ECONOMICS AND THE EUROPEAN UNION Part Three FIGHTING FOR BRITAIN (AGAINST THE US) Article by Peter Brooke, taken from http://www.peterbrooke.org/politics-and-theology/eu-economics/ First published in Irish Foreign Affairs, Vol 15, No 2, June 2021

US v UK

Given the immense stretch of the sterling area and the Empire it isn't immediately obvious why Britain became so quickly and utterly dependent on the United States. From early on Britain was buying large quantities of manufactured goods from the US, indicating that it's own productive capacity was inadequate for fighting the war it had declared. At the same time it was importing raw materials and foodstuffs from the Empire while its own exports were reduced dramatically. Skidelsky's biography of Keynes, p.134,[1] has a table showing Britain's reserves (gold and US and Canadian dollars) declining from £545 million in December 1939, to £70 million in March 1941. The contrast with the US and Germany was dramatic. Was one of the reasons that both the US and Germany, unlike the UK, had invested in large job creation schemes through the 1930s?

The German policy will be looked at shortly. In the US the 'New Deal' had been supported by government spending on an unprecedented scale which in turn had been backed by a massive accumulation of gold, a policy reminiscent of the German policy at the beginning of the First World War, discussed in the first article in this series. Morgenthau and Roosevelt launched a policy of compulsory purchase of gold. All gold holdings worth more than $100 had to be sold to the government at the then going rate which the government then increased dramatically, thus devaluing the paper currency while still accumulating large stocks of what could be called the hard value of gold.

Prior to the 1930s the US had been largely self sufficient, able within its own economy to absorb its enormous economic power both in manufacturing and in agriculture. It wasn't thinking so much in terms of international trade. Indeed one of the first reactions to the 1929 financial crash was, in 1930, to impose the heavy 'Smoot Hawley' tariff on imports. It may be, however, that one of the causes of the crash was that the productive capacity was outgrowing the consumption capacity of the domestic economy. As the thirties progressed, and with the government supported reflation of US industry, Roosevelt and Morgenthau wanted a greater emphasis on exports and this ran up against the protectionist policy being pursued by Britain throughout the Empire and the sterling area (in which sterling had to be used in all international transactions). Britain had further offended by its own devaluation when it went off the gold standard in 1932, breaking the terms on which substantial loans had been negotiated with the New York Fed and the Banque de France, and defaulting on its First World War debt in 1934. The result in the US was a raft of legislation passed by Congress through the 1930s against supplying countries at war,

[1] Robert Skidelsky: *John Maynard Keynes, Fighting for Britain, 1937-1946*, Macmillan 2000. This is the main source for the present article.

legislation Roosevelt had to overcome when the golden opportunity provided by Britain's new state of dependence on the US was presented to him.

In November 1939 the Neutrality Acts were amended by 'cash and carry' legislation devised by the financier Bernard Baruch, a key figure in the organisation of the US economy during and just after the First World War. This was a purely commercial arrangement in which all supplies had to be paid for immediately and carried in British ships. When the British fled from Europe in June 1940 they left behind an enormous amount of military material which had to be replaced. In November 1940 the British ambassador, Lord Lothian, arriving at La Guardia airport, said to the assembled press corps: 'Well boys, Britain's broke. It's your money we want.' According to Skidelsky (p.96) Britain 'needed to order more supplies than ever before, as well as more ships to carry them in because Germany's submarines were sinking so many. And American exporters were insisting on higher advance payments, which reflected "doubts about [Britain's] ability to pay all the bills she was running up" [quote from anther historian - PB]. Britain lost $668m (£167m) in the third quarter of 1940. At this rate it would be virtually out of gold and dollars by the end of the year.' He quotes Lothian referring to 'the fundamental question ... whether the [US] policy is to ... help Britain within the limits of the Neutrality Act but acquiesce in [its] defeat if these half measures do not suffice, or to adopt the policy in America's own interest that it is going to see Great Britain is not defeated whatever it may cost ...'

If the American's were anxious to see that Great Britain wasn't defeated it wasn't so much out of affection for Britain as hostility to Germany. Skidelsky again (p.99):

'he [Morgenthau] *was not so much pro-British as Germanophobe. With America neutral, Britain was the reed that had to be supported,* faute de mieux, *despite the inaptness of imperial Britain as a champion of freedom. Morgenthau also shared the New Deal suspicion of international finance. His aim was to shift financial power from New York and London to Washington. The dollar would become the instrument of a global "New Deal". At the same time, his lack of financial expertise made him dependent on a small group of trusted technicians. Gradually, Feis writes, Morgenthau became "more and more influenced by the viciously assertive staff assembled around him, led by Harry White. They used him, and he used them. . . ,"[2] He would support Britain in the war against Germany, but not to preserve Britain's world position. The United States, not Britain, would be the leader of the postwar free world, the dollar would replace the pound as the world's leading currency. He would do all he could to help Britain, but as a satellite, not as an ally.*

'In 1940 he started putting pressure on the British to sell off their big American companies - Shell Oil, Lever Brothers and Brown & Williamson Tobacco. The Secretary, writes his biographer John Morton Blum, "recognised that the loss of [Britain's overseas] *investments would cripple the British economy after the war, but he maintained that England could not afford to worry about this*

[2] Reference to Herbert Feis: *1933: Characters in Crisis*, Boston/Toronto, Little, Brown, 1966, p.107.

in 1940".[3] *For the first time in its history, Britain found itself a suppliant for means-tested benefits, with Morgenthau running the benefit office. Little wonder he was cast as the villain in Keynes's, and London's, eyes.'*

Keynes (Skidelsky p.103) was to complain in March that Morgenthau 'was aiming to reduce Britain's gold reserves to nil, "treat[ing] us worse that we have ever ourselves thought it proper to treat the humblest and least responsible Balkan country."'

White and Morgenthau were both Jewish - as of course was Bernard Baruch - but regardless of any feelings they might have had as Jews a Fascist Europe would probably be striving for self sufficiency and would not be open to penetration by the newly expansionist US, and there was no reason to believe that Britain making a deal with Germany would bring the protectionist Empire, or even the sterling area, to an end. Hitler would certainly have argued that it was the best way of preserving them and we may easily imagine that that would have been the argument the very pro-British Rudolf Hess brought with him when he made his ill fated attempt at peace negotiations in May 1941 (originally planned in November 1940).[4]

LEND-LEASE

Keynes was charged with conducting most of the British side of the negotiations with the US and the third volume of Skidelsky's biography, subtitled 'Fighting for Britain, 1937-1946' is a long chronicle (500 pages) of successive defeats and, from Keynes's point of view, inadequate compromises. There are three parts to the story - the negotiations over Lend-lease, discussions with White on the post-war institutions that were eventually agreed at Bretton Woods, and negotiations over the loan given to Britain when Lend-Lease was abruptly terminated at the end of the war with Japan.

