexts."[24]

It is not suggested here that all pronouncements made by inter-war economists were wholly accurate. No economist of the period, not even the redoubtable figure of Keynes, can be said to have possessed the facility of consistent judgement: the act of writing in the flow of events guarantees the presence of mistaken associations and erroneous conclusions. As an example of this, we may note Francis Hirst's criticism of Churchill's inflammatory views regarding Nazi Germany's rearmament program.[25] Yet the existence of such errors does not negate the fact that economists used such material to capture an impression of contemporary economic, social and political forces. A similar theme has been presented in a recent article by Federal Reserve economist, Paul Harrison, who argues that the study of seventeenth and eighteenth-century stock market pamphlets provides "direct insights into the institutions, economic behaviour, and economic outcomes of their times."[26] Unless such immeasurable variables are identified and preserved at a particular moment in time, and unless they can be adequately integrated into modern methods of analysis, it is inevitable that modern historical research will resort to wielding Ockham's razor. As Schumpeter once remarked, there is a dangerous tendency amongst economists who employ the techniques of mathematical modelling to treat as non-existent those relationships and forces that cannot easily be formalised.[27]

[24]Wokler, R. (1999) 'The Manuscript Authority of Political Thoughts', *History of Political Thought*, 20, p.109

[25]Hirst, F.W. (1936) 'Mr. Chamberlain's Fifth Budget – Taxation For Defence', *Contemporary Review*, 149 (Jan/June), pp. 658 – 659; Hirst, F.W. (1937) 'The Armament Budget', *Contemporary Review*, 151 (Jan/June), p. 649

[26]Harrison, P. (2004) 'What Can We Learn Today from 300-Year-Old Writings about Stock Markets?', *History of Political Economy*, 36, p. 683

[27]Schumpeter, J.A. (1947) 'Theoretical Problems of Economic Growth', *Journal of Economic History*, 7 (Supplement: Economic Growth), pp. 1 – 9

Let us briefly summarise the preceding paragraphs. The approach of mainstream economics and economic history has presented us with two, interconnected methodological problems: first, excessive belief in the efficiency of research markets when impediments may actually prevent such efficiency; and second, the apparently malignant influence of modern economic analysis in distorting an appreciation and understanding of economic forces in specific historical periods. The ability to reconstruct (as far as possible) impressions and opinions from within the inter-war economic environment contributes to the established historiography by providing an opportunity to catch the vagaries of human nature (or, the subtleties of a "vanished age") without the filters of modern explanatory methods or *ex post* knowledge. It should be stressed that this thesis makes no attempt at a definitive treatment of the inter-war economic debate. Indeed the accompanying bibliography covers only a fraction of the voluminous contemporary literature. No claim is made to have read every book or article written by each member of the selected group of economists, nor to have provided a minutely scrupulous examination of every idea presented in the inspected literature. It should also be stressed that this thesis moves away from the traditional focus on Keynes, with the intention of gaining a broad overview of the inter-war economic debate.

On the basis that a healthy academic discipline requires an eclectic mixture of methodological debates, I claim the topic a legitimate subject for intellectual inquiry.

Source Material

Given that this thesis focuses on a large body of previously neglected material, it is perhaps important to gain some understanding of the selection of particular commentators and non-academic journals.

The vast majority of professional economists surveyed in this thesis were selected on the basis of their initial training in a critical school of economic thought, and their subsequent academic positions at a number of British universities.[28] In many respects we therefore adhere to the established group of academic/professional British economists from first half of the twentieth century.[29] Very occasionally we ignore the above definition of "economist" in order to examine the work of authors who would not normally be included on the established list. It is readily accepted that when including commentators at the margin of the academic debate, there exists the potential danger of obscuring the characteristics of the professional debate by encompassing too large a body of non-professional views. Since there existed "no equivalent of the General Medical Council to prevent unauthorised practitioners eager to prescribe cures"[30], the inter-war period provided an ideal opportunity for pseudo-economic commentators – ranging from well respected business leaders[31] to such figures as Major Douglas[32] and Oswald Mosley[33] – to deluge post-war society with articles and pamphlets proposing remedies covering all aspects of Britain's post-war economic difficulties.[34] No apology is made, however, for introducing into

[28]One noticeable omission from this thesis is Joan Robinson (1903 – 83) who appears to have remained committed to questions of high theory during the inter-war period rather than venturing into the popular press.

[29]For biographical information on many of the established group of academic/professional British economists included in this dissertation, see the Appendix to this work.

[30]Cole, G.D.H. (1931) 'Gold and the Crisis', *New Statesman & Nation*, 2 (24 October), p. 520

[31]Higgs, H. (1920) 'Business Men on Money', *Economic Journal*, 30 (December), p. 511

[32]Major C.H. Douglas (1879 – 1952), possibly the most famous economic "crank" of the inter-war period, whose theory of "social credit" gained political support in Australia, Canada and New Zealand.

[33]Oswald Mosley (1896 – 1980), leader of the British Union of Fascists, who in works such as *Revolution by Reason* (1925) and *Tomorrow We Live* (1938) advocated policies to reduce unemployment.

[34]The democratisation of economic discourse during this period have been attributed by Kadish and Tribe to the growing powers and responsibilities of central and local administration. See Kadish, A. & Tribe, K. (1993) 'The Supply and Demand for Economics in Late Victorian Britain' in Kadish, A. & Tribe, K. (ed) *The Market for Political Economy: The advent of economics in British university culture, 1850 – 1905*, London: Routledge, p. 8. The increased democratisation of economic discourses may be traced back to the early nineteenth century. On this topic, see Fetter, F.W. (1962) 'Economic Articles in the Westminster Review and Their Authors, 1824 – 51', *Journal of Political Economy*, 70, pp. 570 – 596, and Fetter, F.W. (1965) 'Economic Controversy in the British Reviews, 1802 – 1850', *Economica*, 32, pp. 424 – 437

the following discussion a small group of non-professional inter-war economic commentators whose views add an interesting dimension to our understanding of the contemporary debate. This group includes such writers as the social scientist, Alexander Carr-Saunders, the journalist, Harold Cox[35], the industrial commentator John Hilton, and the civil servant and economic advisor, E.M.H. Lloyd.

Turning now from the selection of writers to the selection of their writings studied in this thesis, it should be understood that this has been governed by the desire to capture their immediate impressions of economic events. The desire to impart an immediate view on a particular topic implied that such commentators (both professional and non-professional) were reliant on such transitory forms of communication as newspapers, public lectures and later radio broadcasts.[36] As will be demonstrated throughout this work, this approach did not reflect a desire to popularise economic ideas for their own sake, but a fundamental belief in the therapeutic properties of making economic arguments intelligible and familiar to the general public. Walter Layton, for example, prescribed "the fullest possible publicity" in order to alleviate suspicion, eradicate ignorance, and establish "confidence in the economic system".[37] A more political motive was advocated by Harold Cox, who stated that the elaboration of economic arguments served as a

[35]Although little remembered today, Harold Cox spent much of his life denouncing various aspects of British economic and social policy. As a consequence of this, he was identified by other contemporary writers as an economist. See, for example, Cox's obituary notice in *The Times* (2 May 1936), p. 9, c. C

[36]These broadcasts ("wireless talks") do not appear to have survived (it is doubtful whether they were ever recorded). However, radio lecturers were required to adhere rigidly to a pre-prepared manuscript, many of which were published in the weekly BBC journal, *The Listener*. Due to obvious limitations, this work does not deal with educational value of such radio broadcasts, nor their relation to the inter-war consumption of economic arguments. This idea, together with its cultural significance, is worthy of further investigation.

[37]Layton, W.T. (1925) 'Economic Information: What The Public Out To Know', *The Accountant*, 72 (28 March), p. 519

necessary defence against the "wild fanaticism inspired by Marxist theorists."[38] The contrary view was expressed by the economic heretic, J. A Hobson, who suggested that the efficacy ascribed to such publicity reflected a desperate attempt to defend capitalism from proletarian attack.[39]

It is a central tenet of this work that in order to appreciate the distinct character of inter-war economic commentaries, we must move beyond modern preoccupations with purely scholarly texts – such as the *Economic Journal* – and examine the routes by which economists presented their views to the wider public. Middleton has provided a detailed statistical classification of the rhetorical style of articles published in the *Economic Journal* throughout the inter-war period, and notes that where as during the 1920s academic economists were inclined to discuss problems of post-war reconstruction, by the 1930s this tendency had been swamped by the desire to concentrate on abstract theory.[40] This transition is also observable in the popular literature, and the majority of texts examined in this thesis are drawn from the early post-war period through to the mid-1930s. Given Alfred Marshall's heroic desire to make economic analysis intelligible to the educated masses, we may regard the evolution in the character of both the popular and academic inter-war literature as the disintegration of the Marshallian mission.

Yet the tendency amongst historians to restrict their attention to the *Economic Journal* can be seen to distort the historical record of the inter-war economic debate. This modern preoccupation with such scholarly sources ably illustrates Backhouse's criticism that historians are too often inclined to rely on past judgements regarding

[38]Cox, H. (1922) 'Labour Disillusionment', *Edinburgh Review*, 236 (October), p. 397

[39]Hobson, J.A. (1920) 'The New Industrial Revolution', *Contemporary Review*, 118 (July/Dec), p. 639

[40]Middleton, R. (1998) *Charlatans or Saviours? Economists and the British Economy from Marshall to Meade*, pp. 164 – 167

the historical importance of economic texts.[41] It is for this reason that this thesis seeks to supplement ideas presented in the inter-war scholarly literature with economic opinions presented in such popular periodicals as *The Accountant*, *Contemporary Review*, *The Listener* and *The New Statesman.* Yet the immediacy of such articles ensured that they were seldom written for posterity[42], while information imparted through radio broadcasts was quickly forgotten. Judgements regarding the historical importance conferred upon particular texts are notoriously erratic, and the ephemeral nature of many of the popular methods by which inter-war writers expressed their views may go some way to explain modern academic unfamiliarity with vast areas of the contemporary literature.

Given that their task was essentially propagandist, economists adopted a patient tone and sought to express their views and critiques through unashamedly bold, clear literary strokes. The importance of explaining economic problems in the language of the ordinary citizen elicited an interesting remark from Keynes:

> "[A]n economist must be humble; his field of thought lies in the public sphere. He cannot accomplish, except by persuasion – and simplifying."[43]

Whilst we may reflect on the amazement with which early "wireless" listeners comprehended sounds transmitted over great distances, the instructive capabilities of broadcasting were quickly appreciated by contemporary commentators.[44] Radio favoured the common touch, and we may applaud the ability

[41] Backhouse, R.E. (2002) *The Penguin History of Economics*, London: Penguin Books, p. 7

[42] An interesting exception is D.H. Robertson's 1926 article 'A Narrative of the General Strike of 1926', *Economic Journal*, 36 (September), pp. 375 – 393, in which the author stated his desire to record the main events of the strike in the belief they would prove useful for future historians.

[43] Keynes, J.M. (1922) 'The Stabilisation of the European Exchanges: A Plan For Genoa' (20 April) in *Collected Writings of J.M. Keynes – Vol. XVII: Treaty Revision and Reconstruction*, London: Macmillan, pp. 355

[44] See, for example, comments by the onetime Viceroy of India, Lord Linlithgow, on the educative value of radio broadcasting during the 1929 general election, Linlithgow (1929) 'Letter – Increased Public Interest', *Times* (20 May), p. 11, c. F

with which such regular radio commentators as William Beveridge, Dennis Robertson, and Philip Sargant Florence successfully expressed complex economic ideas in a few succinct sentences.[45]

Humour was also an integral element of their presentation, and the substance of ideas was often hidden behind sparklingly whimsical passages. Yet although numerous pieces were irradiated with humour, this method was employed with caution: humorous asides were intended to explain events, advance an idea, and possibly sweeten a bitter pill. Their task was far from being emotionally vacuous, and reactions against the injustices of the post-war environment are often palpable in their statements.[46]

Possibly the most entertaining example of such inter-war propaganda involved Edwin Cannan's attempt to highlight the injurious economic and social consequences associated with the depreciation of the pre-war monetary unit. This concern had been a feature the war-time and early post-war monetary debate, and was presented by, amongst others, Joseph Shield Nicholson[47], Arthur Pigou[48], and Frederick Lavington.[49] Yet in an appeal before the City of Oxford Profiteering Tribunal in November 1919, Cannan not only condemned the unlimited currency notes available through the Bank of England, but employed his opportunity to the

[45]See, for example, Sargant Florence, P. (1930) 'Organisation verses Personal Skill', *The Listener*, 4 (15 October), p 607; Sargant Florence, P. (1930) 'Rationalisation and the Public', *The Listener*, 4 (29 October), p. 706; Roberston, D.H. (1931) 'Booms and Slumps', *The Listener*, 5 (11 February), p. 233; Robertson, D.H. (1931) 'The Backwash of Progress', *The Listener*, 6 (18 November), pp. 870 – 871; Beveridge, W. (1935) 'Non-Economic Nationalism', *The Listener*, 13 (26 June), p. 1083

[46]See, for example, Clay, H. (1929) 'The Human Effect of Unemployment', *The Listener*, 1 (12 June), pp. 822 – 823

[47]Nicholson, J.S. (1916) 'Inflation of the Currency and the Rise in Prices', *Economic Journal*, 26 (December), pp. 425 – 440; Shield Nicholson, J. (1919) *Inflation*, London: P.S. King & Son Ltd, pp. 78 – 107

[48]Pigou, A.C. (1917) 'Inflation', *Economic Journal*, 27 (December), pp. 486 – 494

[49]Lavington, F. (1921) 'The Social Effects of a Higher or Lower Price Level' in Clapham, J.H. et al *Monetary Policy – Being The Report of a Sub-committee on Currency and the Gold Standard*, London: P.S. King & Son Ltd, pp. 41 – 59

fullest by demanding the immediate prosecution of the Chancellor of the Exchequer on the charge of securing a 23,900 per cent profit on the sale of one-pound currency notes.[50] In performing this action, Cannan was seeking to drawn popular attention to the unpleasant situation in which the war-time and post-war financial recklessness of a supposedly civilised nation was leading to the wholesale disposal of obligations such as life assurances, pensions, rents, and long-term leases. Justice could only be secured, he argued, by ensuring the equivalence of the pre-war and post-war British monetary unit, and hence the equivalence of outstanding fixed monetary obligations.[51]

Limitations of Source Material

We must appreciate the difficulties that are presented when attempting to reconstruct the narrative of the inter-war debate. This is an imprecise pursuit. Ideas are fugitive and elusive; the product of either quiet contemplation or profound debate; they range from the trivial to the profound, implying that the complete details of their origins are unlikely to be preserved for posterity. Occasionally the oral tradition found its way into printed form. On the subject of inter-war public finance, for example, Hugh Dalton noted that many of Pigou's views on public finance had been "delivered in lecture form as long ago as 1909."[52] Yet in the main, historians

[50] Cannan, E. (1919) 'An Attempt at Popular Propaganda: Prosecute the Chancellor of the Exchequer for Profiteering!' (14 November) in Cannan, E. (1997) *An Economist's Protest*, London: Routledge/Theommes Press, pp. 195 – 197. The Town Clerk, upon acknowledged receipt of Cannan's complaint, inquired whether it was intended seriously! (*The Times*, 15 November 1919, p.14, c. A)

[51] Cannan, E. (1922) 'Professor Cassel on Money and Foreign Exchange', *Economic Journal*, 32 (December), p. 513; see also Cannan's 'Preface' to Hargreaves, E.L. (1926) *Restoring Currency Stability*, London: P.S. King & Son Ltd, pp. vii – ix. Following the acrobatic performance of the mark, the German courts adopted a similar principle of pre-war and post-war mark equivalence (*mark gleich mark*) in order to ensure the equivalence of outstanding obligations.

[52] Dalton, H. (1928) 'Review – 'A Study in Public Finance' by A.C. Pigou', *Economica*, No. 23 (June), p. 217

are presented with the almost impossible task of attempting to grasp and evaluate the oral diffusion of economic discourse.[53] The impossibility of recapturing such ideas led G.L.S. Shackle to the most sensible and obvious solution:

> "A word spoken by one pupil and repeated by the teacher to another, no one remembering or even knowing the whole circumstances; a conversation at a college dinner table, casually overheard; a remark at a seminar, subconsciously noted; all this is largely gone beyond anyone's recall. The printed record alone is publicly beyond dispute."[54]

Any attempt to catch the uncatchable, any desire to supplement the surviving material with the wider development and diffusion of ideas, is ultimately futile. The printed word is the only true surviving record. Yet acceptance of the primacy of the printed record cannot disguise the associated limitations. While freedom of thought serves as a necessary condition for intellectual inquiry, such freedom may not extend to the means through which any writer seeks to express his views. A writer may possess sufficient intellectual ability to exploit a particular topic, but the necessities of producing articles for "immediate" consumption imposes restrictions. The distinction between academic inter-war articles and articles for the popular press ably illustrates this point.

The production of articles intended for an academic audience would proceed through various stages of scrutiny and refinement. The nature of the intended audience could also impose restrictions upon the overall style of the work. Surviving

[53]See, for example, Ikeda Y. (2001) 'A lecture notebook of Wilhelm Roscher with special reference to his published work' in Shionoya, Y. (ed.) *The German Historical School: The historical and ethical approach to economics*, London: Routledge, p. 34

[54]Shackle, G.L.S. (1967) *The Years of High Theory: Invention and Tradition in Economic Thought, 1926 – 1939*, pp. 22 – 23

correspondence concerning articles submitted to the *Economic Journal* ably illustrate this point.[55] Furthermore, academic articles require a degree of leisurely examination compared with the hurried reading devoted to newspapers or popular journals. We may note Bernard Shaw's remark that publications such as the *Economic Journal* required reading "more or less thoroughly."[56] The production and presentation of articles for "immediate" consumption would occur within a different environment. Presented with a topic (selected either by choice or imposed upon him by editors), an economist would be required to maximise the content of the article subject to a variety of constraints. The necessity of remaining intelligible to an audience would require the economist to simplify problems, condense topics, and express his ideas as briefly and lucidly as possible, subject to editorial policy, completion deadlines, limitations of space, and the expected demands of his audience. The limitations of space were clearly important, and throughout J. H. Jones's weekly contributions to *The Accountant* we find numerous occasions where discussions extended over several articles. The question of deadlines is also illustrated by Henry Hardman's recollections that Jones's need to produce his weekly article meant that "on press day he often wouldn't turn up for students."[57]

It is therefore obvious that although the printed record serves as our only source for reconstructing past economic interpretations, a comprehensive understanding of the contemporary debate eludes us. With history having bequeathed to us the fragmented remnants of long extinguished thought, we must appreciate our limitations.

[55]Keynes, J.M (1983) *The Collected Writings of J.M. Keynes – Vol. XII: Economic Articles and Correspondence*, London: Macmillan, pp. 784 – 810.

[56] Shaw, G.B. quoted in Holroyd, M. (1989) *Bernard Shaw – Volume II, 1989 – 1918: The Pursuit of Power*, London: Chatto & Windus, p. 371

[57]Interview with Sir Henry Hardman in Tribe, K. (ed.) (1997) *Economic Careers: Economics and economists in Britain 1930 - 1970*, London: Routledge, pp. 22 – 23. An alternative interpretation may, of course, be that Jones was more concerned about supplementing his income through journalism.

Chapter Breakdown

This thesis is organised as follows. In the first main chapter (chapter 2), we investigate contemporary war-time and early post-war interpretations of unemployment, the trade cycle, and growing contemporary awareness of the urgent need for Britain to alter her economic structure. The economic literature of the period reveals a body of economists who were fully aware of the process of economic evolution, and the necessity of Britain's post-war economic transformation. In the same way that agriculture had been surpassed by industry, it was recognised that economic activity would have to develop beyond the confines of industry. The themes that develop in the latter half of this chapter outline the inter-war relationship between persistent unemployment and the failure of the market mechanism to move the economy to its new equilibrium. The third chapter develops from this, and considers contemporary awareness of possible psychological, physical and political impediments that were preventing private enterprise from undertaking the necessary process of development. It is through this argument that we shall attempt to liberate contemporary explanations of unemployment from the prison of the real wage argument. Chapter 4 focuses on contemporary perceptions of impediments to economic evolution brought about by hope of protectionism and imperial integration. We shall also consider the effect of Britain's economic problems on the structure of inter-war economic thought. Chapter 5 shifts the focus slightly by considering the contrasting attitudes amongst economists towards the question of increased inter-war government expenditure, and the importance of such expenditure in facilitating Britain's process of change. Chapter 6 moves away from the themes of economic evolution to consider contemporary discussion of the sterling-dollar exchange rate. K.G.P Matthews has pointed out that any discussion of inter-war exchange rates will be dominated by events surrounding the restoration of the gold standard in 1925 and the financial crisis of 1931.[58] This chapter deals with contemporary interpretations of both of these topics, in addition to a brief discussion of the floating exchange rates from 1919 to 1925, and several different explanations of the movement of sterling from September 1931 through to the spring of 1932. Chapter 7 draws the thesis to its conclusion.

[58]Matthews, K.G.P. (1986) *The Inter-War Economy: An Equilibrium Approach*, p. 64

CHAPTER 2

THE TRADE CYCLE, UNEMPLOYMENT, AND ECONOMIC EVOLUTION

Introduction

Economics does not sit comfortably with the anarchy of military conflict. For economists, the cost of conflict is rarely expressed in terms of government financial estimates, but rather the goods and services that soldiers and munitions workers would have produced had their country not descended into the hell of war. The economic cost of a rifle is not equivalent to some monetary figure, but the services that the labourer would have rendered had he not been required to construct it. As a consequence of this, the general trend of British economic thought prior to the First World War had considered warfare purely in relation to specific aspects of commerce and finance.[59] Even during the First World War, the loss of human lives through the Dardanelles operations led William Cunningham to condemn as morally indefensible the unnecessary loss of human life simply to promote national welfare.[60] A similar theme was presented by Cannan, who feared that the pre-war emphasis on production, distribution, and consumption had led economists to ignore the broader

[59]In connection with the Boer War, for example, see, Hirst, F.W. (1900) 'The War Budget', *Economic Journal*, 10 (March), pp. 105 – 108; Price, L.L. (1900) 'Some Economic Consequences of the South African War', *Economic Journal*, 10 (September), pp. 323 – 339

[60]Cunningham, W. (1915) 'Economic Problems After the War' in Kirkaldy, A.W. (ed) *Credit, Industry, and the War*, London: Isaac Pitman & Sons Ltd, pp. 256 – 259. Cunningham was not suggesting that Britain was better served by starving from insufficient wheat supplies (there was never any actual danger of wartime malnutrition), but simple criticism of the wartime emphasis on consumption. The desire to improve Britain's access to Russian wheat supplies through Odessa or Nicolnieff was later estimated to have caused over 200,000 British casualties. Stevenson, D. (2004) *1914 – 1918: The History of the First World War*, London: Allen Lane, p. 117

canvas of human existence. The pre-war use of the word "country" instead of "nation", for example, or "national" instead of "human", reflected the inexcusable fallacy whereby different countries were treated as "watertight compartments."[61] Yet it can not be denied that if economics was the faithful servant of the peacemaker, the long, grim struggle of the Great War had provided commentators of all intellectual persuasions with an ideal opportunity to offer their opinions on the course of post-war reconstruction. Such endeavour was supported by *The Economist*:

> "Although our primary task is to 'get on with the war'...we are not disposed to discourage those who peer into the darkened future and endeavour to settle the bases upon which we shall have to reconstruct our shattered civilisation."[62]

The confusion of the period, however, as Francis Edgeworth pointed out, ensured that any such opinions or predictions owed more "to the spirit of gambling than the cool calculations of economic men."[63]

Certain elements of the wartime economic literature emphasised the negative forces that were expected to undermine reconstruction. These included the probable disintegration of national unity arising from the inconsistent and, occasionally, illegal actions of autocratic munitions tribunals; encroachment on individual liberty through the liquor restrictions; and the transformation of human beings into mere cannon fodder through the policy of universal conscription.[64] In other quarters, the prospects

[61]Cannan, E. (1915) 'Review – 'The Political Economy of War' by F. W. Hirst', *Economic Journal*, 25 (December), pp. 600 – 601
[62]*The Economist* (21 July 1917), p. 89
[63]Edgeworth, F.Y. (1918) 'Review – 'The Economic Causes of War' by A. Loria', *Economic Journal*, 28 (September), p. 320
[64]Hobson, J.A. (1915) 'England's Changing War-Mind', *The New Republic*, 4 (18 September), pp. 173 – 175; Cole, G.D.H. (1915) 'The Meaning of the Trade Union Congress', *Nation & Athenaeum*, 17 (September), pp. 767 – 768; Cole, G.D.H. (1915) 'Through Terror To Triumph?', *Nation & Athenaeum*, 18, (20 November), p. 288; Hobson, J.A. (1916) 'The War and British Liberties – IV: Liberty As A True War Economy', *Nation & Athenaeum*, 19 (29 July), pp. 524 – 525

of peace appeared to imbue a feeling of prosperity. Economic re-mobilisation, it was argued, would be secured through a physically and morally revitalised labour force, moves towards improved relations between capital and labour, and an enhanced technical and administrative structure.[65] As the social commentator, Arthur Shadwell, observed in 1916: "I am certain that complete recovery from the effects of war...will be a matter of a few years."[66] Writing during the early 1920s, R.H. Tawney remarked that, even during the general election and the extended Christmas festivities of 1918, the threat of post-war unemployment had never entered the public consciousness.[67]

Yet following the sudden cancellation of foreign orders in the engineering, shipbuilding and woollen industries during the autumn of 1920[68], G.D.H. Cole expressed his concern that unemployment, widely recognised as the most socially debilitating of all economic problems, was set to inflict its suffering on many workers, in many branches of industry, over the coming years.[69] For the remainder of the inter-war period, unemployment stood considerably above pre-war experiences and was seen to influence everything from political debates to discussions about crime and alcoholism.[70]

The purpose of this chapter is to explore the gradual evolution of inter-war economic opinion regarding post-war British unemployment. This will take us from

[65]Scott, W.R. 'Economics of Peace in Time of War' in Kirkaldy, A.W. (1915) *Credit, Industry, and the War*, p. 15; Price, L.L. (1916) 'The Economics of the War and Its Sequel', *Economic Journal*, 26 (December), pp. 492 – 493; Marshall, A. (1917) 'National Taxation After The War' in Dawson, W.H. (ed.) *After-War Problems*, London: George Allen & Unwin Ltd, pp. 315 – 316

[66]Shadwell, A. (1916) 'Letter – An Imperial Trade Policy', *The Times* (12 January), p. 9, c. F

[67]Tawney, R.H. (1921) 'The Unemployment Crisis in England', *The New Republic*, 25 (23 February), p. 366

[68]Export volumes fell by 30 per cent between 1920 and 1921. Hatton, M. (1997) 'The macro-economics of the inter-war years' in Floud, R. & McCloskey, D.N (eds.) *The Economic History of Britain Since 1700 – Volume 2: 1860 – 1939*, Cambridge: Cambridge University Press, (2nd edition), p. 337

[69]Cole, G.D.H. (1920) 'The Spread of Unemployment', *New Statesman*, 16 (16 October), p. 38; Cole, G.D.H. (1920) 'The Right To Work', *New Statesman*, 16 (4 December), p. 255

[70]Beveridge, W. (1931) 'Is Credit The Culprit?', *The Listener*, 5 (10 June), p. 973; Hilton, J. (1935) 'In Trouble', *The Listener* 14 (20 November), pp. 930 – 931

war-time and early post-war faith in the curative properties of the trade cycle, through to a growing awareness of permanent changes in Britain's position within the international economy, Britain's response to this situation (including predictions of the structure of the future economy), and growing awareness of the failure of the free market to bring these necessary changes about.

Looking To The Future

In this section, we shall outline three areas of the war-time economic debate: first, predictions regarding Britain's position in foreign markets and the problems of hostility towards Germany; second, the problems of post-war taxation required to cover an parasitic war debt, and third, predictions regarding the course of post-war unemployment.

(1) International Markets and International Relations

There existed a wartime expectation that post-war British trade would benefit from two factors: first, international approval regarding Britain's judicial conduct of the War; and second, the opportunities that a defeated, bankrupt Germany would provide in attracting the attentions of Britain's competitors. The potential threats posed by Japanese industrialisation were largely downplayed, although Hobson did wonder to what extent Japan had seized a trading advantage and encroached upon Britain's Chinese markets.[71] It was believed that American competition had been deflected by the construction of the Panama Canal, which by short-circuiting the

[71] Hobson, J.A. (1916) *Labour and the Costs of War*, London: Union of Democratic Control, p. 8

established ocean routes, would enable American exporters to concentrate on the American Continent, the Pacific, and Far East.[72]

The main wartime concerns regarding international trade centred upon Britain's post-war relationship with the Empire, and the expected political and economic shenanigans of a defeated or victorious Germany. In terms of the former, there was some anxiety that Britain's post-war commercial interests could suffer from having dragged the Empire into a costly and devastating European war without proper consultation.[73] The situation would not prove particularly serious, reasoned Edgeworth, provided that Britain realised the importance of exchanging manufactured goods for essential food and raw materials, understood the attitudes of the wider Imperial family, and did nothing to promote the view that Britain was using the War and its aftermath to benefit her own industry and trade.[74]

Questions involving Germany's economic response to the War had arisen from press reaction to Friedrich Neumann's wartime book *Mitteleuropa* (Central Europe), and the predicted union of the German Empire and Austro-Hungarian States. Given the extent of Germany's nineteenth century organisational superiority, it was widely feared that the creation of a Pan-German *Zollverein* – extending from the North Sea to the Alps, the Adriatic, and the Danube, and comprising some 200 million people – would constitute the aggressive development of a military and commercial union comparable with the British Empire.[75] It appeared essential that Germany did not obtain authority and influence that she could employ for military

[72]Kirkaldy, A.W. (1916) 'Some Thoughts on Reconstruction After The War' in Kirkaldy, A.W. (ed.) *Labour, Finance, and the War*, pp. 5 – 8.
[73]Cannan, E. (1915) 'Strategic Jealousies Masked As Commercial' (20 March) in *An Economist's Protest*, p. 27; Shadwell, A. (1917) 'After-War Problems', *Times Literary Supplement*, Issue 803 (7 June), p. 266
[74]Edgeworth, F.Y. (1917) 'Review – 'After-War Problems' by W.H. Dawson', *Economic Journal*, 27 (September), p. 410
[75]Nicholson, J.S. (1916) 'Review – '*Zur Frage eines Zollbündnisses zwischen Deutschland und Ostro-Ungarn*' by K. Diehl', *Economic Journal*, 26 (December), pp. 524 – 525

purposes. Such concern was certainly expressed by Nicholson, who accepted the discussion of *Mitteleuropa* as quasi-semi-official in its representation of Germany's opposition to Britain's Imperial position.[76] Yet whilst it was possible that the German and the Austro-Hungarian States could supplement each others activities (the former being predominantly industrialised, the latter predominantly agricultural), and that the cultural sophistication of Austria could diminish international hatred of Germany[77], the practical impediments towards the development of such a union led Hobson to dismiss it as nothing more than a medley of vague ideas. Was it really credible, he asked, to suppose that post-war Germany, either victorious or defeated, would possess sufficient political leverage to "persuade" the Balkan and Scandinavian states to abandon their interests in world trade?[78]

Amongst economists, the real danger of *Mitteleuropa* was not seen to lie with the implementation of the actual policy, but the extent to which Press coverage would seek to preserve an overwhelming sense of war-time aggression. This latter fact had been illustrated by British diners who had enthusiastically smashed imported German plates at the Savoy hotel. By persistently condemning the Lusitania atrocity or the use of poison gasses against British soldiers, it was feared that tribal animosities would lead to an over-reaction to any suggestion, however extreme or impractical, regarding Germany's military and economic aspirations. Through continual press attacks against Germany, the usual brevity of national memories, argued Pigou, was being overwhelmed by a primitive, jingoistic response.[79] It was

[76]Nicholson, J.S. (1916) 'Central Europe After The War', *Economic Journal*, 26 (June), pp. 200 – 209
[77]Price, L.L. (1917) 'Review – 'Central Europe' by F. Neumann', *Journal of the Royal Statistical Society*, 80 (January), p. 115
[78]Hobson, J.A. (1916) 'Rival Economic Systems in Europe', *Contemporary Review*, 109 (Jan/June), pp. 194 – 198
[79]Pigou, A.C. (1915) 'Letter – German Methods and English Feelings', *Nation & Athenaeum*, 17 (15 May), p. 222

this situation that a number of economic commentators sought to overcome. By what right did Britain and her Allies claim a monopoly on human emotions? Since it was clear that capitalism could not be divided into isolated national blocks, how could national hostility be divided? Come the eventual peace, it was inevitable that people on both sides of the battle lines would express strong feelings of hatred. The slaughter of London school-children by German aviators, for example, would evoke as much hostility in Britain as the slaughtering of "Karlsruhe school-children…[by] British and French aviators" would generate in Germany.[80] Another war-time argument, presented by Frederick Pethick-Lawrence, suggested that an excessive hatred of Germany could blind Britain to the prospects of an early peace, so either leading her to dismiss any German settlement terms, or to offer unreasonable settlement terms of her own. If this occurred, not only would the world lose the possibility for a speedy cessation of hostilities, but Britain would be required to take sole responsible for any economic repercussions.[81] Hobson took this idea to its extreme, questioned Germany's overall responsibility for the war, and argued the removal of war-time censorship would reveal evidence demonstrating that Germany did not possess sole blame.[82]

(2) Taxation and War Debt

When considering the question of wartime national finance, the economic debate centred on the feasibility and probable consequences of employing either

[80]Cannan, E. (1917) 'The Influence of the War on Commercial Policy' (22 September) in *An Economists' Protest*, pp. 127 – 128

[81]Pethick-Lawrence, F.W. (1915) 'Letter – The Settlement of the War', *Nation & Athenaeum*, 17 (19 June), p. 386

[82]Hobson, J.A. (1915) 'Letter – Approaches to Peace', *Nation & Athenaeum*, 18 (20 November), p. 289

loans or increased taxation to meet the enormous expense of war. Over the course of the War, the nominal rate of British income tax had increased from 1*s*.2*d* in the pound (1913 – 14) to 6*s*. in the pound (1918 – 19), while consultations with the trade unions regarding lowering of the exemption limit (from £160 to £130) had nearly quadrupling the total number of taxpayers. Approximately 26 per cent of war-time expenditure was met out of current revenue[83], with the governments main needs covered by three large loans – £350m (1914), £900m (1915), and 2,127m (1917) – and, from April 1915, short-term borrowing secured through the sale of medium-term bonds and an increased supply of Treasury bills on "tap" (available in any amount, at a fixed rate of interest, without going through the market) and typically redeemable in three to twelve months.[84]

Herbert Foxwell argued that the government had failed to exploit the opportunities provided by Treasury bills by ignoring the obvious fact that continuous borrowing required continuous repayment. Where as it was possible that the maturity date of war bonds would coincided with increased demand for capital for post-war reconstruction (so reducing the demand for renewed subscription on redeemable bonds unless the rate of interest was increased), the security and flexibility of Treasury bills ("the finest financial investment in the world") provided the government with a steady net increase of borrowing over repayments.[85] At the beginning of the war, Keynes had attributed the London markets readiness to accept Treasury bills to the importance the Banks had come to attach to a "due date" (the

[83]Balderston calculates the figure at 26.2 per cent. Balderston, T. (1989) 'War finance and inflation in Britain and Germany, 1914 – 1918', *Economic History Review*, 42, p. 226. During the inter-war period, Hirst estimated the figure at "rather more than 28 per cent." Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, London: Humphrey Milford, p. 167

[84]Morgan, E.V. (1952) *Studies in British Financial Policy, 1914 – 25*, London: Macmillan & Co. Ltd, pp. 106 – 112

[85] The position may be seen as analogous to a bank expecting an excess of deposits over withdrawals.

specified redemption date of the bill) following the financial crisis of 1914.[86] Yet the healthy reception that British Treasury bills continued to enjoy throughout the War (a reception which was not shared by their counterparts in the German market) may be understood by Foxwell's claim that the government had simply continued to pay "unnecessarily" high rates on Treasury bills. In November 1915, Treasury bills had been offered at 5 per cent, reaching 5.5 per cent on 3 month bills and 6 per cent on 12 month bills in July 1916.[87] If Treasury bills had been issued at the flat rate of 3 per cent ("a rate they rarely reached in peace") then, claimed Foxwell, the necessary quantity would have easily been placed.[88]

The government's justification for the superiority of loans centred on the view that, above an optimal taxation rate, reductions in net incomes generated a disincentive effect on productivity. This interpretation, which may be taken as early Treasury presentation of the Laffer curve, was heavily criticised by economists, who believed that ignorance regarding the intricacies of public finance, and an emphasis on the disincentive effects of immediate (war-time) taxation, was diverting attention from the long-term consequences that would arise from increased post-war taxation needed to cover debt charges. [89] By failing to introduce adequate war-time taxation on all classes (thereby minimising the resources available for private consumption, or, conversely, maximising the resources available to the State), economists clearly

[86]Keynes, J.M. (1914) 'Note on Government Loans' (23 October) in *Collected Writings of J.M. Keynes – Vol. XVI: Activities 1914 – 1919*, London: Macmillan, p. 40

[87]Morgan, E.V. (1952) *Studies in British Financial Policy, 1914 – 25*, p. 110

[88]Foxwell, H.S. (1917) 'Letter – War Borrowing', *The Economist* (18 August), p. 247.

[89]For a glimpse at this large, war-time literature, see Hobson, J.A. (1915) 'How Can England Pay The Bill?', *The New Republic*, 3 (10 July), pp. 255 – 257; Pethick-Lawrence, F.W. (1915) 'Letter – A Tax on Capital', *Nation & Atheneaum*, 17 (21 August), p. 677; Hobson, J.A. (1916) *Labour and the Costs of War*, pp. 11 – 15; Pigou, A.C. (1916) 'Letter – The Need for More Taxation', *The Economist* (25 November), pp. 1003 – 1004; Marshall, A (1916) 'Letter – The Need For More Taxation.', *The Economist* (30 December), p. 1228; Pigou, A.C. (1917) 'Letter – The Income Tax', *The Times* (23 April), p. 9, c. E; Pigou, A.C. (1918) 'A Plea For Higher Income-Tax', *Contemporary Review*, 113 (Jan/June), pp. 36 – 38

feared that the government was foolishly ignoring the parasitic quality of an ever-growing, non-remunerative post-war public debt. On a more immediate issue, the importance of raising war-time taxation drew upon concerns regarding the equitable distribution of the financial burden. By what principle of justice, asked Pigou, were those who were "strong in money" entitled to be treated differently from those who risked their lives in the trenches? The Military Service Acts knew nothing of proportionate sacrifice since it was usually the physically strong who were selected and dispatched to the theatre of war. The existence of such battlefield inequalities suggested that the State was fully justified in employing direct taxation against financial strength in order to tackle the burden of indebtedness. [90]

(3) Early Predictions of the Post-war Unemployment

Wartime predictions regarding the direction of post-war unemployment were interpreted within the simple Marshallian framework of supply and demand. In terms of supply, economists predicted that any natural increase in the working population, aged between twenty and sixty, would be off-set by war casualties, with the possible precariousness of post-war international politics necessitating the maintenance of a large military force.[91] The possible depletion of the post-war aggregate labour supply naturally led to questions regarding Britain's ability to retain, even if only temporarily, the female workers who had been recruited for industrial and other war services. It was widely accepted that society could not ignore the effects of the War

[90]Pigou, A.C. (1916) 'Letter – The Need for More Taxation', *Economist* (25 November), p. 1004
[91]Hobson, J.A. (1916) *Labour and the Costs of War*, p. 7

in stimulating the attitude of women towards employment. "Their status in industry," wrote Hobson, "has definitely and permanently risen."[92] Although the substitution of of one sex for another had been limited – many wartime industries having failed to produce a satisfactory supply of skilled female labourers – there remained the hope that confidence and training would enable many women to enter non-industrial occupations such as shop assistants, hotel waitresses, and bank clerks.[93] Through the inclusion of female labour, it was predicted that Britain's post-war aggregate labour supply would not differ significantly from its 1914 level.[94]

The question of post-war demand was directly connected with the rhythmical variations of economic prosperity and adversity, variously described as the "trade cycle" or "industrial fluctuations". By the time of the War, the presentation of a periodic cycle in business activity had replaced earlier ideas regarding industrial or financial "crises".[95] Taken as the pulse of economic life (or the physical manifestation of economic friction), the early twentieth century had seen a variety of attempts to identify the impulses – "real", "monetary" and "psychological" – that induced such fluctuations. With convention having dictated the presentation of the cycle as an automatic sequence, it was widely accepted that recovery would proceed through four successive stages. We may take Sydney Chapman's stylised cycle as representative of these ideas. With account made for the destructive impact of the War, the four stages were outlined as follows: first, an interim break associated with

[92] Hobson, J.A. (1917) 'Shall We Be Poorer After The War?', *Contemporary Review*, 111, (Jan/June), p. 46

[93] Shadwell, A. (1916) 'Economic Problems To Come', *Times Literary Supplement*, Issue 770 (19 October), p. 495; Chapman, S.J. (1918) 'The State and Labour' in Dawson, H.D. (ed.) *After-War Problems*, p. 140

[94] Pigou, A.C. (1916) 'Labour Problems After The War', *Contemporary Review*, 110 (July/Dec), p. 339; Hobson, J.A. (1917) 'Shall We Be Poorer After The War?', (Jan/June), p. 46.

[95] Pigou, A.C. (1900) 'Review – 'Economic Crises' by E.D. Jones', *Economic Journal*, 10 (December), pp. 523 – 526; Pigou, A.C. (1903) 'Review – 'Financial Crises and Periods of Industrial and Commercial Depression' by T.E. Burton', *Economic Journal*, 13 (March), pp. 73 – 74

demobilisation and the transition of industry to civil conditions; second, the tremendous release of war-restrained effective demand associated with the backlog of capital investment and the replenishing of stocks[96]; third, the inescapable problem of reaction; and, fourth, the return to normal conditions.[97] Such was the economic sequel of war. As a brief side issue, it may be noted that this presentation was almost certainly influenced by the course of the post-Napoleonic war cycle. Based on the idea that human nature would not have altered dramatically over the course of a single century, commentators such as Cannan and Nicholson believed that such historical comparisons proved highly instructive.[98]

There is also evidence of a proposed threat of post-war unemployment arising from long-standing concerns regarding the relationship between unemployment and sickness benefit. One unsatisfactory feature of the pre-war German social insurance statistics, for example, had been the realisation that, following the extension of sick-pay from 13 to 26 weeks in 1903, recorded sickness amongst German labourers had shown a persistent increase.[99] Even allowing for the effects of war-time patriotism, concerns regarding genuine physical strain of war, and a belief that their efforts had not been satisfactorily compensated, had led a number of industrial workers to express their intention to "relax" during the post-war period. We may note the following quote, provided by T.S. Ashton and taken from discussions with a war-time trade unionist:

[96]As early as November 1914, Lloyd George was predicting that the inevitable post-war boom would last for "something like four or five years." *The Times* (18 November 1914), p. 12, c. B

[97]Chapman, S.J. (1918) 'The State and Labour', p.145

[98]Nicholson, J.S. (1916/17) 'Trade After The Napoleonic War', *Scottish Historical Review*, 14, p. 374; Cannan, E. (1917) 'Review – 'Economic Annals of the Nineteenth Century, 1821 – 1830' by W. Smart', *Economic Journal*, 27 (March), p. 536

[99]Shadwell, A. (1912) 'National Insurance in Germany', *Times Literary Supplement*, Issue 544, (13 June) p. 242

> "I have been working for forty-two days now without a single day's rest, and it has been going on like this for months. If, after the war, I feel played out, I shall consider I am quite justified in taking a long rest on the club, if I get the chance."[100]

Hobson articulated a similar theme, arguing that the increases in war-time family earnings had been insufficient to compensate for the physical strain of war-time work.[101] This comment illuminates the possible motives of inter-war economic agents. Based on Ashton's examination of war-time attitudes, we are presented with the intriguing possibility that some degree of post-war unemployment represented the feelings of disgruntled workers that their increased war-time physical strain had not received full recognition through family earnings. Under these circumstances, the difference between weekly earnings and benefit was deemed insufficient to overcome the persistent resentment of labour towards increased war-time overstrain.

