

*The Failure of the 'Radical Alternative': Public Works, Deficit Finance and British Interwar Unemployment **

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A dominant theme in studies of British interwar unemployment is the sharp contrast that existed in the field of public policy between the development of an essentially fragmented, *ad hoc* response by governments, supposedly nurtured by political expediency, faltering will-power and intellectual flabbiness, and the emergence of radical pleas for a more positive and planned interventionist programme centred around government-financed schemes of national reconstruction. Two features of the existing literature are particularly relevant in this context. The first is the distinct impression conveyed by some writers that the authorities between the wars singularly failed to adopt radical and enlightened economic policies that *would* have worked to reduce unemployment substantially, partly as a result of their wilful ignorance, or at least inadequate understanding, of the more challenging (if still questionable) branches of contemporary economic theory. Consider Skidelsky: 'The real story of domestic policies of the interwar period is the defeat of the economic radicals by the economic conservatives'.¹ Or Kindleberger's citation of 'instance after instance of what, with hindsight, appears as economic illiteracy... There were many economists and a few public figures... who had domestic remedies which made sense in modern times'.² The second and more specific claim, associated especially with Skidelsky's early work, is that the failure of the Labour Party in this regard arose from its commitment to a form of 'Utopian Socialism' which prevented it from coming to terms with economic reality, encouraging it to search mistakenly for a total solution to the problem of poverty instead of trying more practically to

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¹ R. Skidelsky, *Politicians and the Slump. The Labour Government of 1929-1931*, Harmondsworth: Penguin Books, 1970, p. 11.

² C. KINDLEBERGER, *The World in Depression 1929-1939*, London: Allen Lane, 1973, pp. 23-4.

meet the immediate crisis of unemployment. In Skidelsky's words, 'It was a parliamentary party with a Utopian ethic'.³

The shortcomings of government action are often further highlighted by frequent reference to the contemporary policy prescriptions of Keynes, Henderson, Lloyd George and Mosley. These shared a common emphasis on the need for a purposeful redirection of effort towards domestic economic recovery based on an expansion of loan-financed public investment far beyond a level sufficient merely to compensate for deficiencies within the private sector. As is well known, such arguments were a central concern of Keynes from 1924, formed the basis of the Liberals' 1929 electoral platform, brought Oswald Mosley into direct conflict with the reigning parliamentary consensus of the early thirties and inspired Lloyd George to launch his 'New Deal' in 1935.⁴ They had, moreover, achieved a substantial intellectual following by 1933. By then Keynes, who above all had spearheaded the attack on conventional orthodoxy, had become convinced that the freer movement of interest rates occasioned by the abandonment of the gold standard two years earlier would not in the prevailing economic climate work quickly enough or positively enough to stimulate sufficient investment to generate full employment. It was essential, he therefore argued, for governments to create more optimistic conditions for the expansion of business enterprise by promoting deficit-financed public works rather than relying upon thrift, deflation and the return of normality.

But public works as officially conceived were never destined to achieve a substantial reduction in unemployment. They developed in the early years of the postwar slump purely as emergency measures, necessary to allay unrest and to ease the strain on the revamped unemployment insurance scheme. Insofar as they were based on any radical departure from Edwardian practice, it was in the acceptance by the State of the need to alter the timing of its normal capital expenditure (by advancement or retardation) to counteract the effect of cyclical fluctuations without raising the trend level of expenditure over the course of the business cycle — to 'maintain the aggregate demand for labour... approximately at a uniform level from year to year' as the Labour Party put it. For the most part governments, whether Labour or Conservative, strove purposely to reduce their commitment to public works activity to within the shortest possible period compatible with efficiency and economy. In the event public works managed to cater for but a fraction of the registered unemployed, were least able to be undertaken where they were most needed and proved particularly unsuited to skilled men in industries with little prospect of long-term revival. Why, despite the vigour and urgency with which they were pressed in the twelve years or so after 1924, did alternative policies for public investment fail to evoke a more positive response from government?

³ Skidelsky, *op. cit.*, p. 12.

⁴ For further discussion see Skidelsky, *op. cit.*, D. WINCH, *Economics and Policy*, London: Hodder and Stoughton, 1969.