On the face of it, Lend-lease was an extraordinarily generous arrangement. In a speech in November 1941, Churchill said:

'Then came the majestic policy of the President and Congress of the United States in passing the Lease-Lend Bill, under which, in two successive enactments, about £3,000,000,000 was dedicated to the cause of world freedom, without - mark this, because it is unique - without the setting up of any account in money. Never again let us hear the taunt that money is the ruling power in the hearts

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[3] Reference to J.Morton Blum (ed): *From the Morgenthau Diaries*, *Vol ii: Years of urgency, 1938-41*, Boston, Houghton Mifflin, 1965, p.171.

[4] Albert Speer: *Inside the Third Reich*, New York, Avon, 1971, p. 241, has Hess telling him in Spandau that his proposal was: 'We will guarantee England her empire; in return she will give us a free hand in Europe.'

and thoughts of the American democracy. The Lease-Lend Bill must be regarded without question as the most unsordid act in the whole of recorded history.'[5]

Roosevelt, selling it to the US public, likened it to lending a neighbour a fire hose to put out a dangerous fire. Though there was of course the understanding that the fire hose was unlikely to be returned and would probably be destroyed by the fire - even probably before it reached the neighbour if the U-boats got at it. Roosevelt's isolationist opponent Robert Taft said that 'lending' arms to a neighbour was a bit like lending chewing gum. You really didn't want it back after it had been used.

Roosevelt announced the policy in December 1940. It passed Congress in March 1941 and came into effect in April, by which time it was unclear if Britain would be able to pay for orders it had already placed. This was a period before the German invasion of the Soviet Union when it must have seemed almost out of the question that Britain could actually win the war. The most that could be hoped for was just that Britain wouldn't actually be forced to make terms. Churchill certainly thought that actual victory was impossible unless the US joined in and it seems improbable that Roosevelt would have disagreed. But in the election fought in November 1940 he had promised - in a manner reminiscent of Woodrow Wilson before him - that he would not 'send American boys into any foreign wars.' The argument for Lend Lease was that Britain had to be kept in the war to keep the US out of it, implying that if Britain gave up, the US would have to intervene. But this did not make much sense since, had Britain come to terms with Germany, the US would have been deprived of the means of conducting a European war - it would have been deprived of what Göring (I think) called the aircraft carrier moored off the coast of Europe. As was pointed out at the time by isolationists the policy only made sense if Roosevelt planned to enter the war. Under Lend Lease goods could be transferred to the UK in American ships and Skidelsky (p.101), pointing out that Roosevelt had been Assistant Secretary of the Navy in 1917, speculates that he may have hoped that Germany attacking American ships would provide a pretext for America joining the war. In the event, the need became less pressing when Hitler went to war with the Soviet Union in June. A Lend Lease arrangement was extended to the Soviet Union in October. Hitler declared war on the US, in tandem with Japan, in December.

ARTICLE VII

The Lend Lease legislation passed by Congress authorised aid on 'terms and conditions' specified as 'payment or repayment in kind or property or any other direct or indirect benefit which the President deems satisfactory' (Skidelsky p.126). Responsibility for

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[5] By November a Lend-lease arrangement had been made with the USSR so this is included in the £3,000,000,000 'dedicated to the cause of freedom.' The quote is well known but I have taken it from James Lachlan MacLeod: *The Most Unsordid Act in History?* on the American History News network website.

determining the terms and conditions was given to the State Department under the Secretary of State, the militant free trader Cordell Hull and his Assistant Secretary Dean Acheson. The result was a draft of seven articles which Keynes saw on 28th July. Article VII read:

'The terms and conditions upon which the United Kingdom receives defensive aid from the United States of America and the benefits to be received by the United States in return therefor, shall be such as not to burden commerce between the two countries but to promote mutually advantageous economic relations between them and the betterment of world-wide economic relations; they shall provide against discrimination in either the United States of America or the United Kingdom against the importation of any produce originating in the other country; and they shall provide for the formulation of measures for the achievement of these ends.'

Innocent as that may seem, it prompted an angry response from Keynes:

'It was impossible, he raged, for the British to make such a commitment in good faith. It fastened upon the future an ironclad formula from the nineteenth century. It contemplated the impossible and hopeless task of returning to a gold standard where international trade was controlled by mechanical monetary devices. It banned exchange controls, which were the only way to maintain economies in balance. It allowed all kinds of cunningly devised tariffs which were in fact discriminatory, while prohibiting sound monetary controls. After the war, Britain would have a large surplus of imports over exports and the Article VII formula provided no remedy for this.'

Later, in a letter to Acheson apologising for the violence of his reaction, Keynes developed his argument:

'His reaction, he said, "was the result of my feeling so passionately that our hands must be free to make something new and better of the post-war world; not that I want to discriminate in the old bad sense of that word - on the contrary, quite the opposite. But the word [discrimination] *calls up ... all the old lumber, most-favoured-nation clause and the rest which ... made such a hash of the old world. We know also that won't work. It is the clutch of the dead ... hand. If it was accepted it would be the cover behind which all the unconstructive and truly reactionary people of both our countries would shelter. ... Meanwhile forgive my vehemence which has deep causes in my hopes for the future.'* (Skidelsky, pp.129-131)

Keynes's old ally from the 1920s effort at full employment, Hubert Henderson, now based in the Treasury, and the Bank of England were similarly hostile to Article VII:

'Both Hubert Henderson and the Bank of England disliked the idea of making promises for the future, however vague. The view which they represented was that countries, or groups of countries, should aim to balance their post war trade by the wartime mixture of exchange controls and state trading agreements. This would enable them to maintain stable exchange rates with each other. Article VII, with its ban on discriminatory trading arrangements - those which favoured the exports of one country over another - struck at the heart of this philosophy ...

'The Bank of England minuted: "it can surely be foreseen that we and others will refuse to limit our internal monetary policy by reference to any external standard; that we can never again tolerate conditions in which mass movements of capital are free to overwhelm the international exchanges; that we shall maintain exchange and import controls for an indefinite period; that we shall aim at maintaining the concept and structure of a sterling area; and that we shall retain the liberty to use bilateral negotiations as an instrument for promoting international trade."' (pp.209-10)

But in this case Keynes argued against the idea that the sterling area could be expected to behave as a coherent bloc:

'The Bank attached great importance to import controls to "balance trade". But it did not make it clear whether import controls were to be applied between members of the sterling area or only between the sterling area and the rest of the world. If the latter, they were an extreme form of discrimination; if the former, the sterling area concept became very thin. The Bank's scheme presupposed a pooling of the sterling area's gold and dollar reserves. Under whose control was that reserve to be? Keynes denied that there was enough "solidarity" within the sterling area for Britain to be entrusted with the pooling. It could only be done by an impartial international body.' (p.211)

In the event Roosevelt assured Churchill that Article VII wasn't intended as an attack on Imperial Preference and the impact of it was watered down and combined with other, more interesting aims in the 'Mutual Aid (Lend Lease) Agreement' finally signed in February 1942:

'To that end [the betterment of worldwide economic relations] the [benefits to be provided to the United States of America by the Government of the United Kingdom in return for aid] shall include provision for agreed action ... directed to the expansion ... of production, employment and the exchange and consumption of goods [and] to the elimination of all forms of discriminatory treatment in international commerce and to the reduction of tariffs and other trade barriers ... ' (p.226, fn)

The shift in emphasis away from 'discrimination in either the United States of America or the United Kingdom' to 'discriminatory treatment in international commerce and to the reduction of tariffs and other trade barriers' reflects the shift from the State Department (Hull and Acheson) to the Treasury (Morgenthau and White) and their more ambitious plans for a reorganisation of world trade. Keynes remained the key figure on the British side.