At this point, it is perhaps useful to briefly draw together the main themes of the preceding discussion. We have seen how the war-time mind-set of economists displayed an almost languid acceptance about the general recovery of the pre-war equilibrium. Two of the most interesting themes involved the attempts by economists to instruct the general public as to the dangers of certain aspects of the likely post-war situation. Their approach was one of anticipation: attempt to prevent post-war difficulties by drawing attention to them, and attempting to diffuse then, during the War. The first of these can be seen in their criticism of *Mitteleuropa*, and attempts to undermine jingoistic sentiment by demonstrating that national hostility could not be separated into national blocks. The second example concentrated on the need to draw

[100] Ashton, T.S. (1916) 'The Relation between Unemployment and Sickness', *Economic Journal*, 26 (September), p. 400

[101] Hobson, J.A. (1916) *Labour and the Costs of War*, pp. 1 – 2; Hobson, J.A. (1916) 'Britain's Prosperity', *The New Republic*, 6 (29 April), p. 340

attention to the problems of post-war taxation required to finance an enormous national debt.

The Trade Cycle

We move now to consider the spectacular, short-sighted follies of the post-war boom, the transition to unparalleled depression, and the emerging problem of inter-war unemployment. As we have already seen economists interpreted such problems as a normal movement of the pre-war trade cycle. In the following section, we outline three contemporary presentations of the cycle: psychological, monetary, and underconsumptionist.

(1) The Psychological Interpretation

Proposed by Arthur Pigou and Frederick Lavington, the psychological interpretation of the cycle centred on the destabilising effects of extravagant business estimates regarding the prospective yield on future undertakings. The rhythmic movement of the economy was not explained by the actual benefits secured through good harvests, technical innovations, or the discovery of new gold mines, but by the influence of such events in generating an unreasoned sense of optimism throughout the economic system.[102] If employers' anticipations of the demand for their product contained no error, the demand for labour would depend on the value of the marginal net product of labour. Yet the attitudes of businessmen never remained constant, but

[102] Lavington, F. (1922) *The Trade Cycle: An Account of the Causes Producing Rhythmical Changes in the Activity of Business*, London: P.S. King & Son Ltd, p. 28. This book may be taken as the definitive inter-war presentation of the traditional Cambridge theory of the trade cycle.

were seen to oscillate between errors of optimism and errors of pessimism. Over-confident, exaggerated expectations concerning the future purchasing power of society would lead to exaggerated estimates of the value of the marginal net product of any quantity of labour employed. With forecasting errors exacerbated by the capitalist network of order and credit relations, firms would assume the responsibility of producing goods in anticipation of demand.

By emphasising the inter-dependency of the economic system, and the fact that forecasting errors displayed a multiple tendency, it was believed that the discovery of erroneous post-war profit expectations had generated a herd-behaviour, with small changes having the potential to generate large fluctuations. Economic conditions immediately preceding the war – high prices, large profits and a low percentage of unemployment – had all suggested an error of optimism. Pigou considered it doubtful whether post-war employers would conveniently react with a shift towards pessimism. The psychological reaction associated with the coming of peace had therefore ignited business confidence, so leading to investment in excess of any rational forecast regarding future profitability. When the goods were ready for the market, it was discovered that the demand for them was less than initially believed. The resulting financial losses had not only led to the inevitable problem of business failures and unemployment, but also a swing in the mind of businessmen leading them to underestimate future investment prospects.[103] Based on the assumed cumulative effects of optimism and pessimism, the psychological interpretation identified the abnormal level of post-war unemployment as a direct consequence of the abnormal, post-war boom.

[103] Pigou, A.C. (1916) 'Labour Problems After The War', *Contemporary Review*, p. 338; Pigou, A.C. (1916) *The Finance and Economy of the War*, London: J.M. Dent & Sons Ltd, p. 88; Pigou, A.C. (1924) 'Correctives of the Trade Cycle' in Astor, J.J. et al *Is Unemployment Inevitable? An Analysis and Forecast,* London: Macmillan & Co. Ltd, pp. 91 – 131

(2) The Monetary Interpretation

The orthodox monetary interpretation of the trade cycle developed from the work of R.G. Hawtrey[104], and was adopted by a number of inter-war economists including Herbert Henderson and E.M.H Lloyd. In many respects, the monetary theory of the cycle became the early, dominant contemporary interpretation of Britain's post-war problems.

By its very name, the "pure money" theory suggested that trade fluctuations were, at all times, the product of monetary influences on industry and commerce (money being taken as every class of purchasing power available for immediate use). By having expanded credit facilities to merchants and traders, banks were seen as the initiators of the post-war boom. The expansion of purchasing power had led to a dramatic rise in prices as demand conditions exceeded the available supply of commodities (the process being accentuated by speculative purchases). With merchants operating under the misconceived expectation of large profits, and the belief that demand was, at all times, supported by purchasing power, a reckless placing of orders had ensued. As time progressed, fear and outrage emerged: businesses feared the huge accumulation of stocks, while *rentiers* attacked the continuing increase in prices. The eventual downturn of the cycle was attributed to the decision of banks to raise money rates, and so restrict credits, once they realised that available credits exceeded the amount consider prudent given existing cash reserves. With the government initiating monetary contraction to tackle the problem of inflation, and the banks curtailing credit, pressures to repay overdrafts prevented

[104] See, for example, Hawtrey, R.G. (1913) *Good and Bad Trade: An Inquiry into the Causes of Trade Fluctuations*, London: Constable & Co. Ltd, and Hawtrey, R.G. (1919) *Currency and Credit*, London: Longmans & Co. Ltd.

producers from placing further orders (implying that production for immediate delivery was no longer profitable), large stocks were sold at a loss, and workers were thrown on to the labour market.[105]

(3) Underconsumptionism

J.A. Hobson's theory of underconsumption, which had been heavily criticised before the War[106], attributed unemployment to excessive inequalities in the distribution of wealth. When industry was functioning normally, activity would be directed towards the production of goods for current consumption, with the accumulated surplus income of the rich – arising from physical constraints on consumption and christened "over-saving" – serving as an investment fund for the production of capital goods. In Hobson's scenario, depression had been averted in 1914 through the wartime stimulation of consumption, so ensuring that the productive powers of both capital and labour were maintained at full employment. With the post-war unleashing of pent-up demand, full employment had been maintained for a further two years. During this prosperity, the inherent imbalance between saving, consumption and production had led to the over-production of consumer goods in relation to effective demand. With the rate of production exceeding the rate of consumption once immediate post-war effective demand for repairs and reconstruction had been satisfied, Hobson argued that the recurring

[105] Lloyd, E.M.H. (1922) 'Letter – The Theory of Trade Fluctuations', *New Statesman*, 20 (23 December), pp. 353 – 354; Henderson, H.D. (1923) 'Monetary Policy' (14 July) in Clay, H. (ed.) (1955) *The Inter-War Years and Other Papers*, Oxford: Clarendon Press, pp. 6 – 7; Henderson, H.D. (1924) 'Financial Factors' in 'Financial Factors' in *Unemployment In Its National and International Aspects*, Geneva: International Labour Office, pp. 40 – 47

[106] See, for example, Cannan, E. (1897) 'Review – 'The Problem of Unemployment' by J.A. Hobson', *Economic Journal*, 7 (March), pp. 87 – 89; Price, L.L. (1908) 'Review – 'The Problem of Unemployment' by J.A. Hobson', *International Journal of Ethics*, 19 (October), pp. 132 – 134

process of over-saving and under-consumption had led to the increase in unemployment.[107]

Driving Force of the Boom

The abolition of conscription, the relaxation of war-time restrictions, enormous government expenditure, speculative purchases and rising prices, are generally all assumed to have contributed to the post-war boom. An examination of the early post-war economic literature highlights a slight development on this theme.

Writing in early 1919, Pigou noted that one of the recurring war-time and post-war political messages involved the importance of expanding post-war production in order to ease the nation's crippling burden of War Debts.[108] Given the early post-war belief that Britain would easily recapture her foreign markets, this strand of post-war political rhetoric suggested to Pigou that post-war society had taken the problem of Britain's non-remunerative national debt in hand.[109] This led to the suggestion that the patriotic prescription of increased production to cure the disease of accumulated debt was intensifying the post-war boom. On first examination, this position appears somewhat questionable, especially given the obvious historical interpretation of the post-war boom as a consequence of the release of war-restrained effective demand. However, we can perhaps draw attention to Stanley Baldwin's decision in 1919 to donate £120,000 (approximately one-fifth

[107] Hobson, J.A. (1916) *Labour and the Costs of War*, p. 8; Hobson, J.A. (1917) 'Shall We Be Poorer After The War?', pp. 47 – 48; Hobson, J. A. (1924) *The Economics of Unemployment*, London: G. Allen & Unwin Ltd, pp. 5 – 6

[108] See, for example, *The Times*, (10 April 1918), p. 3, c. A.

[109] Pigou, A.C. (1919) 'The Problem of the National Debt', *Contemporary Review*, 116 (July/Dec), p. 622 – 633

of his accumulated wealth) towards the redemption of Britain's War Debt[110]. Although not offering conclusive proof, such actions do support for the idea that Britain's post-war boom may have been influenced by a sense of patriotic idealism reacting with the established ideas of war-released extravagance.

A separate development on this theme was offered by Cole, who suggested that the extensive recapitalisation of Britain's industrial capacity had been motivated by the effect of wartime financial forces on the capitalist desire for profit. Cole's idea ran as follows. For many years prior to the War, owners of capital had claimed the surplus that remained following the payment of the costs of production. This situation had gradually evolved, with capital no longer ranking as a share of the surplus, but as an element in the cost of production. This new claim, which implied a "reasonable" rate of interest on capital invested in business, was ably illustrated by the cumulative nature of preference shares that stipulated that fixed interest, if not paid in one year, would to be paid in subsequent years. The use of "dividend insurance" also formed the practice of reserving funds in order to stabilise dividend yields over bad periods. Cole believed that the capitalist faith in absurdly high wartime profits and extraordinary dividend payments had become an integral, and dangerous, component of the economic system. It had become the drug to which capitalism was addicted. In this context, the dramatic expansion of Britain's productive capacities did not represent Britain's belief in her *ability* to capture foreign markets, but a desperate *need* to secure those markets in order to satisfy the capitalist demand for excessive profits and dividend payments.[111]

[110] Williamson, P. (1999) *Stanley Baldwin: Conservative Leadership and National Values*, Cambridge: Cambridge University Press, pp. 139 – 140

[111] Cole, G. D. H. (1923) *Out of Work: An Introduction to the Study of Unemployment*, London: Labour Publishing Company Ltd, pp. 25 – 28, 57 – 58

Impediments

It was widely believed amongst economists that Britain's early post-war depression had been unnecessarily exacerbated by impediments. It would, of course, be difficult to consider all the impediments presented in the contemporary literature. As such, we shall concentrate on just six, including changes in wages, the (questionable) influences of taxation, the corrosive influence of government bureaucracy, and the unnecessary handicap imposed on business through a restrictive postal service and inefficient railway network. We shall begin our discussion by considering contemporary views on the increase in war-time and post-war wage rates.

(1) Wages

It is clear from the contemporary literature that, even by the latter half of 1919, there had emerged some anxiety concerning the effect of the Great War on wage-determination. The pre-war wage-system was seen by economists to have reflected the short-run supply and demand for labour, with wages in the long-run tending towards the marginal product of labour. Allowing for difficulties imposed by inflation in calculating wartime and post-war real wages (the nominal wage adjusted for variations in prices) a rough summary of the expected movements did suggest to Barbara Wootton that the post-war price of labour still reflected its marginal product. Yet such vague calculations could not conceal the possibility that a new situation was "struggling to life", particularly given the post-war wage increases in the lower paid ranks of labour.[112] On one level, it was possible that previously "exploited" (low paid) workers had successfully secured wages equal to their marginal product, thereby implying such increases could be reconciled with the standard principles of distribution. Yet it was also believed that something more damaging had occurred, with wages having been permitted to exceed the marginal product of labour. If this was the case, what had altered the mechanisms that had governed the pre-war wage system? For Barbara Wootton and Arthur Bowley, the explanation lay in the wartime intention to guarantee a minimum standard of living through increases in money wages, the use of bonuses and the regulation of wages via the cost of living index. While the intention of the cost of living index had been to eliminate the influence of price fluctuations, it was realised that the actions of impartial wage arbitrators in ascribing all wage increases to the cost of living had caused the cost of living index to mutate into a dangerous force that undermined the commodity interpretation of labour.[113] Bowley identified the sensitivity of the *Labour Gazette* price index as constituting a "potent force in the increase in wages, and therefore of prices." The cost of living statistics reflected changes in the price of food, clothing, fuel and rent, while not specifying a specific standard of living within society. However, there existed a fear that both the press and trade union leaders had identified the cost of living index as an authoritative measure of the standard of living, and the guide against which labour could ensure that it would never again suffer the injurious effects of inflation.[114]

[112] Wootton, B. (1920) 'Classical Principles and Modern Views of Labour', *Economic Journal*, 30 (March), p. 50

[113] Cannan, E. (1920) 'Letter – The Regulation Of Wages', *The Times* (20 October), p. 13, c. D

[114] Bowley, A. (1919) 'The Measurement of Changes In The Cost of Living', *Journal of the Royal Statistical Society*, 82 (May), p. 350; Stamp, J.C. (1923) 'Letter – Adjusting Wages by Prices', *The Times* (18 January), p. 6, c. A

A separate interpretation of the post-war increase in real wages focused on working-class revival of Marxist economic theory. The popular vogue for the Marxist theory of surplus value[115] – the difference between the value of labour power and the value that labour created – appeared to provide socialists with the theoretical justification for post-war wage increases. Neither this interpretation, nor the overall Marxian doctrine, found support amongst the wider economic community: James Bonar dismissed Marx as a deluded agitator whose arguments had been constructed on shoddy foundations[116], while Nicholson, although initially hopeful that Marx's analytical apparatus would throw some light on post-war conditions, eventually denounced him as "the Mad Mullah of socialism."[117]

Yet these direct assessments failed to provide an explanation for the increased post-war support for the Marxian system. Why had the working-class come to accept the theory of surplus value, and so believe that they had captured a larger share of the capitalists' profits? The explanation provided by Keynes did not centre on the actual ability of labour, but the response of capitalists to the Bolshevik Revolution and the lingering threat of domestic revolution. The tirade of socialist propaganda sought to instil the assertion that poverty was the consequence of amoral capitalism, and that only the abolition of capitalism through extreme revolution would enable the workers to secure their desired objectives. While it was probable that the prospects of

[115] See, for example, Cox, H. (1919) 'The Ethical Side of Socialism, *Edinburgh Review*, 230 (July), pp. 199 – 206; Shadwell, A. (1921) 'A Guide To Marxian Controversy', *Times Literary Supplement*, Issue 1003 (7 April), p. 220; Cox, H. (1922) 'Labour Disillusionment', pp. 402 – 405. For a more resent examination of the issue, see Steedman, I. (1990) 'The Economic Journal and Socialism, 1890 – 1920' in Hey, J.D & Winch, D. (eds.) *A Century of Economics: 100 Years of the Royal Economic Society and the Economic Journal*, pp. 65 – 91 and Steedman, I. (2004) 'British Economists and Philosophers on Marx's Value Theory, 1920 – 1925', *Journal of the History of Economic Thought*, 26, pp. 45 – 68

[116] Bonar, J. (1922) 'Review – 'Karl Marx and the Present Unrest' by J.A. Murray Macdonald', *Economic Journal*, 32 (September), pp. 378 – 379

[117] Nicholson, J.S. (1920) *The Revival of Marxism*, London: John Murray, p. v

imminent "red revolution" owed more to the activities of a press, (particularly *The Times* and the *Morning Post*) whose sensational accounts of Russian's economic destruction coloured British perceptions of domestic political and social reality[118], Keynes believed that producers who had accumulated excessive profits during the war-time and post-war boom – "windfall profits" – had, through the prevailing environment of fear, eagerly acquiesced in labour opinion regarding wage increases.[119]

(2) Labour Exchanges

One of the essential themes of the government's post-war response to unemployment reflected the pre-war diagnosis of the immobility of labour between times, places and occupations, and the development of the Labour Exchange system.[120] It had been apparent during the War that the liberation of large numbers of servicemen during the early period of demobilisation (expected to last for the first six months following the cessation of hostilities) would lead to an increase in unemployment. Concern amongst economists had not been directed towards the inevitable rise of unemployment (which, as we have seem, they attributed to the rhythmic movement of the cycle) but in ensuring that central and local authorities did not misconstrue the features of demobilisation and, influenced by their successes at wartime co-ordination, respond with ill-conceived policies. Recognising that any knee-jerk reaction in these circumstances had the potential to retard post-war

[118] Cole, G.D.H. (1920) 'What We Want To Know About Russia', *New Statesman*, 15 (1 May), pp. 95 – 96; Cole, G.D.H. (1920) 'Communism and Labour Policy', *New Statesman*, 15 (7 August), p. 495; Cole, G.D.H. (1921) 'Nonsense About Revolution', *New Statesman*, 18 (10 December), pp. 280

[119] Keynes, J.M. (1921) 'The Earnings of Labour' (11 September) in *Collected Writings of J.M. Keynes – Vol. XVII: Treaty Revision and Reconstruction*, London: Macmillan, pp. 268 – 269

[120] Beveridge, W. (1919) 'Letter – Labour Exchanges', *The Times* (30 October), p. 8 c. C

economic revival, Pigou believed it was essential that the government recognised the importance of the Labour Exchanges in improving mobility. To supplement the existing Labour Exchange system, Pigou proposed legislation that would require discharged soldiers and munitions worker to register with their local Exchange, while at the same time forcing employers to either engage workers through the Exchanges, or to inform them of any labour hired directly.[121]

By the early 1920s, it appeared that the general remedy of improving labour mobility had failed to materialise. This was attributed by D.H. Magregor to a profound distrust of both employers and employees to the Exchange system. On the one hand, employer dissatisfaction was seen to arise from the inability of the Exchanges to provide satisfactory workers, so leading employers to advertise vacancies directly through trade unions (Cox had earlier suggested that only the unemployable bothered to use the system[122]). Amongst unemployed workers, the unpopularity of the Exchanges could be seen in the decision of skilled, manual craftsman to rely on their own efforts rather than face the ignominy of being grouped with general labourers, or a backlash against the discipline of military life, so leading workers to accept casual jobs rather than being forced into a ordered way of life. There were also fears that the general efficiency of the system had been unnecessarily lost when officials, who possessed detailed knowledge of their local economy, were moved to new districts.[123]

[121] Pigou, A.C. (1916) 'Labour Problems After The War', p. 343 – 345; Pigou, A.C. (1918) 'Government Control in War and Peace', *Economic Journal*, 28 (December), p. 373

[122] Cox, H. (1921) 'The Public Purse', *Edinburgh Review*, 234 (July), p. 206

[123] Macgregor, D.H. (1922) 'British Aspects of Unemployment', *Journal of Political Economy*, 30 (December), p. 735 – 739

(3) National Debt and Taxation

Throughout the war and the early post-war period, the problem of Britain's vast War Debt attracted a great deal of attention from economists. We have already seen how, due to the imperative need to procure war supplies, the British government had relaxed the pre-existing financial safeguards. As a consequence of this, Britain's financial position by 1919 was far from enviable. Having risen from £650m at the outbreak of war, the National Debt stood at £7,435m (March 1919), growing to £7,829m (March 1920), before falling back slightly to £7,573m (March 1921).[124]

Several methods for tackling this financial mountain were proposed. Open repudiation was quickly dismissed as equivalent to national bankruptcy, the revolutionary dismantling of the entire political and economic system, and the irrevocable destruction of Britain's international reputation. A more refined suggestion involved "disguised" repudiation through a capital levy. The question was straightforward: was it advisable to impose a one-off levy on "war fortunes" (increments of private capital accumulated during the war) thereby ensuring a speedy, large-scale liquidation of War Debts, or to sustain the burden of taxation over a number of years in order to service annual interest payments, and secure small-scale reduction though a sinking fund? [125]

Criticisms directed towards the proposed capital levy concerned the likely damage inflicted on the productive efficiency of the economy; the difficulties arising from an individuals ability to pay (due to varying personal circumstances); questions

[124] Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, London: Humphrey Milford, p. 170, 174, 182

[125] The most famous proponent of the capital levy proposal, at least amongst academic economists, was Arthur Pigou. See, for example, Pigou, A.C. (1918) 'A Special Levy To Discharge War Debt', *Economic Journal*, 28 (June), pp. 135 –156; Pigou, A.C. (1919) 'Letter – War Fortunes', *The Times* (27 October), p. 8, c. B; Pigou, A.C. (1923) 'Letter – Capital Levy', *The Times* (1 May), p. 9, c. D

concerning the development of an administrative system capable of distinguishing between aggregate existing capital and malignant war-time profiteering; and the effect of a levy in reducing future yields on income-tax and super-tax. It was further doubted whether a capital levy would deliver a "clean break" as a means of relieving the nation's economic problems. Not only did a capital levy fail to guarantee a reduction in future rates of income-tax, but non-guarantee of non-repetition introduced a dangerous element of risk into business activity, reduced post-war productivity, and engender a feeling of injustice amongst private capital. Overall, it was feared that a substantial balance of disadvantages outweighed the potential virtues of the capital levy.[126]

Some semblance of financial stability had been secured by the decision, presented in Baldwin's 1923 budget, to extinguish the debt through a sinking fund, obtained by budgeting for a surplus of revenue over expenditure spread over many years.[127] Baldwin accepted that the discharging of debt through this process could "take a century or two centuries"[128], for a sinking fund set at £45m amounted to less than 0.6% of the total national debt.[129] Although the advocates of the capital levy had failing in their endeavour, Hugh Dalton later believed that their lasting success lay in fending off financial quackery.[130]

There was some dispute as to the detrimental effect of increased post-war taxation. On the one hand, it was argued that increased direct taxation (used to pay for both social reform and interest charges on the national debt) was discouraging the

[126] Stamp, J.C. (1919) 'The Special Taxation of Business Profits in Relation to the Present Position of National Finance', *Economic Journal*, 29 (December), p. 411

[127] The supposed advantages of the sinking fund, most noticeably the savings secured through future conversion operations in order to reduce the rate of interest on government debt, were later criticised by the Colwyn Committee for being much smaller than commonly supposed.

[128] *The Times*, (7 March 1923), p. 7, c. B

[129] Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, p. 196

[130] Dalton, H. (1923) 'The Financial Position', *Contemporary Review*, 123 (Jan/June), pp. 554 – 557

spirit of post-war enterprise, and so undermining the corrective movement of the cycle.[131] For this reason, the belief that Britain was struggling under the "crushing burden" of taxation, relative to the pre-war level, served to make public finance a topic of genuine interest. On the actual increase in post-war direct taxation, we may quote Hirst at some length:

> "In 1913 a taxpayer with £100 a year paid £6 taxation; in 1923 he paid £15. In 1913 a taxpayer with an income of £1,000 a year paid £80; in 1923, he paid £160. In 1913 an income of £5,000 a year paid 9 per cent; in 1923 it paid 32 per cent. In 1913 an income of £10,000 a year paid 11 per cent; and in 1923 it paid 43 per cent. An income of £50,000 a year in 1913 paid 13 per cent; in 1923 it paid 60 per cent."[132]

Human effort was assumed not to be forthcoming if, at the taxation rate of 10*s*, the opportunity to earn an additional £1,000 would only provide the individual with an additional £500. On the other side of the debate, it was questioned whether economic agents really base their actions on a mathematical appreciation of effective tax rates. In one example, offered by the Swedish economist, Gustav Cassel, it was suggested that British industry was not hindered by the distribution of the taxation, but by a deep-seated sense of injustice arising from Britain and Germany's contrasting attitude towards the payment of War Debts. The popular British attitude, at least as visualised by Cassel, suggested that any disadvantages Germany had suffered through her defeat in 1918 had swiftly been overcome by the use of deliberate currency inflation to wipe out the burden of her internal debt. In sharp contrast, British triumph during the War had gradually diminished, and her economic

[131] Nicholson, J.S. (1919) *Inflation*, pp. 110 – 112; Pigou, A.C. (1922) 'Letter – The Burden of Income Tax', *The Times* (11 January), p. 11, c. F Hirst, F.W. (1924) 'Letter – Economy and the Budget', *The Times* (17 January), p. 13, c. D; Jones, J.H. (1924) 'The Future of British Industry' in Astor, J.J. et al *Is Unemployment Inevitable*, pp. 198 – 200

[132] Hirst, F.W. (1927) 'Letter – Ministers and the Economy', *The Times* (24 March), p. 15, c. F

prosperity endangered, through a strong and principled commitment to the communal distribution and payment of War Debts. It was this feeling of injustice, Cassel believed, that served as an obstacle to economic reconstruction: acute resentment and insecurity, generating nationalistic feelings, had prevented any resolution to the ongoing reparations problem, and hence hindered European economic recovery.[133]

A separate idea was the notion of adaptability, with economic agents having come to accept, with good grace or no, that the steady and prolonged pressure of taxation was an annoying, yet inevitable feature of post-war life. Taxation did not serve as a deterrent (or at least a significant deterrent) to private enterprise since society had come to accept that they would, for example, only receive £450 per year instead of £500, or £800 instead of £1,000.[134] As Cole suggested, progressive income-tax did not serve as an economic deterrent for the simple reason that the public had come to accept compulsory deductions with the same amount of grumbling as they would normally give to the state of the weather.[135]

(4) Bureaucracy

A profound sense of war-time patriotism had made the nation more receptive to an increased level of bureaucratic restraint. Nonetheless, Pethick-Lawrence had predicted that the process of demobilisation would coincide with the speedy dismantling of "the great hive of temporary Government offices."[136] While it was

[133] Cassel, G. (1924) 'The Problem of Finding Employment' in Astor, J.J. et al *Is Unemployment Inevitable*, pp. 142 – 143

[134] Scott, W.R. (1918) 'Some Aspects of the Proposed Capital Levy', *Economic Journal*, 28 (September), p. 250; Cannan, E. (1921) 'Review – 'The Fundamental Principles of Taxation' by J. Stamp', *Economic Journal*, 31 (September), p. 353

[135] Cole, G.D.H. (1924) 'The Future of Social Insurance', *New Statesman*, 23 (12 April), p. 7

[136] Pethick-Lawrence, F.W. (1918) 'A Levy on Capital After The War', *Contemporary Review*, 113 (Jan/June), pp. 308 – 309

accepted that there would be some requirement for state assistance during the period of transition[137], the post-war development of an apparently blundering, wasteful, and immovable bureaucratic army was seen to have penetrated virtually every aspect of national and civic life. This was taken to have imposed unnecessary restrictions on economic activity during a period of deep trade depression. In response to the unsavoury aroma of a politically controlled bureaucracy (as illustrated by the system of government adopted in American), Britain had long advocated the benefits of a permanent, politically impartial civil service. Yet for all its supposed ability to produce honourable servants of the State, Britain's civil service did not appear to reflect the characteristics of passive obedience. Those who had secured comfortable war-time positions within the civil service – referred to as "limpets" in the national press[138] – were clearly opposed to the dispersal of their departments.

As evidence of extravagant expenditure throughout the whole post-war bureaucratic machine, the ("Geddes Axe"[139]) Committee on National Economy, noted that, by 1921, the British Navy possessed sufficient ammunition for twenty years consumption, and was happily increasing its supplies at a cost of £2m per year. In addition to this, it was reported that twenty, four-wheel Army vehicles occupied the attentions of nearly 70 personnel (including drivers, cleaners, and mechanics), while out of a total of 25,856 available beds in Admiralty, War Office and Ministry of Pensions hospitals, only 7,735 (29.9 per cent) were occupied. It was later noted that whereas Japan and the United States had engaged in severe cuts to naval expenditure, the extent of British expenditure had, by the early 1920s, enabled her to

[137] Price, L.L. (1919) 'Review – 'The Economic Foundations of Peace' by J.L. Garvin', *Journal of the Royal Statistical Society*, 82 (May), p. 400

[138] See, for example, *The Times* (4 June 1920), p. 13, col. B

[139] One noteworthy feature of this Committee was that although appointed to advise on weeding, felling and pruning public expenditure, the chairman, Sir Eric Geddes, had long been castigated as an administrative megalomaniac with a penchant for grandiose extravagance.

maintain a European naval force greater than at any time since the Napoleonic Wars.[140]

This problem was not restricted to questions of government expenditure and war bonuses paid to a vast army of civil servants and staff of government department. Harold Cox drew particular attention to the problem of unrestrained bureaucratic control over tariff policies. The pre-war policy of a statutory customs tariff had reflected transparent protectionism: manufacturers and traders, entering into long-term arrangements, were shielded by constitutional safeguards that ensured fiscal policies could not be altered without a fresh Act of Parliament. Conditions during the War had weakened such constitutional safeguards, with the necessities of national and economic defence having imposed upon the government the duty of regulating trade. It was this task, and the associated rise in official power, that was seen to have contributed to an air of war-time and post-war bureaucratic arrogance.[141] Through the eradication of constitutional safeguards, and the introduction of bureaucratic import controls, Cox believed that Board of Trade officials had unnecessarily intensified the depression by introducing a powerful element of uncertainty into economic decisions regarding long-term contracts.[142]

(5) Housing

Post-war unemployment, argued Cannan, stood in stark contrast to the enormous war-time transformation from civil to military occupations. The energetic

[140] Higgs, H. (1922) 'The Geddes Reports and the Budget', *Economic Journal*, 32 (June) pp. 257 – 258; Hirst, F.W. (1924) 'Letter – Official Expenditure', *The Times* (16 February), p. 8, c. A

[141] Proposals to impose legal status on these official controls was attempted with the Imports and Exports Regulation Bill, and although remaining in Parliamentary suspended animation for several months, the absence of support outside official circles eventually led its abandonment in 1920.

[142] Cox, H. (1921) 'The New Protection', *Edinburgh Review*, 233 (April), pp. 400 – 401

mobilisation of civil manufacturing for the production of munitions, and the absorption of approximately one-third of the working male population into the armed forces – variously described in the war-time literature as akin to a "second industrial revolution"[143] and "economic miracle"[144] – had secured a dramatic reduction in unemployment. In February 1915, G.D.H. Cole observed that the Amalgamated Society of Engineers had reported only 415 unemployed members from an estimated national membership of 175,000.[145] The success of this transformation also represented the cruellest irony of war: obstacles to production were only removable when nations were locked in military conflict and not when they were engaged in peaceful co-operation.[146] This was not to ignore the problems that such a speedy transformation had presented: British industry found itself handicapped by an absence of goods and chemical processes previously obtained from Germany; there had been obvious rivalries for essential materials (as between munitions and ships for steel, for example); and only special measures had prevented a serious contraction of the building industries. Yet the lingering rhythm of war had not distorted the established measure of British economic life. Whilst Germany had overrun the industrial districts of Belgium, Northwest France, and Poland, neither force nor intrigue had enabled her to disrupt Britain's war-time transformation.[147]

Cannan believed that recognition of Britain's successful war-time transformation served as an important base against which to assess her post-war difficulties. It was apparent that Britain's war-time success had been facilitated by an

[143] Pethick-Lawrence, F.W. (1916) 'The Second Industrial Revolution', *Nation & Athenaeum*, 18 (26 February), p. 760

[144] Hobson, J.A. (1917) 'Shall We Be Poorer After The War?', p. 44

[145] Cole, G.D.H. (1915) 'Trade Union Rules and the War', *Nation & Athenaeum*, 16 (27 February), p. 678

[146] Cannan, E. (1917) 'The Influence of the War on Commercial Policy' (22 September) in *An Economist's Protest*, p. 125

[147] Kirkaldy, A.W. (1916) 'Some Thoughts on Reconstruction After The War' in Kirkaldy, A.W. (ed) *Labour, Finance, and the War*, p. 4

extraordinary eruption of national duty and unity of purpose, leading to Britain's citizens utilising their full potential in order to ensure the production of vital military supplies.[148] He believed that the strength of wartime sentiment had been unnecessarily diluted by public clamouring for reductions in excessive government expenditure (a fact that suggested that acceptance of the high tide of post-war taxation had passed), and post-war government confusion surrounding its grandiose proposal of making the "land fit for heroes to live in."

The history surrounding the early post-war housing schemes can briefly be summarised as follows. Rising war-time expectations regarding the rebuilding of worn-out and insanitary working-class housing (variously estimated by Cole at between 650,000 and 1,400,000 houses[149]) had led to an ambitious state-subsidised housing program through the 1919 Housing and Town Planning Act (the so-called "Addison Act"). Other measure to promote the housing industry included the Victory Construction Company (founded in December 1919) to supply standardised cottages on a large scale, and the introduction of the Housing (Additional Powers) Act to authorised subsidies of up to £15m for private builders. Owing to poor local authority guidance, unscrupulous builders' merchants, manufacturers and private contractors had successfully exploited the provision for state subsidy in order to charge extortionate prices. It was estimated that the average cost per house had increased from £700 in August 1919 to £900 by August 1920.[150] The growing temper of "national economy" during the early 1920s led to the suspension of the scheme

[148] This view was in no way peculiar to British economists. For another contemporary discussion, see Edgeworth, F.Y. (1917) 'Some German Economic Writings About The War', *Economic Journal*, 27 (June), p. 245

[149] Cole, G.D.H. (1921) 'The Moral of the Housing Fiasco', *New Statesman*, 17 (23 July), pp. 433 – 434; Cole, G.D.H. (1924) 'Housing – The Problem of Skilled Labour', *New Statesman*, 22 (12 January), p. 386

[150] Dearle, N. B. (1929) *An Economic Chronicle of The Great War For Great Britain and Ireland 1914 – 1919*, London: Humphrey Milford, p. 323

(with building restricted to already approved projects), and the eventual sacking of the forceful and sincere Minister of Health, Dr. Addison. The principle of a subsidised building scheme was later modified under the ("Chamberlain") Housing Act of 1923, although the success of the scheme in reducing building costs was not reflected in the construction of good quality, working-class accommodation. Private building contractors claimed the lower annual subsidy, available under the Act, but concentrated on satisfying the growing demand for middle-class housing. The situation was redressed, at least in part, by the ("Wheatley") Housing (Financial Provisions) Act of 1924.[151]

The War had demonstrated the important principle that production, distribution and consumption could function smoothly once economic agents identified with a national vision. The absence of an energised post-war national consciousness – in this instance, arising from the government's confused commitment to an adequate, long-term housing policy – was seen to have introduced an unfortunate impediment into the process of economic recovery.[152]

(6) Communications

Before offering some conclusions on the general trend of the early post-war economic debate, we shall briefly consider the issue of communications. It was apparent that the War had awakened an awareness of the interconnections between

[151] Cole, G.D.H. (1921) 'The Moral of the Housing Fiasco', p. 435; Cole, G.D.H. (1922) 'Le Mond Où L'on S'ennuie', *New Statesman*, 19 (12 August), p. 507; Cole, G.D.H. (1923) 'Mr. Chamberlain's Housing Plans', *New Statesman*, 20 (24 March), p. 715; Cole, G.D.H. (1924) 'Housing – The Problem of Skilled Labour', *New Statesman*, 22 (12 January), p. 387; Pollard, S. (1969) *The Development of the British Economy*, London: Edward Arnold Ltd (2nd edition), pp. 254 – 258; Crowther, M. A. (1988) *Social Policy in Britain, 1914 – 1939*, London: Macmillan, pp. 35 – 37, 56 – 57

[152] Cannan, E. (1924) 'Financial Factors' in *Unemployment In Its National and International Aspects*, p. 51

the various modes of communication – including railways, roads, the postal service, telephones, and telegraphs – and their importance in relation to Britain's social and commercial requirements.[153] There had even been discussion of the economic advantages that could arise from the proposed construction of tunnels linking Britain with France, and North-East Ireland with South-West Scotland.[154] By the early-1920s, it was becoming clear that severe problems had engulfed Britain's national communications network. Given the space available, and the overall complexity of the British inter-war transport structure, we shall only deal with fairly broad contemporary concerns regarding postal arrangements and the general character of Britain's railway system.

Dealing first with the postal service, the primary consideration of the Postmaster-General had long been to secure the "self-supporting" ability of the service between each separate budget year. In comparison with the revenue earning branches of government, such strict conditions suggested a situation in which the postal service no longer operated according to Britain's interests, and in particular the interests of industry or commerce. Was it not better, asked William Acworth, at a time when trade was falling off and unemployment rising, for the postal service to run at a loss, provided that the indirect benefit to trade exceeded the direct loss? The decision to abolish the Sunday collection, delivery and dispatch of letters in July

[153] The economic disadvantages of the canal network (primarily the cumbersome system of locks required to lift barges to different levels) had been recognised before the war, and hence was largely excluded from the post-war debate. Acworth, W.M. (1905) 'British Canals', *Economic Journal*, 15 (June), pp. 149 – 155; Cannan, E. (1907) 'Review – 'British Canals' by E.A. Pratt', *Economic Journal*, 17 (March), pp. 95 – 98. It is also interesting that economists paid scant attention to air transport, although we may note Marshall's prediction that the future movement of people and goods would be facilitated the "possible advent of a 'helicopter'" which would "rise from, and descend to, a small private garden by vertical movement." Pigou, A.C. (1919) 'Marshall's 'Industry and Trade'', *Economic Journal*, 29 (December), p. 446

[154] Acworth, W.M. (1919) 'Transport Reconstruction', *Edinburgh Review*, 229 (January), p. 21; Acworth, W. M. (1919) 'The Position and Prospects of the Railways', *Contemporary Review*, 116 (July/Dec), p.509

1921 was seen as an unnecessary impediment to trade, with ample evidence demonstrating that orders posted after the close of business on Saturday were not being delivered until the following Tuesday morning.[155] Further more, decisions to secure income by raising the internal postal rate (from 1½*d.* to 2*d.* and telegrams from 9*d.* to 1*s.*[156]) as well as surcharging foreign letters and circulars, served as an inexcusable obstacle at a time when businesses were seeking to encourage domestic and international trade.[157]

The second area of concern was the national railway system. During the war, patriotic fervour had, not unexpectedly, determined that Britain possessed the finest railway system amongst any of the combatant nations. By the early 1920s, the publication of international statistics, general congestion in docks, warehouses and shunting yards, and the speedy diminution of patriotism, had laid bare grave inefficiencies in the methods of railway carriage. Comparisons demonstrated that merchandising rates (average charge per ton-mile) were higher in Britain than in any of her immediate competitors; the average load of a "fully" loaded truck was generally one-third of its capacity; and average engine loads were less than half the engine's haulage capacity. In addition, schemes of post-war reconstruction, including the Ministry of Transport Act (1919) and the Railway Act (1921), had been unnecessarily sterilised through the growing demand for post-war government economy.[158]

[155] The attitude amongst business leaders regarding the abolition of the weekend service appears to have been mixed. See, for example, *The Times* (26 May 1921), p. 10, c. D; *The Times* (22 August 1921), p. 8, c. F

[156] Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, p. 198. Postal charges were lowered in 1923.

[157] Cole, G.D.H. (1921) 'The Development of the Post Office', *New Statesman*, 17 (7 May), pp. 124; Acworth, W.M. (1921) 'Letter – Cheaper Postage', *The Times* (8 November), p. 13, c. F; Acworth, W.M. (1923) 'Letter – Post Office Methods', *The Times*, (16 March), p. 13, c. F

[158] Acworth, W.M. (1920) 'Letter – Railway Congestion', *The Times* (2 January), p. 6, c. A; Acworth, W.M. (1923) 'Groupings Under The Railways Act, 1921', *Economic Journal*, 33 (March), pp. 37 – 38

Growing Recognition of Changing Conditions

The foregoing discussion has reflected the broad theme of the wartime and early inter-war unemployment debate. As has been shown, the severity of post-war unemployment was attributed to a variety of impediments and complications that had exacerbated an anticipated cyclical depression.

It was believed that the economy possessed sufficient flexibility to overcome such unnecessary and unfortunate impediments. As an example of this, it was suggested that inopportune changes in wage determination, that had co-existed with the abnormal post-war boom (that is to say, the apparent divorce between the marginal product of labour and the wage rate), would be corrected through the inevitable movement of the trade cycle. A different interpretation was provided by Cole, who predicted that the downward flexibility of post-war wage rates did not arise simply from the movement of the cycle, but the absence of effective labour leadership, which was preventing labour from cementing post-war improvements. This problem appeared to be associated with the complexity of directly governing a large, geographically and industrially dispersed labour movement.[159] Even allowing for attempts at democratic control through delegate conferences, Cole believed that the absence of a focused leadership would eventually diminish the communal character of labour, so presenting minimal opposition to employers' demands to reduce wages. [160]

[159] The obvious exception was the Miners' Federation of Great Britain, whose location within mining villages enabled it to take advantage of natural democratic units.

[160] Cole, G.D.H. (1920) 'Trade Unions and Democracy', *New Statesman*, 16 (30 October), p. 98; Cole, G.D.H. (1923) 'The Cost of Living', *New Statesman*, 21 (1 September), p. 586

Given the dominant economic view that the War had failed to destabilise the forces governing the capitalist system, and that the economy possessed sufficient flexibility, it appeared logical that the problem of post-war unemployment, although severe in comparison with pre-war experiences, was nothing more than an evanescent phenomenon. Although offering diametrically opposite interpretations of the forces governing the trade cycle, the long-standing suggestion that each phase of the cycle was a consequence of its preceding stage made it appear inevitable that the post-war economic system would continue to operate according to its pre-war rules. It was believed that the post-war evils of an exaggerated boom and depression represented the re-emergence of an underlying economic system. According to the underconsumptionist interpretation, for example, post-war unemployment reflected a pre-existing problem whereby the rate of production repeatedly exceeded the rate of consumption. Such problems would only be re-solved, reasoned Hobson, through a social distribution of income that balanced saving, consumption and production. Similarly with the monetary interpretation, fluctuations in economic activity arose from fluctuations in the credit cycle. Unless monetary policy was introduced to ensure greater price stability, the cycle would repeat itself once a safe ratio between bank cash reserves and liabilities had been restored.

It is at this point that we must consider the changing character of the inter-war economic debate. Although it is difficult to trace the precise separation between one phase of the debate and the next, by the 1920s it was clear that faith in a temporary depression was co-existing with a more unsettled interpretation of events. It was not simply that the collapse of a dramatic post-war boom had been followed by dramatic unemployment, but that unemployment had remained a permanent feature of the post-war economy. The essence of this revised interpretation was simple: given comparisons between the pre-war and post-war economic system, was it really possible for society to remain committed to the curative movement of the trade cycle? Was it logical to believe that the post-war economy was the continuation of the pre-war system? Faith in the transient nature of economic forces was seen to have served as a dangerous stimulant to erroneous economic analysis. To give an example of this, Cannan argued that a commitment to theories of economic depression that took as their central theme the idea of an inherently consistent trade cycle, only served to distort human appreciation of economic reality. To expect, simply on the bases of experience, that boom would follow depression as regularly as night followed day would, unless treated with some degree of intellectual caution, lead anyone to underestimate the possible significance of changing, real world events. This was not to deny the natural quality of economic fluctuations, but rather to suggest that society in general had to move beyond pre-war theories and give attention to the prevailing economic environment. As an example of this, Cannan criticised economists for giving little, if any, consideration to the long-term psychological consequences that almost certainly accompanied the dramatic transition from pro-longed wartime prosperity to post-war depression.[161]

A more powerful interpretation of Britain's post-war problems rested with the changing structure of capitalism arising from the permanent destruction of pre-war trading relationships. Before 1914, the mutual dependence of nations, particularly in terms of raw material and food supplies, had successfully neutralised the potency of racial barriers and national aggression. Throughout this period, it had been obvious that the gradual eradication of semi-tribal prejudices was propelling nations towards

[161] Cannan, E. (1922) 'Review – 'The Trade Cycle' by F. Lavington', *Economic Journal*, 32 (September), pp. 355 – 359

the introduction of an international political and economic body.[162] With military and political conflict having led to the destruction of four Empires – Tsarist Russia, Ottoman Turkey, Wilhelmine Germany and Habsburg Austro-Hungary – and hence the intensification of national animosities, the desire for peaceful political and economic intercourse had evaporated. As an example of this situation, Edgeworth bemoaned the increasing competition for armaments following the subdivision of post-war Europe into a number of small nations.[163] Whereas pre-war trade had been the product of detailed negotiations, post-war confidence in the international economy had been undermined by the redrawing of political boundaries, the rapid alteration of tariff levels by newly formed, inexperienced authorities, and the emerging system of *tarifs de combat* (interpreted by Hobson as "virtually negotiation by bludgeon"[164]). As post-war faith in the curative properties of the trade cycle diminished, economists actively sought to understand the destructive forces that were undermining the long-standing system of beneficial exchange.

Economic Nationalism and Industrialisation

The horrors of the greatest war the world had then known had made many hopeful that a formally constituted political body would serve as the true basis for

[162] Jevons, H.S. (1907) 'The Development of an International Parliament', *Contemporary Review*, 92 (July/Dec), p. 314; Hobson, J.A. (1915) 'Letter – The International Mind', *Nation and Athenaeum*, 17 (14 August), p. 639; Cannan, E. (1916) 'A Plea For Large Political Units' in *An Economist's Protest*, pp. 83 – 88; Shadwell, A. (1919) 'The Problem of the Age', *Edinburgh Review*, 229 (April), p. 240

[163] Edgeworth, F.Y. (1922) 'Review – 'War and National Finance' by R.H. Brand', *Economic Journal*, 32 (June), p. 218

[164] Hobson, J.A. (1929) 'The United States of Europe', *Contemporary Review*, 136 (July/Dec), p. 547

improved international co-operation.[165] Such desire can be seem in proposals, presented by Keynes, for a European free trade union co-ordinated by the League of Nations.[166] Yet political inflexibility, and the tenacious co-ordination of economic forces according to national prejudice, had long reflected issues of national sentiment and racial ascendancy. While there were efforts to promote international solidarity, the strength of such sentiment dictated that nationality would from then on serve as the guiding principle of economic activity.[167] This form of aggressive, racially motivated hostility to all forms of internationalism had developed from Johann Gottlieb Fichte's utopian vision of an isolated commercial state (*Der geschlossene Handelsstaat*) published in 1800. A large component of the ideology and dialectic of economic nationalism represented a hatred for the impersonal rationalism of economics, and the fear that national character and the strategic safety of the State would be undermined through moves towards international co-operation.[168]

This had many economic implications. One interpretation, provided by Robertson, centred on the post-war influence of economic nationalism on the elasticity of demand for agricultural produce. Agricultural production had emerged from the War relatively undisturbed, but had faced the closure of vital markets in central Europe. Faced with an abundant supply of raw produce, but a dramatically reduced European market, Indian and Argentinean agriculturists had been compelled to accept a substantially lower price for their produce. Provided that agricultural

[165] The attraction of the League of Nations amongst economists was also influenced by the anticipation of improvements in the co-ordinated collection and publication of international statistics. See Loveday, A. (1921) 'The League of Nations and International Trade Statistics', *Annals of the American Academy of Political and Social Sciences*, 94 (March), pp. 156 – 159

[166] Keynes, J.M. (1971) *Collected Writings of John Maynard Keynes – Vol. II: Economic Consequences of the Peace,* London: Macmillan, p. 168

[167] Cox, H. (1918) 'Commerce and Empire', *Edinburgh Review*, 228 (October), p. 397

[168] Daniels, G.W. (1936) 'Economic Theory and National Policy', *Manchester School*, 7, p. 95. For many Central and European Countries, such prejudice also found expression through "artistic nationalism". See Reynard, H. (1928) 'Official Papers – Report on the Present Position and Tendencies of Industrial Art', *Economic Journal*, 38 (March), p. 149

produce could be stored, argued Robertson, normal (pre-war) conditions suggested that a decline in the price of such produce would stimulate the output of non-agricultural producers. However, a sudden or violent swing in prices – such as the dramatic crash of world wheat prices from 86*s*.4*d* per quarter in 1920 to 40*s*.9*d* per quarter in 1922[169] – was seen to produce a highly inelastic demand for agricultural goods. The economic effect of the post-war onslaught of agricultural produce on an increasingly reduced market was clear: a violent change in the elasticity of demand for such produce (implying that reductions in price did not create any increase in the quantity consumed) had led to a substantial reduction in the incomes of large and efficient foreign agriculturists, so preventing them from purchasing British manufactured goods.[170]

By the mid-1920s, it had become apparent that the anticipated convergence of international interests had been overwhelmed by vitriolic hatred and on-going national commitments to economic autonomy. The principles of national prejudice and the politicisation of post-war trade signified the failure of diplomatic efforts to secure international co-operation.[171] Yet while Cannan was prepared to accept post-war economic nationalism as an expression of a patriotic reverence for the State and economic self-sufficiency[172], others were less responsive to the suggestion. Could the reduced levels of post-war trade between geographically close neighbours, coupled with the violent disruption of the international commercial structure, really be attributed to some fervent desire to preserve national character? In the same way that

[169] Pollard, S. (1969) *The Development of the British Economy, 1914 – 1967*, p. 134

[170] Robertson, D.H. (1924) 'Note on the Real Ratio of International Interchange', *Economic Journal*, 34 (June), p. 287; Robertson, D.H. (1926) *Banking Policy and the Price Level*, London: P.S. King & Son Ltd, pp. 14 – 16

[171] Paish, G. (1927) 'The World Economic Conference', *Contemporary Review*, 132 (July/Dec), p. 11; Hobson, J.A. (1929) 'The Saving Faith of Internationalism', *Contemporary Review*, 135 (Jan/June), p. 688

[172] Cannan, E. (1926) 'A Review of 1925' (28 January) in *An Economist's Protest*, pp. 414 – 415

pre-war Germany had employed the Caprivi duties, economists believed that the rise of economic nationalism, and the resulting dislocation of the pre-war system, had to reflect some rational economic motive. This motive was eventually located in the decisions of nations who, having reached a certain stage of economic and social development, had become eager to adopt standardised productive techniques and so advance along the path established by Britain, Germany and the United States.[173]

What had facilitated this economic transformation? One explanation, provided by Cole and Hobson, suggested that, through an instinctive desire to secure profitable export markets, eighteenth and nineteenth century capitalist imperialism had led Britain to invest her surplus financial capital around the globe. It was this investment that had assisted the development of the manufacturing activities of countries such as Brazil, China, Chile, and India.[174] In addition to this, the effects of a protracted international war in obstructing the normal flow of economic intercourse, and an ability to utilise power-driven machines and the advantages of cheap electrical power, had enabled developing nations to accelerate the enlargement of their manufacturing base behind tariff barriers.[175] In one respect, the growth of economic nationalism represented an exaggerated version of the accepted justifications for protectionism. The intellectual defence of limited protectionism – including support of industries deemed essential to national security or the defence of industries in the early stages of development – had long been accepted before the War.[176] Post-war faith in the international division of labour had therefore been undermined by the success of national prejudices in exploiting such justifications for limited protection.

[173] Jones, J.H. (1927) 'The International Economic Conference', *The Accountant*, 76 (23 April), p. 604
[174] Cole, G. D. H. (1923) *Out of Work: an Introduction to the Study of Unemployment*, pp. 32 – 33; Hobson, J.A (1931) 'A World Economy', *New Statesman &Nation*, 1 (18 April), p. 274
[175] Jones, J.H. (1930) 'Changes in World Demand', p. 732; Jones, J.H. (1935) 'Geographic Trends In Industry', *The Accountant*, 92 (16 February), p. 219
[176] Higgs, H. (1920) 'Review – 'Free Trade, The Tariff and Reciprocity' by F.W. Taussig', *Economic Journal*, 30 (September), p. 374

There is one further theme to consider. There was an acceptance amongst inter-war economists that economic development depended on the social and economic conditions prevailing in the countries caught up in the system. This may be seen as similar to Abramovitz's idea of "social capability." It was suggested by Cole that the speed with which foreign countries had developed such industries as textiles, iron, steel and engineering, could not be explained simply by reference to social and economic conditions. There had to be something deeper. The explanation, claimed Cole, lay in the sudden explosion of a desire within such countries to expand their industrial base and so compete with the leading industrialised nations in foreign markets. The War had certainly provided an unrivalled opportunity for capturing Britain's pre-war markets; but it was a pronounced desire to moved beyond such basic activities as breeding cattle and cultivating cereals, and actually assume the trappings of a manufacturing nation, that made the action effective.[177]

The nucleus of the process of international industrialisation – eloquently described by Robertson as "the partial closing of the vast gap...between the comparative effectiveness of different countries in agriculture and industry"[178] – may, as suggested above, be regarded as an early presentation of Abramovitz's "catch-up" hypothesis: low productivity countries, previously reliant upon agriculture or mining, had rapidly advanced through the successful development of a manufacturing base.[179] Irrespective of whether international economic nationalism was the manifestation of economic and political prejudices or the drive towards

[177] Cole, G.D.H. (1927) 'Economic Nationalism verses Common Sense', *New Statesman*, 29 (18 June), p. 303. A modern presentation of this idea can be found in Marrison, A. (2000) 'Legacy – war, aftermath and the end of the nineteenth-century liberal trading order, 1914 – 32' in Wrigley, C. (ed.) *The First World War and the International Economy*, Cheltenham: Edward Elgar, p. 159

[178] Robertson, D.H. (1928) 'Review – 'International Trade' by F. W. Taussig', *Economic Journal*, 38 (June), p. 279

[179] Abramovitz, M. (1986) 'Catching Up, Forging Ahead and Falling Behind', *Journal of Economic History*, 46, pp. 385 – 406

industrialisation, it was apparent that the unification of the world's economic resources through political means had become a distant ideal.

It was gradually realised that Britain's post-war economic malaise arose from a war-time and post-war ignorance of the permanent changes that were occurring in the international environment. Such ignorance had led to the growth of exaggerated expectations regarding the direction of post-war demand and the continued expansion of international markets. Looking back on Britain's immediate economic history (particularly the period from 1914 to 1920), it was recognised that a prolonged war-time boom and false expectations had misdirected both capital and labour into heavily localised and specialised industries which, due to permanent changes in world demand, had come to yield low economic returns.[180] The harsh realities of the post-war economic environment required the economy to move to a new equilibrium.

The Evolution of the Economy

It is a common misconception that, by defining particular time periods and emphasising partial equilibrium analysis, early twentieth century economists ignored the vital, dynamic qualities of the economic system. Writing during the 1950s, both M.M. Postan and Walt Rostow observed that, prior to the Second World War, the theoretical character of the trade cycle ignored the conditions of economic growth.[181] This idea has been reiterated by Landreth and Colander, who note that formal

[180] Cole, G.D.H. (1928) 'Over-Capitalisation', *New Statesman*, 31 (9 June), p. 281; Clay, H. (1929) *The Post-War Unemployment Problem*, London: Macmillan & Co. Ltd, pp. 17 – 23; Scott, W.R. (1930) 'Economic Resilience', *Economic History Review*, 2 (January), p. 295; Robertson, D.H. (1931) 'Our Unstable Economic Progress', *The Listener*, 6 (25 November), p. 908

[181] Postan, M.M. (1953) 'Economic Growth', *Economic History Review*, 6, p. 78; Rostow, W.W. (1959) 'The Stages of Economic Growth', *Economic History Review*, 12, p. 1

attempts at growth theory (or the dynamic extension of trade cycle theory), as an integral component of macroeconomic theory, developed from the work of Harrod, Domar, Solow and Swan during the 1950s. [182] Yet even a brief examination of eighteenth, nineteenth and early twentieth century economic literature suggests that economists were fully alive to the process of economic development. Throughout this period, there had developed a large literature detailing the process of economic transformation, the development of the capitalist spirit, and the position of capitalism in the development of economic civilisation.[183] Yet where as Adam Smith's account of the emergence of "commercial society" reflected a combination of haphazard conditions[184], the enormous eruption of nineteenth century industrialisation had led economists and economic historians to identify a specific feature of the process of economic development. Of particular interest in this respect are Cunningham's *The Growth of English Industry and Commerce in Modern Times* (1892), J.A. Hobson's *The Evolution of Modern Capitalism* (1894), Richard Ely's *Studies in the Evolution of Industrial Society* (1903), and D. H. MacGregor's *The Evolution of Industry* (1911). The invocation of terms such as "growth" and, more importantly, "evolution" should not be underestimated. This profound willingness to draw upon descriptive biological terminology enabled economists and economic historians of all persuasions, to re-conceptualise the forces of that governed economic change. Sir William Ashley's remark that the purpose of economics and economic history was to

[182] Landreth, H. & Colander, D.C. (2002) *History of Economic Thought*, Boston: Houghton Mifflin Company (4th edition), p. 414

[183] For an informative inter-war discussion of this voluminous literature, see Tawney, R.H. (1933) 'Studies in Bibliography – II: Modern Capitalism', *Economic History Review*, 4 (October), pp. 336 – 356

[184] See Parker, N. (1995) 'Look no hidden hands: how Smith understands historical progress and societal values" in Copley, S. & Sutherland, K. (eds.) *Adam Smith's Wealth of Nations: New Interdisciplinary Essays*, Manchester: Manchester University Press, pp. 122 – 143. The absence of any coherent discussion of growth before the eighteenth century is attributed by Brewer to the slow and uneven pace of economic development, Brewer, A. (1995) 'The Concept of Growth in Eighteenth-Century Economics', *History of Political Economy*, 27, pp. 634.

understand the "curve of economic evolution" may be mentioned by way of another example.[185] We should also remember that Marx's doctrine of class warfare was based upon an interpretation of the evolution of the modes of production, while "biological conceptions" of how the economy actively responded to environmental factors was a central component of Marshall's methodology.[186]

It can be seen that contemporary economists and economic historians were drawn towards establishing a direct association between natural evolution and the development of economic civilisation. The continuous process of economic evolution, as reflected in the replacement of vegetable dyes by aniline dyes, private carriage by coaches, or sailing ships by steam ships, reflected the effects of technical innovations or changes in fashion or custom. Similarly, with different countries possessing different advantages, the desirable size of any domestic industry was dictated by the importance of production costs. Britain's inability to compete with American wheat production, for example, had promoted changes in the structure of British agriculture and an increase in domestic milk, butter and meat production.

Overall, Britain's economic evolution was visualised as a chronological sequence, whereby technical innovations and capital accumulation had moved society from pre-economic and primitive structures (hunter-gatherers), to the development of agriculture, the encouragement of domestic manufacturing through steam power and improved transportation, and eventually the development of overseas markets and the international division of labour. Periodic booms and slumps

[185] Ashley, W.J. (1893) 'On the Study of Economic History', *Quarterly Journal of Economics*, 7 (January), p. 122

[186] Hodgson, G.M. (1993) *Economics and Evolution*, Cambridge: Polity Press, pp. 99 – 109. Hodgson notes that the development of Marshall's evolutionary analysis was stimulated by the work of Herbert Spencer rather than that of Charles Darwin. Indeed it was Spencer, and not Darwin, who popularised the term "evolution" during the nineteenth century, and fuelled renewed interest in biological and evolutionary models.

were represented as socially disadvantageous forces that caused the economy to temporarily deviate from its pre-determined path.

By reducing the complexities of development to this generalised form – which is not dissimilar from the Rostovian "take-off" model – the pattern of economic evolution was taken as a fixed and unalterable progression that *all* nations were assumed to follow. In the same way that agriculture had been surpassed by industry, it was accepted that Britain's declining position in post-war international markets necessitated the development of economic activity beyond the narrow confines of industry. Put another way, it was recognised that Britain's long-standing industrial position was nothing more than a passing stage in the natural process of the world's economic evolution. The post-war world did not represent "confusion" compared with the pre-war "normality", nor a general indictment of the capitalist system, but simply evidence of a natural process of economic development and maturity.

The New Economy

Economics dictated that responsibility for organising production rested with the efficient allocation of resources though the activities of the unrestrained market. Whilst it could not be denied that the necessary changes would disadvantage certain groups (especially given the intricate and interconnected character of Britain's economic system), it was anticipated that the magic of the free market – the guiding principle of the "invisible hand" – would secure the necessary changes to the economic system. Through the mechanism of the market, labour and capital displaced by foreign competition would be re-deployed, so leading to a speedy adjustment of the economic equilibrium. But what would this new economic structure look like?[187] While it was perfectly apparent that Britain would face increased competition in international markets, it was clearly impossible for her to disengage completely from international trade.[188] It was therefore believed that as low-grade production passed to countries such as India and China, efficient British firms would develop new export trades concentrating on specialised, quality goods for which world demand was more elastic than for cotton, wool, or coal.[189] Diversification was the foundation of future success, with the inevitable contraction of the economic structure seeing industries "localised in the old centres" yielding "pride of place…to industries of a new type."[190] Through such expanding opportunities, the economy would eventually witness growth and the profitable employment of displaced labour in locally organised, self-contained concerns such as shops, garages, beauty parlours, hotels and restaurants.[191] Reductions in average family size would release income formally expended on children, so leading to increased consumer expenditure, changes in social habits and fashions, and the opening of demand for commodities previously out of the reach of the masses.[192] It

[187] For a sustained contemporary discussion of Britain's inter-war industrial position, and the process of adjustment and specialisation, see J.H. Jones's sixteen part series 'The Future of British Industry' published in *The Accountant* (4 August 1928 – 8 December 1928), and J. Hilton's eleven part series 'Industrial Britain' in *The Listener* (24 January 1934 – 11 April 1934).

[188] Jones, J.H. (1926)' What of the Future?', *The Accountant*, 75 (18 December), p.855; Jones, J.H. (1927) 'The Future of Industry', *The Accountant*, 76 (4 June), p. 836; Daniels, G.W. (1931) 'Overseas Trade of the United Kingdom in Recent Years as Compared With 1913', *Manchester School*, 2, pp. 1 – 9; Daniels, G.W. (1931) 'The Present Economic Situation', *Manchester School*, 2, pp. 71 – 74

[189] Cole, G.D.H. (1931) 'Britain's Economic Future', *New Statesman & Nation*, 2 (22 August), p. 216; Forrester, R.B. (1932) 'Britain's Access to Overseas Markets', *Economic Journal*, 42 (December), p. 52; Hilton, J. (1934) 'What Is The Future of British Industry?', *The Listener*, 11 (11 April), p. 623

[190] Henderson, H.D. (1926) 'The Economic Trend' (6 November) in Clay, H. (ed.) (1955) *The Inter-War Years and Other Papers*, p. 25

[191] Cole, G.D.H. (1928) 'The Mobility of Labour', *New Statesman*, 31 (16 June), p. 320; Cole, G.D.H. (1929) 'Work or Doles?', *New Statesman*, 33 (5 October),p. 768; Brunner, C.T. (1933) 'Economic Trends and Government Interference', *Manchester School*, 4, p. 92

[192] Clay, H. (1931) 'Some Aspects of the World Depression – I', *Journal of the Institute of Bankers*, 52 (December), pp. 521 – 522

was also predicted that the economy would experience an increased appreciation for the work of skilled, individual craftsmen involved in the manufacture of those goods not amenable to the techniques of mass production.[193] Further more, through domestic leisure time, opportunities for travel ("holiday making"), and the increased publicity of Britain's historic towns and countryside, it was believed that the domestic economy would experience increased employment associated with the building and running of holiday resorts.[194]

It can also be seen that while economists believed it essential for Britain to adjust her economic structure, they did not believe that the process would lead to the creation of an economic or social utopia. Increased importance of tourism, wrote Jones, would, by its very nature, lead to an increase in seasonal and casual employment, while the capriciousness of fashion and human nature was expected to lead to an unstable demand for many of the products of the distributive and service industries.[195] It was also feared that the increasing mechanisation and standardisation of the production process (most noticeable following the policy of rationalisation) would stifle humanity's insatiable desire for independence and self-expression. Demoralised workers would be required to face the deadening strain of monotonous repetition, with all vestiges of affinity between the worker had the commodity – a potent mixture of skill, blood, sweat, and tears – gradually eradicated.[196] A natural

[193] Stafford, J. (1930) 'Review – 'Rationalisation and Unemployment' by J.A. Hobson', *Manchester School*, 1, p. 43

[194] Henderson, H.D. (1930) 'The Development of New Industries' (21 August) in Clay, H. (ed.) (1955) *The Inter-War Years and Other Papers*, p. 64; Gregory, T.E. (1930) 'Rationalisation and Technological Unemployment', *Economic Journal*, 40 (December), pp. 564 – 566; Jones, J.H. (1937) 'Expanding Industries', *The Accountant*, 96 (23 January), p. 116

[195] Jones, J.H. (1930) 'Changes in World Demand', *The Accountant*, p. 733; Jones, J.H. (1936) 'Industry and the Seasons', *The Accountant*, 95 (8 August), p. 183; Jones, J.H. (1938) 'Luxury and Leisure', *The Accountant*, 98 (8 January), p. 32

[196] Price, L.L. (1923) 'Industrial Policy', *Economic Journal*, 33 (September) , p. 361; Cole, G.D.H. (1925) 'Bad Temper In Modern Industry', *New Statesman*, 24 (28 March), pp. 709 – 710; Sargant Florence, P. (1930) 'The Science of Industrial Relations', *The Listener*, 5 (8 October), p. 555; Jones, J.H. (1937) 'Speed In Industry', *The Accountant*, 96 (24 April), pp. 575 – 576

desire for freedom and relaxation through activities such as drinking and gambling, could, if taken to extremes, generate unfortunate consequences.[197] The absence of reliable data made it difficult for economists to fully identify the problems associated with the consumption of alcohol. However, legislative measures restricting hours of sale, and industrial measures that compelled greater regularity at the workplace, led to the intuitive conclusion that excessive drinking outside working hours was not a seriously problem. More concern was directed towards the growing workplace craze to substitute gambling for alcohol. The growing drug-like alleviation of boredom through gambling had been recognised by Hobson even before the war. Such desire for sensationalism was not taken as an innocuous feature of modern life – some light relief midst the drudgery of the workplace – but as a dangerous activity in which rational thought was distorted by tortured optimism.[198]

It may be argued that the process of adaptation would have been expected to gain momentum through the wider cultural environment of the period. The historical characteristics of any period are always complex, and as such any claims for *Zeitgeist* ("spirit of the age") should be handled with some caution. Nonetheless, it cannot be denied that the inter-war period's all-pervasive style reflected a freewheeling desire to embrace energy, progress and innovation. Attributed by Marwick to the legacy of the Great War and the public's growing awareness of scientific discoveries[199], post-war society embodied a passionate desire to discard the

[197] The betting tax, introduced in 1926, was strongly opposed by both those who enjoyed gambling, and those who believed the tax was evidence of State endorsement of an evil vice. The tax was abolished in 1929.

[198] Hobson, J.A. (1905) 'The Ethics of Gambling', *International Journal of Ethics*, 16 (January), pp. 135 – 148; Shadwell, A. (1932) 'The Drink Problem', *Times Literary Supplement*, Issue: 1563 (14 January), p. 19; Hamilton-White, W. (1932) 'Current Social Survey – The Drink Problem', *Political Quarterly*, 3 (Jan/March), p. 114; Hilton, J. (1936) 'The Lure of the Football Pool', *The Listener*, 15 (11 March), pp. 484 – 485

[199] Public awareness of this scientific revolution had occurred in November 1919 following the conformation of Einstein's theory of general relativity and the overthrow of established Newtonian principles.

reactionary aspects of the pre-war order, and so embrace a world driven by speed and overflowing with modern ideas, materials and designs. We may briefly note new forms of industrial architecture; the design impulse towards vibrant, geometrically stylised shapes[200]; and the growing freedom of youth as represented in the absorption of American dance music.

There was, however, a strange conflict between this ebullient desire to "break into the world of modernity"[201], and Britain's continuing problem of unemployment. In comparison with other post-war economies, even such minor economies as Bolivia (specialising in tin production) and Cuba (specialising in sugar production), Britain appeared to have lost her spirit of initiative and adaptability.[202] The guiding hand of the market and the forces of self-interest had, for whatever reason, failed to properly materialise. In this context, unemployment represented the physical manifestation of forces that were preventing Britain from exploiting her full potential, and so securing a speedy change in her economic structure.

Summary and Conclusion

In this chapter, we have summarised a large body of contemporary economic literature relating to Britain's inter-war economic problems. Throughout the wartime and early post-war period, belief in the continued security of international markets and the periodicity of the cycle had led many economists to identify unemployment

[200] The widely accepted term Art Deco, symbolising this cultural and aesthetic movement, was born out of the *Exposition Internationale des Arts Décoratifs et Industriels Modernes* held in Paris during the spring of 1925. For a contemporary discussion of its artistic and economic importance, see Reynard, H. (1928) 'Official Papers – Report on the Present Position and Tendencies of Industrial Art', pp. 148 – 150

[201] Marwick, A. (2003) 'The Great War, Mass Society and Modernity' in Benton C. et al (ed.) *Art Deco, 1910 – 1939*, London: V & A Publications, p. 29

[202] Cole, G.D.H. (1926) 'A Challenge to British Capitalism', *New Statesman*, 26 (3 April), p. 771; Robertson, D.H. (1931) 'The Backwash of Progress', p. 870

as a purely temporary phenomenon that would eventually lead to a gradual recovery. In 1921, for example, Keynes believed that Britain was experiencing "an exceptionally severe cyclical fluctuation"[203], while in 1924, Beveridge interpreting Britain's problems as the result of a "cyclical depression of trade with post-war complications."[204]

History had clearly demonstrated that these were false assumptions. Yet this is not to suggest that the early post-war literature is devoid of potentially beneficial material to economic historians. In terms of modern historiography, it is interesting to note that the "real wage" interpretation of inter-war unemployment, traditionally attributed to Jacque Rueff's correlation of British unemployment and real wage movements in *Revue politique et parlimentaire* (December 1925), was actually pre-dated (or, to be more accurate, predicted) in the British literature in articles by Arthur Bowley and, in particular, Barbara Wootton.[205]

Another interesting themes that can be drawn from this literature concerns the different interpretations of the forces that propelled the post-war boom. Instead of attributing the dramatic expansion of Britain's productive capabilities simply to an overriding belief in the stability of international markets and the release of war-restrained effective demand, there was an effort to offer some deeper discussion of the underlying motivation of business men. The first of these centred on the view that increased exports served as a means of alleviating the burden of Britain's unremunerative post-war debt. In this instance, patriotic idealism was mingled with

[203]Keynes, J.M. (1921) 'The Depression in Trade' (4 September) in *Collected Writings of J.M. Keynes – Vol. XVII: Treaty Revision and Reconstruction*, London: Macmillan, p. 259

[204]Beveridge (1924) 'International Trade and Unemployment' in *Unemployment In Its National and International Aspect*, p. 8

[205] The first British presentation of the "real wage" thesis is traditionally attributed to Pigou's 1927 article 'Wage Policy and Unemployment', *Economic Journal*, 37 (September), pp. 355 – 368, and supplemented by other pieces such as Josiah Stamps two 1931 articles – 'Work and Wages – Part I: Fettered By The Dole', *The Times* (11 June 1931), p. 17, c. G, and 'Work and Wages – Part II: The Ban Upon Employment', *The Times* (12 June), p. 17, c. G

the individual utility maximisation of human beings. The second interpretation centred on the importance of human self-interest, and an apparent post-war drive towards securing large profits from expanded export markets in order to satisfy the capitalist demand for excessive profits and high dividend payments.

While the breadth of the contemporary literature makes it impossible to trace a precise delineation between various stands of the economic debate, it is nonetheless evident that, by the mid-1920s, the unremitting presence of unemployment had forced a re-evaluation of this interpretation. As Clay observed in 1929, "no conceivable exaggeration of ordinary trade fluctuation will explain certain features of post-war unemployment."[206] Belief in the inherently rhythmic quality of economic activity appeared to have blinded many economists to changes in the pre-war international relationship between production and consumption. As faith in the curative properties of the trade cycle evaporated, it became apparent that a medley of post-war problems – including the creation of post-war trade barriers, boycotts of British goods, and the industrialisation of many underdeveloped nations – had all contributed to the disintegration of organised and long-established economic bonds. With the expected route to economic recovery having evaporated, and facing the permanent shrinkage of once assured export markets, Britain's position as an international industrial power was declining.

It was recognised that Britain was set upon a voyage of economic transformation in which the domestic distributive and service industries would steadily absorb a larger portion of Britain's industrial and commercial activities. Yet despite a prevailing social spirit of bold dynamism and heroic modernity, the spontaneous operation of market forces failed to materialise. This was not interpreted

[206] Clay, H. (1929) *The Post-War Unemployment Problem*, p. 23

as the instability of capitalism, but merely its restricted operation: the invisible hand was not visible because it was not there. With economic maladjustment widespread, the permanence of post-war unemployment appeared to demonstrate a position of social and industrial morbidity. It is here that we find the gradually development of inter-war attitudes towards the problem of unemployment. For contemporary economists, unemployment represented the huge economic, social and human costs associated with the failure of the market to undertake a necessary process of economic development.

In the following chapters, we shall examine contemporary attitudes towards impediments that appeared to be preventing the economy from discarding its pre-war economic structure, as well as some of the methods that economists attempted to employ in order facilitate Britain's speedy movement to a new equilibrium.

CHAPTER 3

IMPEDIMENTS TO

ECONOMIC DEVELOPMENT

Introduction

As we have seen in the previous chapter, inter-war economists drew particular attention to post-war circumstances that were preventing Britain from undertaking the necessary process of economic evolution. With the existing economic structure seen as suboptimal, the obvious solution was to establish a new economic position.

The purpose of this chapter is to take our first step in understanding how inter-war economists interpreted the inaction of the invisible hand. The first section will draw upon several aspects of the contemporary debate, including the quantitative aspects of population (variously christened "the problem of human numbers"[207] or "the theory of excessive man-power"[208]), the structure and culture of Britain's business community, and the unnecessary obstacles arising from the Government's confused desire to remove "unnecessary" competition between motor transport and the railways.

The second section will shift the focus of our investigations, and examine inter-war suggestions that connected Britain's slow economic transformation with psychological and, more importantly, emotional reactions to post-war events. This

[207] Dalton, H. (1928) 'The Theory of Population', *Economica*, No. 28 (May), p. 29

[208] Stamp, J. (1931) 'Work and Wages – Part II: The Ban Upon Employment', *The Times* (12 June), p. 17, c. G

will draw particularly on contemporary attitudes towards the influence of unemployment benefit and post-war unemployment statistics in depressing the important vitality of the market mechanism. The third section of this chapter will concentrate on the ways in which economists first supported, and then later criticised, the policy of rationalisation.

Population, Migration, and Eugenics

By the early twentieth century, the apparently unshakeable Malthusian fear in the effects of subsistence on the size of the population had transformed itself into a discussion concerning the relationship between population density and national welfare. Evading a philosophical minefield in which national welfare was susceptible to a myriad number of interpretations, and reflecting a keener application of biological knowledge to human society, it was generally accepted that an optimum population density represented a population level which, given prevailing conditions, maximised the average income per member of the community. If, for example, a nation's population density were insufficient to guarantee the economic viability of large capital projects – the building of a railway, for example – material well-being would be less than it would otherwise have been.[209]

Looking at the problem through modern eyes, the instinctive approach would be to argue that since the demand for labour reflects the demands of the population, additions to the population would, *ceteris paribus*, constitute an additional market for goods and services. This theme was certainly accepted by economists such as Ediwn Cannan, John Hilton, J.H. Jones and Lionel Robbins, who questioned the basis on

[209] Dalton, H. (1928) 'The Theory of Population', p. 29; Beveridge, W. (1935) 'Births and Business', *The Listener*, 13 (6 February), p. 226

which post-war unemployment could readily be attributed to the pressures of over-population.[210] For these writers, there appeared not the slighted doubt that Britain's economic readjustment would keep pace with the growth of an able-bodied population. The number of British workers who were accustomed to employment in the large, staple industries would, via the unrestricted market, be profitably absorbed back into the economy through the transformation of these industries or the growth of the service and distributive industries. Over-population, if it existed at all, would be a long-term problem. A potential maladjustment between the actual population and its optimum level – in this instance, over-population – could only be identified following adjustment to the new equilibrium, and if the level of national welfare (average income per member of the community) at the new equilibrium could be demonstrated to be less than that associated with the previous equilibrium.

In contrast to this, the "over-population" interpretation of unemployment, as presented by, amongst others, Robertson and Cox, centred on the relationship between Britain's optimum population density and the effect of long-term economic activity in influencing population distribution. Not only was it assumed that human numbers were regulated, over a number of years, according to the permanence of domestic and international economic circumstances, but also that Britain's inevitable move towards a new equilibrium would necessitate a smaller population density. This argument may be reconstructed as follows.

[210] Robbins, L. (1927) 'The Optimum Theory of Population' in Gregory, T.E. & Dalton, H. (eds.) *London Essays in Economics: In Honour of Edwin Cannan*, London: George Routledge & Sons Ltd, p. 128; Hilton. J. (1929) 'Discussion on Dr. Snow's Paper', *Journal of the Royal Statistical Society*, 92, pp. 361 – 364; Jones, J.H. (1930) 'Remedies for Unemployment', *The Accountant*, 83 (13 September), p. 363; Jones, J.H. (1929) *The Economics of Private Enterprise*, Bath: Sir Isaac Pitman & Sons, Ltd, pp. 403 – 404; Cannan, E. (1931) 'The Changed Outlook in Regard to Population, 1831 – 1931', *Economic Journal*, 41 (December), p. 530; Cannan, E. (1934) 'Letter – Employment and Population', *The Times* (30 August), p. 8, c. 3

By drawing more distant lands closer to the British market, the development of extensive foreign trade towards the end of the eighteenth century had led to an unprecedented population expansion within Britain's manufacturing districts, and the aggregation of large numbers in polluted and soul destroying urban dwellings. This appeared to suggest a direct relationship between the economic structure and the prevailing level of the population: as manufacturing grew, population grew; as manufacturing contracted (as it was required to in the post-war world), Britain's population would be forced to contract. In responding to the loss of export markets, it appeared that Britain was not only required to alter the composition of her existing (pre-war) economic structure, but also the population distribution associated with that particular economic structure. Under these circumstances, surplus population was assumed to consume excessive resources, so inhibiting the necessary process of adjustment to a new equilibrium. Although some reduction in population numbers was already occurring through the slackening of the birth rate (a process that dated back to the mid-1860s) and the stability of the existing mortality rate[211], there were obvious physical limitations to the speed with which human numbers could adjust in response to the speedy passing of pre-war economic circumstances.[212] Population changes could take half a century or more. The number of workers available in, for example, the 1920s represented the effect of exogenous socio-demographic influences that had prevailed throughout the latter half of the nineteenth century.[213] As Robertson wittily observed, there was "a time-lag between the cradle and the

[211] The reasons governing the ebb and flow of human fertility were susceptible to both zoological and economic interpretations. See, for example, Beveridge, W.H. (1927) 'Falling Birth Rate', *The Times* (29 January), p. 8, c. A

[212] Cox, H. (1925) 'Socialism and Unemployment', *English Review*, 40 (Jan/June), p. 31; Robertson, D.H. (1930) 'Too Many Man – Too Little Work', *The Listener*, 4 (6 August), pp. 203 – 204; Cox, H. (1931) 'Our Financial Position and Prospects', *Contemporary Review*, 140 (July/Dec), p. 11

[213] Keynes, J.M. (1922) 'An Economist's View of Population' (11 August) in *Collected Writings of J.M. Keynes – Vol. XVII: Treaty Revision and Reconstruction*, London: Macmillan, p.444

Employment Exchange."[214] The most obvious solution to this problem was emigration.

Before the nineteenth century, the movement of labour had been influenced by the desire for civil or religious liberty. Since that time, the free and decent movement of labour through migration had gone a long way to promote political and economic stability throughout the Empire. During the War, Chapman had predicted that the development of communications and eventual removal of war-time suspensions would lead many unencumbered men, accustomed to the rigours of military discipline and outdoor life, to accept any opportunity to enjoy the almost limitless space provided by the Empire.[215] The situation was comparable with the impression of seeds which, once scattered widely by the wind, would develop into vigorous plants.[216] Post-war statistics demonstrated that England (composed of 51,000 square miles) possessed a larger population per square mile than any other part of Great Britain, or indeed the rest of the self-governing countries of the Empire (composed of 7,395,000 square miles).[217] Yet although the Empire Settlement Act (1922) had been intended to assist the redistribution of population throughout the territories of the Empire, the total number of British subjects emigrating had declined from 389,394 in 1913 to just 136,834 in 1928.[218] While not all economists supported the overpopulation interpretation of unemployment, natural intellectual curiosity led them to examine the problems that were blocking a natural desire to escape Britain's overcrowded slums.

[214] Robertson, D.H. (1923) 'A Word For The Devil', *Economica,* No. 9 (November)p. 207
[215] Chapman, S.J. (1918) 'The State and Labour' in Dawson, H.D. (ed.) *After-War Problems*, p. 144
[216] Cox, H. (1920) 'Population and Progress', *Edinburgh Review*, 232 (October), p. 396
[217] Cox, H. (1923/24) 'The Peopling of the British Empire', *Foreign Affairs*, 2 (January), p. 119
[218] Shadwell, A. (1929) 'British Emigration', *Times Literary Supplement*, Issue: 1453 (5 December), p. 1015. Solomou notes that over the period 1870 – 1913, migration from Britain (as a percentage of the total labour force) was 1.5 per cent, falling to just 0.4 per cent over the period 1925 – 38, Solomou, S. (1996) *Themes In Macroeconomic History: The UK Economy, 1919 – 1939*, p. 78

One supply-side impediment concerned the inherent gregarious qualities of human beings, qualities that had long influenced the concentration of populations in large areas. It was therefore suggested that any man or woman accustomed to the urban or village way of life would be loath to sever bonds with the immediate community simply to endure the isolation of even the most picturesque corner of the Empire.[219] Other recognised factors that fixed people to their home districts included potential anxiety in adapting to differences of race, religion, and customs within alien communities; the effects of British urbanisation in lessening the adaptability of emigrants; questions of travelling costs and the conditions under which assisted passage could be obtained; the influence of Britain's unemployment insurance scheme in reducing pressures on labour; and the question of whether those accustomed to Britain's temperate climate could acclimatise to tropical conditions.[220] On the demand side, both T.E. Gregory and Alexander Carr-Sanders reflected on the corrupting effect of racial prejudices and territorial jealousies. This was typified by the American Immigration Act (1924), the New Zealand Immigration Act (1931), as well as the flagrant denial of the rights of British emigrants to Canada, who, after five years residence, had been deported on the basis that they had become an excessive charge on the Canadian authorities.[221]

Irrespective of the fact that both the pre-war Dominions Royal Commission Report and post-war research by the United States National Bureau of Economic

[219] Cox, H. (1922) 'Empire Migration', *Edinburgh Review*, 236 (July), p. 200; Cox, H. (1923/24) 'The Peopling of the British Empire', *Foreign Affairs*, p. 123

[220] Macgregor, D.H. (1926) 'Official Papers – The Effect on Migration of Schemes of Social Insurance', *Economic Journal.*, 36 (June), pp. 305 – 307; Layton, T. (1928) 'Europe's Role In Future World Trade', *Proceedings in the Academy of Political Science in the City of New York*, 12 (January), p. 151; Cox, H. (1929) 'Parliamentary Government', *Edinburgh Review*, 250 (July), p. 184; Hawtrey, R.G. (1930) *Economic Aspects of Sovereignty*, London: Longmans, Green & Co, pp. 72 – 73

[221] Gregory, T.E. (1931) 'Economic Nationalism', *International Affairs*, 10 (May), p. 296; Carr-Saunders, A.M. (1933) 'Current Social Statistics – Migration', *Political Quarterly*, 4 (July/Sept),p. 425

Research had suggested an exaggerated attitude towards the ability of migration to resolve the problems of unemployment, Cox expressed a preference for the artificial transportation of labour. It was suggested that any appreciable alteration in the distribution of Britain's population could not lie with the simple movement of British workers, but the wholesale transference of entire industries, including machinery, labour force, administrators and their families. Cox's solution rested upon the importance of stimulating Imperial interest in migration, thereby securing outlets for Britain's surplus population and industrial facilities. Provided that a country such as Australia could overcome labour fixation with the effect of migrant labour on the local wage rate, Britain would undertake the wholesale transfer of her location-specific industries – such as the cotton and woollen industries – thereby expanding Australian's domestic manufacturing base while relieving Britain of her unemployment problem.[222]

From a modern perspective, Cox's proposals appear highly improbable. Yet when assessed against the wider backdrop of the inter-war economic debate, Cox's argument does not represent a deranged plan regarding the movement of labour and machinery, but a proposal for overcoming many of the emotional problems that were restricting migration, and so preventing Britain's process of industrial transformation. British workers from urban districts would look more favourably on the policy of emigration if they were certain of retaining their previous jobs and travelled with family and friends. However unrealistic it may appears to modern eyes, it cannot be denied that, in the context of the period, Cox's desire to secure the collective transfer of labour and industry represented a bold solution to the problem of unemployment.

[222] Cox, H. (1923/24) 'The Peopling of the British Empire', pp. 126 – 134; Cox, H. (1929) 'Parliamentary Government', p. 184

From a contemporary perspective, the effects of a policy of emigration – whether intended to resolve the (supposed) problem of overpopulation or not – actually raised serious questions regarding the Britain's long-term social and economic development. For example, the available statistics highlighted a tendency for young male emigrants to exceed the number of female emigrants. An unrestrained policy of emigration would, it was feared, increase the disparity between the sexes, and so raise the proportion of the domestic population that were supported by the increased efforts of non-emigrants. In other words, the cost of looking after the non-working population would be borne by a diminishing proportion of the population. A second difficulty concerned the fact that people wishing to emigrate did not constitute a random sample of the population. This raised questions about the probable effects of emigration in undermining the future physical and intellectual capacity of the nation. Provided that they were confident of their employment prospects in areas of Canada and Australia, the very act of accepting an opportunity for emigration suggested that an individual's ambitions and initiative exceeded those of his neighbour who preferred to remain in Britain. It was clearly feared that any advantages associated with the policy of emigration were significantly outweighed by long-term disadvantages that appeared to restrict Britain's future economic and human evolution.[223]

It can be seen that the economic implications of emigration were being integrated with a eugenic assessment of the likely future nation. Based on a supposed fear that human civilisation was being subverted by harmful racial and physical standards, eugenics reflected a belief that man possessed ultimate authority over the direction of human evolution. While economists did not appear to consider

[223] Carr-Saunders, A.M. (1932) 'Migration Policies and Population Changes', *Political Quarterly*, 3 (April/June), p. 257

themselves biological experts eugenics certainly attracted their attention, with Jones going so far as to suggest that eugenic questions had yet to be fully recognised as "worthy of serious public attention."[224]

Industrial Location and Business Practice

By the inter-war period, analysis of industrial location still remained a comparatively recent development in economic theory. Indeed John Jewkes, writing in 1933, lamented in the absence of any comprehensive theory of location within English economics. Similar to initial acceptance of the trade cycle as an explanation of post-war unemployment, the general acceptance of the Weberian theory of location – and its emphasis on the supply of either ubiquitous or localised raw materials, proximity to markets, distribution of labour and various external economies – had delayed discussion of new ideas and failed to explain why industries remained in certain locations once changing conditions had diminished their need to remain.[225] In a similar way, G.C. Allen cast doubt as to the accuracy of the Weberian formulation, arguing that location was largely a haphazard process, dictated by chance or by advantages that existed at a particular moment in time.[226] It was true that, so long as steam power served as the dominant form of power, there was a tendency for industries to congregate in the mining regions (the strength of this

[224] Jones, J.H. (1937) 'The Fall in the Birth Rate', *The Accountant*, 96 (3 April), p. 477. For wider discussions of the relationship between eugenics and economics, see Pigou, A.C. (1923) 'The Galton Lecture', *Eugenics Review*, 15 (April), pp. 305 – 312 and Stamp, J. (1934) 'Eugenic Influences in Economics', *Eugenics Review*, 26 (July), pp. 107 – 120

[225] Jewkes, J. (1933) 'Review – 'Theory of Location of Industry' by A. Weber', *Economic Journal*, 43 (September), p. 507

[226] It is possible to detect in Allen's treatment of locational theory elements of Dennison's later criticisms concerning the development of a general theory of location. Dennison, S.R. (1937) 'The Theory of Industrial Location', *Manchester School*, 8, pp. 23 – 47

tendency being determined by the cost importance of steam power to the industry). The development of electricity, however, enabled firms to be released from the geographic slavery of the coal fields and congregate in other areas. Decisions for firms to remain in specific areas suggested that there other factors more important than simply the supply of cheap power.[227] To this end, the Weberian theory appeared unable to provide a satisfactory explanation for Britain's post-war difficulties.