HARRY DEXTER WHITE

The contrast between Keynes and White was quite stark. Keynes was the embodiment of privilege, educated at Eton and Cambridge where he was one of the elite group of the 'Apostles', part of the inner circle of the Bloomsbury Group, married to an exotic Russian ballerina. White was the son of Jewish immigrants from Lithuania.[6] He worked in his father's hardware store and only started his university career at the age of 29. Keynes was famous throughout the world after publishing numerous controversial articles aimed both at specialists and at the general public. Most of White's important writings prior to 1940 took the form of internal memoranda for the US Treasury.

James Boughton, historian of the International Monetary Fund, has written an account of White's Treasury writings which may give us some idea of why Morgenthau was so keen that he should be charged with the work of devising a post war settlement. In a Memorandum written in August 1935 - 'Why and how exports should be increased' - he argued that:

'Only two proposals for stimulating exports had any merit: an international agreement to stabilize exchange rates and an expansion of official loans to foreign governments ... A few months later [in a paper entitled The United Kingdom of Great Britain - PB] *... he noted the importance of creating a dollar zone to compete with the sterling area and weaken the influence of sterling as a constraint on US policy. Currency stability, not the relative size of the foreign exchange market, was to be the cornerstone of his strategy for developing the international role of the dollar: "Though it doesn't matter very much whether New York or London does the most foreign exchange business, it is important to have as many currencies as possible linked to the dollar rather than to sterling, if the rate between dollars and sterling is not fixed. The more currencies tied to the dollar (ie exchange rates fixed to the dollar) the less power will British authorities have to influence American monetary policy. The more international business a country does, the more likely will it be to attract other currencies in its orbit of influence, and the more currencies it attracts the greater will be its international business."'*[7]

However he didn't believe that the dollar by itself was sufficient to exercise this attractive power. In 1940 he began work on an ambitious project, in the event uncompleted, under the title 'The Future of Gold':

'"The Future of Gold" argued that the only way any country could induce investors to hold liquid claims on it for extended periods was to create complete confidence that its currency would not be devalued in the foreseeable future. Since no major country would be willing to surrender its sovereignty over the valuation of its currency, the ability to create such confidence was limited. Investors therefore had and would continue to have a preference for gold over currencies or other liquid assets ... "Many decades at least will have to pass before many countries will elect to keep their reserves in the form of some foreign paper currency never redeemable in gold rather than in the

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6 Skidelsky (p.240) says that they had fled 'the Tsarist pogroms' in Lithuania in 1885. So far as I know there weren't any pogroms, let alone 'Tsarist' pogroms, in Lithuania in the 1880s. The pogroms of 1881-2 took place at the far end of the Pale of Jewish settlement in Novorussia, South East of present day Ukraine.

7 James M.Boughton: *Why White, not Keynes? Inventing the postwar International Monetary System*, International Monetary Fund, IMF Working Paper, March 2002, pp.7-8.

form of gold or currency redeemable in gold." Moreover, he rejected on time-inconsistency grounds the idea that countries could credibly effect a co-operative agreement to fix exchange rates without an anchor to gold. Confronted with the possibility of devaluing (or imposing exchange restrictions) as the "lesser evil" rather than contracting the economy, "the sovereign power will usually elect to pursue the lesser evil."' (p.8)

The problem as seen from White's point of view was to ensure that the post-war world would be a safe place for American exports. To this end it was necessary to ensure that the world - much of it wrecked by the war - should be able to pay for American exports; and secondly that it could be relied on to pay in a currency that could be trusted, meaning, essentially, a currency tied to gold.

The problem from Keynes's point of view was different. Since the 1920s he had been concerned with unemployment, and his solution - the idea that is regarded as typically 'Keynesian' - was to ensure that there was sufficient demand in the economy to absorb a level of production that would keep people in employment. But this implied a closed economy. If the money put in peoples pockets was spent on imports, it would not contribute to maintaining employment in the domestic economy.

KEYNES ON 'NATIONAL SELF-SUFFICIENCY'

In 1933, in the context of Britain going off the gold standard and De Valera coming to power in Ireland on a protectionist platform, Keynes gave a lecture in Dublin on 'National Self Sufficiency', an important social event attended by the leading members of both the main political parties. According to Skidelsky's account, as they gathered for this address by the most famous British economist, the Treatyites were looking self confident while the anti-Treatyites looked uncomfortable, but as the talk progressed the 'smiles faded from one side and appeared on the other.'[8]

Keynes began by evoking his own formation as a free trader but quickly went on to say:

'It is a long business to shuffle out of the mental habits of the pre-war nineteenth century world. It is astonishing what a bundle of obsolete habiliments one's mind drags round even after the centre of consciousness has been shifted.'

Among those 'obsolete habiliments' was the idea of international free trade as a means of solving the problem of poverty, serving 'the great cause of liberty, of freedom for personal initiative and individual gift' as well as 'international concord and economic justice between nations, and the diffusion of "the benefits of progress."'

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[8] Skidelsky: Keynes, vol ii, p.479, quoting James Meehan: *George O'Brien, a biographical* memoir, Gill and Macmillan, 1980. The talk was the first Finlay Lecture delivered at University College, Dublin, on April 19, 1933, published as John Maynard Keynes: 'National Self sufficiency', *The Yale Review*, Vol. 22, no. 4 (June 1933), pp. 755-769. It is (March 2021) accessible on the internet at http://jmaynardkeynes.ucc.ie/national-self-sufficiency.html

But the results, he went on to say, had been disappointing so that:

'it does not to-day seem obvious that a great concentration of national effort on the capture of foreign trade, that the penetration of a country's economic structure by the resources and the influence of foreign capitalists, that a close dependence of our own economic life on the fluctuating economic policies of foreign countries are safeguards and assurances of international peace. It is easier, in the light of experience and foresight, to argue quite the contrary.

'The protection of a country's existing foreign interests, the capture of new markets, the progress of economic imperialism - these are a scarcely avoidable part of a scheme of things which aims at the maximum of international specialisation and at the maximum geographical diffusion of capital wherever its seat of ownership. Advisable domestic policies might often be easier to compass, if the phenomenon known as "the flight of capital" could be ruled out. The divorce between ownership and the real responsibility of management is serious within a country, when, as a result of joint stock enterprise, ownership is broken up between innumerable individuals who buy their interest to-day and sell it to-morrow and lack altogether both knowledge and responsibility towards what they momentarily own. But when the same principle is applied internationally, it is, in times of stress, intolerable. I am irresponsible towards what I own and those who operate what I own are irresponsible towards me.'

With the general diffusion of specialist knowledge and skills a much greater degree of self sufficiency was now possible:

'over an increasingly wide range of industrial products, and perhaps of agricultural products also, I become doubtful whether the economic loss of national self-sufficiency is great enough to outweigh the other advantages of gradually bringing the producer and the consumer within the ambit of the same national, economic and financial organisation. Experience accumulates to prove that most modern mass-production processes can be performed in most countries and climates with almost equal efficiency.

'Moreover, with greater wealth, both primary and manufactured products play a smaller relative part in the national economy compared with houses, personal services and local amenities which are not equally available for international exchange; with the result that a moderate increase in the real cost of the former consequent on greater national self-sufficiency may cease to be of serious consequence when weighed in the balance against advantages of a different kind. National self-sufficiency, in short, though it costs something, may be becoming a luxury which we can afford, if we happen to want it.'

He goes on to argue why we should want it:

'The nineteenth-century free-trader's economic internationalism assumed that the whole world was, or would be, organised on a basis of private competitive capitalism and of the freedom of private contract inviolably protected by the sanctions of law in various phases, of course, of complexity and

development, but conforming to a uniform type which it would be the general object to perfect and certainly not to destroy.'

'Rule-based international order', anyone? But:

'I have become convinced that the retention of the structure of private enterprise is incompatible with that degree of material well-being to which our technical advancement entitles us, unless the rate of interest falls to a much lower figure than is likely to come about by natural forces operating on the old lines. Indeed the transformation of society, which I preferably envisage, may require a reduction in the rate of interest towards vanishing point within the next thirty years. But under a system by which the rate of interest finds a uniform level, after allowing for risk and the like, throughout the world under the operation of normal financial forces, this is most unlikely to occur. Thus for a complexity of reasons, which I cannot elaborate in this place, economic internationalism embracing the free movement of capital and of loanable funds as well as of traded goods may condemn my own country for a generation to come to a much lower degree of material prosperity than could be attained under a different system.'

He goes on to condemn the reliance on commercial profit as the criterion of successful policy:

'The whole conduct of life was made into a sort of parody of an accountant's night-mare. Instead of using their vastly increased material and technical resources to build a wonder-city, they built slums; and they thought it right and advisable to build slums because slums, on the test of private enterprise, "paid," whereas the wonder-city would, they thought, have been an act of foolish extravagance, which would, in the imbecile idiom of the financial fashion, have "mortgaged the future"; though how the construction to-day of great and glorious works can impoverish the future, no man can see unless his mind is beset by false analogies from an irrelevant accountancy ...

'If I had responsibility for the Government of Ireland to-day, I should most deliberately set out to make Dublin, within its appropriate limits of scale, a splendid city fully endowed with all the appurtenances of art and civilisation on the highest standards of which its citizens were individually capable, convinced that what I could create, I could afford and believing that money thus spent would not only be better than any dole, but would make unnecessary any dole. For with what we have spent on the dole in England since the war we could have made our cities the greatest works of man in the world. Or again we have until recently conceived it a moral duty to ruin the tillers of the soil and destroy the age-long human traditions attendant on husbandry, if we could get a loaf of bread thereby a tenth of a penny cheaper.'

He concludes:

'once we allow ourselves to be disobedient to the test of an accountant's profit, we have begun to change our civilisation. And we need to do so very warily, cautiously and self-consciously. For there is a wide field of human activity where we shall be wise to retain the usual pecuniary tests. It is the State, rather than the individual, which needs to change its criterion. It is the conception of the

Minister of Finance as the Chairman of a sort of joint-stock company[9] *which has to be discarded. Now if the functions and purposes of the State are to be thus enlarged, the decision as to what, broadly speaking, shall be produced within the nation and what shall be exchanged with abroad, must stand high amongst the objects of policy.'*

Actually, that isn't quite how he concludes. He concludes with some warnings against a too extreme and uncompromising economic nationalism, with Russia as the prime example. He sees dangerous tendencies in 'the blond beasts of Germany' but thinks it is still too early to judge.

'MERCANTILISM' AND FREE TRADE

I don't know if Keynes ever spoke so bluntly to a British audience in favour of the greatest possible degree of economic self sufficiency but the central argument of the 'General Theory', published only three years later, has little to say on international trade or the balance of payments, a criticism made at the time by Hubert Henderson. The book however does end with chapters on the 'Trade Cycle' and on 'Mercantilism, the Usury Laws, Stamped Money and Under-consumption'. These are presented as 'notes' rather than fully worked out ideas but the notes on mercantilism in particular are relevant to the ideas Keynes developed for the organisation of post-war trade.

They are a defence of the mercantilist view that the balance of payments was a problem that required to be regulated by government action against the classical *laissez faire* view that, given the gold standard, balance of payments problems would sort themselves out of their own accord. According to this view, a country that exported 'too much' would receive an influx of gold from the importing country which would have the effect of pushing prices up. The loss of gold from the importing country would have the effect of pushing prices down. Thus the importing country with its lower prices would gain an advantage over the exporting country with its higher prices and the balance of trade would flow in the other direction. Keynes comments in relation to this apparently absurd proposition: 'The extraordinary achievement of the classical theory was to overcome the beliefs of the "natural man" and, at the same time, to be wrong ... One recurs to the analogy between the sway of the classical school of economic theory and that of certain religions. For it is a far greater exercise of the potency of an idea to exorcise the obvious than to introduce into men's common notions the recondite and the remote.' Keynes's wartime proposal for an International Clearing union was, precisely, aimed at curtailing free trade in order to prevent the emergence of balance of payments problems.

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[9] Or, in the modern form of this absurdity, Angela Merkel's Swabian housewife - the comparison of the state budget to the household budget.

Skidelsky insists that Keynes was an 'internationalist' but I think we can already see quite clearly the difference between Keynes and White. White saw international trade as an ideal to be worked for and developed to the highest possible degree. Keynes saw it as a problem that had to be addressed and dealt with. He complained that:

'in an economy subject to money contracts and customs more or less fixed over an appreciable period of time, where the quantity of the domestic circulation and the domestic rate of interest are primarily determined by the balance of payments, as they were in Great Britain before the war, there is no orthodox means open to the authorities for countering unemployment at home except by struggling for an export surplus and an import of the monetary metal at the expense of their neighbours.[10] *Never in history was there a method devised of such efficacy for setting each country's advantage at variance with its neighbours' as the international gold (or, formerly, silver) standard. For it made domestic prosperity directly dependent on a competitive pursuit of markets and a competitive appetite for the precious metals. When by happy accident the new supplies of gold and silver were comparatively abundant, the struggle might be somewhat abated. But with the growth of wealth and the diminishing marginal propensity to consume, it has tended to become increasingly internecine.'* [11]

SCHACHT'S 'NEW PLAN'

He was doubtless aware that he hadn't dealt with the problem adequately in the General Theory. He believed, though, that he could see the outlines of a solution in the system that was being put in place in Germany by Hjalmar Schacht.