For several economists, including Allen, Ashton and Jones, post-war Britain's lethargic economic reorganisation arose from the economic heritage of once-powerful, specialised areas, such as Lancashire and the cotton industry. It was this culture of industry that was seen to be preventing both business and labour from actively responding to the new economic environment. In sharp contrast, areas that had faced a more varied form of industrial life appeared more alert to new business prospects. The case of Birmingham and the Black Country provided a perfect example, for although suffering the loss of older industries since the end of the War, the bewildering diversity of their economic history had enabled these areas to successfully attract newer firms specialising in rubber, electricity, artificial silks and motor vehicles, and so display the necessary flexibility that post-war industry had to achieve.[228]

A further impediment to the necessary process of adaptability was identified in the attitudes and character of Britain's industrial leadership ("the incompetence of our boards of directors"[229]). First, many "captains of industry", argued Josiah Stamp,

[227] Shadwell, A. (1929) 'The Location of Industries', *Times Literary Supplement*, Issue: 1450 (14 November), p. 908; Jones, J.H. (1935) 'Geographic Trends In Industry', pp. 218 – 219; Jones, J.H. (1938) 'The Location of Industry', *The Accountant*, 98 (12 March), p. 370

[228] Allen, G.C. (1930) 'Labour Transference and the Unemployment Problem', *Economic Journal,* 40 (June), p. 243; Aston, T.S. (1930) 'Review – 'The Industrial Development of Birmingham and the Black Country, 1860 – 1927' by G.C. Allen', *Economic Journal,* 40, pp. 270 – 271; Jones, J.H. (1935) 'Some Aspects of Industrial Change', *The Accountant*, 92 (19 January), p. 75

[229] Cox, H. (1930) 'Some Real Causes of the Slump', *Contemporary Review*, 138 (July/Dec), p. 561

had left school early, sweated their way to a position of power, and were firmly committed to the belief that there were few, if any, commercial benefits to be derived from technical training and education. British industry, he argued, was being governed by a group of peremptory business leaders who embodied the 'look at me – I have managed without it' spirit.[230] Second, whereas feudal domination of the countryside had vanished though the growing ability of tenants to become owner-farmers, business management appeared unable to rid itself of dynastic and semi-feudal attitudes. As many contemporary writers observed, industrial authority was, more often than not, handed to an individual – the heir apparent – who, having received no training in business comparable with that required in the legal or medical professions, found himself unprepared for the role he was required to fulfil.[231]

The overall discussion of hereditary and the personality of business leaders did not represent an unjustified attack on the age composition of British boards. As Jack Stafford observed, it was often impossible for anyone to tell when wisdom and experience decayed into senility.[232] Yet it was clear that human difficulties at the heart of post-war British business were impeding the necessary forces of economic change. It was, of course, possible that without the principle of business heredity, the economy would be forced to contend with the equally troublesome situation of "seasoned" captains of industry clinging tenaciously to office. However, the poor standing of business leadership was not regarded as having been in anyway assisted by the excessive secrecy with which it regularly enveloped its affairs. Businesses of all sizes appeared to oppose the widespread availability of information, fearing that

[230] Stamp, J. (1930) 'The Management of Industry', *The Listener*, 4 (12 November), p. 790

[231] Sargant Florence, P. (1930) 'Review – 'The Next Ten Years' by G.D.H. Cole', *Political Quarterly*, 1, p. 302; Sargant Florence, P. (1930) 'Rationalisation and the Public', p. 706; Clay, H. (1932) 'The New Industrial Organisation', *The Listener*, 7 (30 March), pp. 459 – 460; Jones, J.H. (1938) 'Leadership and Industrial Development', *The Accountant*, 99 (16 July), p. 69

[232] Stafford, J. (1933) 'Review – 'Financial Democracy' by M. Miller and D. Campbell', *Manchester School*, 4, p. 124

disclosure of their financial position would either serve as the prelude to further Government interference, or ignite fresh competition within the industry and so depress the rate of profit. The attitude was, in its turn, reinforced by company legislation, whose purposes, argued Cole, was to reveal the minimum of information needed to prevent basic fraud while preventing shareholders, investors, and even workers from receiving information to which they were properly entitled.[233]

Legal Impediments

Economic theory suggested that depression would act to stimulate the development, transmission, absorption and exploitation of cost-saving inventions in the production process. The stimulus to invention arises from a multitude of sources, and it is apparent that when considering such motivations, the economist and historian is attempting to cover very debatable ground. A brief list of sources, however, could include the natural element of human curiosity; a response to existing, yet imperfect scientific knowledge; the division of labour, in which specialisation leads to increased considerations of technical production; or, possibly more cynically, the expectation of financial gain. The success of such activity necessitated a fair and effective framework of laws. As Gilbert Walker observed: "Legal rule and precept can deflate, promote and discourage economic tendencies."[234] In this vein, it was suggested by Arnold Plant that the flow of post-war scientific or labour-saving inventions had been restricted by the feeble character of British patent legislation. Although having generated a large literature during the

[233] Cole, G.D.H. (1926) 'The Case For Industrial Publicity', *New Statesman*, 27 (10 July), pp. 351 – 352; Cole, G.D.H. (1927) 'Industrial Efficiency', *New Statesman*, 27 (10 July), p. 597

[234] Walker, G. (1939) 'Road Transport – Economics and Law', *Modern Law Review*, 3 (June), p. 21

nineteenth century, particularly from writers such as Jeremy Bentham and John Stuart Mill, the question of patent legislation and the flow of inventions had largely become a forgotten area of economic thought.

The recognised purpose of a patent for inventions was to grant the inventor monopoly control over the disposal of his invention for a set period of time (usually sixteen years with the possibility of a ten-year extension). In a strict economic sense, the patent system enabled the possessors of monopoly rights to raise the price of using their invention, according to the limits determined by the elasticity of demand, in order to secure a larger profit than would other wise be obtained. The guarantee of the legal preservation of ideas, so ensuring financial remuneration, was taken to stimulate inventive activity in those areas that were expected to prove the most remunerative.

One difficulty with British patent legislation, argued Plant, concerned the complex legal difficulties associated with distinguishing a scientific discovery from its patentable application. Many activities did not fall under patent protection, and although many persistent scientists pressed their claims for even short-term patent protection[235], it was feared that the incentive towards innovation was diminished as their inventions were freely adopted by their competitors. A second difficulty involved the system of reward, given that the existing patent laws operating in the favour of one individual or one section of the many participants involved in the invention process. With only one application capable of satisfying the patent legislation, the priority of applications (sometimes even by minutes) ensured that the

[235] We may note the draft convention for the protection of scientific discoveries (the so-called "Ruffini proposals"), submitted by the Intellectual Co-operation Commission of the League of Nations to the Assembly of the League in the summer of 1923.

activities of other applicants were rendered redundant.[236] Thus, uncertainty surrounding the legal status of inventions and priority of a patent monopoly was seen to neutralise the supposed stimulus of patent legislation to the spirit of invention.

Bureaucracy

As with during the early post-war period, part of the debate surrounding impediments to economic development included questions of bureaucracy. In some quarters, it must be said that the civil service received support: Clay saw central administration as the "principle safeguard of English liberty"[237], while Keynes feared that reductions in expenditure, although popular amongst taxpayers, would achieve little beyond crippling the activities of a necessary and efficient civil service.[238] In other quarters, the civil service was dismissed as an unnecessary, or at least inefficient, component within post-war British life. An immovable bureaucratic force appeared to have provided endless excuses and exaggerations to justify its existence and expand their functions. An inability to secure departmental economies was intensified by rules that entailed constant reference to departmental heads whose salaries, in turn, were calculated on the basis of their overall departmental size.[239] As Hirst pointed out in 1927, bureaucracy was "too strongly entrenched to be easily retrenched."[240] The Ministry of Labour, for example, had entrusted the Labour Exchanges with the administration of the unemployment insurance acts. Although, as

[236] Plant, A. (1934) 'The Economic Theory Concerning Patents for Inventions', *Economica*, 1 (February), pp. 32 – 42
[237] Clay, H. (1932) 'Do Politics Hamper Public Enterprise?', *The Listener* (17 February), p. 242
[238] Keynes, J.M. (1927) 'A Note on Economy – II', *Nation & Athenaeum*, 41 (21 May), p. 207
[239] Hirst, F.W. (1924) 'Letter – Official Expenditure', *The Times* (16 February), p. 8, c. A
[240] Hirst, F.W. (1927) 'Letter – Economies Long Promised', *The Times* (4 February), p. 15, c. F

suggested in chapter 2, the Labour Exchange system was distrusted by both employers and the unemployed, it was believed that growing pressures within the civil service bureaucracy had secured their continued existence. Where as it could be argued that the decision sprang from a desire to prevent benefit fraud, Cole had earlier doubted whether the savings achieved were sufficient to balance the dramatic increase in costs arising from centrally controlled administrative procedures.[241] Aside from the machinery of administration – particularly a complicated system of stamps and cards for twelve million registered accounts – it was feared that the basis of the multiplication of tasks in order to justify the multiplication of civil servants had introduced unnecessary friction. One example of this was the requirements imposed by the "genuinely seeking work" clause (abandoned in 1930) and the stigma of the Means Test. Instead of providing appropriate assistance, the ever tightening yoke of bureaucracy either forced able-bodied benefit claimants to recite the name of firms that they had visited over the course of the week, or were subjected to unnecessary questioning regarding the family income. Further more, evidence supplied by unemployed workers suggested that once they had become ineligible for benefit, exchange officials, although having first hand contact with claimants, concentrated on dovetailing applications and vacancies for those unemployed workers who remained a charge on the benefit scheme.[242] Compared with the apparent minimal effect of the Exchanges in providing employment, and their general time wasting over mere futilities, there was obvious concerns as to the extent to which national

[241] Cole, G.D.H. (1922) 'Can We Dispense With The Ministry of Labour', *New Statesman*, 18 (18 February), p. 550

[242] Jones, J.H. (1932) 'Trade Customs and Restrictions', *The Accountant*, 87 (10 September), p. 329

sentiment would tolerate such slovenly bureaucratic activities and intrusion into individual freedom.[243]

Transport

During discussions surrounding the Motor Traffic Regulation Bill (1909), the then Prime Minister had described motor vehicles as "a rich man's toy"[244]; by the 1930s, motor vehicles had become a general necessity. In 1914, the total number of registered motor vehicles totalled 389,000, of which 132,000 were private cars. By 1929, the total number of registered cars had risen to nearly 2.2m, of which 981,000 were private cars.[245] In some quarters, suggestions that motor vehicles were essential to foster a new industrial system were simply dismissed. It appeared wrong to assume that a new phase of development had to be associated with a new means of communications. Was the speed and ability of the modern motor vehicle, it was argued, really sufficient to undermine the power of the railways? Based on the view that the only conceivable function of motor vehicles was to increase the convenience, and not the speed, of transporting goods or people, Clay saw no useful purpose in the development of motor vehicles and road haulage.[246] In a similar fashion, Cox attacked the unnecessary disfigurement of the English countryside brought about by road widening and construction schemes.[247]

[243] Cole, G.D.H. (1924) 'The Possibilities of Administrative Reaction', *New Statesman*, 24 (25 October), p. 70; Hirst, F.W. (1927) 'Letter – Ministers and the Economy', *The Times* (24 March), p. 14, c. F; Hilton, J. (1937) 'The Public Services in Relation to Unemployment', *Journal of Public Administration*, 15 (July), p. 5

[244] Clay, H. (1931) 'Some Aspects of the World Depression – I', *Journal of the Institute of Bankers*, p. 517

[245] Pollard, S. (1969) *The Development of the British Economy, 1914 – 1967*, p. 150

[246] Clay, H. (1928) 'The Liberal Industrial Report', *Economic Journal*, 38 (June), p. 201

[247] Cox, H. (1931) 'The Economy Report', *Contemporary Review*, 140 (July/Dec), p. 289

For other contemporary commentators, motor transport held an important position within the future development of the national economy. One of the most obvious relationships, as Christopher Brunner pointed out, was between the developing motor vehicle industry and the oil industry. Many of the modern forms of transport – motor vehicles, motor boats, etc – were all dependent on petroleum products for their fuel, while the materials for building the roads, such as bitumen, were obtained from the fractional distillation of crude oil. There were also clear social advantages, especially with the use of private cars, motor-buses, and motor-cycles in bringing town-dwellers to country villages, so stimulating a cosmopolitan outlook that had been checked by the War.

The economic and social benefits of the internal combustion engine had to be set against the problems of increased road congestion (with more merchandise and passenger traffic diverted from the railways on to the roads); the loss of human lives through an increased passion for speed (a point emphasised by the 1929 Royal Commission on Transport); a weakening of the social and moral responsibility of society through diminishing church attendance; and a growing national reluctance to take exercise.[248] This later point had been appreciated before the War, for as C.F. Bickerdike had noted, there was a curious separation between the number of spectators who expressed their admiration at the physical prowess of footballers but who never bothered to take exercise themselves. The development of transport perpetuated the fear that the "mechanical substitution for muscular labour" (such as

[248] Brunner, C.T. (1929) *Road Versus Rail: The Case for Motor Transport*, London: Ernest Benn Ltd, p. 122; Brunner, C.T. (1930) 'The Economics of Oil', *Manchester School*, 1, pp. 35 – 41; Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, p. 68

the use of a tramcar instead of walking even short distances) would, in the long term, lead to the creation of a lazy and unhealthy nation.[249]

For other economists, it was clear that any action that restricted the development of road transport also impeded Britain's process of economic transformation. It was therefore seen as highly unfortunate that representations from the coal industry had persuaded the government to impose a tax of 1*d.* a gallon on heavy oil, thereby increasing the transport cost of lorries or barges fuelled by Diesel, as well as affecting those efficient agriculturists who used kerosene for their tractors.[250] A further example of this was the Road and Rail Traffic Act (1933). Section I of the Act stipulated that the carriage of goods by road was to be co-ordinated via a licensing scheme. There were three license categories: A ("public carriers") valid for 5 years; B ("limit carriers") valid for 2 years; and C ("private carriers who do not carry for hire") valid for 3 years. The Licensing Authorities were permitted to grant or refuse applications for A or B licenses (category C applications were granted freely), and, in seeking to uphold the interests of the general public, stated that licences would not be granted unless the haulier and his customers could provide oral evidence demonstrating the benefits and convenience of road transport over existing transport facilities (usually the railways). Further more, since all licences were time limited, each applicant seeking renewal had to demonstrate a continuing need for his service, and that during the period of the previous licence, his vehicles had been fully employed. Disappointed applicants or objectors were permitted to appeal before the Licensing Authority Appeal Tribunal. Gilbert Walker argued that Britain's overriding interest in the creation of an efficient motor vehicle

[249] Bickerdike, C.F. (1903) 'Review – 'Studies In The Evolution of Industrial Society' by R.T. Ely', *Economic Journal*, 13 (December), pp. 600 – 601
[250] Brunner, C. T. (1933) 'Economic Trends and Government Interference', p. 96

transport system had been jeopardised by an official desire to prevent "wasteful competition".

For road hauliers, rates for the different classes of goods were determined by free competition, with the consignor only paying the actual costs of haulage, while the costs associated with maintaining the road network were transferred to taxpayers. This contrasted with the inflexible rate-structure followed by the railways, whose costs covered both the transportation of passengers and general merchandise, and the maintenance of a large rolling stock and thousands of miles of sidings.[251] It had been estimated that, even by early 1920s, road hauliers had successfully undercut rail rates by between 20 to 30 per-cent, and so secured a large proportion of post-war merchandise traffic.[252] With technical advances in the commercial motor industry passed on to the trader in the form of lower rates for road transport, it made economic sense to allow a trader to transfer his goods from rail to road. However, Walker noted that both the Authority and Tribunal displayed a disdain for economic principles, refused to consider evidence relating to the reduced rates for road transportation, and suffered from a lack of guidance regarding the interpretation of the term "wasteful competition". The overall effect, therefore, had been to "block the door to any expansion of the road transport business above the level of the base period, 1932/3."[253]

[251] Walker, G. (1933) 'The Economics of Road and Rail Competition', *Economic Journal*, 43 (June), p. 222

[252] Acworth, W.M. (1922) 'Letter – Road Transport', *The Times* (10 February), p. 6, c. A

[253] Walker, G. (1939) 'Road Transport – Economics and Law', *Modern Law Review*, 3 (June), p. 26

Psychological and Emotional Impediments

As noted in the previous chapter, economics assumes that the market will translate individual rationality into social rationality. This important assumption, however, ignores the influence of psychological and emotional impediments. By introducing emotional reactions into their explanations of Britain's apparent inability to move to a new economic equilibrium, inter-war economists were taking their interpretation of human behaviour beyond the confines of strict economic theory, and so attempting to draw upon real human motivation.

In order to distinguish emotions from more visceral factors, such as pain or hunger, it is probably convenient to define them as involuntary responses to perceptions of external (real world) events. Economists and economic historians would not explicitly deny the potential effect of emotions such as affection and empathy. As T.S. Ashton observed, if economic historians disregard the influence of emotions or sentiment on the attitudes of eighteenth and nineteenth century industrialists, how are we to explain the construction of the Nonconformist chapels or the anti-slavery campaign?[254] Nor could economists deny that powerful emotions could colour a persons attitudes and interfere with rational understanding and the decision making process. Despite this, there had been comparatively little attempt to incorporate emotions into the general body of modern economic theory.[255]

[254] Ashton, T.S. (1924) 'Review – 'Capital and Steam Power, 1750 – 1800' by J. Lord', *Economic Journal*, 34 (December), p.619

[255] For a modern critique, see Elster, J. (1998) 'Emotions and Economic Theory', *Journal of Economic Literature*, 36, pp. 47 – 74, and Leowenstein, G. (2000) 'Emotions in Economic Theory and Economic Behaviour', *American Economic Review*, 90, pp. 426 – 432

The idea that emotional factors could influence economic relations can be traced throughout the war-time and early post-war literature. As mentioned in chapter 2, the ability with which economists dismissed the practical aspects of the policy of *Mitteleuropa* (Central Europe) did not imply that they were ignorant of the potential damage that British fears and hatreds, once stimulated by the vitriolic rhetoric of the Press and Anti-Germany Leagues, could have in undermining the international economy.[256] We may presume that hostility towards the problem of *Mitteleuropa* was abated during the "coupon" election of 1918, with Coalition candidates making clear their intentions to extract from Germany huge war indemnities. To give another example, Cannan had suggested that the powerful force of war-time passionate patriotism had assisted the war-time transition from a civil to a military economy, and that this had been undermined by a confused housing policy during the early 1920s.

In the following section, we shall examine three examples, presented by inter-war economists, concerning the disruptive effect of emotional and psychological reactions in impeding Britain's economic development.

(1) Unenlightened Fears

Britain's response to the post-war situation, argued Clay, was in no way different from that of primitive society. It was well recognised that primitive man had attributed unpleasant, extraordinary or inexplicable events (such as bad harvests or solar eclipses) to the malevolent power of supernatural forces. Clay believed that this sense of fear and amazement still existed within twentieth century British

[256] Hobson, J.A. (1916) 'Rival Economic Systems in Europe', pp. 194 – 198; Hobson, J.A. (1916) *Labour and the Costs of War*, p. 8

society. The extent of post-war distress and confusion had therefore led different sections of society to endow human agencies, be it "socialism" and "capitalism" (or, more personally, "the capitalist"), with diabolical powers. It was a situation of unenlightened fear: people simply reacted against what they did not understand. It was this fear that Clay believed was serving to undermine the established principles of the market, so preventing the economy from responding quickly enough to changing conditions. The widespread belief that malevolent forces were governing Britain's destiny, suggested Clay, was preventing society from appreciating, and hence facilitating, Britain's inevitable economic change.[257]

(2) Diminishing Industrial Prestige

A slightly different perspective was presented by, amongst others, J.H. Jones and G.D.H Cole. Where as Clay believed that economic transformation was restricted by an ignorance of the post-war economic environment, Cole and Jones believed that that Britain was reacting to a recognition of the reality of the economic situation.

Throughout the eighteenth and nineteenth century, Britain had established her industrial, commercial, and financial prestige by exporting a few, comparatively simple commodities produced by the great staple industries. By the mid-1920s, it was becoming a matter of serious doubt whether she could retain this impressive position.[258] Britain's apparent inability to respond to the new conditions was therefore seen to reflect a combined sense of anger, disillusionment, and despair at the thought of Britain having to relinquish her long held position as the world's most

[257] Clay, H. (1931) 'Irresponsibility In Economic Life, *Political Quarterly*, 2 (Jan/March), pp. 77 – 79
[258] Cox, H. (1926) 'England's Treasure By Trade', *Edinburgh Review*, 243 (April), p. 401

powerful economic nation. Brunner succinctly summarised the position when he observed that there was a "natural psychological tendency" for many classes within society to reflect on the "spacious days of mid-Victorian prosperity."[259]

This, however, was only one side of the problem. While it was clear that the economy had enjoyed some post-war success in motor manufacturing, electrical engineering, and the production of artificial silks, there appeared to be a lingering hostility at the prospect of miscellaneous domestic trades replacing industrial manufacturing. Although post-war society had increased the proportion of national income devoted to the consumption of goods and services beyond the subsistence needs of food and clothing, the development of many of the distributive and service industries – such as the sale of motor-cycles, gramophones, cigarettes or newspapers, and even extending to decorating chocolates or enamelling golf balls[260] – appeared to signified the loss of those standards that had represented Britain's industrial power. Any economic success associated with the expansion of domestic production, appeared insufficient to counteract the loss of Britain's pre-war position amongst manufacturing nations. What was lost on the swings, could not be made up on the roundabouts.[261]

Britain was caught between two forces: on the one hand, psychological depression appeared to be inhibiting Britain's transformation; on the other, any events that suggested that labour and capital could be profitably employed within the staple industries dispelled a sense of despondency, discouraged diversification, and generally disrupting the necessary momentum towards readjustment. The temporary

[259] Brunner, C.T. (1933) 'Economic Trends and Government Interference', p. 92

[260] Hilton, J. (1934) 'Industrial Britain – V: Hands and Machines', *The Listener*, 11 (21 February), p. 323

[261] Jones, J.H. (1927) 'The Future of Industry', p. 836; Cole, G.D.H. (1926) 'Fordism', *New Statesman*, 27 (9 October), p. 730; Cole, G.D.H. (1928) 'Need We Export More?', *New Statesman*, 30 (25 February), p. 616; Jones, J.H. (1930) 'Changes in World Demand', p. 733; Jones, J.H. (1937) 'Expanding Industries', p. 115

closure of the Ruhr pits during the French and Belgian occupation, and the granting of coal subsidies in 1925 and 1926, had insulated Britain from post-war economic reality and so delayed the inevitable process of adjustment. Similarly, a bumper crop in the United States had led to a catastrophic fall in the price of raw cotton. With such a fall in prices expected to stimulate consumption, it was logical that Lancashire would expect a recovery in the demand for cotton goods. The dangerous feature was that unless Lancashire appreciated the temporary nature of the revival of cotton, it would interpret it as a return to normal conditions. It was only through such high profiled failures as the Cotton Yarn Association, and the realisation that excess productive capacity could not be longer justified in relation to likely future conditions, that fully exposed the necessity for Britain to change.[262]

(3) Perceptions of Unemployment

A third psychological impediment that may be glimpsed in the literature, lurking in disparate sources, concentrated on the publics' reaction to an inaccurate comparison between pre-war and post-war unemployment. The most obvious example of this involved the mighty outpouring of facts and figures provided by Government departments. In many instances, statistics that were the by-product of government activities were of extreme importance: the Health Insurance Acts had brought to light social conditions and incipient illnesses that could be easily treated, while the land tax survey had enabled better valuation of death duties.[263] Yet it was

[262] Keynes, J.M. (1926) 'The Position of the Lancashire Cotton Trade', *Nation & Athenaeum*, 40 (13 November), pp. 209 – 210; Jones, J.H. (1927) 'The Future of Industry', p. 836; Cole, G.D.H. (1928) 'Over-Capitalisation', p. 281; Robertson, D.H. (1928) 'Review – 'International Trade' by F. W. Taussig', p. 279; Jewkes, J. (1928) 'Review – 'Lancashire Under The Hammer' by B. Bowker', *Economic Journal*, 38 (December), pp. 613 – 614; Clay, H. (1932) 'What is Rationalisation?', *The Listener*, 7 (27 January), p. 148

[263] Jones, J.H. (1925) 'Employment Subsidies', *The Accountant*, 73 (4 July), p. 2

feared that through an exaggerated degree of confidence in the published unemployment statistics, post-war society had fallen into a vicious circle where by the presentation and perception of post-war unemployment reacted upon the actual level of unemployment. In order to gain a better understanding of this, we must first consider attitudes towards the operation of the unemployment insurance scheme.

At the beginning of the nineteenth century, the State had attached few, if any, restrictions on employment and private enterprise; by the beginning of the twentieth century, public opinion had forced the introduction of legislation relating to the safety, hygiene and remuneration of labour. Fuelled by the proposals of the Poor Law Commission (1905 – 1909), this general extension of State activities demonstrated that, by the outbreak of the Great War, Britain had discarded the cloak of nineteenth century morality. The development of the national unemployment insurance scheme therefore served as a remarkable experiment in economic and social organisation.[264] Provided at reasonable cost, administered through the Unemployment Exchanges, and with apparent safeguards against abuse, the intention of the scheme was to ease the needless suffering of people who, through no fault of their own, were relegated to the ranks of the unemployed.

When first introduced in 1911, the insurance scheme had applied to a select group of occupations. Proposals for the gradual extension of the scheme had been eroded by the War, and by August 1920 it had been applied to the majority of all trades (with the exception of agricultural workers and domestics)[265]. The events that followed this situation appeared to present an unsavoury sequence of events. Covering the period 1922 to 1929, the level of recorded unemployment had averaged

[264] Macgregor, D.H. (1922) 'British Aspects of Unemployment', pp. 726 – 729

[265] Beveridge had earlier claimed that with the proper preparations for post-war reconstruction having been "lost in the sands of reconstruction", the Government had fallen back on the exchanges and unemployment benefit as the only practical means of tackling unemployment. Beveridge, W. (1919) 'Letter – Labour Exchanges', p. 8 c. C

11.5 per cent, compared with pre-war trade union estimates of just 4.5 per cent.[266] There was one obvious question: had the provision of financial relief – the "dole" – diminished the incentive to work, and so increased the evil it was intended to remedy?[267]

For the vast majority of inter-war commentators, any suggestion that there existed a large body of idle, thriftless individuals, prepared to abuse the insurance scheme rather than seek gainful employment, was dismissed as palpable nonsense. The suggestion that money benefits acted as an opiate to relax individual effort were dismissed by Barbara Wootton as an insult to both the unemployed and the administrators of the insurance scheme[268], while Cannan argued that it was nothing short of insanity to suppose that there existed a widespread inclination to accept benefit over standard rates.[269]

There were several reasons for this criticism. The first, and the most obvious, reflected the prevailing interpretation of post-war unemployment, which identified the problem as a consequence of Britain's slow adaptation to post-war conditions. The second criticism centred on the relationship between unemployment benefit and weekly earnings. Was it reasonable to believe, asked Cole, that 15*s.* for men and 12*s.* for women was sufficient to maintain a reasonable standard of existence?[270] This was taken as further evidence that a worker would never express a preference for leisure over employment. The possibility that man could, though habit, become accustomed to benefit, was also dismissed on the grounds that natural pride would always dictate

[266] Beveridge, W. (1931) 'Diagnosing the Disease of Unemployment', *The Listener*, 5 (20 May), p. 836

[267] The suggestion that inter-war unemployment was a consequence of unemployment benefit and the liberal conditions of eligibility is now synonymous with Benjamin and Kochin's 1979 article 'Searching for an explanation of unemployment in inter-war Britain', *Journal of Political Economy* 87, pp. 441 – 478

[268] Wootton, B. (1924) 'Financial Factors' in *Unemployment In Its National and International Aspects*, p. 66

[269] Cannan, E. (1930) 'The Post-War Unemployment Problem', *Economic Journal*, 40 (March), p. 46

[270] Cole, G.D.H. (1924) 'The Future of Social Insurance', p. 8

a preference for employment over charity. In this sense, the suggestion that State assistance had contributed to a situation of deliberate unemployment was dismissed according to a philosophical impression of the natural, unblemished character of labour.[271]

This is not to suggest that all economic commentators accepted this interpretation. For example, an inherent belief in the unblemished character of the labour force did not find favour with Harold Cox. Although applauding the principle of alleviating human suffering through social policies, Cox believed that the introduction of the Labour Exchange system, and the universality of an unprotected public finance system, had distorted the hard-working and fair-minded characteristics of the labour force. Post-war unemployment had been exacerbated by the impersonal abstraction of State assistance. Men who had once been proud of their independence had gradually succumbed to the temptation of the dole.[272] It was also suggested by Henderson that the incentive of the "dole" had altered the economic significance of temporary stoppages, so leading dishonest workers to deliberately engineer the temporary breakdown of machinery, or the non-delivery of materials, in order to receive benefit.[273]

While maintaining that labour expressed a long-term preference for wages over benefit, the majority of economists were forced to accept that there could be short-term factors that had lead labour to accept benefit. In doing this, they turned to consider the influence of unemployment benefit on the demand for labour. In contrast to seasonal fluctuations in the coal and building industries that lay beyond

[271] Jones, J.H. (1925) 'Remedies for Unemployment', *The Accountant*, 73 (18 July), p. 85; Beveridge, W. (1931) 'Social Malingering', *The Listener*, 5 (17 June), p. 1014

[272] Cox, H. (1921) 'The Public Purse', *Edinburgh Review*, 234 (July), pp. 192 – 194; Cox, H. (1927) 'Franchise Reform', *Edinburgh Review*, 246 (July), p. 197; Cox, H. (1931) 'Our Financial Position and Prospects', p. 9

[273] Henderson, H.D. (1930) 'The Present Unemployment' (10 July) in Clay, H. (ed.) *The Inter-War Years and Other Papers*, p. 57

human control, many influences on employment were deemed to be under the direct rule of employers. Given the complexity of the procedures associated with employment – hiring and appointing labour to particular roles, providing them with a wage, and selling their product at an economically acceptable price – it was suggested that the introduction of the benefit scheme had increased the sensitivity of employers' demands for labour with respect to prevailing (or expected) economic conditions. By diluting the incentive of employers to retain their workforce during bad conditions, it appeared that the dole had succeeded in increasing unemployment.[274]

Before the War, employers were seen to have retained their workforce during slack periods in order that they could speedily increase production once prosperity returned. The implicit assumption was that there were costs associated with dismissing workers, for unless the firm was able to quickly re-establish their workforce once conditions improved, there would necessarily arise the expense and inconvenience of locating and training new workers. Initially intended to instil a sense of national responsibility for unemployment, it was believed that employers had quickly appreciated the convenience that a public unemployment benefit fund provided. Put simply, it allowed employers to indiscriminately discard workers when economic conditions deteriorated, re-hire them once conditions improved, while providing the reasonable certainty that, between the two periods, the dismissed workers would not be forced to search for a new job. To quote Cannan:

[274] Cole, G.D.H. (1920) 'The Unemployment Bill', *New Statesman*, 15 (17 July), p. 411; Clay, H. (1921) 'Letter – Unemployment: The Registration of Labour', *The Times* (10 February), p. 6, c. A. It is perhaps worth pointing out that this argument, although present in the post-war debate, can also be found in the pre-war literature. See, for example, Ashley, W. (1910) 'Unemployment and Trade Unions', *Economic Journal*, 20 (December), pp. 573 – 574

> "To throw numbers of your employees out for short intervals to suit your convenience is obviously less likely to create friction, and is therefore more likely to be profitable, when the person thrown out can draw on a common fund raised by stamp duties on employment and other taxes."[275]

There were obvious variations on this theme. In responding to the reduction in export trade, for example, the insurance scheme had encouraged Lancashire spinners of American and miscellaneous cottons to organise "short-time" amongst its workforce. Although raising the cost of production within the cotton industry, the system of organised short-time ensured a systematic distribution of work across a system of alternative shifts, so leading labour to alternate between work and claiming benefit.[276]

The ability of both firms and employees to draw upon a common insurance scheme – equivalent to securing a subsidy from public funds – was interpreted as creating a ceaseless, short-term movement of men in and out of employment. This has two implications. First, as Beveridge made clear, such situations constituted neither genuine unemployment nor deliberate malingering, but rather soul-destroying, enforced idleness.[277] The second implication was that by claiming unemployment benefit, such activities increased yet further the recorded level of unemployment (which was already high due to the industrial depression), so generating an exaggerated perspective on the problem of post-war unemployment.

This presented economists with an interesting situation, and forced them to consider the possibility that Britain's inability to adapt to post-war conditions was a reflection of the public's own awareness of, and exaggerated reaction to, the ongoing

[275] Cannan, E. (1930) 'The Post-War Unemployment Problem', *Economic Journal*, 40 (March), p. 46

[276] Keynes, J.M. (1926) 'The Position of the Lancashire Cotton Trade', pp. 209 – 210; Clay, H. (1928) 'Unemployment and Wage Rates', *Economic Journal*, 38 (March), p. 12

[277] Beveridge, W. (1931) 'Social Malingering', pp. 1014 – 1015; Beveridge, W. (1932) 'How Unemployment Insurance Works', *The Listener*, 8 (21 December), p. 877

presentation of unemployment. This situation appeared to have been intensified by an irresistible national urge to compare pre-war and post-war unemployment statistics.

Estimates of pre-war unemployment, having been constructed from trade union returns (some figures dating as far back as 1854), ignored unemployment amongst unskilled workers. It was nonetheless accepted that, even in good times, the actual level of pre-war unemployment was higher than that recorded by the unions.[278] Post-war unemployment statistics also failed to constitute an official census in that they were influenced by the administrative requirements of the insurance scheme, and only included those who, for a variety of incentives, had "lodged" their insurance cards at the Exchange in order to draw benefit. The tendency to ignore some proportion of the unemployed from the statistics remained, as with the "black coat" (non-manual or professional) workers who refused to endure the ignominy of registering for benefit, and the unemployed labourers who constantly moved from one trap ward to another.[279] Yet while economists were prepared to question the *Labour Gazette*'s statistic of *x* million unemployed, belief in the work of highly-trained officials, and faith in the British spirit of democracy, appeared to have led the general public to slavishly accept government unemployment figures as a definitive economic pronouncement.[280]

With post-war unemployment statistics increased by both Britain's inability to move the economy to its new equilibrium and the problem of "enforced idleness", it appeared that the nation was trapped in a vicious circle. With unquestioning faith

[278] Macgregor, D.H. (1907) 'Labour Exchanges and Unemployment', *Economic Journal*, 17 (December), p. 586. The Ministry of Labour discontinued publishing the trade union index in 1926, although numerous economists continued to employ them for the purpose of illustration. See, for example, Beveridge, W. (1931) 'Diagnosing the Disease of Unemployment', p. 836

[279] Hilton, J. (1934) 'Are the Unemployment Figures Accurate?', *The Listener*, 12 (14 November), p. 823

[280] Cole, G.D.H. (1924) 'The Need For Publicity', *New Statesman*, 24 (6 December), p. 259; Jones, J.H. (1937) 'Government Statistics', *The Accountant*, 97 (30 October), p. 581

in the veracity of government statistics (presumably transmitted through the press), and comparisons with equally erroneous pre-war statistics seen to exaggerate Britain's post-war position, the resulting negative psychological feedback effects contributed to a perception of diminishing economic power, and hence a widespread and prolonged climate of fear and insecurity.[281]

Government Use of the Unemployment Insurance Scheme

Before proceeding to the inter-war economic debate surrounding rationalisation, we shall briefly consider G.D.H. Cole's argument that the "dole" had provided successive (Conservative) governments with the financial incentive to delay the implementation of centrally controlled policies aimed at adjusting industry to changing economic conditions. In this scenario, it was the Government, and not the unemployed, who were seen to have expressed a preference for the "dole". Irrespective of the cost to the community of leaving the unemployed to rot in idleness on the dole or poor relief, successive governments were taken to have fallen back on the "dole" simply because it was the cheapest and easiest course of action.

The cost of providing unemployment insurance established "clear" financial facts: maintenance was set below the wage rates that would prevail if work were available; there were no overhead costs beyond those of the Employment Exchanges; and the cost of the scheme was secured through local rates rather than national taxation that would have been the responsibility of the Exchequer.[282] By providing a

[281] Jones, J.H. (1927) 'Unemployment', *The Accountant*, 77 (6 August), p. 191; Beveridge, W. (1931) 'Is Dear Labour A Cause of Unemployment?', *The Listener*, 5 (3 June), p. 932; Dalton, H. (1934) 'Our Present Discontents', *The Listener*, 12 (24 October), p. 694; Beveridge, W. (1936) 'An Analysis of Unemployment – I', *Economica*, 3 (November), pp. 358 – 360

[282] This situation had changed significantly by the early 1930s, when the huge indebtedness of the unemployment fund forced it to rely on loans from the national exchequer.

cheaper alternative to state economic control, Cole believed that the "dole" was leading to a significant deterioration in the mental and physical capacity of the labour force, and preventing Britain's advancement towards any kind of permanent recovery.[283]

Influenced by the Villages of Co-operation, the schemes of the Social-Democratic Federation, and the moving bodies of labour that had built Britain's railway network during the nineteenth century, Cole's policy initiative centred on the enrolment of unemployed workers into a National Labour Corps, with the ultimate aim of overhauling the economy through slum clearance schemes, land reclamation, and a national scheme of electrification.[284] It should be pointed out that other economists were sceptical of Cole's proposals for what amounted to a State directed Industrial Revolution. Sargant Florence, for example, argued that the "romantic halo" surrounding Cole's proposals had obviously blinded him to their practical limitations. Not only would the scheme require extensive consultation ("The Labour Corps can't be let loose on the fiat of an administrative order"), but it was seen as highly doubtful that such a body could overcome the psychological backlash arising from the enforced separation of families simply so that the unemployed father or son could clear slums or slag heaps.[285]

[283] Cole, G.D.H. (1923) *Out of Work: An Introduction to the Study of Unemployment*, p. 7; Cole, G.D.H. (1928) 'Mr Churchill and the Rate Payer', *New Statesman*, 30 (18 February), p. 586; Cole, G.D.H. (1928) 'The Mobility of Labour', p. 319; Cole, G.D.H. (1928) 'Finding Work', *New Statesman*, 32 (29 December), p. 319

[284] Cole, G. D. H. (1929) *The Next Ten Years in British Social and Economic Policy*, London: Macmillan & Co. Ltd, p. 55.