I gave a short account of Schacht's 'new plan' in the first essay in this series, quoting from the testimony of his assistant in the Reichsbank, Otto Puhl.[12] Although the details are complicated, the essential principle was a series of bilateral trade agreements aimed at ensuring that the imports of one party would always be balanced by exports to the other, and vice versa. Skidelsky (pp.228-9) describes the scheme as follows:

'Under Schacht's New Plan of September 1934, bilateral clearing agreements were made with twenty-five countries in Europe and Latin America, designed to balance trade with Germany and each partner at fixed exchange rates, The partner was only allowed to sell as much to Germany as it bought from Germany, The aim of the system was to conduct foreign trade without foreign exchange. It was in effect a pure barter system between pairs of countries. By 1938, some 50 per cent of Germany's trade was conducted through bilateral clearings; only 20 per cent was settled through the 'free' foreign exchange market.

[10] The policy pursued so successfully by Roosevelt and Morgenthau.

[11] J.M.Keynes: *The General theory of employment interest and money*, London, Macmillan, 1936, pp.348-9.

[12] Peter Brooke: 'Economics and the European Union, Part One: Germany before 1945', Irish Foreign Affairs, Vol 13, No 4, December 2020. Also accessible at http://www.peterbrooke.org/politics-and-theology/eu-economics/part-one/

'Under a bilateral clearing agreement, a German importer from, say, Hungary, instead of paying reichsmarks to the Hungarian exporter for exchange into pengos, would pay the reichmarks into the Hungarian Central Bank's clearing account with the Reichsbank. German exporters to Hungary were paid reichsmarks from this account. The opposite process took place in Budapest. No actual exchange of national currencies took place. Credits which accumulated in the clearing of country A for its exports to country B could be used only to purchase imports from country B. The individual exporters in either country received payment in their own national currency from their central bank to the extent that importers made corresponding in-payments.'

Under this system both the 'creditor' (the exporting nation) and the 'debtor' (the importing nation) were subject to a discipline that prevented the exporting country from overwhelming the importing country and thereby disrupting the efforts of the state to structure the economy for its own ends - in the German case rearmament and full employment. We may note in passing that under Schacht's system it would have been impossible for Germany to do to Greece what it was able to do under the system devised by Jacques Delors.

According to an account published early in 1939:

'It is a system whose primary aim is to prevent the flight of capital, and thus to render impossible any resistance by capitalists. This is a rather important conclusion because, as we know, in France an attempt to rearm on anything like the Nazi scale, whilst maintaining free exchanges, has hitherto been doomed to failure by the fact that as soon as the State expanded its expenditure the private entrepreneur used the deficit to disinvest his capital and thereby nullified the effect the State expansion. Owing to the curtailment of private expenditure, employment did not increase to the maximum possible. Under the Nazi system, no such sabotage is possible.

'Secondly, this system of foreign exchange control enables the Government to equate German exports and imports irrespective of the state of trade abroad and the size of the national income at home. If the demand for German products at a certain price should fall, that does not mean that Germany's national income has to fall until the demand for foreign goods is automatically curtailed sufficiently through a fall of income and employment, to equate exports and imports. Equilibrium is achieved by stiffening priorities on imports or by paying increased subsidies on exports. Thus, irrespective of the state of trade abroad, full employment can be maintained at home. The burden of the worsening of the terms of trade is not borne through fluctuation of employment, but directly. The fall of export prices below internal production costs does not prevent exports - nor does it involve losses for the individual exporter.

'This is a very important point. We have been hearing a good deal lately about unfair competition by Nazi Germany through granting of subsidies. We were also told that if these subsidies were increased the German standard of life would continuously decrease and there would a "breakdown" of the system. A worsening of the terms of trade through a fall of foreign demand for German commodities is obviously unfavourable for the Germans. It is very questionable, however, whether

they lose more by pushing their exports at the cheaper price and shifting the burden on to consumers (they could, but have not, shifted it on to "rearmament"; hitherto private consumption provided the "cushion") or whether they would lose more by adopting the individualist system, permitting the national income to shrink until an equilibrium is reached between imports and the new level of exports.' (pp.239-40)[13]

Thomas Balogh, who wrote this account, is described by Skidelsky (p.201) as a protégé of Hubert Henderson whom Keynes later (as he himself got more drawn into the American scheme) characterised as a 'Schachtian'. While Skidelsky calls Henderson a 'national capitalist', he calls Balogh a 'national socialist'. Balogh was to be influential in Britain in the post-war period. He continues his account of the German economy immediately before the war, perhaps indicating at least one of the reasons why Britain might have begun considering the possibility of war with Germany:

'There is, moreover, a further and even more dangerous aspect of German planned economy in foreign trade. The fixing of internal prices enables the Nazi entrepreneurs to give long-term contracts to producers in foreign countries at fixed mark prices. Hence they eliminate any risk of price fluctuations to the producers of those commodities. Germany mainly imports foodstuffs and raw materials. But as the price of foodstuffs and raw materials is very variable the fact that Germany can make long-term contracts at fixed prices is a very important inducement for the producers in those countries to conclude trade agreements with Germany. If, however, they conclude these agreements they must adapt their production to the German market. Hence they will be less able to sell elsewhere, and naturally that will in time establish a buying monopoly in favour of the Nazis. As soon as this monopolistic power is strong enough, Germany will be able to impose on these people her own terms, and they will then not be able to fight since alternative outlets for their products on favourable terms will not be available. Hence these satellite States will have to bear part of the burden of German rearmament. In this way we have a double threat, so far as the foreign trade relations of Germany and the world are concerned, against our commerce. The first threat is the possibility of Germany, by maintaining full employment, offering goods at cheaper prices than any individualistic producer is able to do, the second is that by using the planned method of economy she can obtain a favoured position.' (p.240)

It is often said (including by Keynes himself) that Schacht's bilateral agreements were designed to give Germany an unfair advantage with her trading partners, but according to Skidelsky (p.229):

'In fact, Germany often bought above, and sold below, the world market price: the terms of trade moved against Germany in the 1930s, and it failed to alter them in its favour till 1942, during the war itself. Germany was interested, not in exploiting its monopoly position, but in buying as much, and selling as little, of the materials it needed for rearmament. The bilateral clearing system,

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[13] Thomas Balogh: 'The economic background in Germany', *International Affairs (Royal Institute of International Affairs, 1931-39)*, Vol.18, No.2 (March-April 1939), pp.227-48. I have added the division in paragraphs.

operated at an overvalued exchange rate, enabled it not to buy cheap and sell dear, but to buy more for less.'

Skidelsky gives as his authority an American economic historian, Larry Neal. Neal reviews an existing controversy on the question and concludes:

'If the German goal in negotiations of clearing agreements with smaller countries was to attain economic advantages, there were basically only two ways to attain it: either the exercise of monopsony power, which forced the small trading partner to accept lower than competitive prices on its products imported by Germany, or the use of monopoly power, which forced the small country to pay higher than competitive prices on the German exports it purchased.[14] *The first technique appears to be what one textbook suggests was used when it states, "as Germany soon discovered, a lack of balance in its trade with other exchange control countries provided a means whereby it could take advantage of its buyer's position to exploit countries largely dependent on Germany for their support market." The difficulty with this suggestion is that the prices offered by Germany to its trading partners for its imported commodities were consistently above both the world price and the internal price within the partner country. Thus, the foreign foodstuffs it purchased from south-eastern European countries were acquired at prices from 20 to 40 per cent above the world market price. Basch cites the case of Germany paying prices for Romania's soybeans that were several times those charged overseas. Further, Germany on average paid more for the same commodity when it was imported from a clearing-agreement country than when it was imported from a non-clearing country.'*[15] (p.394).

He discusses the possibility raised by Balogh that this was a policy of 'entrapment', that 'Greater future gains were purchased at the expense of present gains' or that 'Germany's unprofitable pricing policies were designed for political purposes' but concludes: 'In either case it appears from the evidence that Germany made a considerable investment over a number of years (at least five) to achieve a monopoly position that it never exploited.'

FUNK'S 'NEW ORDER'

Schacht was out of office by 1940 and it was his successor, but close collaborator, Walther Funk, who was responsible for the 'New Order' - the reorganisation of Western Europe after the fall of France. A Japanese economic historian says that once the Schacht 'new plan' had been established:

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[14] Neal is using the word 'monopsony' to refer to the condition of a buyer without competition and 'monopoly' to refer to the condition of a seller without competition. In the previous extract instead of 'monopsony' Thomas Balogh talked about a 'buying monopoly'.

[15] Larry Neal: 'The Economics and finance of bilateral clearing agreements: Germany, 1934-8', *Economic History Review*, New Series, Vol 32, No.3, August 1979, pp. 391-404.

'there remained a problem of multilaterally clearing of bilaterally unsettled balances. The "New Order" which Dr.Walter Funk, the German Economic Minister and President of the Reichsbank, announced on 25 July 1940, was a resolution to the above problem by establishing a multilateral clearing system with Berlin as the central clearing house for European payments. The reichsmark would be the international currency within the German-controlled area but the national currencies of the different countries would be remain [sic. would remain? would be retained?]. *Their national currencies will be stabilized in relation to* [the] *reichsmark which would remain stable in relation to gold or the U.S. dollar. Mark balances in the German-Danish clearing account, for example, could also be used to settle Swedish claims. Dr. Funk insisted that this currency scheme would be entirely divorced from gold and adopted from the doctrine of nominalism by Knapp who said that "the currency does not depend for its value upon its gold cover, but on the value which the State gives it".* [The] *currency scheme under* [the] *"New Order" was the first practical plan for a post war monetary and economic order.'* [16] (p.30)

According to Skidelsky Keynes made no mention of the 'Schachtian' system prior to 1940, not even in the Preface to the German edition of the General Theory, published in 1936.[17] But in 1940, while developing his own ideas for a post-war international order, he expressed a quite lively interest. To continue Iwamoto's account:

'In November 1940 Keynes was asked by Harold Nicholson, the Minister of Information, to prepare a counter proposal for German propaganda of "New Order". Keynes replied to this request:

"In my opinion about three-quarters of passages quoted from the German broadcasts would be quite excellent if the name of Great Britain were substituted for German [sic] *or the Axis, as the case may be. If Funk's plan is taken at its face value, it is excellent and just what we ourselves ought to be thinking of doing."*

'In a memorandum entitled the Proposal to Counter the German "New Order", *dated on 25 December 1940, circulated on 1 December* [sic. January?], *Keynes expressed a certain sympathy with the German proposal based on Schachtian bilateralism. In the memorandum he says: "After the last war* laissez-faire *in foreign exchange led to chaos. Tariffs offer no escape from this. But in Germany Schacht and Funk were by force of necessity to evolve something better. In practice they have used their new system to the detriment of their neighhbours. But the underlying idea is sound and good." He goes on to say: "The most definite of the German plans so far is* [the] *currency scheme of Dr Funk ... It has only one merit, namely that it avoids some of the abuse of the old* laissez-faire *international currency arrangement, whereby a country could be bankrupted, not*

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[16] Takekazo Iwamoto: 'The Keynes plan for an International Clearing Union reconsidered', *The Kyoto University Economic Review*, 1997, 65(2): pp.27-42. The English is sometimes a little awkward.

[17] p.230.Skidelsky quotes his preface to the German edition as saying that his '"theory of output as a whole", while "applicable" to German conditions, was "worked out having the conditions of Anglo-Saxon countries in mind - where a great deal of laissez-faire still prevails"'. Skidelsky then comments, rather surprisingly: 'It is a pity that he did not put the adjective "rightly" or "fortunately" after "laissez-faire"'. As if Skidelsky has forgotten that Keynes was constantly inveighing against laissez-faire.

because it lacked exportable goods, but merely because it lacked gold ... The arrangement we are now slowly perfecting, by which international exchange returns to what it alway should have been, namely a means for trading goods against goods [ie barter - PB], *will outlast the war."* [A] *similar point was repeated in his first draft of the ICU* [International Clearing Union - PB], *about ten months later:*

> *"Dr. Schacht stumbled in desperation on something new which had in it the germs of a good technical idea. This idea was to cut the knot by discarding the use of a currency having international validity and substitute for it a* [system that?] *amounted to barter, not indeed between individuals, but between different economic units … The fact that this method was used in* [the] *service of evil must not blind us to its possible technical advantage in* [the*service of a good cause … I expound in a separate paper a possible means of still retaining a currency having an unrestricted international validity. But the alternative to this is surely not a return to the currency disorders* [of] *the epoch between the wars, mitigated and temporarily postponed by some liberal Red Cross work by the United States, but a refinement and improvement of* [the] *Shachtian device."*'[18]

Skidelsky (pp.196-7) gives an interesting quote from Keynes in a private letter written in November 1940:

'If Hitler gets his new Europe going properly, with barter replacing gold ... and with all the nations playing the cultural and ethnographical roles allotted to them, while the Vatican provides the slave states with a philosophy of life, then England can be made to look like an intolerably disruptive pirate nuisance in the eyes of Europe. We would become the real aliens, the Protestant dissenters, the Berbers of the North. In Hitler's favour is the fact that he has the will and ambition to govern Europe and that Rome, Berlin and Munich are the natural places to do it from. But as long as the blockade is effective he is compelled to loot, and while he has to loot the conquered territories, his propaganda must fail.'

That might give us some idea of what the British thought they were doing, keeping the war going when there was still no guarantee of the entry of the US.

SKIDELSKY'S RELATIONSHIP WITH KEYNES

Skidelsky, I suspect, is inclined to understate the influence of Schacht on Keynes or, it might be better to say, the similarity of their thinking. How one reads Keynes may depend on how seriously one takes his Dublin speech on national self-sufficiency. Is it just a passing thought or does it express an idea he was aiming for - freedom from the market, the profit motive and, especially, the pressure from international finance and international trade? If the latter is the case then his defeat at the hands of the Americans and White was

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[18] pp.30-31. I have suppressed Iwamoto's italicisation of certain passages. His source for the quotations is a book I haven't read, Armand von Dormael: *Bretton Woods, birth of a monetary system*, Macmillan, 1941.

more or less complete. By Vol iii of his biography, Skidelsky wants him to be an international free trader (as he is represented in the first biography by his friend and colleague, Roy Harrod) but, by the immediate position of Britain as a country with a huge balance of payments deficit, tempted into the Schachtian 'barter' system - clearing arrangements designed to prevent as far as possible balance of payments problems from impacting on the organisation of the domestic economy.