[285] Sargant Florence, P. (1930) 'Review – 'The Next Ten Years' by G.D.H. Cole', p. 300

Rationalisation

Thus far, we have seen how inter-war economists presented a damning dossier of the failings of the British economy. Industry appeared physically and psychologically weighed down by the industrial structure of the nineteenth century. It was becoming increasingly apparent that realisation of what was wrong did not, of itself, provide the cure. Where was the solution to be found? Contemporary views regarding the influence of government social expenditure in curing Britain's emotional and psychological reactions will be examine in chapter 4. At the moment, we shall concentrate on proposals that aimed at promoting recovery and increasing national welfare through the deliberate "reconditioning" of Britain's entire economic organisational technique.[286]

The themes of this proposal, christened "rationalisation", were succinctly defined by Cole:

> "In the odes which are chanted in praise of rationalisation…the goddess is always represented as cheapening the costs of production of all commodities which she touches with her wand of scientific organisation."[287]

More formally, the idea represented a system of economic organisation intended to secure the greatest possible mechanisation and standardisation of the production process – including materials, machines, transport, factory buildings, and the workforce – thereby reducing excess capacity, lowering costs for the producer through the displacement of labour by machinery, and securing profits from a smaller

[286] Macgregor, D.H. (1929) 'Official Papers – Final Report of the Committee on Industry and Trade', *Economic Journal*, 39 (June), p. 295
[287] Cole, G.D.H. (1929) 'Rationalisation', *New Statesman*, 34 (9 November), p. 152

margin on the sale of an increased quantity of goods. Sargant_Florence drew attention to the contrasting position of the British and American motor industries: in Britain, unnecessary duplication was the consequence of around sixty factories seeking to produce a variety of models; in America, specific factories specialised in the production of one or two models. Through the reorganisation of the manufacturing and administrative aspects of companies, rationalisation had enabled American consumers to enjoy variety without unnecessary duplication.[288]

As a movement, rationalisation appeared to have its origins in Germany's war-time military transformation, and a later response (*Rationalisierung*) to the crippling conditions of the Versailles Treaty. The loss of Alsace and Lorraine had forced the German iron and steel industry to establish Vereinigte Stahlwerke AG and concentrate production in a small number of extended plants. Through the formation of a giant combine, IG Farben, the German chemical industry had overcome the loss of her pre-war dye-stuffs monopoly, and engaged in large-scale scientific experiments (most noticeably the hydrogenation of oil from coal).[289] This basic presentation of the rationalisation movement was questioned by Shadwell, who drew attention to the conflicting attitudes of British and Continental producers. Amongst British producers, Germany was identified as the heart of the rationalisation movement. One possible explanation for this sprang from the war-time and early post-war belief that no matter how badly Germany was defeated, the superiority of her economic organisation, coupled with the spur of necessity, would ensure her

[288] Sargant Florence, P. (1930) 'Review – 'The Next Ten Years' by G.D.H. Cole', p. 299; Sargant Florence, P. (1930) 'Rationalisation and the Public', p. 706

[289] Feldenkirchen, W. (1987) 'Big Business in Interwar Germany: Organizational Innovation at Vereinigte Stahlwerke, IG Farben, and Siemens', *Business History Review*, 61, pp. 417 – 451

united and disciplined response.[290] Yet in Germany, *Rationalisierung* was not identified as an endogenous response to the War, but the systematic application of the principles of scientific management as outlined before the War by the American writer, F. W. Taylor.[291] Even though there appeared little to support claims regarding the long-term sustainability of Germany's kaleidoscopic industrial evolution, what had occurred, and the location in which it had occurred, appeared enough to convince British trade unionists and producers of the need to make "pilgrimages to the shrines of Krupp and of Thyssen."[292]

The ability to strip "rationalisation" of any contemporary meaning, and so reveal its theoretical core, only demonstrated that the idea was nothing more than re-packaging of long-established economic principles for a post-war audience. Was it not a fact that profit-conscious producers were always striving to secure improvements in industrial efficiency?[293] What was so novel about the idea of systematic industrial exploitation associated with rationalisation? Following a reasoned examination of the policy, this theme was developed by several commentators: Sargant Florence doubted whether the policy differed "from the 'trustification' which exercised Socialist and university circles in pre-war days"[294]; Gregory believed that it echoed old debates between Ricardo, McCulloch, Babbage and Senior[295]; while Hobson simply dismissed the project as pedestrian.[296] In many

[290] See, for example, Stamp, J.C. (1922) *Wealth and Taxable Capacity*, London: P.S. King & Son Ltd, pp. 132 – 133

[291] Shadwell, A. (1929) 'Social Economics – II: Practical', *Times Literary Supplement*, Issue: 1420 (18 April), p. vi

[292] Robbins, L. (1927) 'Review – 'Das Schicksal des Deutschen Kapitalismus' by M.J. Bonn', *Economic Journal*, 37 (December), p. 613

[293] Robertson, D.H. (1931) 'The Backwash of Progress', p. 870

[294] Sargant Florence, P. (1930) 'Review – 'The Next Ten Years' by G.D.H. Cole', p. 298

[295] Gregory, T.E. (1930) 'Rationalisation and Technological Unemployment', p. 553

[296] Hobson, J.A. (1932) 'Review – 'The Social Aspects of Rationalisation' by I.L.O', *Political Quarterly*, 3 (July/Sept), p. 457

respects, the phrase "rationalisation of industry" was nothing more than an affectation ("like saying *terra firma* for firm earth").[297] This idea was echoed by both Shadwell and Hilton, who believed the widespread adoption of the term had arisen from its general vagueness (so covering all conceivable ideas) while providing expression and encouragement to post-war attitudes.[298] The drive towards decisive action, the essential dynamism of capitalism that had so long been lacking from the post-war economy, had found expression in the constant (and increasingly tiresome) repetition of a word that, although devoid of theoretical originality, captured the post-war spirit of modernity.[299]

Criticisms of Rationalisation

Would rationalisation be successful in alleviating Britain's difficulties? Was rationalisation a "a nasty medicine" capable of resolving the problem, or just "a process of slow poisoning"?[300] One attack against the scheme was provided by Robbins, who argued that the theoretical foundations of rationalisation did not reflect the representation of established economic principles, but rather the development of a policy that demonstrated capitalism's denial of its essential character. Put simply, rationalisation articulated capitalism's growing desire to manipulate production, refusal to accept the burden of risks associated with competition, and the belief that

[297] Macgregor, D.H. (1934) *Enterprise, Purpose & Profit*, pp. 33 – 34
[298] Shadwell, A. (1929) 'Rationalisation', *Edinburgh Review*, 250 (October), p. 293; Hilton, J. (1934) 'Putting Industry's House in Order', *The Listener*, 11 (14 March), p. 449
[299] Macgregor, D.H. (1927) 'Recent Papers on Cartels', *Economic Journal*, 37 (June), p. 248; Macgregor, D.H. (1931) 'The Problem of Unemployment – IV', *The Listener*, 5 (28 January), p. 138
[300] Sargant Florence, P. (1930) 'Rationalisation and the Public', *The Listener*, 4 (29 October), p. 706

any economic undertaking, irrespective of expected levels of demand, possessed the moral right to secure a profit.[301]

A second difficulty concerned the technical changes associated with rationalisation, and the necessary reduction in the amount of labour directly required to produce each unit of output. This raised an obvious concern: could rationalisation bring about greater unemployment? Based on economic theory, it was only sufficient to state that unemployment was a possible consequence. A proper appreciation of the effects of the policy required some account of the elasticity of demand for the product. If the elasticity of demand was greater than unity, a small reduction in the price of the good would generate a more than proportionate increase in the quantity demanded. A higher derived demand for the product would therefore lead to the reabsorbition of labour within the industry. Yet although theoretically possible, economists expressed some scepticism as to whether reality was sufficiently forthcoming. It was certainly true that as the price of men's ready-made suits, gramophones, radios (wirelesses), and silk stockings fell, consumption, and hence production, had increased. Yet writers including Cannan, Clay, Cole and Hobson doubted the sufficiency of the demand elasticity for the output of the rationalised industries (and hence the ability of industry to spread the costs of standardisation across an expanded market), while also fearing that the elimination of loss making firms would lead to a desperate struggle amongst the survivors. [302] Macgregor also questioned the sustainability of the rationalised industries, with the shift of power

[301] Robbins, L. (1927) 'Review – 'Das Schicksal des Deutschen Kapitalismus' by M.J. Bonn', pp. 614 – 615

[302] Cole, G. D. H. (1929) 'Where Stands the Industrial North?', *The Listener*, 1 (30 January), p. 106; Cole, G.D.H. (1929) *The Next Ten Years in British Social and Economic Policy*, p. 36; Cannan, E. (1930) 'The Post-War Unemployment Problem', p.49; Hobson, J.A. (1930) 'Review – 'The Post-War Unemployment Problem' by Henry Clay', *Political Quarterly*, 1, p. 138; Clay, H. (1932) 'What is Rationalisation?', p. 147; Hobson, J.A. (1932) 'Review – 'The Social Aspects of Rationalisation' by I.L.O', p. 457

from the single firm to the wider industry increasing the position of organised labour.[303]

Under the rationalisation system, the importance of knowledge was taken into account, and the virtues of the technologist repeatedly extolled. Yet whilst such judgement appeared to represent the authority of trained engineers, there was some doubt as to whether businessmen were prepared to accept such technical evaluations. Where as businessmen were always sensitive to the question of capital and running costs, it was probable that an emphasis on technical facts would led engineers to err on the side of optimism when calculating cost estimates relating to the installation of new equipment, and the likely cost implications for the idleness of plant and machinery. If a plant operated at full capacity on a regular basis, factories employing heavy expenditure on fixed capital could be run at a lower cost. Yet the prevailing fear amongst businessmen, at least as far as Jones saw it, involved the experiences of post-war economic history and that fact that no plant ever operated at full capacity with such regularity. Over a number of years, inevitable fluctuations in demand would raise the cost of idleness. This suggested that the authority of trained, professional technologists did not automatically imply that their proposals always constituted realistic business proposals. [304]

A further concern involved the necessary supply of financial capital needed to facilitate the increased scale of plant and factory associated with standardisation and mass production. In order to do this, many businesses were transformed into joint stock companies whose shares would be sold to individuals. Yet the process of attracting funds was generally through appointing directors well known to the

[303] Macgregor, D.H. (1930) 'Review – 'Trust and Corporation Problems' by H. R. Seager & C. A. Gulick', *Economic Journal*, 40 (June), p. 305

[304] Jones, J.H. (1936) 'Problems For Research', *The Accountant*, 95 (19 December), pp. 835 – 836

investing public – either through aristocratic, political or sporting activities. This suggested that the development of mass-production and joint-stock companies were unlikely to alter the technical expertise of the management.[305]

A concern that occasionally surfaced in the contemporary literature related to the moral problems associated with the process of rationalisation. The competitiveness of nineteenth century private enterprise had long been taken as an important social safeguard against mistakes: if managerial or technical errors were made, the effects were unlikely to extend beyond the single firm. Yet by concentrating production in particular factories, and increasing the scale of economic activity, it was feared that rationalisation imposed a governmental structure upon large sections of the British economy.[306] No matter how modern or dynamic the process of rationalisation appeared, organisation and control always remained the responsibility of fallible human beings. The post-war potential for technical and administrative error was therefore deemed to be as great under rationalisation as during the nineteenth century. Yet due to the sheer scale of the rationalised system, the effects of all managerial decisions were magnified. This implied that any miscalculation had the potential to affect the destiny of a great many people.[307] It was seem as impossible to compare the emotional and moral extent of pre-rationalisation and post-rationalisation attitudes towards decision making and economic activity. Hilton feared that the research instincts of scientists had been tempered by this instinct, arguing that technical developments had been restrained by increased post-war commercial complexities and the associated difficulty in predicting the result of any actions. It was suggested that scientists were morally

[305] Sargant Florence, P. (1930) 'Organisation verses Personal Skill', p. 607
[306] Macgregor, D.H. (1934) *Enterprise, Purpose & Profit*, p. 129
[307] Jones, J.H. (1936) 'Some Neglected Aspects of Rationalisation', *The Accountant*, 94 (25 April), p. 648; Jones, J.H. (1938) 'Leadership and Industrial Development', p. 70

restrained from making important decisions on the basis that they did not know whether the industrial exploitation of their research would assist or arrest economic recovery.[308] A similar situation may be found in regard to the female labour supply. As mentioned in chapter 2, the war-time demand for munitions, coupled with the drainage of men from industry into the armed forces, had necessitated the inclusion of old-age pensioners and women in order to supplement a depleted labour supply. It was widely predicted that employers and trade unions could not ignore the effects of the War in stimulating social attitudes towards the employment of women, and would have to undertake careful scrutiny of the conditions under which women could be safety employed.[309] Yet throughout the post-war period, with business assumed to be highly cost conscious, and given the disparity in wage rates between the sexes, Sargant Florence expressed surprise that firms had not exploited the war-time predicted substitution of female for male labour. One obvious explanation was that employers had simply given little thought to the efficiency of female workers. A far more non-economic explanation, and one that Sargant Florence reported as having been a genuine response by at least one employer, involved the view that prevailing levels of unemployment morally prevented firms from dismissing members of their male workforce.[310]

By the late 1930s, Jones had become suspicious as to the appropriateness of subordinating the "spirit of the age" to economic needs. In a somewhat strange way, Jones demonstrated his argument in terms of the post-war design impulse towards modern architecture. Although standing as a vast architectural monument to the

[308] Hilton, J., Scott Watson, J.A, & Huxley, J. (1934) 'A Three-Cornered Survey of Industrial Britain', *The Listener*, 11 (17 January), p. 105

[309] Chapman, S.J. (1918) 'The State and Labour' in Dawson, H.D. (ed.) *After-War Problems*, p. 140

[310] Sargant Florence, P. (1931) 'A Statistical Contribution to the Theory of Women's Wages', *Economic Journal*, 41 (March), p. 23

process of industrialisation, the post-war period had seen much talk of the "hideous factories" and the "miles of monotonous and ugly streets" that characterised the industrial north. Yet Jones believed that the growth of post-war industrial regions in the South were "nothing to boast about". The post-war style certainly embodying the character of the modern age. Yet in comparison with the aesthetic qualities of Leeds and Bradford, the new industrial towns were nothing more than shoddily constructed dormitories. In comparison with the eighteenth and nineteenth century spirit that had developed the industrial north, the post-war spirit was dismissed as superficial and wholly devoid of any lasting beneficial economic properties.[311]

Summary and Conclusions

In this chapter, we have gone some way to understanding a central theme of the inter-war economic debate. In the traditional historical interpretation of inter-war unemployment, emphasis is placed on the divergence of the real wage and productivity that led to the creation of an unemployment equilibrium. It should not be forgotten that the "real wage" thesis was present within the inter-war literature, and was highlighted by Pigou as an important problem that "pre-war economics never found itself called upon to study."[312] Yet the examples that we have considered in this chapter have suggested that such an interpretation represented only one element of the debate.

Throughout the 1920s and 1930s, economists believed that the continuing presence of unemployment symbolised Britain's lethargic response to the necessary transformation of her economic structure. While this did not suggest the imminent

[311] Jones, J.H. (1935) 'Materialism', pp. 631 – 633
[312] Pigou, A.C. (1927) 'Wage Policy and Unemployment', p. 360

collapse of capitalism, it did lead economists to consider the forces that were unnecessarily obstructing private enterprise. There appeared to be little consensus regarding many of the "physical" impediments to economic development, with some economists dismissing any association between persistent unemployment and population, and others questioning the future importance of motor vehicles.

In attempting to gain some understanding these impediments, economists moved outside the arid postulates of economic theory by attempting to draw upon different impressions of human motivation. The most important theme that we have seen in this chapter, and one that we shall return to in subsequent chapters, concerned contemporary assessment of the prevailing emotional and psychological environment. This appeared to develop from several areas, ranging from simple ignorance of the changing post-war world to a reaction against the sudden change in Britain's industrial and commercial supremacy, and the proposed new balance between the industrial and service sectors of the domestic economy. Throughout the nineteenth century, Britain's prosperity, accumulated wealth and international trade was the envy of the entire world. The diminishing position of post-war manufacturing and international trade as a sign of national economic strength, and hence a determinant of national identity, was seen to have a devastating effect on the operation of the market. A further possible factor involved the psychological effect of the continual presence of unemployment. This was attributed to the operation of the national unemployment insurance scheme in increasing the recorded level of unemployment, and the nation's unquestioning acceptance of government statistics. The effect of an exaggerated comparison between Britain's pre-war and post-war economic position was seen to have contributed to an intensified feeling of helplessness and apathy. The effects of such psychological and emotional reactions were easy to see. With post-war trade conducted under the narrowest of margins, and constantly under review, a reaction against Britain's diminishing industrial power, or the demoralising effect of long, continual unemployment, was sufficient to keep capital and labour below the margin of profitable employment.

Rationalisation, which was seen by many politicians and business leaders to be a path to economic salvation, was both praised and criticised by economists. The fact that rationalisation was identified by several writers as signifying a "second industrial revolution"[313] demonstrates the perceived contemporary appreciation of the need to reinvigorate industry through the wider social and cultural spirit of dynamism and modernity. Yet although the policy overcame the psychological impediments to change, it was seen to have failed its is supposed task as a catalyst to sustainable economic recovery by bringing in its wake several other problems.

[313] Cole, G.D.H. (1926) 'Fordism', p. 730; Sargant Florence, P. (1930) 'The Science of Industrial Relations', p. 555; Jevons, H.S. (1931) 'The Second Industrial Revolution', *Economic Journal*, 41 (March), p. 1

CHAPTER 4

FREE TRADE, PROTECTION,

AND IMPERIAL INTEGRATION

Introduction

As the wave of protectionism passed across inter-war Europe, Britain economists were unfaltering in their commitment to an economic doctrine that had dominated British commercial policy since the mid-nineteenth century. The doctrine of Free Trade reflected the classical presentation whereby countries benefited from specialisation in the production of those goods in which they possessed a comparative advantage, with the surplus exchanged with other nations. Through this policy, nineteenth century British consumers had long enjoyed the advantages of cheap food, with producers benefiting from a supply of raw materials.

The first significant reversal of Britain's free trade position had come with the "McKenna duties" imposed in September 1916. This had involved a 33.3 per cent *ad valorem* tariff intended for the express purpose of discouraging the importation of gramophones, musical instruments, watches, cinematograph film and motor vehicles, thereby assisting the war-time foreign exchange and saving shipping space for food and raw materials.[314] The second development had involved the Safeguarding of Industries Act (1921), with the intention of defending the so-called "key industries"

[314] Rooth, T. (1993) *British Protectionism and the International Economy: Overseas Commercial Policy in the 1930s*, Cambridge: Cambridge University Press, p. 37; Kitson, M. & Solomou, S. (1990) *Protectionism and Economic Revival: The British Interwar Economy*, Cambridge: Cambridge University Press, p. 2

(those producing selected chemicals and scientific instruments) and protecting the domestic market from an influx of imports arising from the rapid depreciation of foreign currencies.[315]

The inter-war economic literature clearly reflected various aspects of the debate surrounding international free trade and protectionism, including assessments of the technical and administrative issues associated with the protectionist policies[316], some attempt at statistical measurement of Britain's changing export position[317], as well as further re-examination and re-articulation of the long-established criticisms of protection.[318]

Yet even allowing for the tentative development of Britain's commercial policy, economic liberalism during the early inter-war period had successfully defended itself against two main challenges: the prevailing enthusiasm for protectionism amongst European nations (a theme that we explored in chapter 2), and Stanley Baldwin's advocacy of protectionism in 1923.[319] The only firm economic

[315] A total of 6,500 items were listed under the Safeguarding Act, with an *ad valorem* duty at a rate of 33.3 per cent. The Act was intended to operate for only five years, but was renewed by the Conservative Government in 1926 for a further ten years. Industries who claimed to be suffering from foreign competition were invited to submit their case for "safeguarding" before the Board of Trade. Those that were successful, and received tariff protection for a five year period, included cutlery, gloves, wrapping and packing paper, and "hollow ware" (pots and pans for domestic use).

[316] Gregory, T.E. (1921) *Tariffs: A Study in Method*, London: Charles Griffin & Co. Ltd

[317] See, for example, Flux, A. (1926) 'British Export Trade', *Economic Journal*, 36 (December), pp. 551 – 562; Loveday, A. (1929) 'The Measurement of Tariff Levels', *Journal of the Royal Statistical Society*, 92, pp. 487 – 516; Bowley, A.L. (1929) 'The Numerical Importance of Foreign Trade', *The Economist* (9 February), p. 277 – 278; Daniels, G.W. (1931) 'Overseas Trade of the United Kingdom in Recent Years as Compared With 1913', pp. 1 – 9

[318] Gregory, T.E. (1923) 'Free Trade: Facts and Figures – I', *Nation & Athenaeum*, 34 (24 November), pp. 307 – 308; Gregory, T.E. (1923) 'Free Trade: Facts and Figures – II', *Nation & Athenaeum*, 34 (1 December), pp. 339 – 340; Beveridge, W.H. (1931) (ed.) *Tariffs: The Case Examined*, London: Longmans, Green & Co. This book was the product of the deliberations of a "committee" of economists, who included William Beveridge, T.E. Gregory, John Hicks, Walter Layton, Arnold Plant, and Lionel Robbins.

[319] Rooth, T. (1993) *British Protectionism and the International Economy: Overseas Commercial Policy in the 1930s*, pp. 36 – 37. For a contemporary discussion of Baldin's tariff proposals, see, for example, Hirst, F.W. (1923) 'Letter – Mr. Baldwin's Pledge', *The Times* (1 October), p. 13, c. F; Hirst, F.W. (1923) 'Letter – Mr. Baldwin's Pledge', *The Times* (12 October), p. 8, c. A; Keynes, J.M. (1923) ' 'Free Trade – I', *Nation & Athenaeum*, 34 (24 November), pp. 302 – 303; Keynes, J.M. (1923) 'Free Trade – II', *Nation & Athenaeum*, 34 (1 December), pp. 335 – 337

support for a tariff (in this instance a "revenue tariff" to raise between £50 and £75m) emerged when, in the spring of 1931, a quarrel within the Economic Advisory Council over-flowed into the national press. It was this debate, initiated by Keynes and forcibly criticised by Robbins, that contributed to the political climate that saw the introduction of the Abnormal Importations (Customs Duties) Act in November 1931 and the Import Duties Act in February 1932.[320]

The successful defence of free trade during the early inter-war period was not unexpected. Henderson noted an inverse relationship between price variations and national support for protection: rising prices may be assumed to lead to a preoccupation with the cost of living, while falling prices, and their associated with depression and unemployment, lead to growing demands for defence of the domestic market.[321] The impression given is that through the economic characteristics of the post-1918 boom (rising prices, low unemployment, etc.) and electoral dissatisfaction with Baldwin's 1923 protectionist proposals, the economic and political climate of the early inter-war period was not capable of fostering the abandonment of free trade. Yet as unemployment became a persistent feature of the post-war British economy, economists found themselves faced with the growing popular demand for protectionist policies.

In this chapter, we shall examine two questions. The first involves contemporary economic attitudes towards protection and imperial integration, and their effects in hindering Britain's economic development. The second question

[320] For the contemporary literature surrounding the "revenue tariff" debate, see Keynes, J.M. (1931) 'Proposals For A Revenue Tariff', *New Statesman & Nation*, 1 (7 March), pp. 53 – 54; Robbins, L. (1931) 'A Reply to Mr Keynes', *New Statesman & Nation*, 1 (14 March) pp. 98 – 100; Daniels, G.W. & Gregory, T.E. (1931) 'Letter – A Revenue Tariff', *New Statesman & Nation*, 1 (14 March), p. 103; Plant, A. (1931) 'Letter – A Revenue Tariff', *New Statesman & Nation*, 1 (14 March), p. 103.

[321] Henderson, H.D. (1930) 'The Falling Price Level and its Implications' (24 April) in Clay, H. (ed.) (1955) *The Inter-War Years and Other Papers*, pp. 52 – 53

concerns the historical significance of Free Trade within British economic thought, and the possible effect of this in motivating inter-war academic resistance to protectionism.

Domestic Impediments to Economic Development

The main economic fears concerning domestic protection rested on a combination of demand-side and supply-side factors, and their potential effect in increasing unemployment. The demand-side issues could be put very simply: a reduction in imports would, *ceteris paribus*, reduce foreign purchasing power and with it foreign consumption of British goods. The theoretically response to this was to increase Britain's short-term foreign lending to those countries affected by Britain's tariff in order to offset the reduction in purchasing power and so maintain employment in Britain's export industries. Both Robbins and Beveridge doubted the sustainability of such a measure, arguing that it placed Britain in the ludicrous position of hindering a foreign nation's trade through the introduction of a tariff, while simultaneously lending her more money.[322] On the supply-side, it was probable that the disruption to resource supplies would disadvantage many industries by increasing the cost of essential raw materials, and so introducing a margin of added value into the production process.[323] Those among the press and general public who actively promoted protection of the iron and steel industry, for example, were

[322] Robbins, L. (1931) 'Economic Notes on Some Arguments for Protection', *Economica*, No. 31 (February), p. 55; Beveridge, W.H. (1932) 'Letter –Tariff Revenues', *The Times* (26 March), p. 10, c. A

[323] Contemporary ideas concerning the direction of resources flows, and the margin of protection in the production process, correspond with the modern historical debate surrounding "effective protection rates." This emerged in response to the complications resulting from the inconsistent implementation of the nominal tariff.

significantly less in number than those domestic and export industries that utilised imported iron and steel as inputs in their production process, such as shipbuilding, railway construction, even down to the manufacture of pipes and cutlery.[324] Thus, the exclusion of Continental iron and steel through the introduction of a significantly high tariff implied that both domestic and export orientated industries would, without an appropriate rebate, face higher costs. Statistical corroboration of this view has been presented by modern research: Capie's calculation of effective protection rates demonstrated that shipbuilding suffered from negative protection throughout the 1930s[325], while work by Broadberry[326] and Foreman-Peck[327] has argued that the Import Duties Act in February 1932 had, at best, a modest impact on output and employment.

Another problem was the apparently malignant policy of "dumping", whereby manufacturers (in America of Germany, for example) who had reaped the benefits of large-scale production, and were saddled with surplus goods, would discriminate against their domestic market in favour of foreign consumers and so sell abroad at an exceptionally low price. The most malicious example of this was taken to be "predatory dumping", whereby producers were seen to deliberately sell at "sacrifice prices" in a foreign market in order to destroy foreign manufacturers and so establish a future monopoly.[328] Britain's commitment to free trade appeared to be compelling British manufacturers to compete with foreign goods in the British market. The overall complexity of "dumping" – such as the underlying motives and

[324] Cox, H. (1931) 'The Drift Towards Protection', *Contemporary Review*, 139 (Jan/June), p. 418

[325] Capie, F. (1994) *Depression and Protectionism: Britain Between The Wars*, Hampshire: Gregg Revivals, pp. 114 – 118

[326] Broadberry, S.N. (1986) 'Aggregate supply in inter-war Britain', *Economic Journal*, 96, pp. 467 – 481

[327] Foreman-Peck, J.S. (1981) 'The British Tariff and Industrial Protection in the 1930s: An Alternative Model', *Economic History Review*, 34, pp. 132 – 9

[328] One such example was the attempt of the German Steel Union (*Stahlwerksverband*) to gain control of the iron and steel industries in Lombardy through predatory dumping in Italy and Switzerland.

the recipients of the benefits – ensured that it served as a fertile ground for pseudo-economic judgements.

One explanation for this, offered by Jones, concerned the nebulous character of the term, thereby enabling politicians, press, and the public to distort reality, and associate "dumping" with any good imported in the ordinary course of international trade.[329] This, in turn, led to the apparently hypocritical attitude toward "dumping", with the public reacting against a policy that was commonly employed by British producers and retailers within the British market. The common practise of summer and winter sales, whereby British shopkeepers sharply reduced prices in order to "dump" surplus stock, was not know to elicit complaints from domestic consumers. This suggested that antagonism towards the strategy of "dumping" had been invested with a powerful political character. As Lindley Fraser pointed out, criticisms of "dumping" (and hence growing support for measures to support domestic industry) was the political manifestation of a disturbing attitude in which international trade was recognised as the supreme mechanism of economic warfare, and a possible harbinger of full military conflict.

Yet once society was made to adopt a more long-term perspective on the policy, it was clear that "dumping" actually damaged the practising nation with the benefits accruing to its "victims". For example, "dumping" by foreign firms – such as German cartels or Asian sugar producers – occurred at the expense of their own domestic well-being, for not only did their consumers suffer, but the increased price of inputs in the production of other commodities raised the overall costs of production. The benefits to the "victim" nation could be seen in Britain's response to

[329] Jones, J.H. (1927) 'Dumping – I', *The Accountant*, 77 (13 August), pp. 221 – 222

"bounty-fed" sugar during the nineteenth century, for although cheap imports destroyed the domestic beet industry (the operation of comparative advantage), both consumers and the sugar using industries benefited. In 1898 it was calculated that Germany, France, Holland, and Belgium had between them gifted Britain a present of some £3¼ millions in sugar bounties.[330]

Agriculture

When Britain had served as the workshop of the world, the growth of manufactured exports had fuelled an increasing dependence on the import of foodstuffs. With submarine warfare having undermined Britain's naval supremacy, and coupled with the shrinkage of Britain's post-war export markets, politicians such as Lloyd George and Sir Alfred Mond called for a revised balance between industrial activity and domestic agricultural production. Whilst it suited nineteenth century attitudes to downplay the importance of agriculture, they argued, international conditions appeared to necessitated a re-examination of domestic agricultural production. Aside from serving as an impetus to land reclamation, increased employment, agricultural scientific work, and the standardised control over farming methods, the inter-war national outlook appears to be one in which agriculture was an essential ingredient to Britain's future national well-being.[331]

The economic criticisms levelled against such views were many and varied. First, the argument that the development of the countryside would provide a ready supply of vigorously healthy recruits in the event of war was dismissed by Gregory

[330] Fraser, L.M. (1931) 'Dumping', *Review of International Co-operation*, 24 (July), pp. 241 – 244

[331] This theme may also have been influenced by the evidence of the 1911 Census of England and Wales, which had shown a small, but significant increase in the number of agricultural labourers over the decade 1901 – 1911 (the first such increase since 1811 – 1821).

as "intellectually beneath contempt."[332] Second, agricultural import duties would have place an intolerable burden on domestic welfare. Not only did the vagaries of the British climate suggest the disturbing possibility that such duties would raise domestic cereal prices to the point where they would generate an internal crisis, but also that the desire to reduce Britain's dependence on imported foods (particularly refrigerated meat from Argentina) would necessitate a change in domestic consumption towards cheaper, less nutritious foodstuffs (the so-called "back to porridge" thesis).[333]

Third, it was feared that national support for protectionism was too heavily influenced by war-time conditions – particularly the aforementioned submarine menace which prevented farmers from securing the necessary supplies of machinery, labour and fertilisers – and a belief that protectionism was justified on the basis of scientific research into the properties of the soil and crop cultivation. Yet where as efficiency and specialisation could, under suitable conditions, reduce industrial costs and increase demand, agricultural rationalisation was limited by the conditions of the soil, the influence of the weather, and the landlord-tenant relationship.[334] Even if it were possible to apply scientific knowledge to "growth of bananas…in Hyde Park", wrote Charles Orwin, producers could not ignore the commercial aspects of agricultural production: the success of the venture was not reflected in the fact that bananas could be grown, but the cost of the whole process, and the price that the fruit would realise in the market.[335]

[332] Gregory, T.E. (1931) 'Economic Nationalism', *International Affairs*, 10 (May), p. 294

[333] Forrester, R.B. (1923) 'Review – 'Food Production in War' by T.H. Middleton', *Economica*, No. 8 (June), p. 153

[334] Macgregor, D.H. (1931) 'Review – 'The Future of Farming' by C.S. Orwin', *Economic Journal*, 41 (June), p. 254

[335] Orwin, C.S. (1924) 'Review – 'The Foundations of Agricultural Economics' by J.A. Venn', *Economic Journal*, 34 (June), p. 244

While economists and statisticians faced profound difficulties in accurately defining the standard of crop conditions and harvest yields[336], the unashamed supporters of British agriculture appeared to display an unstoppable, and occasionally libellous, tendency to undersell the efficiency of British agricultural production. This tendency had received unnecessary publicity through the war-time Middleton Report on German Agriculture. By having concentrated on a technical relationship between food production and the calorific content (or "energy value") of the food produced, the Middleton Report had reached the well publicised conclusion that German agricultural production fed 71 people per 100 cultivated acres, while Britain fed a mere 51 people. British agriculturists was seen to be less adept at growing crops compared with their German counterparts. Early criticism of this argument was provided by Hawtrey, who argued that such comparisons were "hardly credible" given the obvious inferiority of the German soil.[337] Yet it was feared that the official character of Sir Thomas Middleton's claims (or misrepresentations) had engendered a lasting belief in the inefficiency of British agriculturists. It was clearly Macgregor's fear that post-war agriculture had fallen pray to protectionist demands simply on the basis of an abstruse concept – calorific content – which never entered into any agriculturists decision making process.[338]

[336] Venn, J.A. (1926) 'Review – 'The Grain Supply of England During the Napoleonic Period' by W.F. Galpin', *Economic Journal*, 36 (June), p. 260; Venn, J.A. (1927) 'Official Papers – The Agricultural Output of England and Wales, 1925', *Economic Journal*, 37 (September), p. 486

[337] Hawtrey, R.G. (1917) 'Note on Mr. Middleton's Pamphlet on German Agriculture', *Economic Journal*, 27 (May), p. 144

[338] Macgregor, D.H. (1925) 'The Agricultural Argument', *Economic Journal*, 35 (September), pp. 394 – 395

Given diminishing faith in the principles of international co-operation, and suspicion at the idea of a large scale trading partnership with either Europe or America, it appeared inevitable that British public opinion would turn its attention to the idea of Imperial integration.[339] Consisting of Great Britain, India, the self-governing Dominions, and the Crown Colonies, the Empire represented the political, economic and cultural manifestation of the indomitable British spirit of adventure and individual enterprise: ambitious explorers and merchants had risked their lives and fortunes cutting through the wilderness, establishing communications, and distributing British goods (and British rule) to the remote corners of the globe.

Post-war attitudes towards Imperial union had partly been influenced by the role of the Empire in providing food and clothing for British soldiers during the War, and the effects of a devastating military conflict in engendered a sense of insecurity amongst the British people.[340] Before the War, questions concerning an Imperial defensive union had concentrated on Joseph Chamberlain's intention of distributing the enormous cost of Imperial Defence between the taxpayers of the Empire. In the post-war world, Britain's attention to the Empire was influenced by a practical desire to guarantee the safety of essential food supplies against possible future aggression.

On more economic grounds, imperial union appeared to represent the logical extension of Britain's historical relationship with the Empire, and her desire to secure an expanding market for British manufactured goods. Yet whilst it could not be denied that the Empire ignited the patriotism of the nation, economists were much

[339] Rooth, T. (1993) *British Protectionism and the International Economy: Overseas Commercial Policy in the 1930s*, p. 71

[340] Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, p. 55

more critical. On the one hand, Cole dismissed all forms of economic integration as the grasping attempts of international capitalism to extract yet more surplus value from labour.[341] For others, the economic consolidation of the Empire was dismissed as nothing more than an over-romanticised interpretation of Britain's imperial history that ignored existing commitments and administrative impediments.[342] It was suggested by Gregory, for example, that Rothermere and Beaverbrook's Empire Crusade Campaign (later the United Empire Party) had been conducted "with an atmosphere of cinematographic mediaevalism"[343], while Robbins dismissed their proposals as nothing more than a paradise for reactionaries ("Eldorado banal de tous les vieux garçons").[344]

Even allowing for territorial expansion following the War, British exports to the Empire accounted for less than half of her total export trade (Britain's principle customers for coal were France, Italy, Belgium, and Germany) while existing overseas commitments, most noticeably long-term investment in Argentina (estimated at £350m), reinforced her trading connections with non-Empire countries.[345] Increased post-war marketing of Empire goods in foreign countries made it doubtful whether Canada, Australia, South Africa and India would freely relinquish fiscal autonomy and commercial policies simply to support Britain's desire for economic self-sufficiency. This was the realisation of the war-time fear, mentioned in chapter 2, that the political repercussions of the War were loosening the

[341] Cole, G.D.H. (1924) 'Europe Ltd.', *New Statesman*, 23 (4 October), p. 727

[342] Hirst, F.W. (1926) 'Mr. Churchill's Second Budget', *Contemporary Review*, 129 (Jan/June), p. 703; Cox, H. (1931) 'The Drift Towards Protection', p. 420; Beveridge, W. & Hicks, J.R. (1931) 'The Possibilities of Imperial Preference' in Beveridge, W. (ed) (1931) *Tariffs: The Case Examined*, pp. 135 – 147

[343] Gregory, T.E. (1930) 'Empire Free Trade', *Political Quarterly*, 1 (April), p. 231

[344] Robbins, L. quoted in Skidelsky, R. (1992) *John Maynard Keynes: The Economist As Saviour, 1920 – 1937*, London: Papermac, p. 375

[345] Cox, H. (1931) 'The Drift Towards Protection', p. 421

bonds of Empire.[346] It may be argued that the independent attitudes of many countries had been stimulated by a desire to present themselves as active members of the League of Nations.

Not only was it extremely unlikely that the development of historical and political affiliations would support an Imperial unit within the League of Nations[347], economists clearly believed it was impossible for imperial free trade to overcome existing economic commitments and political intransigence. Empire countries would simply not endorse a trade policy that had the potential for injuring existing domestic or international economic relations.[348] Even before the War, the world had seen little evidence of imperial economic unity: the largest market for Canadian lumber had been in the United States, while the bulk of Indian exports had been directed to Continental markets.[349] In terms of political intransigence, Hirst and Cox highlighted the activities of manufacturers and merchants in Bombay, Bengal, and Calcutta, who took great pleasure in successfully restricting British exports to Indian markets (their task having been greatly eased by the actions of the ineffective, protectionist Viceroy, Sir George Schuster).[350]

A further difficulty to the scheme of Imperial self-sufficiently involved the necessary preferential treatment to the purchase of Empire goods. While appearing socially beneficial, both Lionel Robbins and John Hicks feared that such a move

[346] Cannan, E. (1915) 'Strategic Jealousies Masked As Commercial' (20 March) in *An Economist's Protest*, p. 27; Shadwell, A. (1912) 'National Insurance in Germany', p. 242; Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, p. 54

[347] This idea was thrown into complete doubt following the refusal of the League of Nations Economic and Financial Committee to recognise Europe as an economic area.

[348] This argument may be seen as an extension of contemporary criticism regarding Aristide Briand's proposals for a great confederation of European states within the orbit of the League of Nations. See, for example, Layton, T. (1928) 'Europe's Role In Future World Trade', p. 157; Hobson, J.A. (1929) 'The United States of Europe', pp. 548 – 552; Steiner, Z. (2005) *The Lights That Failed: European International History, 1919 – 1933*, Oxford: Oxford University Press, pp. 414 – 415

[349] Clay, H. (1924) 'An Economic Revolution', *Times Literary Supplement*, Issue: 1191 (13 November), p. 720

[350] Cox, H. (19300 'Some Real Causes of the Slump', p. 560; Hirst, F.W. (1931) 'An Emergency Budget', *Contemporary Review*, 139 (Jan/June), p. 684

signified the growth of indirect protectionism. The operation of an import board could eliminate speculation by enabling Britain to secure long-term, bulk purchase contracts with Dominion producers. Britain would, for example, contract to take 40 per cent of Canadian wheat production at a fixed price for five years. However, any potential economies in transport secured through long-term contracts would be overshadowed by the dangers inherent in establishing long-term fixed prices. The impossibilities of predicting future Canadian harvests, and hence future Canadian wheat prices, implied that administrators of Imperial import boards were deprived of any objective criterion against which to establish prices. With the downward trend of post-war agricultural prices (a trend which both Robbins and Hicks predicted would continue), and the likely inability of Britain's import boards to revise long-term contracts once established, it was feared that British consumers would face indirect protectionist through their inability to obtain the cheapest supplies of wheat.[351]

Psychological Effects of Protectionism

What may we glean from this brief review of contemporary criticisms regarding protection? What is the basic characteristic of this criticism? In chapter 3, we outlined the relationship that inter-war economists had draw between Britain's post-war industrial sclerosis and psychological and emotional reactions to Britain's post-war economic position. To briefly recapitulate, it was suggested that the spirit of enterprise had been undermined by, amongst other things, a national belief in malevolent forces or distress at Britain's diminishing industrial prestige.

[351] Hicks, J.R. (1931) 'Quotas and Import Boards' in Beveridge, W. (ed) (1931) *Tariffs: The Case Examined*, pp. 226 – 227; Robbins, L. (1931) 'The Economic of Import Boards – A Criticism of Mr. Wise's Proposals', *Political Quarterly*, 2 (April/June) pp. 217 – 218

On first glance, it would appeared that the collective clamouring of the Trade Union Congress and British press for industrial and agricultural protection, or the extensive economic and political consolidation of the Empire, served as a means to reinvigorate the faded spirit of enterprise. For example, a secure Imperial market for British manufactured goods, or a strong domestic agricultural sector, could easily be identified as providing a refreshed sense of momentum, and hence a stimulant to economic recovery. For economists, the widespread public belief that economic salvation lay with either domestic protection or Imperial integration served as a fundamentally dangerous impediment to economic recovery.

Economic co-operation within such a designated geographic area – the formation of an Imperial Trading Unit – appeared to be an improvement on the perceived immorality of vulgar protectionism: whereas tariffs and quotas represented the general discouragement of imports, a co-operative economic unit reasserted the international division of labour and the economic principles of trade liberalisation. Yet it was clear that existing economic commitments and administrative difficulties undermined any suggestion that Britain could gain from Imperial economic integration. Not only was it high debatable whether concessions by the Dominions and Colonies would be sufficient to reduce Britain's dependence on international trade, but there was also little prospect of the Dominions opening their markets to British goods. The vision of a close-knit Imperial unit was therefore viewed by many economists as an unrealistic and dangerous dream.

A similar approach may be discerned with the protection of domestic agriculture, and the move towards the enlargement of an outdated, pre-industrial form of existence. The introduction of the British Sugar Subsidy Act (1925), or the duty on foreign hops for the benefit of hops growers in Kent and Sussex, was seen by Hirst as the first steps towards a fateful redevelopment of Britain's agricultural sector.[352] In an extreme example, Jones noted the situation amongst some of the inhabitant of Saskatchewan, whose desire to escape the world's economic problems had led them to adopt a depressing, self-sufficient existence based on logging, fishing and small-scale agriculture.[353]

Influence on Economics

Thus far we have assumed that inter-war economists were seeking to promote the doctrine of free trade in order to defend Britain's economic transformation from the long-term, malevolent effects of protectionism. Allowing for the minutiae of the debate, the contemporary economic literature reflected a desire to demolish pseudo-economics ideas that were seen to be impeding economic development. Yet there may also be something else to consider. The act of promoting free trade may not have simply represented a desire to promote Britain's economic regeneration, but a desperate attempt to defend the academic reputation of economics. There are two themes to this idea.

Whilst it is possible, and indeed practical, for historians to distinguish between specific time periods, it is impossible to confine the development of ideas in such a way. In chapter 2, we saw how many of themes of the early inter-war unemployment debate were extensions of pre-war themes. Similarly, the character of the inter-war free trade debate cannot be taken simply as a product of its own time, but rather viewed as the remnants of the tariff reform debate evoked by Joseph Chamberlain before the War. Given that the persistence of protectionist thought

[352] Hirst, F.W. (1926) 'Mr. Churchill's Second Budget', *Contemporary Review*, p. 695; Hirst, F.W. (1929) 'Safeguarding In Theory and Practice', Contemporary Review, 135 (Jan/June), p. 294

[353] Jones, J.H. (1935) 'Some Aspects of Industrial Change', p. 75

illustrated the nation's inability to grasp the essential elements of economic analysis[354], the tariff reform debate had served as an excellent opportunity for economists to apply their expertise to a practical economic problem.[355] As McCready pointed out: "if Chamberlain paid little attention to the economists, they paid ample to him."[356]

The academic lines of the pre-war debate were quickly drawn: the historical school – comprising, amongst others, William Ashley, William Cunningham, Herbert Foxwell and Langford Price – supported Chamberlian's protectionist proposals; the abstract-deductive (neo-classical) economists – led by Charles Bastable and a reluctant Alfred Marshall – championed free trade. The main themes of the abstract-deductive manifesto, published in *The Times* in August 1903, argued that protectionism would prove "materially detrimental" to Britain's economic prosperity, given that such a policy, once introduced, would "extend beyond the limits at first assigned to it" and become "very difficult to extirpate."[357] Although, as already detailed, resort to short-term protectionism could be justified along the lines of encouraging trades that operated in unpleasant conditions and defending industries in the early stages of development, there remained a fear that, once the "emergency" had passed, the development of vested interests would obstruct the reversal of the policy, and so make the cost of return to free trade discouragingly heavy. Protectionism, in other words, was the equivalent of an economic demon that the nation would have difficulty in eradicating. Edgeworth had succinctly expressed such

[354] Price, L.L. (1892) 'Review – 'The Commerce of Nations' by C.F. Bastable', *Economic Journal*, 2 (June), p. 324; Nicholson, J.S. (1904) 'Review – 'Free Trade, Protection, Dumping, Bounties, and Preferential Tariffs' by H.A. Agacy', *Economic Journal*, 14 (March), p. 61

[355] For a concise discussion of the tariff reform debate, see Middleton, R. (1998) *Charlatans or Saviours? Economists and the British Economy from Marshall to Meade*, pp. 137 – 138

[356] McCready, H.W. (1955) 'Alfred Marshall and Tariff Reform, 1903: Some Unpublished Letters', *Journal of Political Economy*, 63, p. 259

[357] Bastable, C.F. *et al* (1903) 'Professors of Economics and the Tariff Question', *The Times* (15 August), p.4, c. B

anxieties in 1903 when he wrote that protectionism engendered "not only its own kind, but also the evils of jobbery and corruption".[358] The same view was repeated by Beveridge in 1931, who argued that the removal of tariffs had never been secured "without bitter opposition."[359]

During the pre-war, tariff reform debate, this interpretation of protectionism had been rejected by members of the historical school: Price argued that free trade economists emphasised the dangers of protectionism while ignoring the dangers associated with preserving free trade[360]; Foxwell believed the whole tariff issue was "more political than scientific" and questioned the right of economists to "prejudge these issues by a pronouncement which assumes scientific authority"[361]; while Cunningham questioned the authority of various eminent signatories to the free trade manifesto, arguing that they had selected a hypothetical situation "without reference to any country or any particular stage of economic development".[362] By the end of the tariff reform debate, however, the abstract-deductive school had triumphed, and the doctrine of free trade was unassailable. The debate had also ensured that economists were now largely of one mind and one book – Marshall's *Principles of Economics* became the dominant textbook of English economics. The uncritical support for free trade during the 1920s testifies to the theoretical dominance of the neo-classical position, with all proposals for long-term protectionism destroyed by the force of comparative advantage. As Edgeworth wrote: "Art after art may expire, but the law of comparative cost will continue to act."[363]

[358] Edgeworth, F.Y. (1903) 'Review – 'The Tariff Problem' by W. J. Ashley', *Economic Journal*, 13 (December), p. 574

[359] Beveridge, W.H. (1931) 'Letter – A Revenue Tariff', p. 103

[360] Price, L.L. (1903) 'Professors of Economics and the Tariff Question', *The Times* (15 August), p.4, c. B

[361] Foxwell, H.S. (1903) 'Professors of Economics and the Tariff Question', *The Times* (20 August), p. 10, c. C

[362] Cunningham, W. (1903) 'Professors of Economics and the Tariff Question', *The Times* (20 August), p. 10, c. C

[363] Edgeworth, F.Y. (1903) 'Review – 'The Tariff Problem' by W. J. Ashley', p. 573

Did the intellectual dominance of free trade influence the attitudes of inter-war economists? The voluminous nature of the inter-war economic literature clearly illustrates the demand for the opinions and diagnoses of economists. Under these circumstances, an economist's intellectual credentials were highly important. While the primacy of the printed record renders any speculation regarding the private attitudes towards protectionism redundant, it is clear that the doctrine of free trade had primacy over the public pronouncements of economists. Given the intellectual hegemony of the abstract-deductive approach, and the fact that the main supporters of the historical school were, by the 1920s, elderly men, there was no body of credible academic economic opinion publicly prepared to support protectionism. One reason for the defence of free trade is therefore clear: any economist who advocated protectionism was liable to be branded a heretic. As Marrison has pointed out:

> "Declaring one's protectionism was an act of personal exposure, not only unpleasant, but also fruitless unless others in their thousands joined suit."[364]

But was this the only motive? The continual economic confusion of the inter-war period, and the lingering possibility of descending into the murky pool of protectionism endangered the credibility of the abstract-deductive school. This view was reflected in the declining acceptance of the ideological relationship between *laissez-faire* and free trade, which, as the American economist, Jacob Viner noted, although a source of great strength during the nineteenth century had, by the 1930s, become an "embarrassing *mésalliance*."[365] Such an interpretation was also presented by Cole, who argued that the classical presentation of the "international division of

[364] Marrison, A. (1996) *British Business and Protection, 1903 – 1932*, Oxford: Clarendon Press, p. 431

[365] Viner, J. (1931) 'The Tariff Question and The Economist – I', *Nation & Athenaeum*, Vol. 48 (7 February), p. 594

labour" served as an ideological contrivance constructed in response to an ill-developed, international economic system that had now passed.[366] To quote Cole at length:

> "[E]conomists may continue to dream of the superior advantages of a free trade world; but there is no more chance of their dreams coming true than there is that Europe will return to the localised economic system of the middle ages."[367]

In terms of the position and reputation of British economic thought, such ideas were profoundly significant. For inter-war economists, the doctrine of free international trade lay at the heart of established economic thought. By refining Smith's principles, and establishing the relationship between production, distribution, and free trade, Ricardo had successfully placed the theory of international trade at the pinnacle of Anglo-saxon economic theory.[368] For Mill, the theory had signified both the complexity and beauty of political economy.[369] Under these circumstances, the advent of protectionism not only appeared to obstruct Britain's economic regeneration, but also undermined the intellectual position of a large body of English economic theory that had developed from the late eighteenth century. This view was clearly expressed by G.W. Daniels, who feared that the potential dominance of protectionism would expose free trade to the attack that it had been nothing more than a mere "episode in economic history", and so foster the view that the "practical application" of economics only possessed validity so long as particular economic

[366] Cole, G.D.H. (1929) *The Next Ten Years In British Social and Economic Policy*, p. 23
[367] Cole, G.D.H. (1933/34) 'Planning International Trade', *Foreign Affairs*, 12, p. 235
[368] Tribe, K. (1995) 'Natural liberty and *laissez-faire*: how Adam Smith became a free trade ideology' in Copley, S. & Sutherland, K. (eds.) *Adam Smith's Wealth of Nations: New Interdisciplinary*, pp. 28 – 29
[369] Mill, J.S. quoted in Edgeworth, F.Y. (1903) 'Review – 'The Tariff Problem' by W. J. Ashley', p. 571

conditions prevailed.[370] Such a prospect was clearly disturbing, for if the general public accepted that free trade was only applicable to a particular historical period, economics lost it ability to ascend to the intellectual prestige of a science.

Summary and Conclusion

One of the themes that can be drawn from this chapter involves the difference in the character of the inter-war protectionist debate and that associated with the theoretical and quantitative aspects of modern historiography. Whereas modern historiography has tended to be pre-occupied with the reciprocal effects of a tariff on macroeconomic variables – include the impact on wages of tariff-induced price increases; adjustments to the money supply brought about by changes in wages and prices; the reaction of the exchange rate to changes in the money supply; and the resulting impact of exchange rate on import prices – the inter-war debate appeared largely one sided in its defence of Free Trade.[371]

This characteristic of the inter-war debate is reflected in the importance that economists attached to Britain's need to adjust her economic structure in response to the changing international economic landscape. It was deemed essential that Britain did nothing to promote forces that would prevent producers and manufacturers from enjoying the advantages of international trade, and so weaken the process of transformation. As Lionel Robbins made clear, it was essential that Britain did

[370] Daniels, G.W. (1936) 'Economic Theory and National Policy', pp. 91 – 92

[371] Broadberry, S. (1986) *The British Economy Between the Wars: A Macroeconomic Survey*, pp. 134 – 136; Eichengreen, B. (1991) 'Review – 'Protectionism and Economic Revival' by M. Kitson & S. Solomou', *Journal of Economic History*, 51, p. 489. This is not to suggest that inter-war economists were ignorant of such reciprocal effects. For an interesting contemporary appreciation of this reciprocal relationship, whereby an appreciation in the exchange rate could reduce the effectiveness of the tariff, see Gregory, T.E. (1934) *The Gold Standard and Its Future*, London: Methuen & Co. Ltd, (3rd edition) pp. 66 – 70

nothing to "set up machinery" with the potential to "impede the process of adjustment."[372] In order to neutralise national support for the lingering, petty devices of protectionism, and so facilitate the move towards recovery, economists sought to expose the impracticality of confused proposals, while at the same time promoting cosmopolitanism and the merits of unfettered, international trade.

The romanticised impression of economic prosperity secured under cover of the British flag or by the return to "a sort of Garden of Eden"[373] was seen as a dangerous absurdity that promoted either unrealistic expectations of the future direction of the economy, or a return to an outdated mode of economic existence. A reinvigorated spirit of enterprise did not lie with proposals whose basic effect was to distract attention and resources from the necessary forward development of Britain's industrial and commercial structure. [374] There was also a further problem, for it was clear that each demand for protection, however presented, not only called into question the moral and material aspects of Britain's allegiance to internationalism (which was the essence of Britain's long-term economic and political security[375]), but also undermined the emotional strength of the domestic economy. "Safeguarding", for example, signified a lingering form of protectionism which, although hidden behind a new disguise (a word that "bamboozled" the nation[376]) amounted to an open proclamation of Britain's domestic manufacturing failure,

[372] Robbins, L. (1931) 'The Economic of Import Boards – A Criticism of Mr. Wise's Proposals', p. 212

[373] Guillebaud, C.W. (1925) 'Some Popular Economic Fallacies', *The Accountant*, 73 (28 November), p. 860

[374] Cox, H. (1926) 'The Imperial Conference', *Edinburgh Review*, 244 (October), p. 393; Cole, G.D.H (1930) 'The Trades Union Congress on Empire Trade', *New Statesman*, 35 (5 July), p. 401; Shadwell, A. (1930) 'Letter – Unemployment', *The Times* (27 August), p. 11, c. F; Beveridge, W. & Hicks, J.R. (1931) 'The Possibilities of Imperial Preference' in Beveridge, W. (ed.) (1931) *Tariffs: The Case Examined*, p. 143; Gregory, T.E. (1931) 'Economic Nationalism', *International,* p. 299

[375] Hobson, J.A (1931) 'A World Economy', pp. 274 – 275

[376] Hirst, F.W. (1929) 'Safeguarding In Theory and Practice', p. 292

thereby strengthening those negative attitudes towards the domestic market that many economists were seeking to neutralise.

Yet economists did not approach the problem in a purely detached manner, since any actions in undermining the policy of free international trade also weakened the position of the prevailing, neo-classical doctrine. The advent and potential dominance of economic nationalism could lead society to believe that the long-established theory of international trade possessed validity only as long as particular economic conditions prevailed. Free trade may be seen as the piece of driftwood that economics clung to in an attempt to survive the storm.

CHAPTER 5

GOVERNMENT EXPENDITURE

Introduction

Pre-war discussions of Britain's financial system had largely concentrated on the history of the Exchequer and the means by which compulsory payments were extracted from citizens. It had been well recognised that a satisfactory taxation system was never easy to achieve in practice, and the debate had centred on the equitable transfer of wealth, and the idea of taxable capacity.[377] Emphasis on the means by which revenue was raised (as opposed to the ways in which receipts were spent) had ensured a strength of resentment against so much as a penny increases in income tax.[378] This approach to the question of public finance had, of course, reflected the simple construction of Britain's nineteenth century economic system and the established Ango-Saxon attitude towards the State's role in maintaining domestic peace and providing adequate defence against external aggression.[379]

By the 1920s, dramatic increases in government departmental expenditure, and the communal provision of old age pensions, education, social insurance and health services had become an integral feature of society. For this reason, questions regarding government expenditure held an interesting place in the post-war economic

[377] Taxable capacity – the difference between the total quantity of production and the total quantity of consumption – had received considerable attention during the latter years of the nineteenth century in relation to the alleged over-taxation of Ireland. Stamp, J.S. (1922) *Wealth and Taxable Capacity*, , pp. 109 – 110

[378] Jones, J.H. (1938) 'Then and Now', *The Accountant*, 99 (17 December), p. 827

[379] Stamp, J.C. (1919) 'Review – 'Parliament and the Taxpayer' by E.H. Davenport', *Journal of the Royal Statistical Society*, 82 (March), p. 235; Dalton, H. (1921) 'Some Recent Contributions to the Study of Public Finance', *Economica*, No. 2 (May), pp. 199 – 200

debate.[380] Having said this, the vast majority steered away from discussing the political character of government expenditure and published little on the formal presentation and procedure that surrounded the Public Accounts.[381]

In this chapter, we shall examine economic attitudes towards increases in post-war government expenditure. We shall not here be dealing with contemporary attitudes towards the "art" of public finance[382], such as the equality, certainty and convenience of taxation, post-war borrowing[383], government attitudes towards the reduction and conversion of the National Debt, or even Churchill's raid on the Road Fund in 1926 and 1927.[384] This chapter will concentrate on inter-war attitudes towards the economic and social consequences associated with the distribution of revenue, and their effect on Britain's economic development.

[380] Throughout the early 1920s, Cox had christened this situation "sqandermania" and attributed it to the unquestioning acquiescence of cabinet ministers in the face of a well-organised, bellicose socialist movement. See, for example, Cox, H. (1919) 'The Ethical Side of Socialism', pp. 202 – 206; Cox, H. (1921) 'The Public Purse', p. 198; Cox, H. (1922) 'Politics and Unemployment', *Edinburgh Review*, 235 (January), p. 201; Cox, H. (1922) 'Labour Disillusionment', pp. 402 – 405.

[381] For a sustained contemporary discussion on the content and presentation of the government's inter-war financial statements, see the annual assessments published by Francis Hirst in the *Contemporary Review* – (1925) 'The Budget', 127 (Jan/June), pp. 681 – 689; (1926) 'Public Finance in 1925', 129 (Jan/June), pp. 17 – 24; (1927) 'Mr. Churchill's Third Budget', 131 (Jan/June), p. 545 – 552; (1927) 'Mr. Churchill's Fourth Budget', 133 (Jan/June), pp. 689 – 697; (1929) 'Churchillian Finance: The Fifth Budget', 135 (Jan/June), pp. 681 – 687; (1930) 'Mr Philip Snowden's Second Budget', 137 (Jan/June), pp. 681 – 690; (1931) 'An Emergency Budget', 139 (Jan/June), pp. 681 – 687; (1931) 'The Second Budget of 1931 – And Why it was Necessary', 140 (July/Dec), pp. 429 – 437; (1932) 'The First Protectionist Budget', 141 (Jan/June), pp. 681 – 688; (1933) 'Mr. Chamberlain's Second Budget', 143 (Jan/June), pp. 641 – 650; (1934) 'Mr. Chamberlain's Third Budget', 145 (Jan/June), pp. 641 – 649; (1935) 'Mr. Neville Chamberlain's Fourth Budget', 147 (Jan/June), pp. 641 – 648; (1936)'Mr. Chamberlain's Fifth Budget – Taxation for Defence', 149 (Jan/June), pp. 651 – 659; (1937) 'The Armament Budget', 151 (Jan/June), pp. 641 – 649; (1938) 'Sir John Simon's Budget', 153 (Jan/June), pp. 641 – 649; (1939) 'Sir John Simon's Second Budget – Appearance and Reality', 155 (Jan/June), pp. 651 – 658

[382] Hawtrey defined financial decisions were an "art" in that they were the products of "expedients rather than general principles". Hawtrey, R.G 'What is Finance?', *The Accountant*, 78 (7 January), p. 18

[383] For a detailed contemporary discussion of War-time and Post-War Borrowing, see Hargreaves, E.L. (1930) *The National Debt*, London: Edward Arnold, pp. 230 – 262

[384] On a separate issue, one of the more curious features of inter-war public finance concerned Churchill's gratitude towards a large number of millionaires, whose deaths over the period 1928 – 29, had facilitated a large increase in the yield on Death Duties.

As we suggested in chapter 2, war-time and early post-war attitudes toward taxation fell into two categories: first, the detrimental influence of burdensome post-war taxation; and second, the adaptability of society to the sustained pressure of taxation. The remnants of this latter idea passed through to the mid-1920s, with Jones suggesting that complaints about post-war taxation had been exaggerated, and that that taxation only influence a person to the extent it made them work harder in order to maintain a certain standard of living. If existing taxation had been a grave menace to industry, he argued, society would have been subjected to desperate calls for currency inflation, or at the very least, a levy on accumulated wealth. The fact that these had not occurred (the demands for a capital levy were gradually dying away) demonstrated that taxation was not a significantly detrimental problem.[385]

By the early 1930s, Jones was forced to concede that the notion of adaptability had been insufficient to circumvent the psychological barrier of permanent direct taxation.[386] In accepting this position, Jones fell into a large group of economists who believed that the burden of taxation was indeed having an injurious effect upon the economy.[387]

A second difficulty centred on the public reaction to the cryptic character of taxation theory. It was, of course, inevitable that economic discussions of taxation theory, particularly with regard to the technical difficulties of assessing income tax,

[385] Jones, J.H. (1925) 'Taxation and Trade', *The Accountant*, 73 (19 September), pp. 419 – 420; Jones, J.H. (1925) 'Taxation and Capital', *The Accountant*, 73 (26 September), pp. 467 – 468

[386] Jones, J.H. (1932) 'Taxation and Employment', *The Accountant*, 87 (5 November), p. 571

[387] See, for example, Hirst, F.W. (1924) 'Letter – Economy and the Budget', p. 13, c. D; Hirst, F.W. (1925) 'Letter – Taxation and Economy', *The Times* (23 April), p. 8, c. C; Hirst, F.W. (1927) 'Letter – Economies Long Promised', p. 15, c. F; Cole, G.D.H. (1928) 'Mr. Churchill and the Rate Payer', p. 585; Clay, H. (1928) 'Unemployment and Wage Rates', p. 2; Knoop, D. (1930) 'The Burden of Heavy Taxation on Industry and Trade', *Manchester School*, 1, p. 19; Clay, H. (1931) 'Dr Cannan's Views on Unemployment', *Economic Journal*, 40 (June), p. 335

would retain a theoretical bias. What happened when real income was not expressed in monetary terms? Was the unit of assessment to be based on the individual (for unmarried persons) or on the couple (for married persons)? [388] Unless such abstract discussions were undertaken, claimed Stamp, important questions surrounding taxation and the distribution of total economic welfare would flounder helplessly in a morass of fragmentary statistics.[389] Similarities may also be found in questions concerning the theoretical problems arising from calculating changes in economic welfare associated with the redistribution of income.[390]

The prospect of unremunerative economic activity, coupled with an apparent national disdain for the ambiguous character of taxation theory, was taken to be exerting a discouraging effect on the essential spirit of capitalist enterprise, thereby restricting Britain's economic evolution, as well as sterilising the ambitions and abilities of the growing generation.

From this point, however, attitudes towards taxation and expenditure split into two distinct groups. The essence of the argument boiled down to the differing views as to the advantages or disadvantages of the ways in which post-war taxation was being employed to balance taxpayers' sacrifices against government services. The first group, which signified a more, old-fashioned, political-economic approach, argued that Britain's economic prosperity and the fabric of her social life, was not only being prejudiced by high rates of direct and indirect taxation, but also excessive

[388] Knoop, D. (1920) 'The Royal Commission on the Income Tax', *Economic Journal*, 30 (June), pp. 260 – 271; Pigou, A.C. (1920) 'The Report of the Royal Commission on the British Income Tax', *Quarterly Journal of Economics*, 24 (August), pp. 607 – 609. The Royal Commission on British Taxation had been appointed to consider measures for resolving the inequalities and complications of the taxation system without lowering its yield.

[389] Stamp, J.C. (1919) 'The Special Taxation of Business Profits in Relation to the Present Position of National Finance', p. 407; Stamp, J.C. (1922) *Wealth and Taxable Capacity*, pp. 108 – 109; Stamp, J.C. (1932) 'Debatable Points in Taxation', *The Listener*, 8 (9 November), p. 650

[390] Dalton, H. (1920) 'The Measurement of the Inequality of Incomes', *Economic Journal*, 30 (September), p. 348; Lavington, F. (1921) 'Review – 'Some Aspects of the Inequality of Incomes in Modern Communities' by H. Dalton', *Economic Journal*, 32 (June), p. 215

levels of unproductive expenditure associated with the panoply of social welfare services. The second group was much more optimistic in its attitude, for although repeating concerns about the pressure of post-war taxation, they recognised that it was pointless expecting social expenditure to return to its pre-war level. This led to the view that social expenditure, if organised and presented in the correct way, could actually overcome the psychological problems of increased taxation and so benefit Britain's transformation. This connection with the question of economic development, and hence the problem of prevailing unemployment, implied that, for at least some economists, government expenditure took on a far deeper meaning. We shall briefly consider each group in turn.

Critical View of Government Expenditure

It was obviously impossible, argued writers such as Hirst and Cox, to finance the enormous increase in post-war public expenditure simply through compulsory levies such as income tax, surtax, and death duties. Some proportion of government revenue had to be financed through expenditure on commodities for which the demand was fairly inelastic.[391] Indirect taxation (or indirect contributions) therefore placed a disproportionate burden on relatively poor consumers, for although there were certain elements of indirect taxation the working class did not pay – tax on male servants, for example – they were required to pay taxation on items of normal consumption such as beer, sugar, tea and tobacco. It was clearly impossible to calculate the individual burden of indirect taxation with any degree of mathematical precision. Yet since it was reasonable to presume that both a millionaire and an

[391] Jones, J.H. (1929) *The Economics of Private Enterprise*, p. 431

ordinary labourer would consume equal quantities of staple items such as tea or tobacco on a daily basis, indirect taxation on such items constituted an absolute burden on the poorest and most vulnerable classes of society. Such actions could hardly be classified as an acceptable form of social justice: duty on beer (which, over the course of the period, increased by twelve times its pre-war rate[392]) was a real injustice to poorly-paid agricultural workers, while duty on sugar deprived children of a valuable food supplement. It was also doubtful whether the inequitable burden of indirect taxation was offset by the provision of social services. Based on his own calculation, Cox believed that the total cost of old age and widows' contributory pensions, unemployment benefits, and sickness benefits was less than the estimated revenue transferred through compulsory, indirect taxation.[393]

A second dangerous consequence was seen to arise from the effects of the provision of milk and school meals on post-war parental responsibility. Whereas Macgregor and Carr-Saunders believed that the increased participatory role of the government reflected the growing aspirations of parents for their children[394], Cox argued that social policies only succeeded in revealing the most dissolute aspects of human nature. Based on the principle that individuals attached little value to what they got for nothing, the provision of such services led Cox to believed that post-war society was experiencing a profound diminution in parental interest and responsibility for the general wellbeing of their children. A similar criticism was directed at education. By making children slaves of the examination system, it was feared that schools and universities were producing a body of adults, largely uneducated as regards the importance of new scientific and technical

[392] Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, , p. 239
[393] Cox, H. (1927) 'Franchise Reform', pp. 195 – 196
[394] Macgregor, D.H. (1926) 'Family Allowances', *Economic Journal*, 26 (March), pp. 3 – 4; Carr-Saunders, A.M. (1937) 'Nutrition and Social Policy', *Political Quarterly*, 8, pp. 231 – 232

developments[395], whose only hope of employment was within the constantly expanding ranks of the civil service.

According to this interpretation of government expenditure, the excessive provision of public money was completely wasted, given that there appeared to be little useful economic outlet for a supposedly intellectually stimulated work force. Instead of contributing to a productive economy, social expenditure was seen to impede economic development by expanding yet further the corrosive effects of bureaucracy, while at the same time creating an emotionally stunted and mulish workforce.[396]

Support for Government Expenditure

The support for increased government expenditure covered several themes. We shall consider just three: the ability of expenditure to improve labour relations; the importance of education to the nations future productivity (human capital accumulation); and the ability of education, in its widest possible sense to overcome the nation's anxieties regarding Britain's economic future. This is not to suggest that economists were unquestioning in their acceptance of such expenditure. As will be seen below, a commitment to the benefits of government expenditure – particularly education – led to questions as to whether such expenditure was being used to its full advantage.

[395] Hilton, J., Scott Watson, J.A, & Huxley, J. (1934) 'A Three-Cornered Survey of Industrial Britain', p. 105

[396] Cox, H. (1923) 'A Conservative Program', *Edinburgh Review*, 237 (January), pp. 205 – 208; Cox, H. (1931) 'Our Financial Position and Prospects', p. 15; Cox, H. (1931) 'The Economy Report', p. 291

(1) Labour Relations

The shock of Britain's war-time transformation had revealed the realities of productivity losses incurred through class friction. The assiduity with which the labour movement had long adhered to union regulations, and the virtual sanctity conferred upon industrial arrangements, dictated the response of both labour and employers to industrial disputes. The effect of this had been to prevent all but the most imaginative from escaping accustomed modes of thought and union working rules. It necessarily followed that Britain's post-war transformation would be better assisted improved through harmonious industrial relations. We may consider Keynes and Robertson's suggestions regarding the ability of social expenditure to neutralise labour discontent. It was a possible labour view that employers' contributions to the health and unemployment insurance schemes had been financed by a (disguised) flat-rate deduction from wages. Inter-war industrial disruption was therefore seen to arise from a perceived attack on working class incomes. The provision of social services had the potential to ease industrial and social tensions by demonstrating to the working class that they could obtain substantial economic and social improvements without resorting to industrial disruption.[397]

(2) Education

It was clear that, prior to the 1891 abolition of fees in elementary schools, the inability of parents to meet the cost of education for their children was having serious

[397] Keynes, J.M. (1930) 'The Question of High Wages' in *Collected Writings of J.M. Keynes: Vol. XX: Activities, 1929 – 31*, London: Macmillan, pp. 13 – 16; Robertson, D.H. (1931) 'The World Slump' in Pigou, A.C. & Robertson, D.H. *Economic Essays and Addresses*, London: P.S. King & Son Ltd, p. 127

implications for the nation's general prosperity. Even in the post-war world, compulsory elementary education cost the State and local authorities more than most wage-earners would have been prepared to spend on their children. Under these circumstances, life for pallid children, raised and left to roam in overcrowded towns, appeared to centre on the mere mechanics of existence. This deplorable situation, which could never be compensated by an apparent indifference to pollution and noise, deprived growing generations of opportunities for vigorous development, and the nation of their full physical and intellectual abilities. It was feared that many children were leaving school without receiving proper elementary education or basic instruction in how to become proficient in a particular trade.[398] It was later suggested that the poor intellectual standard of the general labour force had been worsened through the pre-war actions of capitalists in drawing the more competent and ambitious workers from the shop floor and appointing them as supervisors and foremen.[399] With the belief that economic advancement required more than the physical strength of the labour force, the drainage of the intellectual pool and the absence of basic instruction served as a real, yet unmeasured, waste of human capabilities.

In the context of the inter-war economic debate, expenditure on education (rising from £31.8m in 1913 to £88.8m in 1931[400]) and the development of an enlightened education system, took on a new importance. Economic progress was not based on some exogenous unobservable process, descending like manna from heaven, but was influenced by education and the efficiency of labour inputs. It was

[398] Jevons, H.S. (1909) 'The Causes of Unemployment – I: Defects in Elementary Education', *Contemporary Review*, 95 (Jan/June), pp. 548 – 565; Jevons, H.S. (1911) 'Insurance and Training for the Unemployed', *Contemporary Review*, 99 (Jan/June), pp. 415 – 424

[399] Price, L.L. (1919) 'Labour Problems: Past, Present and Future', *Economic Journal*, 29 (June), p. 194. The implication of this was that those appointed to position of supervisors no longer considered themselves members of the working class.

[400] Cox, H. (1931) 'The Economy Report', p. 285

recognised that Britain's speedy adjustment to changed, post-war conditions would be influenced by national investment in the knowledge and skills base of "the human instruments of production"[401], and hence the ability of producers to utilise the increased energy and intellectual capacity of the labour force.[402] The scheme followed through into vocational education and the increased versatility of the nation: workers who had previously possessed only one vocational skill would acquire experience and ability in a variety of occupations.[403] It was also possible that improved education, and the ability to infuse interest in spiritual, intellectual, or recreational activities and amusements would go some way to compensate for the strain and monotony of repetition that characterised the modern production process.

There was a further advantage to expenditure on education. It was clearly recognised that the detrimental effects on productivity would be realised if taxpayers adopted a hostile attitude towards taxation. How could tax-payers be persuaded to accept something that they saw as economically damaging and wholly unintelligible? Arguments that focused on the importance of the compulsory re-distribution of income in overcoming the narrowness of working-class existence were simply not sufficient. Instead, it appears that contemporary writers sought to neutralise the detrimental effects on productivity by promoting awareness of the economic benefits associated with social expenditure. What the prejudiced taxpayer was inclined to dismiss as a net burden, the economist would, were applicable, seek to describe as productive expenditure that generated discernible benefits for business and society. Current outlays were justified on the basis of future productive benefits, thereby demonstrating that taxation required to finance social legislation policy was not a net

[401] Dalton, H. (1928) 'Review – 'A Study of Public Finance' by A.C. Pigou', p. 219

[402] Clay, H. (1932) 'The Economic Limits of Expenditure on Social Services', *Manchester School*, 3, p. 98

[403] Carr-Saunders, A.M. (1933) 'Current Social Surveys – Vocational and Adult Education', *Political Quarterly*, 4, p. 251

burden. To this end, Clay proposed improvements in the collection of government statistics in order to facilitate the publication of a "social budget" which would provide taxpayers with statistical proof of the benefits accruing from increased social expenditure.[404]

(3) Overcoming Anxieties

Education not only assisted the transition to a new equilibrium through improvements in the economic potential of human agents, but in a more subtle, far-reaching manner. We have already seen how inter-war economists identified emotional and psychological problems as an impediment to economic adjustment. Yet through a better appreciation of changing international and domestic economic conditions, an educated and instructed population could develop the confidence and flexibility required to reinvigorate market forces and so move the economy to its new equilibrium. To give one example of this, the agricultural economist, John Venn, noted that British farmers consistently promoted the view that they were subject to a crippling taxation burden arising from rates, tithe, land tax and income tax. This attitude appeared to have been fuelled by long-term rural attitudes towards social and religious issues, and a widespread ignorance regarding the activities of foreign agriculturists. Measures to educate farmers, argued Venn, and so explain the true position of domestic and international agriculture, were seen to be far more beneficial than alterations in taxation policy.[405]

Education was seen to extend beyond school or university education and the development of the technical skills of the labour force into the provision of important

[404] Clay, H. (1932) 'The Economic Limits of Expenditure on Social Services', p. 104

[405] Venn, J.A. (1928) 'The Incidence of Taxation in Agriculture', *Economic Journal*, 38 (December), pp. 570 – 572

public facilities, such as debating societies, and the urban and rural extension of the library system. Such facilities would develop the initiative and resourcefulness of the population, and so promote the mobilisation of a wider, educated democracy. Public exposure to library collections would demolish a psychological attitude that saw the private purchase of books as an extravagance[406], stimulate the national expression of ideas, and so facilitate the wider diffusion of knowledge.[407] Instead of dismissing public libraries as a scheme that allowed "servant girls...to read Miss Braddon"[408] at the expense of taxpayers and ratepayers, Cole believed that it was essential for society appreciated the educational benefits that resulted from a publicly available store of books.[409]

Questions About Education Expenditure

The importance of government expenditure in education led into other areas of the contemporary debate. One such example involved the government's action to combat the inequalities arising from family size and the distribution of wages. Given that wage rates were not determined according to family size – a fact that enabled childless workers to enjoy a surplus above their married co-workers – a proposed family allowance scheme would have seen the distribution of "allowances" (or "endowments") such that families larger than the average size received a larger family income compared with those smaller than the average size.[410]

[406] Keynes, J.M. (1927) 'Are Books Too Dear?', *Nation & Athenaeum*, 40 (12 March), pp. 786 – 788

[407] It was with some disdain that Cole later reported that only 15 per cent of national library expenditure was devoted to the purchase of books. Cole, G.D.H. (1927) 'The Public Library', *New Statesman*, 29 (16 July), p. 440

[408] Mary Elizabeth Braddon (1835 – 1915), popular, and extremely prolific Victorian novelist, once described as "the Queen of the circulating libraries."

[409] Cole, G.D.H. (1922) 'The Use of Public Libraries', *New Statesman*, 19 (1 July), p. 352

[410] Macgregor, D.H. & Rathbone, E. (1929) 'Should Wages be Supplemented by Family Allowances?', *The Listener*, 1 (27 February), pp. 237 – 238

Although the family allowance system was not introduced in Britain until after the Second World War, proposals for the system during the inter-war years raised a number of concerns amongst economists. The most obvious concern involved the machinery of public finance, for if the huge amount required to finance the allowance scheme (estimated at not less than £100m) was secured through income-tax, it would almost certainly reduce expenditure in other, and possible more economically beneficial, areas of social policy.[411] A second criticism focused more directly on the question of education, and reflected what Macgregor believed was a conflict between the idea of a "standard" family and the inevitable heterogeneity of satisfactions. Given that human pleasures, and hence expenditure patterns, altered between individuals and across times, the idea that the State could specify some form of "standard" family size was dismissed as palpable nonsense. Under the proposed system of direct family subsidies, the unmarried workers would be legally required to transfer a larger proportion of his income to the State. This implied that the increased opportunities available to married men and their families occurred at the expense of unmarried men. Yet fulfilment for the unmarried worker could involve a decision to satisfy his intellectual curiosity through the Adult Education Movement. The introduction of a family allowance scheme would therefore restrict him to the associated standard of living, so reducing any personal benefits for education in addition to any beneficial externalities for the wider economy.[412]

The dramatic rise in the cost per pupil also led to economic discussion regarding the quality of education and the technical questions regarding education reform. The British education system was widely regarded as an antiquated relic

[411] Cole, G.D.H. (1926) 'Family Endowment', *New Statesman*, 27 (24 April), p. 38
[412] Macgregor, D.H. (1926) 'Family Allowances', p. 4

staffed by inadequately trained teachers and operating in dilapidated buildings.[413] In 1924, the Chief Medical Officer's Report drew attention to draughty classrooms, inadequate playgrounds, and lack of sanitary accommodation (particularly in rural areas). The attitude of "economy" regarding school education would not only reduce the intellectual quality of a future workforce, but also deteriorated human dignity and aggravate health problems. While Cole believed that clamorous demands for public economy had, by the spring of 1924, evaporated from the national debate, it appeared to survive within local government by councillors who were committed to fulfil their election pledge to "ply the Geddes axe."[414] If the expenditure was recognised as grant aid from the Board of Education, Cole argued, there was a possibility something would be done to repair defective school buildings. However, for the vast majority of the time, it appeared that the inspectors did not both to draw attention to the appalling conditions within schools simply because they believed it would be a waste of their time.[415]

In other areas, the desire to secure public funds had led the Universities to repeatedly extol the benefits of education. Yet, as Cole again noted, the academic soliciting of public money brought to the fore questions regarding the "financial affairs and general behaviour" of Universities.[416] Did the time-honoured methods through which students absorbed information truly accord with the same economic and social purpose the Universities purported to provide? While established teaching methods possessed clear administratively advantages – attendance at lectures and tutorials demonstrated a students application to their studies, for example – Cole

[413] Cole, G.D.H. (1924) 'Other People's Children', *New Statesman*, 23, (10 May), p. 118; Cole, G.D.H. (1924) 'The Possibilities of Administrative Reaction', p. 69

[414] Cole, G.D.H. (1924) 'Mr Wheatley's Difficulties', *New Statesman*, 23 (24 May), p. 181

[415] Cole, G.D.H. (1924) 'Health In The Schools', *New Statesman*, 24 (22 November), p. 195

[416] Cole, G.D.H. (1922) 'University Reform', *New Statesman*, 19 (15 April), p. 35. Following the war, Oxford and Cambridge Universities had only averted financial crisis through separate grants of £30,000 per year and an influx of ex-servicemen.

expressed reservations as to their overall utility in equipping students with the elasticity of thought required for success in the post-war commercial environment.[417] There was also concern regarding the exaggerated expectations that university education instilled in students, most noticeably the belief that they would speedily enter well-paid positions of responsibility. University education was simply not seen as comparable with the degree of vocational flexibility required by employers. Freshly graduated students were of comparatively little value of businesses, owing to their lack of practical experience of the business environment.[418]

Summary and Conclusions

In this chapter, we have seen how different groups of inter-war economists approached the broad question of government expenditure, and connected it with Britain's post-war economic difficulties. We have see that while the majority of economists criticised post-war taxation, the question of government expenditure elicited different responses. One approach to this issue expressed a critical reaction against what was seen as the damaging social and economic consequences of excessive, unproductive, social expenditure.

A second approach was much more supportive of government expenditure, arguing that revenue secured through taxation could, if properly organised and promoted, be utilised as an engine for economic and social improvement. In the preceding chapters, we have seen how economists believed that the influence of erroneous economic arguments (protectionism and Imperial integration, for

[417] Cole, G.D.H. (1922) 'The Doubtful Value of Lectures in University Education', *New Statesman*, 20 (7 October), p. 8

[418] Keynes, J.M, Benn, E. & Walls, E. (1927) 'University Men In Business' (16 February) in *Collected Writings of J.M. Keynes: Vol. XIX: Activities, 1922 – 1929*, London: Macmillan, pp. 649 – 661; Jones, J.H. (1937) 'Some Notes on Training', *The Accountant*, 97 (24 July), p. 115

example), and the effects of psychological and emotional reactions was hindering Britain's post-war transformation. Under these circumstances, the act of demonstrating the importance of social expenditure reflected an attempt to nullify a negative psychology by advancing a positive psychology.

Expenditure on such measures as health, unemployment insurance, and old age pensions had the potential to reduce labour disputes and class friction by demonstrating to the working class that improvements in their post-war standard of living were provided socially. Similarly, increased publicity about such expenditure – particularly expenditure on education to promote human capital accumulation – could be used to overcome producers' resistance towards taxation by demonstrating that social expenditure enabled producers to draw upon a more efficient labour force. In this instance, economists were proposing a form of psychological legerdemain, for by appealing to the self-interests of different sections of the community – trade unions drawn towards aggregate welfare gains, producers concerned with positive productivity effects – the procedure appeared to serve as a constructive means of overcoming the combined problems of class friction and acute hostility towards taxation.

Expenditure was also seen to generate a significant positive educational externality in terms of whetting an immediate appetite for knowledge and stimulating freedom of thought. Through such education, the nation would eradicate entrenched pseudo-economic ideas and emotional reactions that were restraining the process of change. The nation's ability to adopt a more cosmopolitan outlook would instil an awareness and acceptance of Britain's changing economic position.

CHAPTER 6

EXCHANGE RATES

Introduction

Our investigation thus far has concentrated on contemporary interpretations of Britain's inter-war economic development. While this proves a sufficiently wide area of inquiry, it would be a fundamental error to exclude from our investigation some discussion of contemporary opinions concerning exchange rate fluctuations.

The intellectual mindset of pre-war British economics was inclined to ignore questions relating to exchange rates and currency stability. The pages of the *Economic Journal*, taken as a reflection of the trend of academic interest, demonstrate that between its inception in 1891 and the outbreak of the Great War, there appeared a mere 29 articles dealing with currency questions, of which 16 were devoted to solely Indian monetary issues. Occasional references do suggest some appreciation of exchange rate questions. The fall of the silver exchange below its 1905 – 07 level, and its effect in stimulating Chinese exports, for example, led Adam Kirkaldy to appeal for a re-evaluation of the importance of the subject.[419] Yet in the main, economists expressed absolute faith in the effortless efficiency of the existing monetary system while an atmosphere of intellectual apathy dismissed the theory of exchange rates as "abstruse", "uninteresting" and "mysterious."[420] The pre-war exchange between different currencies had been determined by corresponding

[419] Kirkaldy, A. (1915) 'Review – 'The Panama Canal and International Trade Competition' by L. Hutchinson', *Economic Journal*, 25 (September), p. 426
[420] Flux, A. (1924) *The Foreign Exchanges*, London: P.S. King & Son Ltd, p. 1

valuations of gold. With the quantity of gold in one sovereign equivalent to $4.8665, the freedom to transfer gold between countries ensured that the pre-war rates of exchange did not vary. With most leading currencies redeemable in gold, and with gold possessing universal purchasing power, the stability of the monetary unit appeared assured.

Britain's war-time and early post-war inflation problems had caused an escalation in the price level relative to that of the United States. The depreciation of the currency unit, and the apparently temporary breakdown in the established exchange system had ensured that, by 1920 "the nine pence of 1911 had dwindled…to four pence."[421] This, coupled with the prohibition on the exportation of gold, brought questions of exchange rates and currency stability to prominence. Since the autumn of 1915, the sterling-dollar exchange had been artificially maintained ("pegged") fractionally below the pre-war level. When the artificial support was terminated in March 1919, the exchange fluctuated wildly, falling from $4.765 (the war-time "peg") to $3.81 by December, touching $3.195 by early February 1920, before rising to within sight of the pre-war parity during the winter of 1922 – 23. In retrospect, it was inevitable that the volatility of the post-war foreign exchange market would bring about renewed interest in the theory of exchanges. The fickleness of currency exchanges following the breakdown of the Bretton Woods system in the 1970s serves as a perfect illustration of the extent to which scholarly interest is galvanised during periods of exchange-rate instability.

The first section of this chapter will concentrate on inter-war impressions surrounding the volatility of the sterling-dollar exchange during the period 1919 – 1925, and contemporary perceptions of the purchasing power parity theory. The

[421] Jones, J.H. (1926) 'Currency Stability', *The Accountant*, 74 (9 January), p. 37

second section focuses on events surrounding the restoration of the gold standard in 1925. The final section deals with the contemporary debate that surrounded the unanticipated European financial crisis of 1931, and growing market concerns regarding Britain's deteriorating financial position.

Index Numbers, Speculation, and the Sterling-Dollar Exchange

Eichengreen had suggested that the inter-war misalignment of price levels serves as the "point of departure" for virtually all discussions of exchange rate problems.[422] While the intellectual history surrounding the influences of price levels on the rate of exchange may be traced to the sixteenth century Salamancan School, the systematic development of purchasing power parity, as a theory of exchange-rate disequilibria, is attributable to the war-time writings of the Swedish economist, Gustav Cassel.[423]

In the modern historiography, fluctuations in the sterling-dollar exchange, covering the period 1921 – 25, correspond to the theory of exchange rates predicted by fundamentals. An econometric assessment presented by Thomas during the early 1970s attributed the determination of the exchange to a variety of fundamentals, including levels of real incomes, British and American price levels, and the interest rate differential between the two countries.[424] A separate review, conducted by

[422] Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 - 1939*, New York: Oxford University Press, p. 104

[423] Whether Sweden's abandonment of the gold standard in early 1916 stimulated the development is PPP is open to debate. There is evidence to suggest that Cassel had formulated his theory before 1914.

[424] Thomas, L.B. (1973) 'Behaviour of Flexible Exchange Rates: Additional Tests from the Post-World War I Episode', *Southern Economic Journal*, 40, pp. 167 – 182

Hodgson, also emphasised the high explanatory power of fundamentals.[425] A distributed-lag model developed by Hodgson and Phelps concluded that price-level movements explained 94-per-cent of variations in the sterling-dollar exchange between April 1919 and April 1925.[426] Similar views were reflected in the inter-war literature. For example, based upon separate investigations of the movements of British and American monthly price indices over the period 1919 to 1921, both Norman Crump[427] and J.H. Jones[428] concluded that the exchange had adjusted to reflect relative price movements in the two countries subject to the seasonal influence of short-term credit requirements to cover agricultural transfers.[429] This suggested that the primary difficulty in securing a speedy return to gold lay with a general fixation with the nominal value of the exchange (which, of course, had fallen relative to its pre-war level), and hence a general ignorance that descriptions of "high" or "low" exchange rates were irrelevant without some reference to purchasing power parities.

The fact that inter-war economists identified movements in the sterling-dollar exchange in terms of the respective price levels has several important implications. First, the development of index numbers in many European countries had been stimulated by the spectre of post-war inflation, and the importance of such indices in the use of purchasing power parity calculations. Yet the use of price indices inevitably called forth the troublesome question of measurement. In an ideal world, precision in definition and representatives of commodities would leave no room for

[425] Hodgson, J.S. (1972) 'An Analysis of Floating Exchange Rates: The Dollar-Sterling Rate, 1919 – 1924', *Southern Economic Journal*, 39, pp. 249 – 257

[426] Hodgson, J.S. & Phelps, P. (1975) 'The Distribution Impact in Price-Level Variations on Floating Exchange Rates', *Review of Economics and Statistics*, 57, p.61

[427] Crump, N. (1921) 'A Review of Recent Foreign Exchange Fluctuations', *Journal of the Royal Statistical Society*, 84 (May), pp. 432 – 435

[428] Jones, J.H. (1922) 'Foreign Exchange', *The Accountant*, 66 (18 March), pp. 377 – 382

[429] The special conditions associated with agricultural fluctuations, and later the restoration of the gold standard, will be considered in greater depth below.

ambiguity. In reality, the construction of a perfectly accurate index number – be it arithmetic, harmonic, or geometric – was impossible. If we consider the economists who examined the construction and reliability of price indices – the most obvious examples being Bowley[430] and Edgeworth[431] – we may argue that their attachment to the subject arose from a deeper interest in mathematics and statistics. It can therefore be seen that the majority of economists ignored the theoretical difficulties associated with the construction of index numbers. Indeed, Hawtrey believed that the use of index numbers in calculating the sterling-dollar purchasing power parity demonstrated the operation of a fully efficient market: commodity dealers rapidly translating prices from one currency into another according to the prevailing rates of exchange.[432]

Yet having said this, inter-war economists did not accept what Barkai has described as the "clear-cut dependence of the rate of exchange on comparative price levels."[433] It is well documented that the chequered history surrounding the purchasing power parity doctrine has led to a misconception. Although monetary factors were identified as the primary long-term influence on exchange rates, Cassel did *not* argue that such monetary conditions were the sole determinant of the exchange.[434] Even allowing for the apparent statistical verification of the purchasing power parity doctrine, many inter-war economists did not accept that the position of

[430] Bowley, A.L. (1926) 'The Influence on the Precision of Index-Numbers of Correlation Between the Prices of Commodities', *Journal of the Royal Statistical Society*, 89 (March), pp. 300 – 319; Bowley, A.L. (1928) 'Notes on Index Numbers', *Economic Journal*, 38 (June), pp. 216 – 237

[431] Edgeworth, F.Y. (1918) 'The Doctrine of Index-Numbers According to Professor Wesley Mitchell', *Economic Journal*, 28 (June), pp. 176 – 197; Edgeworth, F.Y. (1923) 'The Doctrine of Index-Numbers According to Mr. Correa Walsh', *Economic Journal*, 33 (September), pp. 343 – 351; Edgeworth, F.Y. (1925) 'The Plurality of Index-Numbers', *Economic Journal*, 35 (September), pp. 379 – 388

[432] Hawtrey, R.G. (1921) 'Discussion on Mr. Norman Crump's Paper', *Journal of the Royal Statistical Society*, 84 (May), p. 443

[433] Barkai, H. (1993) 'Productivity Patterns, Exchange Rates, and the Gold Standard Restoration Debate of the 1920s', *History of Political Economy*, 25, p. 7

[434] Holmes, J.M. (1967) 'The Purchasing Power-Parity Theory: In Defence of Gustav Cassel as a Modern Theorist', *Journal of Political Economy*, 75, p. 686

the sterling-dollar exchange could be purely expressed by relative price movements. The most obvious non-monetary influence was speculation. Yet since the sterling-dollar exchange had only deviated from its purchasing power parity to the extent of agricultural fluctuations, many contemporary writers did not believe that speculation had exerted any significant influence. This view is, on the whole, consistent with the main findings of modern historiography: research conducted by Thomas dismissed the effect of speculation on the exchange during the early 1920s[435], while an examination of contemporary financial reports led Hodgson to conclude that speculative movements, if they existed, followed cycles of very short duration.[436]

The consistent position of the sterling-dollar exchange contrasted with the increasing divergence of the actual sterling value of franc, mark and lira, and the calculated purchasing power rates. This latter situation appeared to have arisen from two influences. The first of these involved "inflation expectations", whereby speculators formed their expectations in the light of the purchasing power parity doctrine, and were seen to have become extremely anxious regarding the attitudes of the French, German, and Italian governments towards future currency expansion.[437] The act of discounting the expected effect of future currency expansion, argued Gregory, ensured that many speculators would only accept such currencies on increasingly worse terms for sellers.[438] Bickerdike, however, questioned the plausibility of the "inflation expectation" argument. If there was an immediate depreciation in the external purchasing power due to speculation of inflation, he

[435] Thomas, L.B. (1973) 'Behaviour of Flexible Exchange Rates: Additional Tests from the Post-World War I Episode', p. 181

[436] Hodgson, J.S. (1972) 'An Analysis of Floating Exchange Rates: The Dollar-Sterling Rate, 1919 – 1924', p. 254

[437] Pigou, A.C. (1920) 'Some Problems of Foreign Exchange', *Economic Journal*, 30 (December), p. 469

[438] Gregory, T.E. (1921) 'Discussion on Mr. Norman Crump's Paper', *Journal of the Royal Statistical Society*, 84 (May), p. 449; Gregory, T.E. (1921) *Foreign Exchange Before, During and After the War*, Oxford: Oxford University Press, p. 90

reasoned, why were dealers in other commodities – wheat, for example – not immediately raising their prices (internal purchasing power) in anticipation of the same phenomenon? To the modern observer, Bickerdike's argument appears to reflect an ignorance of the asymmetric relationship between the adjustment speed of asset markets and goods markets. Nonetheless, for him, the relationship between the depreciation of the German mark and variations in German retail prices did not correspond with the scenario presented by writers who emphasised the importance of currency inflation. It was his contention that the continuation of war-time trade restrictions, such as import restrictions or increased transport costs, prevented private traders from exploiting profit opportunities by selling American goods in Europe. This situation was seen to exert a continuing influence on European exchange rates.[439]

The second speculative influence reflected the so-called "underworld of commerce and finance" who, according to E.M.H. Lloyd, successfully encouraged speculation in European currencies.[440] This view was reiterated some years later by Paul Einzig, who characterised the early post-war period as a "golden age" of exchange rate speculation, when everyone, "big or small, from Vienna to Valparaiso", readily gambled on the movement of the German mark and French franc.[441]

Let us briefly summarise the preceding discussion. While it was accepted that "inflation expectations" were influencing the movement of the main European currencies during the early 1920s, the relationship of the dollar exchange and the

[439] Bickerdike, C.F. (1921) 'Review – 'Foreign Exchange, Before, During and After the War' by T.E. Gregory', *Economic Journal*, 31 (December), p. 520; Bickerdike, C.F. (1922) 'Internal and External Power of paper Currencies', *Economic Journal*, 32 (March), pp. 30 – 38

[440] Lloyd, E.M.H. (1921) 'Reparations: A Revue in Five Acts', *New Statesman*, 18 (10 December), p. 279

[441] Einzig, P. (1934) 'Speculation in Exchanges', *The Banker*, 30 (May), p. 112. When compared with the madness of the 1920s, exchange speculation during the 1930s had become a rich man's game.

calculated purchasing power parities was seen by economists to dismiss any suggestion that there existed a ceaseless drive of day-to-day speculators influencing the movement of the sterling-dollar exchange. This theme, as we have suggested, corresponds with modern historiography. Yet within the contemporary literature, there remained the view that the doctrine of purchasing power parities did not provide a direct valuation of the sterling-dollar exchange. According to many economists, the main exchange deviated from it purchasing power parity based on the influence of short-term credit requirements to cover seasonal agricultural transfers. It is this latter theme that we shall now explore.