Skidelsky is now known as a champion of the relevance of Keynes to the modern economy and it was as a champion of Keynes that he initially embarked on the huge project of the biography. When he wrote his account of the travails of the Labour government in 1939-31[19], he came to the conclusion that the men who had the solution to the problem were Keynes, Mosley and Bevin. The immediate result was his biography of Mosley, which nearly wrecked his academic career, not because it isn't a good and useful study but because it was undiplomatically enthusiastic about its subject. In the course of writing the Keynes biography, however, he seems to have come to the conclusion that the limitations of Keynes's leading ideas had been exposed by the events of the 1970s. The third volume ends with quite a severe critique of Keynes's thinking from a broadly free market perspective. He was raised (if that's the right word) by Margaret Thatcher to the House of Lords where he sat on the Tory benches, resigning the Tory whip, however, in protest against the party's support for the war on Serbia. It was with the Great Financial Crash in 2008, which exposed the wrongheadedness of the Friedmanite approach (the belief that booms and busts could be moderated by tweaking interest rates), that he turned again to Keynes, publishing the appropriately titled 'Return of the master' in 2009.

He admits this in a talk he gave in 2011 when he says:

'The extent to which I had swallowed the non-Keynesian message comes out in an article I wrote for the FT in 2001. Basically I endorsed the view that monetary policy could do all the fine tuning needed to 'stabilise expectations', though I covered myself by wondering whether it would be enough to deal with a serious drop in business confidence. I called this 'minimum Keynesianism'. (FT, 16 August 2001).

'This was the period of the 'Great Moderation'. I now look back on it as reminiscent of the Roaring Twenties, which were supposed to go on forever. Then we had the collapse of 1929 followed by the collapse of the Credit Anstalt in 1931, Austria's special contribution to the Great Depression. Then, as later, monetary policy was supposed to have cracked the problem of the business cycle. 'Keynes also believed this in the 1920s, but I, and others, had much less reason to do so after the Keynesian Revolution; yet we did.

'The collapse of the banks in 2007-8 showed that the financial system – the system which drives investment – was just as naturally unstable as it always had been. We should have been warned by

[19] Robert Skidelsky: Politicians and the slump - the Labour Government of 1929-1931', Penguin Books, first published in 1967.

the East Asian crisis of 1997-8, but like many others I assumed this was a phenomenon of 'immature financial markets' and 'crony capitalism' which could not happen in the West.

'But George Soros rightly pointed out in 2008 that 'the salient feature of the current financial crisis is that it was not caused by some external shock….The crisis was generated by the system itself'.

'This is what Keynes had always claimed: the market system lacked a thermostat and its temperature was likely to oscillate wildly unless controlled by the government.' [20]

Keynes had of course been formed in the classical school and he was a realist, both in terms of knowing how to express himself persuasively to a nation soaked in liberal free trade ideology, and in knowing that getting practical results always involved compromise (and in seeking compromise one can have an advantage in starting out from an extreme position). In the case of the discussions with the US, Keynes wanted above all to secure American commitment to a plan by which countries that had fallen into balance of payments difficulties could be helped, and he wanted the Americans (against the still powerful isolationist instinct) to provide financial assistance to post-war Europe in general and to Britain in particular. Even if the plan eventually agreed at Bretton Woods fell far short of his own ideal scheme (which he himself described as 'utopian') he could still feel that he had secured these two aims. Hence, Skidelsky would argue, his abandonment of the Schachtian side of his thinking 'having persuaded himself that the American replacements - Bank and International Monetary Fund - were almost as good. To his left-wing disciples, this was a betrayal based on self-delusion; to disciples like Harrod and Meade, it showed that his heart was always on the internationalist side. To the historian it seems as if Keynes (and Britain) had little choice' (pp.207-8).

THE 'INTERNATIONAL CLEARING UNION' AND THE 'INTERNATIONAL STABILISATION FUND'

The first draft of Keynes's proposal for an International Clearing Union came in two papers written in September 1941 - 'Post War Currency Policy' and 'Proposals for an International Currency Union.' Skidelsky describes it as a marriage of 'the Schacht-Funk "clearing" approach with the banking principle.'

Where there was a trade imbalance, the credit due to the exporting country could, up to a certain limit, be paid by the Clearing Bank in the form of bank money, later called 'bancor', which could only be given to the country's central bank. The limit was imposed by an overdraft facility, or quota, 'equal to half the average value of the country's total trade for the five last pre-war years.' (Skidelsky's account is on pp.206-7. In trying to summarise it I'm taking a risk and the keen reader may want to consult the original.) The total overdraft

[20] Robert Skidelsky: *Keynes for the 21st century*, a talk given to the Renner Institute in Vienna, May 18, 2011, accessible at http://www.skidelskyr.com/site/article/keynes-for-the-21st-century/

facility for all countries concerned came to something like $25 bn. A debtor country whose overdraft averaged more than a quarter of its allowed quota would be allowed to devalue its currency by up to 5%; if it was more than half it could be required to do so as well as to sell to the bank any free gold, and prohibit capital exports. Beyond that limit it might be expelled. But, and this is crucial, a similar discipline was imposed on creditor countries, requiring an upward revaluation of their currency and eventually 'credit balances exceeding quotas at the end of the year would be confiscated and transferred to the Reserve Fund.' Interest was to be charged not just on the debtor 'overdrafts' but also on the creditor surpluses. Ideally 'at the end of the year the sum of bancor balances would be exactly zero' which, if I've understood it aright, would amount to a multilateral barter system.

National currencies would stand in a 'fixed but adjustable relation to a unit of ICB's bank money, which itself was expressed in terms of a unit of gold. But this link with the gold standard was a fiction. Whereas bank money could be bought with gold, it could not be sold for gold ... Keynes's long-run purpose was to de-monetise gold so that central banks would lose any incentive to hoard it.[21] Bank money would be the ultimate reserve asset of the system.' Keynes represented his scheme as an alternative, indeed as the only possible alternative to Schachtianism but we might be reminded of what was said above in Iwamoto's account of Funk's New Order: 'Dr. Funk insisted that this currency scheme would be entirely divorced from gold and adopted from the doctrine of nominalism by Knapp who said that "the currency does not depend for its value upon its gold cover, but on the value which the State gives it"'.

Keynes first saw White's proposals in July 1942 and White first saw Keynes's proposals in August. A 'Joint Statement by Experts on the Establishment of an International Monetary Fund' was issued in Washington and London in April 1944, opening the way for the Bretton Woods conference in July. Between those two dates there were lengthy discussions about the details of the two plans, involving other countries, most notably Canada but also including the 'governments in exile' of countries still under German occupation. So far as I can see the result of those discussions was a steady whittling away of everything that was interesting and distinctive in Keynes's plan and an acceptance - including by Keynes himself - of something very nearly resembling the original proposal from White with its two institutions, a World Bank and an International Stabilisation Fund.