Agricultural Transfers

The following outline of the influence of agricultural fluctuations on the sterling-dollar exchange reflects a contemporary appreciation of the post-war environment surrounding exchange rates and the continuing need to settle debts in foreign currencies. In the pre-war economy, the timing of the purchase of seasonal agricultural products – wheat, tobacco, cotton, for example – had long meant that industrialised nations were indebted to the agricultural countries during the autumn and winter months. In order to ensure that they obtained the necessary quantities, on the best terms, once the harvests were collected, the industrialised nations established financial preparations for the purchase of agricultural goods during the late summer and early autumn months.[442] Such transactions reflected seasonal requirements for short-term credits. The pre-war certainty of the gold points had financed such activity, so leading to the smooth transfer of floating balances between London and

[442] Dearle, N. B. (1929) *An Economic Chronicle of The Great War For Great Britain and Ireland 1914 – 1919*, p. 321

New York. In the post-war world, the abandonment of the gold standard had dramatically altered this situation. Whilst normal agricultural pressures remained, the loss of exchange rate security had presented bankers with the impossible task of satisfactorily calculating arbitrage profit. This implied that the pre-war requirements of seasonal credits to finance crop movements ceased to be an activity of arbitrage banking, and increasingly became the province of specialised exchange speculators. In a world of uncertain exchange rates, and given the combined shortage of both professional exchange speculators and speculative capital, it was evident to both Keynes and Bickerdike that a substantial movement in the exchanges in the late summer and autumn months was required to entice increasingly wary speculative capital with at least the prospect of securing profits at a later date.[443] In other words, the downward movement of the sterling-dollar exchange during the autumn months, and the one significant point of deviation between the exchange and the calculated purchasing power parity, was therefore interpreted as a deliberate measure to facilitate the transfer of agricultural goods by reducing exchange risks for speculative capital. It is perhaps worth pointing out that by 1924, economists had begun to downplay the influence of agricultural transfers. By this stage, it was clearly Jones's view the while seasonal transfers had influenced the sterling-dollar exchange prior to 1924, such forces after this date had had been off-set by the transfer of liquid capital from New York to London and the growing mood of optimism.[444] We shall return to this theme below.

[443] Bickerdike, C.F. (1920) 'The Instability of Foreign Exchange', *Economic Journal*, 30 (March), pp. 121 – 122; Keynes, J.M. (1923) 'The Foreign Exchanges and the Seasons' (19 May) in *Collected Writings of J.M. Keynes: Vol. XIX: Activities, 1922 – 1929*, London: Macmillan, pp. 89 – 90; Keynes, J.M. (1971) *Collected Writings of John Maynard Keynes: Vol. IV – A Tract on Monetary Reform*, London: Macmillan p. 91

[444] Jones, J.H. (1925) 'Five Per Cent', *The Accountant*, 72 (14 March), p. 421

What does the above discussion tell us? First, it is important to appreciate that the intellectual climate of the period was drawn towards the relationship between agriculture and economic activity. Before the War, Herbert Stanley Jevons had attempted to present fresh evidence to support his father's idea of a "solar commercial cycle", with fluctuations in trade associated with the periodicity of sunspots and weather cycles.[445] It should not be forgotten that a large proportion of Robertson's trade cycle theory centred on the effects of variations in the exchange value of agricultural goods against the products of other industries[446], and reflected his belief in the importance of agriculture within the wider sphere of human existence. Suggestions that agricultural production could easily be absorbed into the general theories of economic activity were erroneous according to Robertson's interpretation of the economy.[447]

Agriculture is therefore significant in illuminating both inter-war views on the relationship between agriculture and industry, but also understanding the questions that surrounded the need to facilitate agricultural movements in a period when the long-held stability of the gold standard had vanished. The War may have (temporarily) destroyed the security of the gold standard, but it had been unable to destroy the forces of nature. Yet it is this contemporary relationship between agriculture and economic activity that modern historiography had tended to ignore. In his study, Thomas admitted (briefly) that the regression residuals of his econometric model did suggest the existence of seasonal patterns:

[445] See, for example, Jevons, H.S. (1909) 'The Causes of Unemployment – III: Trade Fluctuations and Solar Activity', *Contemporary Review*, 96 (July/December), pp. 165 – 189; Chapman, S.J. (1910) 'Review – 'The Sun's Heat and Trade Activity' by H.S. Jevons', *Economic Journal*, 20 (September), pp. 399 – 401

[446] Robertson, D.H. (1915) *A Study of Industrial Fluctuations*, London: P.S. King & Son Ltd.

[447] A similar view was later expressed by Roy Harrod, who argued that the general characteristics of agriculture were incompatible with the theory of imperfect competition. Harrod, R.F (1936) 'Imperfect Competition and the Trade Cycle', *Review of Economic Statistics*, 18 (May), pp. 84 – 85

> "The seasonal element in the residuals probably reflects seasonal patterns in demand for (or availability of) particular products (and thus foreign exchange) that are independent of price level and income level phenomena."[448]

In this instance, seasonal exchange variability is not reflected in the construction of the model but is inferred from the movement of fundamentals and econometric techniques.

Without going into great detail, it is sufficient to say that by having concentrated on fundamentals, and so largely ignoring the influence of agricultural transfers or market reaction to the absence of long-established exchange stability, economic historians have ignored market attitudes that could have influenced early inter-war exchange rate movements.

The Return To Gold

In this section we shall concentrate on contemporary discussion of events surrounding the restoration of the gold standard in April 1925.

From the end of the War, it had appeared that gold had lost its prestige as the ideal international standard of value. In 1919, for example, Hawtrey had pointed to the growing concern that stability in the value of gold was dependent on both the quantity of accumulated gold stocks relative to the annual supply, and the continuing demand for gold as currency. With the war-time adoption of paper currency having contracted the demand for gold, liberated gold supplies had exceeded world industrial demands. America's switch from debtor to a creditor nation had also

[448] Thomas, L.B. (1973) 'Behaviour of Flexible Exchange Rates: Additional Tests from the Post-World War I Episode', p.170

altered the position of world gold supplies. With America demanding payment for exports (instead of the pre-war position of the United States exports representing payment of interest and loans on European capital), and the external value of the European currencies remaining below their internal values, both gold stocks and the annual mine production had been thrown onto the American market (where gold had retained its currency function).[449] The need to secure international monetary stability therefore provided ample opportunity for action. Bastable argued that post-war currency disturbances afforded an ideal opportunity for society to make a bold and expansive effort to introduce internal currency reform (such as the decimal system) and develop a new international standard of value (thereby implementing the ideas of the Paris Conference of 1867).[450] Yet although the gold standard had lost its international prestige, and was no longer regarded as a "royal road to economic prosperity"[451], any deficiencies inherent in the system appeared immaterial given the wider effects of disrupted international trade in relation to the world's economic wellbeing. As Hawtrey and Cannan pointed out, it was the limited nature of the difficulties associated with restoring the gold standard that ensured that the gold standard was the most desirable standard for the immediate future.[452]

By early 1925, the fervour of excitement that gripped the foreign exchange market appeared only to have been exceeded by "interest in the scoring board at the Adelaide cricket ground", with any weakness in the pound creating "almost as much

[449] Hawtrey, R.G. (1919) 'The Gold Standard', *Economic Journal*, 29 (December), p. 431
[450] Bastable, C.F. (1920) 'Review – 'War-Time Financial Problems' by H. Withers', *Economic Journal*, 30 (March), p. 95
[451] Robertson, D.H. (1921) 'The Restoration of a Gold Standard' in Clapham, J.H. et al *Monetary Policy – Being The Report of a Sub-committee on Currency and the Gold Standard*, London: P.S. King & Son Ltd, p. 65
[452] Hawtrey, R.G. (1919) 'The Gold Standard', p. 434; Cannan, E. (1925) 'The British Gold Standard Restored' (23 May) in *An Economist's Protest*, p. 408

disappointment as the fall of an English wicket."[453] The appreciation of the sterling-dollar exchange over the latter half of 1924 and early 1925 – from approximately $4.20 to $4.80 – was viewed with both enthusiasm and concern. On the one side, market enthusiasm was clearly a consequence of the expected psychological and material benefits that a restored gold standard would provide to the international economy. This theme is reflected in both Drummond and Barki's comments that the restoration of the gold standard signified a belief in the return of prosperity through the revival of world trade.[454] Amongst contemporary commentators, it is reasonable to suppose that the previous close correlation between the actual sterling-dollar exchange and the calculated purchasing power parity suggested only a minute possibility that the exchange would depart from purchasing power parity in the immediate future. The evidence suggested that Britain was bound upon a return to gold.

On the debit side, the sterling-dollar exchange appeared to represent a highly precarious force, strongly influenced by market enthusiasm and capable of reversal at any movement. It was perfectly possible that since the inducement to purchase sterling diminished as the exchange neared the pre-war parity, the sudden profit taking instinct of speculators would cause a sharp decline. Thus, although apparently settled in its movement towards parity, uncertainty surrounding both the nature and permanency of the forces generating the transfer of liquid balances led a number of economists to examine the process through which the restoration of gold was being conducted.

[453] Jones, J.H. (1925) 'The Return to Gold', *The Accountant*, 72 (31 January), p. 181

[454] Drummond, I.M. (1986) *The Gold Standard and the International Monetary System, 1900 – 1939*, London: Macmillan, p. 30; Barkai, H. (1993) 'Productivity Patterns, Exchange Rates, and the Gold Standard Restoration Debate of the 1920s', pp. 3 – 7

Our story may be examined from two perspectives: the "historical" perspective and the "contemporary" perspective. The "historical" perspective concerns the importance of relative price levels, discount rate polices, and the Gold Embargo Act. The first important feature involved the Federal Reserve Board's decision, over the course of 1924, to reduce its rediscount rate in stages (from 4.5 per cent to 3.5 per cent in June and to 3 per cent in August), while the Bank of England raised its rate from 4 per cent to 5 per cent. The effects of the lower American discount rate generated a rise in the American price level, so facilitating an alteration in the value of the dollar in terms of other currencies. It is worth nothing that, based on his econometric model, Hodgson concluded that a 1 per-cent increase in the American price level had been sufficient to generate a 1.29-per-cent appreciation in sterling.[455]

The "pro-Gold Embargo Act" argument has fixed its ideas on a common theme. Writers including Pollard, Broadberry and Eichengreen have sought to argue that the assistance of liquid balances in moving the exchange towards parity reflected speculators seeking to secure a profit by buying in expectation that the pre-war parity would be restored before the beginning of 1926. This expectation was seen to have been strengthened by the anticipated expiry of the Gold and Silver Export Control Act on 1 January 1926, while the return of a Conservative government in 1924 made it unlikely that the Act would be extended.[456] In this scenario, each intermediate link in the chain is tested and deemed secure, for as sterling moved towards it pre-war

[455] Hodgson, J.S. (1972) 'An Analysis of Floating Exchange Rates: The Dollar-Sterling Rate, 1919 – 1924', p. 252

[456] Pollard, S. (1969) *The Development of the British Economy, 1914 – 1967*, p. 218; Broadberry, S. (1986) *The British Economy Between the Wars: A Macroeconomic Survey*, p. 123; Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 – 1939*, p. 165

parity during late 1924 and early 1925, the British authorities were forced to either accept the return to gold or delay it.

The "contemporary" perspective centres on the forces that governed contemporary expectations around the period 1924 – 1925. Contemporary economists argued that the rise of the exchange rate was a reflection of optimistic expectations, fuelled by particular economic and political conditions at that moment in time, regarding the rejuvenation of the British and European economy. This is not to suggest that contemporary economists ignored the importance of fundamentals. It is clear that contemporary appreciation of Cassel's purchasing power doctrine had led economists to interpret the movement of the sterling-dollar exchange partly in this light.[457] Yet in seeking to explain the forces governing the dollar value of sterling, economists adopted a more diffuse appreciation of the prevailing economic and political environment. Their overall impression appears to have been influenced by the view that the dramatic appreciation of the exchange exceeded the rate that could be justified by the relative price levels of the two countries, even with the discount rate differential operating in Britain's favour. For example, Jones's asserted that there were "other things in life than discount rates"[458], while Keynes emphasised "abnormal factors" that were influencing the transfer of liquid capital.[459]

What were these "abnormal factors"? The main explanation drew attention to the actual time period – the mid-1920s – and the expected renaissance of the international, and particularly the European, economy. In order to gain some understanding of this, we must first recall the extent of contemporary faith that both

[457] Jones, J.H. (1925) 'The Return to Gold', *The Accountant*, 72 (31 January), pp. 181 – 182; Jones, J.H. (1925) 'Bank Rate and Deflation', *The Accountant*, 72 (21 March), p. 460

[458] Jones, J.H. (1925) 'The Bank Rate Controversy', *The Accountant*, 72 (28 March), p. 499

[459] Jones, J.H. (1925) 'The Return to Gold', p. 181; Keynes, J.M. (1925) 'The Return Towards Gold', *Nation & Athenaeum*, 36 (21 February), pp. 707 – 709

the war-time and early post-war economic literature had expressed towards the recurring movement of the trade cycle. As we saw in Chapter 1, the post-war depression had initially been viewed as a temporary phenomenon that would be eventually corrected through the normal movement of the cycle. While economists came to question the curative properties of the cycle, post-war extrapolation of the pre-war cycle had led many others to identify the mid-1920s as the expected date for post-war economic recovery. This expectancy was clearly fuelled by a number of events. First, French and Belgian occupation of the Ruhr in 1923, and the subsequent disruption of German coal production, had served as a fillip to the British coal industry, and so contributed to a partial British recovery during 1923 – 24. Secondly, the Conservatives electoral defeat in December 1923, and the formation of the first Labour Government, had forced an extraordinary shift in Britain's political landscape. Whereas this initially appeared to reinforce the threat of socialism, Snowden's budget statement was unexpectedly benign, reducing government expenditure to a tolerable level, and following many of the principles of Conservative finance.

In retrospect, the tone of Snowden's budget was not entirely unexpected: Baldwin had expected to win the general election (thereby allowing an inexperienced Prime Minister to impose his authority[460]), while the Labour government had come to power half-way through the financial year. Yet it was the sensible nature of Snowden's budget speech, argued George Paish, which relieved business anxieties regarding the intended policies of the new government.[461] Not only had Labour steered clear of introducing penalising taxation, but businesses had been freed from the Corporation Profit Tax (although this had been largely ineffective in generating

[460] Williamson, P. (1999) *Stanley Baldwin: Conservative Leadership and National Values*, pp. 27 – 29
[461] Paish, G. (1924) 'Financial Conditions Abroad', *Current History (New York)*, 20 (June), p. 524

revenue), while may others, ranging from middle-class tenants to "eaters of lollipops and drinkers of ginger-beer", had enjoyed concessions.[462] Snowden's decision to repeal the 33.3 per cent *ad verolem* McKenna Duties on motor cars, pianos, watches and clocks, as well as reducing duties on, amongst other things, tea (8 *d.* to 4 *d.*) and sugar (2¾ *d.* to 1¼*d.*) led an astonished Francis Hirst to describe Labour's first budget as an endorsement of the "gospel of Cobden" and outright rejection of the "gospel of Marx."[463] In one gesture, it appeared that free trade had regained the momentum it had lost since 1914.[464] G.D.H. Cole expressed a belief that the Labour Party had, by 1923, thrown aside the "naked and largely unreasoned simplicity" regarding working-class solidarity in order to "broaden its appeal, and become a party really speaking to all classes."[465] The general conclusion, as E.M.H. Lloyd observed, was that the society had not been frightened by "Socialist finance."[466]

A third theme concerned the prevailing mood of European optimism. This had been stimulated by the decisive actions of Hungary, Poland and Spain in tackling their financial problems; the successful German stabilisation of the Rentenmark following its introduction in November 1923; and, possibly most significantly, a desired settlement of the Reparations issue following the publication of the Dawes Plan in April 1924.[467] Cole also reflected on the moderate resumption of diplomatic and economic relations with Soviet Russia, and expressed the hope that this would influence the stability of trade relations with other European countries.[468] This was

[462] Lloyd, E.M.H. (1924) 'A Transition Budget', *New Statesman*, 23 (3 May), p. 85
[463] Hirst, F.W. (1924) 'Free Trade – Its Annus Mirabilis', *Contemporary Review*, 126 (July/Dec), p. 153
[464] A different interpretation was provided by Shadwell, who argued that Labour's advocacy of free trade was, in reality, the political endorsement of Marx's claim that free trade hastened the onset of revolution. Shadwell, A. (1924) 'Letter – Socialism and Free Trade', *The Times* (9 July), p. 15, c.F
[465] Cole, G.D.H. (1923) 'The Labour Voter', *New Statesman*, 22 (1 December), p. 234
[466] Lloyd, E.M.H. (1924) 'A Transition Budget', p. 87
[467] Paish, G. (1924) 'Financial Conditions Abroad', p. 524 – 535
[468] Cole, G.D.H. (1924) 'First Steps Towards Industrial Revival', *New Statesman*, 22 (26 January), p. 444

not to ignore the potential sources of international concern: political and economic worries in India, South Africa, and South America, and the dramatic fall in the Japanese exchange (attributable to Japans reconstruction following a devastating earthquake in September 1923) all provided sources of financial anxiety. Yet in the main, the transfer of liquid capital was taken as the physical manifestation of increased investors' confidence in the European economy resulting from the publication of the Dawes Plan.[469]

In a slightly different context, Jones argued that exchange movements reflected the response of both British and American investors regarding the likely effect of the Dawes Plan on the relative position of American and European investments. Jones argued that the publication of the Dawes Report had led British and American investors to liquidate American investments based on the expectation that future net rates of interest on American (domestic) investments, irrespective of the Wall Street boom, would diminish relative to rates obtainable in Europe. This appears to reflect market activity based on Keynes's famous idea that the prosperity of Europe depended on the "prosperity and enterprise of Germany." [470] This decision was further fuelled by the appreciation of the exchange: as the sterling-dollar exchange rose, the dollar value of British investments in America declined. This combination of forces was identified as another cause behind the transfer of liquid capital, and hence the movement towards parity.[471] It is worth noting that during the autumn of 1924, Keynes had doubted the success of the Dawes Plan, arguing that its

[469] For a contemporary discussion on the Dawes Plan, see Hobson, J.A. (1924) 'The Economics of the Dawes Plan', *Contemporary Review*, 126 (July/Dec), pp. 279 – 286; Guillebaud, C.W. (1924) 'The Economics of the Dawes Report and the London Agreement', *Economic Journal*, 34 (December), pp. 540 – 555

[470] Keynes, J.M. (1971) *Collected Writings of John Maynard Keynes – Vol. II: Economic Consequences of the Peace*, p. 10

[471] Jones, J.H. (1925) 'The Return to Gold', p. 182

provisions would tend to deter foreign investment in Germany.[472] This prediction was quickly proved false, with the influx of American capital alone increasing by $102.9m between 1924 and 1925.[473] Having been forced to change his opinion, Keynes identified a different mechanism to Jones, and argued that the Dawes Report had provided an ideal European outlet for American optimism engendered by the Wall Street investment boom.[474]

The Foreign Exchange Crisis of 1931

Historians have traditionally interpreted the sterling crisis of July – September 1931 within the wider context of European financial instability. On 11 May 1931, Austria's most important commercial bank, the *Kredit-Anstalt*, found itself in serious difficulties. This apparently domestic financial crisis had far-reaching consequences, especially in light of extensive foreign investments in Central European.[475] In Germany, for example, successive balance of payment deficits, and demands for working capital, had been met by a combination of long-term and short-term foreign loans secured in London, New York, Holland, Sweden and Switzerland.

The developing shock to international confidence precipitated a large-scale withdrawal of foreign loans as bankers scrambling to improve the liquidity of their

[472] Keynes (1924) 'The Dawes Scheme and the German Loan', *Nation & Athenaeum*, 36 (4 October), pp. 7 – 8

[473] Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 – 1939*, p. 150

[474] Keynes, J.M. (1925) 'The Return Towards Gold', pp. 707 – 709

[475] Foreign claims on the Kredit-Anstalt alone amounted to £15m. Jack, D.T. (1931) *The Crisis of 1931*, London: P.S. King & Son Ltd, p. 5. In his autobiography, Paul Einzig claimed that a visit to Vienna in June 1931, to investigate the collapse of the *Kredit-Anstalt*, had led him quickly to the conclusion that Britain would shortly be forced off the gold standard. He abstained from publishing his views in his daily newspaper column, *Lombard Street*, on the ground that it would only have intensified the ongoing crisis. Einzig, P. (1960) *In The Centre of Things*, London: Hutchinson & Co. Ltd, p. 82

positions. Late in May 1930, the crisis spread to Germany with the Reichsbank losing \$250m in international reserves during the first three weeks of June. This situation was only temporarily allayed in late June by the announcement of the Hoover proposal for a one-year moratorium on principle and interest payments on all public international debts.[476] Although eventually agreed, Hoover's proposal was initially delayed by the indecisive response of the French Government. Eventually a rediscount credit of £20m granted by the Central Banks of England, France and America, in conjunction with the Bank of International Settlements, temporarily alleviated the difficulties faced by the Reichsbank. Increasing foreign uncertainty, however, and the bankruptcy of the North German Wool Combine, renewed foreign withdrawals, and eventually forced the German government to temporarily close all banks and savings banks by decree. Similar suspensions were followed in Vienna, Romania, Latvia, and Poland.

With frantic attempts by foreign banks to strengthen their liquidity, the Bank of England began to lose gold for export.[477] Before 1914, London's financial system had able to balance the loss of short-term funds through its bill portfolio. By 1931, however, London's bill portfolio no longer consisted of "first class commercial bills", but bills frozen by international moratoria or Treasury bills that were unacceptable abroad.[478] This forced the Bank of England's gold reserves to meet the strain.

Of the two main government publications during this period – the ("Macmillan") Committee on Finance and Industry and the ("May") Report of the

[476] Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 – 1939*, p. 277
[477] Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 – 1939*, pp. 280 – 281
[478] Pollard, S. (1969) *The Development of the British Economy, 1914 – 1967*, p. 226

Committee on National Expenditure – contemporary attention was focused on the former. When established, the Macmillan Committee had been intended to discharge one particular function: an examination of the effect of post-war economic conditions on Britain's economic and financial system. The inter-war period saw the publication of many official reports, including the Colwyn Committee on Taxation and the National Debt, and the series of reports of the Balfour Committee on Industry and Trade. Yet although all of these dealt with aspects of the economic situation, no government publication had been so eagerly awaited as that of the Macmillan Report, and the supposed authoritativeness with which it was expected to detail the economic landscape.

If irony serves as the lifeblood of history, then Stamp's remark that the report had "set out to enlighten the general uninstructed state of the public mind"[479] appears curiously ironic given the position of the Report's conclusions in the historical evaluation the ensuing crisis. The role of the Macmillan Report in the financial crisis is traditionally explained by reference to its publication in July 1931, and its estimation of London's net short-term debtor position of approximately £254m. This unenviable position had arisen from an unhealthy use of employing short-term funds in long-term investments that could not readily be realised. Yet it is curious to note that amongst all of the eminent economists who offered their opinions on the Report during the summer months of 1931, not one of them argued that the Report's revelations regarding London's short-term assets justified the extent of the ensuing financial crisis. Indeed Robertson was eager to applaud the Committee for its success in calculating the extent of London's net balance of short-term indebtedness.[480]

[479] Stamp, J.C. (1931) 'The Report of the Macmillan Committee', *Economic Journal*, 41 (September), p. 424

[480] Robertson, D.H. (1931) 'Views on the Macmillan Report – II', *Banker*, 19 (September), p. 189

Stamp did raise the suggestion that events following the Reports publication had "amply justified" its conclusion that the influx of foreign short-term balances served as a potential weakness for the exchanges, but failed to elaborate on the relationship between the Report and the ongoing financial situation.[481] Instead, immediate impressions focused on the stylistic and analytical quality of the Report in relation to the Committee's original terms of reference[482]. For example, Cole viewed it as a "great advance on any previous document dealing with banking policy"[483]; Robertson described it as "excellently written", with "page after page of lucid description and interesting analysis"[484]; Stamp regarded it as "easily the best up-to-date text-book of the financial system"[485], while Hobson saw it as the "fullest and most searching study of the monetary apparatus of this country that has been made."[486] Of all the economists who commentated on the Report, Jones was possibly the most critical of the Committee's work, and dismissed the purported "mosaic representation of the economic system" as nothing more than a "crude and unenlightening summary" assembled from various League of Nations reports.[487]

The second report – which attracted less attention amongst economists[488] – was the ("May") Report of the Committee on National Expenditure published on 31 July. In the historical interpretation, this was seen to have strengthened market fears regarding Britain's deteriorating financial position. The May Committee had been

[481] Stamp, J.C. (1931) 'The Report of the Macmillan Committee', p. 429
[482] The Macmillan Report was divided into two main sections – "Historical and Descriptive" and "Conclusions and Recommendations" – followed by several addenda written by various committee members.
[483] Cole, G.D.H. (1931) 'Money, Wages and Expansion', *New Statesman & Nation*, 2 (18 July), p. 70
[484] Robertson, D.H. (1931) 'Views on the Macmillan Report – II', p. 189
[485] Stamp, J.C. (1931) 'The Report of the Macmillan Committee', p. 425
[486] Hobson, J.A. (1931) 'Off The Gold Standard', *Contemporary Review*, 140 (July/Dec), p. 555
[487] Jones, J.H. (1931) 'The Macmillan Report – I', *The Accountant*, 85 (1 August), pp. 139 – 141
[488] For contemporary discussion on the May Report, see Keynes, J.M. (1931) 'Some Consequences of the Economy Report', *New Statesman & Nation*, 2 (15 August), p. 189; Jones, J.H. (1931) 'National Economy', *The Accountant*, 85 (23 August), pp. 287 – 290; Keynes, J.M. (1931) 'Notes on the Situation', *New Statesman & Nation*, 2 (29 August), p. 246; Cox, H. (1931) 'The Economy Report', pp. 284 – 292

established following calls for an independent review of government finances given the enormous increase in expenditure at a time when trade depression had reduced yields on taxation. The Report concluded that government policy was biased in favour of expenditure, and argued that an immense impending budgetary deficit – estimated at £120m – could only be avoided by stiff reductions in rates of remuneration in the public services, the abolition of some Government departments and services, and the postponement of development schemes (the total proposed economies amounting to £97m).[489]

As the financial crisis developed, Jones adhered to a belief that the weakness of sterling did not reflect Britain's financial position, and indeed went so far as to argue that there was no direct connection between the two phenomena.[490] The severity of the ongoing economic depression made it obvious that very few industrialised nations could have escaped a deterioration in income from "invisible" items in the balance of payments (particularly earnings from shipping and foreign investments). A similar conclusion reflected estimates of London's net short-term liability, with the Macmillan Reports categorically stating that the position of London's total net liabilities in March 1931 (£254m) showed a continuing downward trend, with a reduction of £20m from the end of 1930, and a reduction of £48m from the total net liability at the end of 1928.[491] Not only had Britain demonstrated her commitment to the noble principles of internationalism by continuing to invest in foreign long-term securities (in contrast to France and America's decision to retain much of their surplus capital in liquid form[492]), but the strength of her financial system (through her position as a creditor nation) appeared to make it definite that

[489] Pollard, S. (1969) *The Development of the British Economy, 1914 – 1967*, p. 213
[490] Jones, J.H. (1931) 'The Macmillan Report – III', *The Accountant*, 85 (15 August), p. 253
[491] Jack, D.T. (1931) *The Crisis of 1931*, pp. 16 – 17
[492] Jones, J.H. (1931) 'The Macmillan Report – II', *The Accountant*, 85 (8 August), p. 197

Britain could weather any financial crisis. Even following the international moratoria – leading to £5m of Austrian debts rendered illiquid, an estimated £70m of German debts frozen, and the Chilean government's deferral of interest payments on British loans – many expressed their faith in the strength of the financial system.[493]

It was simply not credible, argued Jones, so suppose that, even allowing for the international depression and the creeping paralysis affecting Europe's financial system, that the actual position of Britain's finances could precipitate the withdrawal of liquid balances on such a dramatic scale.[494] As Hobson pointed out shortly after Britain's departure from gold, Britain's overseas financial position and the problems concerning the budget deficit had been recognised for months by those who carefully followed economic events.[495] This led to the suggestion that some intermediary was jeopardising the stability of sterling by presenting a distorted impression of Britain's true financial position. This intermediary was identified as the British and foreign Press who, acting as the relentless oracles of doom, were seen to be forcing the withdrawing of foreign balances by presenting lurid and inaccurate images of Britain's financial position.

In many ways, the reaction of the Press appeared perfectly natural. The majority of the public had long expressed a preference for excitement (as demonstrated by their love of sporting events) while being generally averse to dense commentary on political or financial events. The Press had therefore responded to the public's preference for excitement by exaggerating the significance of domestic and world events. To quote Cole on this matter:

[493] The extent of Britain's foreign assets, and her continued ability to liquidate them, was used by the General Council of the Trades Union Congress as evidence to condemn Government plans to reduce unemployment payments during the financial crisis.
[494] Jones, J.H. (1931) 'The Macmillan Report – III', p. 253
[495] Hobson, J.A. (1931) 'Off The Gold Standard', p. 554

> "[T]he handling of the political [and economic] crisis and the comments upon it in such newspapers as the *Times* have been such as to make the situation very much worse than it need have been."[496]

Hirst also reported that newspapers in the United States and Europe were actively spreading "the evil tidings" of Britain's financial position[497], while Jones stated that, even though the weakness of sterling did not reflect Britain's financial position, the nation would only have the Press to thank were she to face a severe exchange crisis.[498] Having travelled to America in early September 1931, and with his sources of information restricted purely to the American newspapers, Jones later remarked that the American press had drawn particular attention not only to Britain's financial position, but also the short lived naval mutiny in Invergordon.[499] It is interesting to note that while American attention on the naval mutiny drew upon the disputes that had heralded the Russian and German Revolutions, the Invergordon situation does not appear to have attracted the attentions of economists resident in Britain during the crisis.

The attitude of the British Press during this period was also taken to be a response to another theme, namely the public's long-standing ignorance regarding local and national finance. The controversy that had surrounded the publication of the Geddes and the May Reports, claimed Clay, clearly demonstrated that the public was "vague in its ideas" towards all areas of public expenditure.[500] Instead of attempting to properly understand the course of post-war national balance sheets, Hirst believed that the nation had for too long taken refuge in the claim that public

[496] Cole, G.D.H. (1931) 'Was It A Bankers Conspiracy?', *New Statesman & Nation*, 2 (29 August), p. 245

[497] Hirst, F.W. (1931) 'The Second Budget of 1931 – And Why It Was Necessary', *Contemporary Review*, 140 (July/Dec), p. 431

[498] Jones, J.H. (1931) 'National Economy', p. 287

[499] Jones, J.H. (1931) 'The Departure From Gold', *The Accountant*, 85 (31 October), p. 567

[500] Clay, H. (1932) 'The Economic Limits of Expenditure on Social Services', p. 85

finance accounts were impenetrable to all but the "high priests of a specialised cult."[501]

Cox believed that the origins of a national indifference to all questions of public finance arose from the creation of a peremptory House of Commons following the 1911 Parliament Act, and the influence of an enlarged electoral franchise on political decision making and financial responsibility.[502] We shall briefly outline Cox's argument.

The move towards full electoral equality, following the Representation of the People Acts (1884 and 1918) had created constituencies composed of tens of thousands of voters. While it was true that a greater number of people had been brought within the income-tax limits, the distribution of the burden of direct taxation only fell upon a comparatively small proportion of the electorate. In 1918 – 19, only 4% of aggregate government revenue was secured through direct taxation on working class incomes.[503] Even in 1930, the number of voters equalled approximately 25 million, while the number of income tax payers barely amounted to 2.2 million.[504] This had developed into a situation, Cox believed, in which prospective Members of Parliament tailored their political and financial messages for financial extravagance to the majority (the least responsible members of society who paid little, if any direct taxation, and were ignorant of public finance) rather than the minority. Further more, the creation of huge constituencies ensured that candidates, irrespective of their party allegiances, required the full weight of a carefully organised party political machine in order to win their campaign. This appeared to have created a situation in which each elected member was forced to become the

[501] Hirst, F.W. (1931) 'An Emergency Budget', *Contemporary Review*, 139 (Jan/June), pp. 684 – 685
[502] Cox, H. (1927) 'The House of Lords', *Edinburgh Review*, 246 (October), pp. 393 – 394
[503] Whiting, R.C. (1990) 'Taxation and the Working Class, 1915 – 24', *Historical Journal*, 33, p. 897
[504] Cox, H. (1931) 'The Economy Report', p. 288

obsequious servants of an authoritarian political machine, with tyrannical discipline ensuring that each member of the parliamentary party follow the prescribed course.[505]

The extension of the local and parliamentary franchise established a secondary problem by divorcing electoral attitudes from financial responsibility. This constitutional anomaly had been intensified by the local government administrative procedure referred to as "compounding of rates", under which owners of residential or commercial properties received commissions for paying the rates instead of leaving payment to the occupants. With what appears to have been a widespread belief that the payment of rates was the administrative responsibility of the landlords, such a system served as a great convenience for tenants: rates were collected with rents on a weekly basis, so relieving any concern in meeting the half-yearly charge (although, overall, the tenant paid more to the landlord for the privilege). This situation had, according to Cox, created the deplorable effect of isolating the majority of the working-class electorate from any interest in questions of finance (beyond the confines of their own household), and so relieving local and national authority of any serious electoral pressure on behalf of economy.[506]

Taking Cox's argument in conjunction with the others outlined above, we are presented with an impression that the financial markets throughout the summer of 1931 were not reacting to a genuine appraisal of Britain's financial position, but an over-sensationalised accounts provided by a British Press who were largely ignorant of financial affairs. The *Times* editorial for Wednesday 19 August, for example, was

[505] Cox, H. (1929) 'Parliamentary Government', pp. 178 – 179; Cox, H. (1931) 'Our Financial Position and Prospects', p. 12
[506] Cox, H. (1927) 'Franchise Reform', pp. 198 – 201

insistent "on the extreme urgency of the situation", and the need for immediate action to prevent a financial crisis.[507] The problems posed by an uneducated Press had been noted in other circumstances throughout the inter-war period. In 1922, E.M.H. Lloyd had attacked press coverage of the Auditor-General Report on Britain's war-time state trading activities as a flagrant misrepresentation of the facts.[508] In the same year, Josiah Stamp suggested that the national attitude towards the problem of taxable capacity had been unduly influenced by a hasty remark by Reginald McKenna, delivered before the National Union of Manufacturers in June 1920, that the maximum limit of Britain's taxable capacity was £1,000m. Stamp believed that the press had seized upon McKenna's off-the-cuff remark as an authoritative calculation, thereby giving it "currency as a kind of axiom in a way that he [McKenna] would not have desired."[509]

With the announcement that London's short-term assets were insufficient to cover her short-term liabilities, the foreign exchange market bore the brunt of evaporating confidence in Britain's economic and financial stability. The Bank of England attempted to obtain credits from the Bank of France and the Federal Reserve Bank of New York. However, the foreign banks required assurances that the opposition parties would support the government in their attempts to follow an economic program aimed at securing a balanced budget. Cole developed upon this idea, arguing that foreign demands concerning Britain's future budgetary policy had been initiated by press coverage of Josiah Stamps and Jacque Rueff's "very dubious calculations about the effect of the dole on unemployment."[510] Cole believed that the

[507] *The Times* (19 August 1931), p. 11, c. B
[508] Lloyd, E.M.H. (1922) 'State Trading, 1917 – 1921', *New Statesman*, 20 (28 October), p. 101
[509] Stamp, J.C. (1922) *Wealth and Taxable Capacity*, Ltd, pp. 123 – 125
[510] Cole, G.D.H. (1931) 'Was It A Bankers Conspiracy?', p. 245. Two articles written by Stamp – entitled 'Work and Wages' – had appeared in *The Times* on 11 and 12 June 1931.

hesitancy of the foreign banks in giving assistance indicated that they were influenced by Rueff's economic theory, leading to the belief that the unemployment benefit was the root cause of Britain's economic difficulties, with the 1930 – 31 budget deficit reflecting the attractiveness of benefits relative to wages. A reduction in unemployment benefit was taken as the key to ensuring economic stability.

By early August 1931, the Deputy Governor of the Bank of England warned that unless the government acted quickly, that Britain would be bankrupted. A National Government, made up of representatives from all three parties, was established in August 1931, thereby presented the impression that Britain was united in tackling the ongoing financial crisis.

In a radio broadcast delivered in early September 1931, Clay attempted to illustrate the full extent of Britain's financial position. Instead of arguing that foreign suspicions of Britain's finances had been guided by economic theory or exaggerated Press speculation that Britain was teetering on the edge of a financial precipice, Clay believed foreign financiers were merely responding to post-war events in Austria (1920) and Germany (1922 – 23).

Britain's difficulties, Clay argued, stemmed from financial intransigence: not only was all Government expenditure regarded as "sacrosanct", but there was tendency to downplay the dangers of inflation. "We are inclined," he argued, "to look down on the Germans and other Continental nations because they let their currencies slip." Yet given Britain's precarious position – with neither the budget nor her international accounts balanced – Clay believed that Britain could not ignore the dangers of inflation. Clay sought to dismiss the possibility of abandoning the gold standard by highlighting the dangerous consequences that the abandonment of gold would have on unemployment and the problem of economic recovery. It was also conceivable, he argued, that a sudden collapse in the exchange could lead foreign exporters to refuse payment in sterling. In short, unless the gold standard was preserved, Britain faced a dismal future.[511]

Yet whereas Clay was pessimistic in early September 1931, Keynes showed signs of remarkable optimism. It is interesting to wonder whether this optimism was actually a disguise for a deliberate stratagem. During August and September 1931, Keynes suggested that Britain could convert disaster into success by winning the hegemony of a new Currency Union within the Empire countries, and with a new currency unit created by devaluing all currencies within the Union by at least 25 per cent. The main suggestion was that the British government should "demand an international conference" to settle the gold standard issue. Given the aggregate nature of the world's problems, it appears surprising that Keynes contemplated the possibility that the British government could "demand" any such conference. On first examination, it may suggest that Keynes did not believe the crisis to be a significant danger to the stability of the exchange. Yet on closer examination, a proposed conference appeared to represent a deliberate attempt to secure the continuation of the gold standard. Before any such conference could meet, Keynes argued, it would be necessary for Britain to introduce emergency measures to restrict foreign exchange dealings and prohibit the export of domestic capital. Although Britain would not seek to raise any further credits abroad, she would submit to a further drain on gold. The intention was not simply to preserve London's financial prestige, for with London the hub of the financial system, connected via a network of credit, Keynes believed that his proposal represented the only chance of "saving the financial structure of the whole world." The proposed measures represented a deliberate stratagem, an attempt to turn the tables on other nations: if Britain was not

[511] Clay, H. (1931) 'The Pound In Danger', *The Listener*, 6 (16 September), p. 441

seeking to raise further credits, and was not seeking to prevent a drain on gold, it implied that Britain was not staking her reputation on preserving the gold standard. If Britain were forced off gold, it would have been due to others nation's deciding not to "play the rules of the game."[512] Through this act of brinkmanship, Keynes was hoping that the conference would save the international gold standard, albeit on new and modified terms.

All such attempts were to no avail, and following a continuing rapid drain on the Bank of England's gold reserves throughout September, the newly formed National Government was forced to suspend gold convertibility.

Post-September 1931: Agriculture, Patriotism, and Inflation

Following devaluation in September 1931, sterling was required to take its chance on the foreign exchange market. The sterling exchange movements during the immediate post-gold standard period are well documented: sterling fall from $4.86 to $3.24 by early December 1931, remaining at around $3.40 – $3.45 during January and February 1932, before rising to $3.80 by late March.[513]

[512] Keynes, J.M. (1931) 'A Gold Conference', in *Collected Writings of J.M. Keynes: Vol. XX: Activities, 1929 – 31*, London: Macmillan, pp. 598 – 602

[513] Dimsdale, N.H. (1981) 'British Monetary Policy and the Exchange Rate 1920 – 1938', *Oxford Economic Papers*, 33, p. 329. Throughout the spring of 1932 there were calls for an efficient mechanism capable of off-setting speculative movements in the sterling exchange. The British government eventually established the Exchange Equalisation Account (or Fund), so heralding the era of large-scale currency manipulation. For a contemporary discussion of the events leading up to the creation of the Account and its subsequent activities see Einzig, P. (1932) 'Exchange Control', *The Banker*, 24 (October), pp. 19 – 21; Einzig, P. (1933) 'The Exchange Equalization Account', *The Banker*, 25 (March) pp. 206 – 210; Einzig, P. (1936) 'Decline in Foreign Exchange Business', *The Banker*, 38 (April), pp. 52 – 54; Einzig, P. (1936) 'The Exchange Equalization Account's New Tactics', *The Banker*, 38 (May), pp. 124 – 127; Einzig, P. (1937) 'Exchange Equalization Account and Forward Dollars', *The Banker*, 42 (April), pp. 34 – 38

Both Broadberry and Eichengreen have interpreted these dramatic movements as an instance of exchange rate "overshoot", with the differential adjustment speeds of asset market relative to goods markets causing the exchange rate to deviate ("overshoot") its long-run purchasing power parity equilibrium value.[514] The rudimentary principles of this idea may be found in the following quote, written by Noel Hall in 1935:

> "[E]arly in 1932 it seemed that, as a result of the rapid liquidation of the financial crisis, the pound would rise externally before the internal system had had time to adjust itself to the new level of the exchanges."[515]

The eventual rise of sterling during the spring of 1932 has been attributed to growing market confidence following the repayment of French and American credits used up during the defence of sterling the previous September, and diminishing fears of financial disorganisation and an inflationary spiral under a regime of unbalanced budgets.[516] In the case of the dramatic fall of the exchanges, the modern interpretation rests on the operation of differential adjustment speeds, with the subsequent rise of sterling interpreted through the mechanism of market expectations. An examination of articles written during or immediately after the period of exchange volatility offers a number of different interpretations.

Contemporary economic interpretations began from a simple question: given that from April 1925 until September 1931, the sterling-dollar exchange had remained at approximately $4.86, what had caused the exchange to move so

[514] Dornbusch, R. (1976) 'Expectations and Exchange Rate Dynamics', *Journal of Political Economy*, 84, pp. 1161 – 1176; Broadberry, S.N. (1986) *The British Economy Between the Wars: A Macroeconomic Survey*, p. 127; Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 – 1939*, p. 302, n. 28

[515] Hall, N.F. (1935) *The Exchange Equalisation Account*, London: Macmillan, p. 3

[516] Eichengreen, B. (1992) *Golden Fetters: The Gold Standard and the Great Depression, 1919 – 1939*, p. 303

dramatically from its par value following the suspension of gold? Suggestions that the dramatic fall in the exchange reflected the disparity between American and British prices were dismissed as an inadequate explanation. Writing almost immediately after the suspension of the gold standard, economists such as Jones, Gregory and Einzig believed that the influence of relative price movements had been smothered by a combination of short-term forces that had both pressed and restrained the downward movement of the exchange.

On one level, the increased demand for transfer facilities was interpreted as the response of American investors who, having been unable to liquidate their British investments prior to 21 September, where now anxious to transfer their capital. This situation was complicated by the fact that an increased demand for foreign exchange was coming to a market in which the supply of foreign funds – secured through shipping earnings and interest payments – had been reduced due to the world economic depression.

Returning to the old theme of seasonal variability in the exchanges, it was argued that the depreciation in the exchange had arisen from the unfortunate coincidence between the abandonment of gold and the seasonal movement of agricultural imports. Sterling was traditionally strong during the summer months and weak during the winter months due to the seasonal purchase and payment of foreign goods. For many years, trade had been facilitated by liquid capital and temporary credits, both of which were drawn upon to supply foreign exchange. With British liquid capital having been frozen by international moratoria, the absence of the crucial stabilising force had led to a precipitate fall in the exchange.[517] Jevons added

[517] Jones, J.H. (1931) 'The Fall in Sterling', *The Accountant*, 85 (12 December), p. 764; Jones, J.H. (1932) 'The Rise in Sterling', *The Accountant*, 86 (12 March), p. 328

that the exchange had suffered from the general uncertainty surrounding British tariff policy.[518] Given the long shadow of the political and economic crisis, the attention turned to what Gregory and Robertson believed was a reinvigorated sense of British patriotism. This sense of patriotism, however, was identified in different locations. The first example, suggested by Robertson, concentrated on a negative view of patriotism, with fears that government expenditure cuts (and in particular the effects on teachers' salaries) would awaken "a sense of patriotic guilt" amongst the better off members of the community, and so lead them to reduce their consumption of domestically produced goods and services. Although unconnected with the question of the exchange rates, the fact that Robertson expressed this view in the context of the post-September 1931 environment should serve to reinforce our own awareness of the importance that contemporary writers attached to the theme of patriotism.[519]

Gregory's view was more straight forward: the feeling of national unity evoked by the abandonment of the gold standard, and the general nature of Britain's economic predicament, led individuals to express a preference for domestic over foreign holidays. It was therefore suggested that the decision of British citizens to restrain from taking foreign holidays had reduced the demand for foreign exchange.

Attention now centred on examining those forces that were preventing the exchange from falling further. The fact that the reduction in the exchange value of sterling had reduced the value of sterling debts was seen to have generated an inter-temporal shift in the demand for foreign currencies. Given this favourable, yet wholly unexpected, opportunity provided by the departure from gold, Gregory believed that foreign debtors had purchased sterling, in excess of what they would

[518] Jevons, H.S. (1931) 'Letter – Value of the Pound', *Times* (5 December), p. 6, c. B
[519] Robertson, D.H. (1931) 'The Economic Situation', *Cambridge Review*, 53 (23 October), pp. 48 – 49

other wise have bought, and so supported the exchange. The exchanges had therefore been prevented from falling further at that particular moment in time as well as, *ceteris paribus*, prevented from rising further than it would have done in the future.[520]

Sterling's durability as a commodity centred on the stability of the domestic price level. There had existed a fear that while Britain's departure from gold would confer a bonus on her export industries, any potential benefits would be off-set by the rise in the price of vial imported raw materials and food-stuffs. Increases in the price of imported commodities would alter the cost of living, thereby creating an increase demand for higher wages, and so initiating an inflationary spiral. Given this threat, Jones believed it was necessary for Britain to speedily abandon the cost of living as the regulator of wages and salaries, and only allow wage adjustments sufficient to "remove excessive inequalities." Such a policy would, he argued, secure confidence in the world as to Britain's intentions, and so prevent any further depreciation of the exchange. Precisely how Jones proposed to assess any "excessive inequalities" by abandoning a cost of living measure is unclear.[521] In other quarters, the issue of post-devaluation inflation was seen to have originated from market fears regarding the return of a Labour government during the October 1931 general election. Cole took it upon himself to refute the "charges of cowardice and irresponsibility" levelled against Labour. Market fears did not reflect "reckless propaganda" regarding the Labour Party, he argued, but a worry regarding "British honesty" if any government sought to deliberately stabilise the exchange rather than allowing market forces to

[520] Gregory, T.E. (1932) *The Gold Standard and Its Future*, London: Methuen & Co. Ltd (2nd edition), p. 68

[521] Jones, J.H. (1931) 'The Departure From Gold', *The Accountant*, 85 (31 October), pp. 567 – 568

determine the level.[522] It was certainly suggested by Gregory that the success of the National Government during the general election[523] owed a great deal to the fear of unbalanced budgets and inflation (even though every political party had disclaimed any intention to resort to such a policy).[524] In retrospect, it is probable that support for the National Government was also influenced by the electorates' acceptance of protectionism, and the expectation of contracting preferential arrangements with the Dominions. As we have already argued, these were themes that contemporary writers sought to undermine, both to assist Britain's economic development and defend the structure of economic theory.

By the spring of 1932, there was a growing belief that the threat of inflation had been exaggerated. While economic theory had predicted an increase in the cost of living index, the unfavourable consequences of the devalued exchange had not occurred: unemployment had fallen, the cost of living index had recorded only a slight increase, while various indices suggested that prices had actually fallen over the period 1930 – 31. Gregory attributed this unexpected situation to a variety of factors. First, the fear of being charged with "profiteering", especially given the economic confusion during the autumn of 1931 and the persistence of the world depression, was seen to have diminished the willingness of both producers and retailers to raise prices to the extent of the fall in sterling. Secondly, Britain's abandonment of gold had been followed by "practically the entire raw-material producing world", thereby reducing Britain's dependence on gold standard countries, and so maintained prices at a constant level.[525]

[522] Cole, G.D.H. (1931) 'The Danger of Inflation', *New Statesman & Nation,* 2 (24 October), pp. 505 – 506

[523] The result was a virtual landslide for the National Government, with the coalition winning 554 seats in the House of Commons, of which some 473 were Conservative.

[524] Gregory, T.E. (1932) 'Whither The Pound?', *Nineteenth Century,* 111 (April), p. 433

[525] Gregory, T.E. (1932) 'Whither The Pound?', pp. 432 – 436

Expectations Regarding London's Future Position

A more rounded interpretation of the movement of the exchanges following Britain's departure from gold was provided by Paul Einzig, and representing what he believed was the central attitude of the financial markets. Over the autumn of 1931 and the early spring of 1932, Einzig published several articles in which he attempted to assess the impact of the abandonment of gold on the various markets – discount market, bullion market, and foreign loans market – that characterised London's financial system. The importance of the interconnected structure of London's financial system was clear for all to see: bullion transactions had a prominent position in the foreign exchange market, with foreign firms dealing in bullion maintaining sterling accounts in London.[526]

Einzig suggested that the fate of the sterling exchange was not connected with fears of inflation, but with questions regarding London's future role as an international financial centre. This theme reflected Foxwell's earlier pronouncement that London's acknowledged position as the centre of international finance ensured that sterling was more than a mere unit of account.[527] For Einzig, exchange movements were a manifestation of evolving market assessments regarding London's, and hence sterling's, future role within the international financial system. Let us reconstruct this argument.

As a consequence of market uncertainty, it was suggested that British banks had directly contributed to the dramatic movement of the exchanges during the latter half of 1931. This effect had its origins in the established banking practice that while foreign banks maintained large sterling balances in London, British banks had failed

[526] Einzig, P. (1932) 'The Future of the London Bullion Market', *Banker*, 21 (February), p. 237
[527] Foxwell, H.S. (1922) 'The Pound Sterling', *The Accountant*, 67 (25 November), p. 769

to develop adequate balances in foreign financial centres. With the gold standard suspended, and doubt surrounding sterling's future role as a "universal means of payment", British banks had hurriedly sought to accumulate balances of francs, reichmarks and guilders in foreign centres. In other words, the desire of British banks to protect themselves against uncertain future commercial needs was seen as contributing to exchange rate volatility.[528]

Even before the gold standard had been suspended, Einzig argued, the decline in foreign demand for sterling bills was evidence of a growing international distrust towards British banking houses. Following Britain's departure from gold, this distrust was seen to have turned to a fear (or a hope) that London would be permanently eliminated from the discount market. This appeared to have strengthened both Paris and New York's attempts to capture London's dominant position within the international system. Yet by January 1932, wrote Einzig, distrust had turned to support as foreign financiers had come to recognise the indispensable character of the London discount market to international trade. "While the dollar and franc remain stable," he wrote, "French banks have failed by the dozen and American banks by the hundred."[529] British banks possessed astrength of international goodwill and respect that could not easily be destroyed. Any prestige lost through the depreciation of sterling had been counteracted by the international communities' realisation of the strength and stability of Britain's financial system.

It was evident that the activities of the London bullion market had significantly increased following the suspension of the gold standard. Apart from the continued supply of South African gold, both Einzig and Jones believed that London bullion brokers and refiners had been kept busy by large shipments from India, a

[528] Einzig, P. (1931) 'Future of the London Exchange Market', *The Banker*, 20 (November), p. 110
[529] Einzig, P. (1932) 'Future of London's Discount Market', *The Banker*, 21 (January), pp. 34 – 36

result of the appreciation of gold in terms of the rupee at a time of Indian economic and political uncertainty.[530] A similar argument is presented by Balachandran, who suggests that with the rupee pegged to sterling, the depreciation of sterling caused the price of gold, expressed in both currencies, to rise.[531] Yet where as Einzig and Jones saw the appreciation of gold in terms of the rupee as a direct consequence of the abandonment of gold, Balachandran identifies it as an indirect force that modified the effects of suspension.

As with the London discount market, Einzig believed that, following the events of September 1931, Paris had acted on the assumption that her bullion brokers and refiners possessed the ability to establish a gold market capable of rivalling, if not over-taking, London's privileged position.[532] Uncertainty regarding the stability of the franc had ensured the successful operation of an active retail gold market throughout France. It was this that appeared to have generated the belief that Paris was capable of capturing London's position as the world's leading gold market. But while Paris possessed a strong domestic gold market, it gradually became apparent that her ability to establish an international gold market would have necessitated the re–routing to Paris of gold already marketed in London. In this respect, London possessed a strong organisational advantage arising from the regularity of shipping routes between India and South Africa. Further more, it was becoming increasingly apparent that France possessed inadequate large-scale refining facilities. Attempts by the Comptoir Lyon-Alemand to exploit existing under-utilised facilities collapsed with the failure of the firm.[533] The realisation that gold was continuing to flow into

[530] Einzig, P. (1932) 'The Future of the London Bullion Market', p. 234; Jones, J.H. (1932) 'The Rise in Sterling', *The Accountant*, 86 (12 March), p. 328

[531] Balachandran, G. (1996) *John Bullion's Empire: Britain's Gold Problems and India Between the Wars*, Richmond: Curzon Press, p. 180

[532] Owing to Federal Reserve policy, Einzig did not believed that the New York market had seriously considered establishing an open gold market.

[533] Einzig, P. (1932) 'The Future of the London Bullion Market', pp. 234 – 236

London, and the fact that no other financial centre was capable of capturing London's predominant position as the world's leading open gold market, were both seen to have contributed to growing confidence in the London financial system by the spring of 1932.

Although not exerting a strong influence on the foreign exchange market, Einzig's nonetheless believed that some account had to be made regarding the effect that the resumption of large-scale foreign lending had on international attitudes toward London. Before 1931, Britain's foreign loans had largely been directed towards the Dominions and South America. During this period, other financial centres had sought to expand their operations. The belief that London would be the first among the great leading centres to resume foreign loan activities arose from a belief that the problems of defaults during the 1931 crisis had discouraged many foreign investors. If foreign governments and foreign borrowers required loans, it was to London that they would turn.[534]

In attempting to view the situation through Einzig's eyes, we may form the following conclusions. Einzig presented his assessment of the effect of changing circumstances, and evolving market expectations regarding the future of sterling and London's financial system, within the framework of supply and demand. Following Britain's departure from gold, there was uncertainty surrounding whether sterling had permanently lost its status as the principle international currency, coupled with uncertainty whether London had permanently lost her role as the world's banker. This marked degree of uncertainty manifested itself in a dramatic swing in the sterling exchange, first with foreign balances hurriedly withdrawn from London, and second with British banks hurriedly acquiring foreign balances in other financial

[534] Einzig, P. (1932) 'Future of London's Foreign Loan Market', *The Banker*, 22 (April), pp. 21 – 23

centres. Once it became apparent that neither New York nor Paris were capable of capturing London's discount market or open gold market, and with growing optimism surrounding the future of the foreign loans market, liquid balances were transferred back to London. Elements of these themes were repeated by Jones, who argued that while both America and France desired to possess the world's most powerful financial centre, this desire was not equalled by their abilities or temperaments: America appeared unable to demonstrate the strength of her financial machinery, while France was dismissed due to her unwillingness to fully accept the responsibilities that such a position would entail.[535] For Einzig, the sterling-dollar exchange had benefited once reticence had disappeared, and international respect and confidence had enable London to re-establish her position as the financial centre of the international economy. By April 1932, we find Einzig remarking that "in spite of the suspension of the gold standard, London has retained her supremacy as the world's best foreign exchange market and bullion market."[536]

Income Tax Payments

The final section that we shall consider in this chapter concentrates on a theme developed in Einzig's 1933 book, *The Comedy of the Pound,* in which he presented another interpretation of the movement of sterling during the early months of 1932. Einzig argued that the depreciation and subsequent revival of sterling after September 1931 reflected not simply evolving market expectations regarding the stability of London's financial system, but also psychological reactions amongst

[535] Jones, J.H. (1929) 'London and New York As Financial Centres', *The Accountant* 81 (19 October), p. 459; Jones, J.H. (1931) 'The Departure From Gold', pp. 567 – 568

[536] Einzig, P. (1932) 'Future of London's Foreign Loan Market', pp. 21 – 23

foreign financiers to impressions of Britain's actions in overcoming the financial crisis. The most important of these, he argued, was the "spectacular phenomenon of income tax payments".[537]

In an emergency budget (10 September 1931), the newly formed National government had both raised the standard rate of income tax from 4*s*.6*d*. to 5*s*., while reducing the exemption limit for unmarried persons from £130 to £100, and for married persons from £225 to £150.[538] With the next instalment of the income tax set for 1 January 1932, the nation had been requested not to defer income tax payments until the final notice. The national response to this was reported in *The Times* on 2 January 1932:

> "The request of the nation for early payments of the three-quarters instalment of income-tax which fell on New Year's Day met with a most satisfactory response in London yesterday. The offices of the collectors of income-tax in the City were kept "phenomenally busy" in the words of an official. He said that it was the most active New Year's Day in their experience, and afforded striking evidence of the patriotic way in which every one seemed anxious to help in the national necessity."[539]

In Birmingham, it was claimed that the percentage of the total charge for one district alone was "about six times" that of the 1931 level; Cardiff officials reported they had "never known anything like it"; while an official in Leeds described the rush to pay as "entirely without precedent."[540] Following the publication of the returns, it was reported that Exchequer receipts had "improved in a period of nine days to the extent of...£9,583,000".[541] Although pressure on collectors eased by the

[537] Einzig, P. (1933) *The Comedy of the Pound*, London: Kegan Paul, Trench, Trubner & Co Ltd, p. 56
[538] Hirst, F.W. (1934) *The Consequences of the War on Great Britain*, p. 224
[539] *The Times* (2 January 1932), p.7, c. E
[540] *The Times* (5 January 1932), p. 12, c. E
[541] *The Times* (13 January 1932), p. 12, c. F

second week of January, there remained hopes that, until the end of March, such sizeable payments of income tax and surtax would continue. Although there was little material effect of such early payments, Einzig argued that the foreign Press had interpreted such actions as a sign of Britain's response to the importance of sound finance. Put another way, the prompt payment of income-tax was seen to have exerted a dramatic psychological effect on foreign investors perception of sterling.

Summary and Conclusion

In this chapter, we have examined inter-war economic discussions surrounding the movement of the sterling-dollar exchange from 1919 to 1925, and events surrounding the abandonment of the gold standard in September 1931.

On first examination, these themes appear to be distinct from ideas presented in previous chapters. Yet on closer examination, it can be seen that their presentation complements our ongoing theme of understanding contemporary perceptions of the economy. In this respect, exchange rates represents one of the most interesting areas for understanding different approaches to the question of inter-war market psychology.

In several instances, we have been presented with contemporary belief that forces acting on the exchange rates exceeded anything that could be ascribed to the movement of discount rates, the expiry date of the Gold and Silver Export Control Act, or the revelation of London's financial position. By adopting a broader perspective, and so moving beyond the influence of fundamentals, economists believed that exchange rates were based on insecure, and constantly changing degrees of confidence. Their task was therefore to attempt to identify and understand the influences that were leading to such evolving moods of confidence.

CHAPTER 7

CONCLUSIONS

> "Let it be acknowledged that for a long time to come there are likely to be many honest and hard-working and intelligent men who will be interested in economic theory: let it be acknowledged, likewise, that there are likely to be a number, – small, indeed, in America and England, but still noticeable – who also are honest and hard-working and not altogether unintelligent, who will be interested in economic history."
>
> William Ashley[542]

In this dissertation, we have attempted to examine the impression of the inter-war British economy presented in the academic and popular writings of a variety of contemporary commentators. As was made clear in the introduction, this work has not served as yet another foray into the history of inter-war economic thought, but rather an attempt to examine economic commentaries within in a defined historical period. This has proved an extraordinary trail, for in attempting to embrace the means by which inter-war economists attempted to instruct interested and inquiring "man in the street", we have come to appreciate the extent, frailty and novelty of contemporary economic opinion. Although never serving as a perfect substitute for modern methods of analysis, our attempt to convey some sense of this interpretation of inter-war events has provided an interesting perspective from which to survey and contemplate the study of inter-war economic history. This final chapter will summarise the main findings of the study, offer some assessment of the potential

[542] Ashley, W.J. (1893) 'On the Study of Economic History', pp. 122 – 123

benefits of such an investigation to the study of inter-war economic history, and raise suggestions for further avenues of investigation.

Initially expressing faith in the rhythmic influence of the trade cycle, and hence the temporary nature of Britain's economic difficulties during the early post-war period, inter-war economists eventually came to accept that the pre-war international economic system had been permanently undermined. Through the transformation of the international environment – brought about by a protracted international war, the growth of economic nationalism, and the industrialisation of many foreign countries (the latter being a consequence of the imperialistic tendencies of nineteenth century British capitalism) – it was recognised that Britain's economic structure would have to evolve.

It was logical to expect that the shock to the existing international economic system would set in motion dynamic changes within the British economy. Through human self-interest and the speedy redistribution of capital and labour, it was expected that Britain would experience the contraction of her export industries (although she would still remain an exporting nation) and the expansion of the domestic distributive and service industries. As the 1920s wore on, it became increasingly apparent that the self-adjusting mechanism of capitalism – the "invisible hand" – had failed to assert itself. In a wider cultural sense, it appeared that some force, or combination of forces, was preventing British industry from capturing the exuberant social dynamism of the post-war period. A large proportion of post-war Britain's protracted unemployment problem was therefore attributed to a variety of physical and physiological factors that had restricted the operation of the free market. Unemployment, in other words, was fused with impediments to economic development.

A variety of explanations were offered to account for this problem, and it is here that we see the potential relevance of understanding inter-war economic literature. The ability to visualise the inter-war economy through the eyes of contemporary writers serves to throw fresh light on old, established themes. Time and again, we have seen how inter-war economists were drawn to forces that extended beyond what, to us, would appear to be the confines of mainstream economic theory. In their effort to understand the forces that were impeding Britain's economic transformation, economists adopted an almost romantic appreciation of the idea that economic action (or, in this instance, inaction) was dictated by powerful emotional forces present within post-war society. One example of this can be seen in the influence of emotional reactions to the loss of Britain's industrial supremacy, and its effects in sterilising the entrepreneurial spirit. In this instance, the desire to preserve the pre-war economic structure was not connected with financial concerns (such as the huge investments that had taken place during the post-war recapitalisation boom), but Britain's emotional and historical investment in the culture of industrialisation. Post-war Britain was seen to be weighed down by her nineteenth century industrial successes, and hence reacting against the loss of once prominent export industries, and the apparently abhorrent prospect of having to rely on domestic concerns – such as shops, garages, hotels and restaurants – for her future economic prosperity.

We have seen other examples of such ephemeral emotional and psychological forces. For example, the combined effects of unemployment insurance in increasing the recorded level of post-war unemployment, and continual comparisons with pre-war and post-war unemployment statistics. Both of these features appeared to present a vicious circle of continuous unemployment. There was also seen to be important psychological effects from the use of particular words: the use of the term "rationalisation" appeared to reinvigorate the economy (even though it was the repackaging of established economic principles), while such terms as "protectionism" or "safeguarding" appeared to perpetuate an unfortunate feeling of domestic manufacturing failure. In another example, such descriptions as "Empire Free Trade" or "Imperial integration" were taken to present an over-romanticised impression of Britain's economic history, thereby impeding the process of post-war development by diverting effort and resources towards schemes that economists believed had little prospect of success.

By appreciating the diffuse elements of human nature, economists were seeking to understand the relationship between the prevailing culture and Britain's post-war economic difficulties. The power of the free market appeared to be directly connected with the nation's perception of economic reality. Time and again we have seen reference to questions of how the public accessed and assimilated information. The ways by which past economic agents formed their impressions of economic forces is a topic that modern historiography has yet to properly examine. During the inter-war years, the most obvious means available to the public to obtain information was through the Press. Whether deliberate or not, the actions of the Press had the potential to massage economic reality and give voice to erroneous economic opinions. One of the surest ways to bring about economic recovery, wrote Harold Cox, was through "a more independent, a more disinterested, and a more enlightened Press."[543]

As with so much of economics, the task facing the economist was one of persuasion: to attempt to clear away those problems – both real and, perhaps more importantly, imaginary – that were obstructing a necessary process of change. Post-

[543]Cox, H. (1930) 'Some Real Causes of the Slump', p. 561

war economic development could only be achieved once society had embraced the idea of change, and was not weighed down by the debilitating emotional baggage of industrialisation, or erroneous belief in Imperial economic integration or domestic protection. In order to stimulate the process of transition, economists sought to neutralise a negative psychology by advancing a positive psychology. The quicker that such erroneous interpretations were exposed, it was argued, the quicker the economy would move from a redundant economic structure to one that would provide future economic success.

The research presented here suggests that the main benefits to be derived from the study of contemporary economic texts resides with those areas in which human nature plays a much more vital role, such as impediments to economic transformation and the forces that influenced the movements of the exchange rates. The study of the contemporary literature relating to the subject of public finance appears to yield little in the way of fresh perspectives on events. A possible explanation for this may involve the policy implications of government expenditure. Social reform measures, secured through the proceeds of taxation, were identified by many economists as a means of overcoming impediments and so facilitating the transition to a new economic structure.

When we move into the area of exchange rates, we discover a different contemporary approach to the questions of psychology. We have seen how inter-war economists believed that confidence was a primary influence on the movement of the exchanges. Explanations surrounding the restoration of the gold standard did not focus on interest rates or the Gold Embargo Act, but on the relationship between the appreciation of sterling and the more diffuse, optimistic signals regarding the revival of the European economy. Similarly, it was believed that forces surrounding the departure from gold in September 1931 was attributed to erroneous Press speculation. The movement of sterling through the autumn of 1931 and early spring of 1932 was related to changing moods of confidence regarding the British economy and, more importantly, the expected future position of sterling as an international currency and London as an international financial centre.

In many respects, it is not surprising that inter-war economists drew ideas concerning psychology and emotions into their interpretations of ongoing, real world events. During the War, Cunningham had drawn attention to Adam Smith's warning, presented in *The Theory of Moral Sentiments* (1759), that human motivation could never be explained purely by "the trinkets of frivolous utility."[544] Economists during the inter-war period were, of course, well acquainted with the works and ideas of the classical economists. It is only in the modern academic environment where, as we explained in the introduction, economics and economic history is increasingly drawn towards what Joan Robinson called the "thickets of algebra", that a proper appreciation of such ideas are lost, or at least obscured. Even if economic historians avoid mathematical or econometric techniques, it is the assumptions and the modes of thought of modern research – particularly the principle of self-interested utility maximisation – that forms the basis for their understanding of economic psychology. This is in no way to suggest that such methods are wholly inappropriate or unsuited to the task. Rather it is to suggest that, when applied to a specific historical period, they may fail to fully illuminate human motivations that operated in particular contexts. Given that inter-war economists were writings in the flow of events, it must be accepted that their works contain errors. Yet at the same time, interpretations with an immediate proximity to events may also yield subtleties that are lost through the panoramic vision achieved through a separation from events and the plethora of

[544] Adam Smith quoted in Cunningham, W. (1915) 'Economic Problems After the War' in Kirkaldy, A.W. (ed) *Credit, Industry, and the War*, London: Isaac Pitman & Sons Ltd, p. 260

statistics and modern methods of analysis. It is not suggested that the study of such contemporary economic texts should be a priority for historians, but rather that they contribute to a more heterogeneous methodology. It is through the study of such material that we have the potential to interact with ideas different from that contained in the modern historiography, and so gain a different perspective on inter-war economic events.

APPENDIX

Dramatis Personae[545]

Acworth, William Mitchell (later Sir William) (1850 – 1925): Expert on railway economics; member, Board of Trade Committee on Railway Accounts and Statistics (1906); chairman, Committee on Indian Railway Policy and Administration (1920 – 21).

Allen, George Cyril (1900 – 1982): Economist; Lecturer in Economics, Birmingham University (1925 – 1929); Professor of Economics, Hull University (1929 – 1933); Professor of Economics, Liverpool University (1933 – 39, 1944 - 1945); Councilor to Advisor on Economic Reconstruction of Japan (1945 – 1947).

Ashley, William James (later Sir William) (1860 – 1927): Economist and economic historian; Professor of Political Economy and Constitutional History, Toronto University (1888 – 92); Professor of Economic History, Harvard University (1892 1901); Professor of Commerce, Birmingham University (1901 – 25).

545 Given that all ideas exist in relation to the individual who qualifies and humanises them, it is important to provide some biographical information on many of commentators included in this dissertation. This section has been compiled from *The Times* Obituary Index and the biographical appendices to Moggridge, D.E. (1992) *Maynard Keynes: An Economist's Biography*, London: Routledge, pp. 859 – 911; Skidelsky, R. (1992) *John Maynard Keynes: The Economist as Saviour, 1920 – 1937*, pp. 685 – 708; and Middleton, R. (1998) *Charlatans or Saviours? Economists and the British Economy from Marshall to Meade*, pp. 370 – 379

Ashton, Thomas Southclifte (1889 – 1968): Economic historian; Lecturer in Economics, Sheffield University (1912 – 19); Reader in Currency and Finance, Manchester University (1927 – 44); Professor of Economic History, LSE (1944 – 54)

Bastable, Charles Francis (1855 – 1945): Economist; Professor of Jurisprudence and Political Economy, Queen's College, Galway (1883 – 1903); Professor of Jurisprudence and International Law, Trinity College, Dublin (1902 – 08); Regius Professor of Laws, Trinity College, Dublin (1908 – 32).

Beveridge, William Henry (later Lord Beveridge) (1897 – 1963): Economist, social reformer and administrator; Director of Labour Exchanges (1909 – 16); Minister of Munitions and Food (19125 – 18); Director, LSE (1919 – 37); Liberal Member of Parliament, (1944 – 5).

Bonar, James (1852 – 1941): Senior civil servant and internationally renowned expert on classical economics; junior examiner, Civil Service Commission (1881 – 95); senior examiner, Civil Service Commission (1895 – 1909); Deputy Master of Royal Mint (Ottawa Branch) (1907 – 19).

Bowley, Arthur Lyon (later Sir Arthur) (1869 – 1957): Economist and statistician; Professor of Economics and Mathematics, University College, Reading (1907 – 13); Professor of Statistics, London University (1919 – 1936); Director, Oxford University Institute of Statistics, (1940 – 44).

Brunner, Christopher Tatham (1903 – 1962): Economist and oil executive, pioneer in the study of the economics of road transport and the oil industry; Head of Statistical Department, Shell-Mex & B.P. Ltd (1927 – 1947); Managing Director, Shell-Mex & B.P. Ltd (1962).

Cannan, Edwin (1861-1935): Economist; Lecturer in Economics, L.S.E, (1897 – 1907); Professor of Political Economy, L.S.E, (1907 – 26).

Carr-Saunders, Alexander Morris (1886 – 1966): Social scientist, concerned primarily with social biology and the study of population; Charles Booth Professor of Social Science, Liverpool University (1923 – 37); Director, L.S.E, (1937 – 56).

Cassel, Gustav (1866 – 1945): Swedish economist; Professor of Political Economy, Stockholm University (1904 – 33); Member of the Gold Delegation of the League of Nations (1929 – 32); Swedish delegate to World Economic Conference (1933).

Chapman, Sydney John (later Sir Sydney) (1871 – 1951): Economist and civil servant; Stanley Jevons Professor of Political Economy, Manchester University (1901 – 18); Permanent Secretary, Board of Trade (1919 – 27); Chief Economic Advisor, H.M. Government (1927 – 32); vice-chairman, Central Price Regulation Committee (1940).

Clay, Henry (later Sir Henry) (1883 – 1954): Economist; Lecturer in Economics to the Workers' Educational Tutorial Classes (1909 – 1917); Jevons Professor of Political Economy, Manchester University (1922 – 7); Professor of Social Economics, Manchester University (1927 – 30); Economic Advisor to the Governors of the Bank of England, (1930 – 1944); Economic Advisor, Board of Trade (1941 – 44).

Cole, George Douglas Howard (1889 – 1959): Socialist political theorist, writer on economic and social questions; Reader in Economics, Oxford University (1925 – 44); Chichele Professor of Social and Political Theory, Oxford University (1944 – 57); co–author of detective novels and short stories with his wife, Margaret Isabel Cole.

Cox, Harold (1859 – 1936): Economist and journalist; Cobdenite free-trader, staunch adherent of the orthodox school of economics, and energetic denouncer of the evils of bureaucracy; Secretary of the Cobden Club (1899 – 1904); Liberal Member of Parliament (1906 – 09); editor, *Edinburgh Review* (1912 – 29).

Crump, Norman (1896 – 64): Journalist; city editor, *Sunday Times* (1939 – 1960); Recognised expert on railway signalling.

Cunningham, William (1849 – 1919): Economic historian and Church of England clergyman; Chaplain, Trinity College, Cambridge (1880 – 91); Lecturer in Ecclesiastical history, University of Cambridge, (1886 – 90, 1908 – 10); Tooke Professor of Economics and Statistics, King's College, London (1891 – 97).

Dalton, (Edward) Hugh John Neale (later Lord Dalton) (1887 – 1962): Economist and Labour politician; Lecturer in Economics, LSE (1919 – 25); Cassel Reader in Commerce, LSE (1925 – 36); Chancellor of the Exchequer (1945 – 1947).

Daniels, George William (1878 – 1937): Economist; Reader in Administration, Manchester University (1920 – 21); Professor of Commerce, Manchester University (1921 – 27); Stanley Jevons Professor of Political Economy, Manchester University (1927 – 37).

Edgeworth, Francis Ysidro (1845 – 1926): Polymath with a penchant for recondite language; Tooke Professorship of Economic Science and Statistics, King's College, London (1888 – 90); Drummond Professor of Political Economy, Oxford University (1891 – 1922); editor, *Economic Journal* (1890 – 1911); co-editor, *Economic Journal* (1919 – 26).

Einzig, Paul (1897 – 1973): Transalvanian born financial and political journalist, regarded as an authority on international finance; contributor to *Financial News* (1921 – 45); *Financial Times* (1945 – 56).

Florence, Philip Sargant (1890 – 1982): Economist; Lecturer in Economics, Cambridge University (1921 – 9); Professor of Commerce, Birmingham University (1929 – 55).

Forrester, Robert Blair (1886 – 1953): Economist; Special Investigator, Government of Iraq (1928 – 30); Professor of Economics and Political Science, University College of Wales, Aberystwyth (1931 – 1951)

Flux, Alfred William (later Sir Alfred) (1867 – 1942): Economist, statistician, and civil servant; Stanley Jevons Professor of Political Economy, Owens College, Manchester (1898 – 1901); William Dow Professor of Political Economy, McGill University, Montreal (1901 – 08); Statistical Advisor, Board of Trade (1908 – 32).

Foxwell, Herbert Somerton (1949 – 1936): Economist and bibliographer; Professor of Political Economy, University College, London (1882 – 1896); Lecturer on Currency and Banking, L.S.E, (1896 – 1922).

Fraser, Lindley Macnaghter (1904 – 1963): Economist and broadcaster; Procter Visting Fellow, Princeton University (1926 – 27); Eastman Fellow, Brookings School of Economics (1927 – 28); Jaffrey Professor of Political Economy, University of Aberdeen (1935 – 1940); Head, BBC German Service (1946 – 63)

Gregory, Theodor Emanuel Gugenheim (later Sir Theodore) (1890 – 1970): Economist; Assistant Lecturer in Economics, L.S.E (1913 – 19); Cassel Professor of Economics, L.S.E (1927 – 37); Professor of Social Economics, Manchester University (1930 – 32); Member, Irish Free State Banking Commission (1934 –37); Economic Advisor, Government of India (1938 – 46).

Guillebaud, Claude William (1890 – 1971): Economist; Girdlers' Lecturer, Cambridge University (1943 – 56); nephew of Alfred Marshall.

Hall, Noel Frederick (1902 – 1983): Economist; Senior Lecturer in Economics, University College, London (1929 – 35); Professor of Economics, Economics, University College, London (1935 – 40); Development Advisor, West Africa (1943 – 45); Principle of the Administrative Staff College (1946 – 61).

Hawtrey, Ralph George (later Sir Ralph) (1879 – 1975): Economist and H.M. Treasury Economic Advisor; civil servant, H.M. Treasury (1904 – 1919); Director of Financial Inquiries, H.M. Treasury (1919 – 47); Visiting Professor of Economics, Harvard University (1928 – 9); Price Professor of International Economics, Royal Institute of International Affairs (1947 – 52).

Henderson, Herbert Douglas (later Sir Hubert) (1890 – 1952): Economist and journalist; Lecturer in Economics, Cambridge (1919 – 23); Editor, *The Nation and Athenaeum* (1923 – 30); Joint Secretary, Economics Advisor Council (1930 – 4); Economic Adviser, H.M. Treasury (1939 – 44); Drummond Professor of Political Economy, Oxford (1945 – 51).

Hicks, John Richard (later Sir John) (1904 – 89): Economist; Lecturer in Economics, LSE (1926 – 35); Lecturer in Economics, Cambridge University (1935 – 8); Professor of Political Economy, Manchester University (1938 – 46); Drummond Professor of Political Economy, Oxford University (1952 – 65); Nobel Laureate (1972).

Higgs, Henry (1864 – 1940): Economist and one-time Principle Clerk, H.M. Treasury (retired 1921); joint editor of *Economic Journal* (1892 – 1906); Inspector General of Finance, Egypt (1912 – 15); lecturer in economics, Bangor University (1926 – 1929).

Hilton, John (1880 – 1943): Civil servant and industry commentator; journalist, *Yorkshire Post* (1911 – 21); assistant secretary (later Director of Statistics), Ministry of Labour (1919 – 31); Montague Burton Professor of Industrial Relations, Cambridge University (1931 – 1943); Director of Home Publicity, Ministry of Information (1939 – 40).

Hirst, Francis Wrigley (1873 – 1953): Writer on economic and political affairs, and disciple of the school of Mill, Cobden and Gladstone; lecturer in Political Science, L.S.E (1897 – 1900); editor of *The Economist* (1907 – 1916); editor of *Common Sense* (1916 – 21); married Helena Cobden, grand-niece of the apostle of free trade, Richard Cobden.

Hobson, John Atkinson (1858 – 1940): Economic heretic, sociologist, journalist, and imperial critic. Hobson laboured for many years to construct a synthesis of the social sciences, and was regarded by many of his more tolerant contemporaries as a latter day John Stuart Mill.

Jack, Daniel Thomson (1901 – 1984): Economist; David Dale Professor of Economics, King's College, Newcastle-upon-Tyne (1935 – 61); chairman, Air Transport Licensing Board (1960 – 70).

Jevons, Herbert Stanley (1875 – 1955): Economist; Professor of Economics and Political Science, University College of South Wales (1905 – 11); Professor of Economics, Allahabad University (1914 – 23); Professor of Economics, Rangoon University (1923 – 30); British Advisor, Ethiopian Embassy (1942 – 55).

Jewkes, John (1902 – 1988): Economist, authority on the economics of the Lancashire cotton industry; Assistant Secretary, Manchester Chamber of Commerce (1924 – 26); Lecturer in Economics, Manchester University (1926 – 30); Director, Economic Research Section, Manchester University (1930 – 36); Professor of Social Economics, Manchester University (1936 – 46); Professor Economic Organisation, Oxford University (1948 – 69).

Jones, John Harry (1881 – 1973): Economist; Assistant Lecturer in Economics, Liverpool University (1907 – 09); Lecturer in Economics, Glasgow University, (1909 – 13); Professor of Economics, Leeds University (1919 – 46); Chairman, Nova Scotia Royal Commission of Economic Enquiry (1934).

Keynes, John Maynard (later Lord Keynes) (1883 – 1946): Economist, civil servant and journalist; civil servant, India Office (1906 – 08); editor, *Economic Journal* (1912 – 1945); economic advisor, H.M. Treasury (1915 – 19); chairman, *Nation and Athenaeum (*1923 – 31); chairman, *New Statesman and Nation* (1931 – 46); economic advisor, H.M. Treasury (1940 – 46).

Kirkaldy, Adam (1867 – 1931): Economist; Professor of Finance, Birmingham University (1906 – 18); Sub-commissioner for Trade Exemption (West Midlands); Ministry of National Service (1918 – 19); Professor of Economics and Commerce, University College, Nottingham (1919 – 31).

Knoop, Douglas (1883 – 1948): Economist and economic historian; Lecturer in Economics, Sheffield University (1909 – 20); Professor of Economics, Sheffield University (1920 – 1948).

Lavington, Frederick (1881 – 1927): Economist; staff, Board of Trade (1911 – 18); Lecturer in Economics, Cambridge University (1918 – 21); Girdler's Lecturer in Economics, Cambridge University (1921 – 27).

Layton, Walter Thomas (later Lord Layton) (1884 – 1966): Economist and administrator; Lecturer in Economics, Cambridge University (1912 – 19); Editor, *The Economist* (1922 – 28); Chief Adviser, Ministry of Production (1942 – 3). One of the few economists to have published in the Economic Journal while still a first-year undergraduate.

Lloyd, Edward Mayow Hastings (1889 – 1968): Civil servant, economic advisor, and expert on the control and rationing of food supplies; Ministry of Food (1917 – 19); League of Nations (1919 – 21); Empire Marketing Board (1921 – 26); Assistant Director, Food (Defence Plans) Department (1936 – 42); under-secretary, Ministry of Food (1947 – 53).

MacGregor, David Hutchinson (1877 – 1953): Economist; Professor of Political Economy, Leeds University (1908 – 19); Stanley Jevons Professor of Political Economy, Manchester University (1919 – 22); Drummond Professor of Political Economy, Oxford University (1922 – 45); Assistant Editor, *Economic Journal* (1925 – 37).

Marshall, Alfred (1842 – 1924): Founder of the Cambridge School of Economics; Professor of Political Economy; University College, Bristol (1877 – 83); Professor of Political Economy, Cambridge University (1885 – 1908).

Nicholson, Joseph Shield (1850 – 1927): Economist and chess expert of *The Times*; Professor of Political Economy and Mercantile Law, Edinburgh University (1880 – 1925).

Orwin, Charles Stewart (1876 – 1955): Agricultural economist and historian; director, Research Institute in Agricultural Economics, Oxford University, (193 – 45); member, Agricultural Wages Board (1917 – 21); assessor, Agricultural Tribunal (1922 – 4); member, Food Council (1925 – 33).

Paish, George (later Sir George) (1867 – 1957): Economist, noted authority on the economic statistics of overseas trade; Joint Editor, *The Statist* (1900 – 1916); member of the Departmental Committee on Railway Accounts (1906 – 08); Adviser to the Chancellor of the Exchequer(1914 – 16).

Pethick-Lawrence, Frederick William (later Lord Pethick-Lawrence) (1871 – 1961): Politician, women's suffragist, and commentator on economic policy; editor, *The Echo* (1902 – 05); editor, *Labour Record and Review* (1905 – 07); joint editor, *Votes for Women* (1907 – 14); Labour Member of Parliament for West Leicester (1923 – 31); Labour Member of Parliament for East Edinburgh (1935 – 45); Financial Secretary, Treasury (1929 – 31); Secretary of State for India and Burma, (1945 – 7).

Pigou, Arthur Cecil (1877 – 1959): Doyen of early twentieth century neo-classical economists; Girdlers' Lecturer in Economics, Cambridge University (1904 – 08); Professor of Political Economy, Cambridge University (1900 – 43).

Plant, Arnold (later Sir Arnold) (1898 – 1978): Economist; Professor of Commerce, Cape Town University (1923 – 30); Professor of Commerce, L.S.E (1930 – 65); chairman, Social Science Research Council (1955 – 62); chairman, Industrial Injuries Advisory Committee (1955 – 65).

Price, Langford Lovell Frederick Rice (1862 – 1950): Economist and economic historian; staff, International Statistical Institute (1895 – 1896); Lecturer (later Reader) in Economic History, Oxford University (1907 – 21).

Robbins, Lionel Charles (later Lord Robbins) (1898 – 1984): Economist; Lecturer in Economics, L.S.E (1925 – 7); Lecturer in Economics, New College, Oxford (1927 – 9); Professor of Economics, L.S.E (1929 – 61); Director, Economic Section of the War Cabinet (1941 – 5); Chairman, *Financial Times* (1961 – 70); Chairman, Committee on Higher Education (1961 – 64).

Robertson, Dennis Holme (later Sir Dennis) (1890 – 1963): Economist; Lecturer in Economics, Cambridge University (1924 – 28); Girdlers' Lecturer, Cambridge University (1928 – 30); Reader in Economics, Cambridge University (1930 – 8); Cassel Professor of Money and Banking, L.S.E (1938 – 44); Professor of Political Economy, Cambridge University (1944 – 57).

Scott, William Robert (1868 – 1940): Economist and economic historian; Lecturer in Political Economy, St Andrews University (1899 – 1915); Adam Smith Professor of Political Economy, Glasgow University (1915 – 40).

Shadwell, Arthur (1854 – 1936): Commentator on socio-economic, industrial, and public health issues; special correspondent on Russian and German cholera epidemic, *The Times* (1892); labour correspondent, *The Times* (1908 – 1928); editor, *The Democrat* (1922 – 23).

Stafford, Jack (1909 – 1982): Economist; Lecturer in Economics, Manchester University (1930 – 41); member, Central Statistical Office (1941 – 48); Director of Statistics, Board of Trade (1948 – 72).

Stamp, Josiah Charles (later Lord Stamp) (1880 – 1941): Statistician, business administrator, public servant, and recognised expert on British taxation system; Assistant Secretary, Board of Inland Revenue (1916 – 19); Director, Bank of England, (1928 – 41); Chairman, Survey of Financial and Economic Plans (1939 – 41).

Tawney, Richard Henry (1880 – 1962): Economic historian and political thinker; Assistant Lecturer in Economics, Glasgow University (1906 – 08); Reader in Economic History, L.S.E (1923 – 31); Professor of Economic History, L.S.E (1931 – 49); married Annette Jeannie Beveridge, sister of William Beveridge.

Venn, John Archibald (1883 – 1953): Agricultural economist and adviser to the Ministry of Agriculture; statistician, Ministry of Agriculture, (1919 – 21); Lecturer in the History and Economics of Agriculture, Cambridge University, (1921 – 1949).

Walker, Gilbert James (1907 – 1982): Economist, expert on transport economics; Assistant Lecturer in Economics, Birmingham University (1930 – 34); Director of Statistics, British Supply Mission, Washington D.C. (1942 – 45); Professor of Commerce, Birmingham University (1955 – 74).

Wootton, Barbara Frances (later Baroness Wootton) (1897 – 1988): Economist, social philosopher and public servant; Research officer, T.U.C and the Labour Party (1922 – 26); Head of Department of Economics, Sociology and Social Studies, Bedford College (1944 – 52); Nuffield research fellow, Bedford College (1952 – 57).

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