Most obviously gone was Keynes's proposal that there should be a single reserve currency, the bancor, which could only be used for international trade and which was not gold based. Keynes, as we have seen, had wanted a 'one way convertibility'. Bancor could be given in exchange for gold but gold could not be given in exchange for the bancor. The bancor itself was a pure *fiat* currency. Countries would have access to it, not on the basis of

[21] The policy pursued through the 1930s by both the US and France.

contributions of their own, but of a calculation of their pre-war trade capacity. Keynes's long term ambition was that the purely paper bancor would replace gold as the principle reserve. Keynes fought for the bancor to the end, at least in a new form given by White, the unitas. To quote a history of the IMF;[22]

'One apparently fundamental difference between the two countries' officials concerned the proposed international currency, called by Keynes "bancor" and by White "unitas." It has been seen above that for Keynes this would have been a true medium of exchange, in which loans would have been made by the Clearing Union, but that for White it was no more than a standard of value, which could be discarded without impairing in any way the working of the Stabilization Fund.

'At the outset of the discussions in Washington, Keynes put forward a memorandum in which he sought to imbue unitas with the qualities which he had proposed for bancor. His motives for this proposal were complex; they included ... (3) the advantage that the holder of unitas could utilize the credit anywhere rather than having a claim against an individual country, and (4) a belief that the structure of the Fund could be more simply and understandably stated in terms of unitas than of a "mixed bag" of currencies ...

'Keynes' proposal was resisted by the U.S. officials, who suggested that the British, "unable to secure the redistribution of real gold, proposed to create a substitute out of thin air." ... While not admitting the third and fourth points, they countered that the effect of Keynes' proposal would be the same as that of the Clearing Union itself, namely, to expand the U.S. commitment beyond its contribution.'

Keynes had argued in favour of a single specialist currency against the 'mixed bag' of currencies which required a complicated process of juggling the claims all the different currencies might have on each other. It is difficult to believe that he didn't recognise that the aim the Americans were working towards - certainly the main consequence of the final outcome - was that there would be a single currency - the dollar, backed by gold.[23] Keynes's bancor would, of course, have been independent of the dollar.

Basic to Keynes's conception was that creditors would be disciplined as well as debtors and that the disciplinary process would be, so to speak, automatic. The consequences of excessive debits or excessive surpluses and the conditions under which loans would be given would be known and would be purely quantitative, activated when the debt or

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[22] *The International Monetary Fund 1945-1965 : Twenty Years of International Monetary Cooperation Volume I: Chronicle, Chapter 1: The Keynes and White Plans (1941–42)*, a book available on the IMF website, ascribed to the IMF as author. It can be downloaded in book form. Had I done so (I read it online) I could have given page references. But life is too short.

[23] Hence this extraordinary passage in Skidelsky's account of the Bretton Woods agreement (p.352): 'A little noticed amendment to Article IV (section 1) laid down that the par values of currencies should be expressed in terms of gold *"or in terms of the US dollar of the weight and fineness in effect on 1 July 1944."* This made the dollar, the only gold-convertible currency, the key currency of the new system. While every other currency could devalue against the dollar, the US dollar could be devalued only against gold.' (my emphasis - PB). Did Keynes really fail to notice the importance of this?

surplus reached a certain level. His discipline was a matter of automatically allowing or requiring the exchange value of the national currency to be changed. Basically he wanted to preserve the greatest possible autonomy for the national economies to pursue policies that would favour full employment. White on the other hand was concerned chiefly with the disciplining of debtor countries in such a way as to ensure that they could pay their debts. In addition to the quantitative conditions for giving loans, there would be qualitative conditions, concerning the proper use of the money that was to be issued. The Fund was to be furnished with a team of specialists charged with developing policies for the internal reorganisation of the economy in difficulty. And everything was calculated to put obstacles in the way of changing the value of the currency.

A British Treasury spokesman, Sir David Waley, complained:

'We lose part of our freedom to alter the exchange rate and thus to some extent our internal policy for maintaining maximum production and full employment may be prejudiced by our obligations under the scheme. In return we, so long as the Fund thinks we are behaving reasonably [nb - PB], *obtain a credit in dollars or other needed currencies, until these currencies become "scarce." Thus we cannot count for certain on any precise amount of facilities and have given up part of our birthright for a mess of pottage which is likely to disappear from the menu just when our appetite is keenest.'*

He goes on, however, to explain why the British accepted it. It should be said that once the idea of the bancor had been dropped it was really obvious that, despite the 'mixed bag' of currencies the scheme would be dependent on the dollar and the good will of the Americans:

'But, despite these inevitable limitations, the Stabilization Fund scheme is surely far better than no scheme at all.… The Stabilization Fund scheme provides Member States with considerable reserves and thus does a good deal, at any rate, to facilitate a policy of expansion when that policy is needed to avoid a slump.'[24]

When the British agreed to the Joint Statement issued in April it was understood that there would be a 'transitional period' during which the conditions embodied in the statement - including 'the proposal to fix the gold value of sterling and to limit the United Kingdom's right to change this value' would not apply, and that 'the United Kingdom would not commit itself to accept the Fund until it saw how the difficulties of the transition period were to be met.'. Recommending the Joint Statement in the House of Lords Keynes (he had been made 'Baron Keynes of Tilton' in 1942), cited the transitional phase as one of its merits. Somewhat bizarrely (still quoting the IMF history) he said that 'the Fund would have the duty to approve changes in exchange rates that were required to make these rates

[24] ibid.

conform to the needs of domestic policies' and that 'these proposals are the exact opposite of the gold standard.'

Skidelsky comments (p.336):

'He seemed to advocate the monetary plan as a way of maintaining the sterling area and imperial preference system, whereas the Americans all too clearly wanted to dismantle both. He claimed Britain's right to determine its own exchange rate, when the Americans wanted a fixed exchange rate system. When told in Washington a little later that his line of defence had greatly embarrassed White and others, Keynes replied that it had been the only way to save the Fund from political extinction at Westminster ...'

After quoting Roy Harrod representing Bretton Woods as a triumph for Keynes's 'new economic theory', Skidelsky concludes more realistically (p.357):

'Keynes gave the Bretton Woods Agreement its distinction not its substance. The Agreement reflected the views of the American, not the British, Treasury, of White not Keynes. The British contribution tended, finally, towards the negotiation of derogations, postponements and escape clauses. The Agreement was shaped not by Keynes's 'General Theory' but by the US desire for an updated gold standard as a means of liberalising trade. If there was an underlying ideology, it was Morgenthau's determination to concentrate financial power in Washington. As the 'Commercial and Financial Chronicle' pointed out "The delegates did not reach an 'agreement'. They merely signed a paper which looked like an agreement." There was a transition period of indeterminate length.'

I started work on this essay with the aim of setting the scene for the account of post-war developments based on the analysis by Joseph Halevi. I had thought that the initial framework for the post-war developments had been established at Bretton Woods. In fact, however, although the institutions of the World Bank and International Monetary Fund did indeed come into existence through Bretton Woods, it was only later that their pernicious influence began to be felt. In the event the plans laid by Roosevelt, Morgenthau and White were, temporarily, swept aside by a radical change in the direction of American policy which occurred around 1947. That will be discussed in the next article in this series.