II

It is easy to appreciate how the notion of a 'missed opportunity' has been allowed to colour assessments of the nature and effectiveness of interwar unemployment policy given the authorities' predilection for ameliorative, *ad hoc* emergency schemes in the face of vigorously expounded alternative strategies involving direct action on a national scale. Such an approach must be treated cautiously. It serves on the one hand to exaggerate the extent to which the failure to adopt unorthodox economic 'remedies' resulted from the unfortunate delay with which influential economists, notably Keynes, formulated proposals with the required intellectual precision and logical consistency to win political approval. On the other hand it serves to minimize the existence of more fundamental obstacles to the adoption of policies which with hindsight may appear as the only common-sense ones to have chosen. Insofar as proposals for deficit-financed public works along Keynesian lines are concerned, the key to understanding the alleged gap between opportunity and reality lies not in the observed robustness of economic science as it was called into service nor in the inherent characteristics of political parties — whether 'Utopian' or gradualist — but rather in the strength and influence of a political and economic orthodoxy inside and outside of Whitehall which elevated within official circles the acceptance of particular policy goals which were essentially incompatible with the effective reduction of mass unemployment.⁵

It is tempting nevertheless to argue that until Keynes himself provided a convincing elucidation of the theoretical model by which effective policies could be formulated for the solution of chronic unemployment governments could hardly have been expected to have adopted alternative policies which at the time of their most vigorous exposition lacked sufficient intellectual rigour to challenge the ruling canons of classical economic theory. The very shortcomings of many of the proposals pressed upon the government adds weight to such an argument. It is quite clear, for example, that although there was within the labour movement of the early 1920s an intuitive grasp of the necessity to maintain or expand the level of consumption in order to increase employment,⁶ neither the Trades Union Congress nor the Labour Party actually embraced the idea of deficit-financed 'pump-priming' for the sake of creating work, nor did either fully appreciate the financial implications of any expanded programme of

⁵ Cf. Pollard's assertion that 'Socialism was... not so much the cause for inaction... as the victim of actions taken without regard to it'. 'The Great Disillusion', *Bulletin of the Society of Labour History*, 16, Spring 1968.

⁶ Incorporating for example demands for the provision of 'built-in' stabilizers, notably increased sickness, old-age and unemployment benefits, and for the establishment of legal wage minima.

public works.⁷ Although the Independent Labour Party supported schemes of public works it was more preoccupied with promoting social justice than with defending unorthodox budgets. Under-consumptionists such as J.A. Hobson supported public works but insisted that they be accompanied by measures of progressive taxation directed towards the redistribution of wealth in favour of wage-earning classes. The emphasis was upon income as the determinant of savings and investment precluding therefore any systematic use of monetary or fiscal controls to stimulate investment.⁸

The support given in the 1920s to the more limited device of altering the timing of existing levels of capital expenditure over the course of the business cycle was not accompanied by any systematic analysis of the proportion of public to total demand and its likely effect upon employment. Furthermore, in the absence of regular detailed data as to the composition of the unemployed, their duration of unemployment and their life-cycle of employment and unemployment, there could be no guarantee that those individuals most in need of a job would necessarily be those with the ability or the opportunity to gain employment from any work created during a period of depression.

The 'radical' programmes of the late 1920s in support of national schemes of public works were by no means free of ambiguity, vagueness or inconsistency. Although the Liberal Party's proposals of 1929 are noteworthy for their early if somewhat rudimentary exposition of a dynamic policy, implicitly recognizing the role of the multiplier,⁹ of expectations, and of the accelerator,¹⁰ they were attacked as unrealistic because they were not presented in any finite terms, envisaging no upper limits to the process of cumulative expansion. The Liberals' repeated claim that public works expenditure would pay for itself from savings on the unemployment fund and from increased Exchequer receipts ignored the fact that the former item would be a form of extra budgetary relief and that income tax and commodity tax receipts would be subject to a time lag following any effective rise in incomes.¹¹

The Labour Party's somewhat heady plans for national reconstruction were

⁷ See *Unemployment: A Labour Policy*, (Report of the Joint Committee on Unemployment Appointed by the Parliamentary Committee of the Trades Union Congress and the Labour Party Executive), January 1921, p. 8. T.U.C., *Annual Report* 1923; D.I. MACKAY, K.J.C. FORSYTH and D.M. KELLY, 'The Discussion of Public Works Programmes, 1917-1935: Some Remarks on the Labour Movement's Contributions', *International Review of Social History*, XI, 1966.

⁸ J.A. HOBSON, *The Economics of Unemployment*, London: Allen and Unwin, 1931, pp. 78-81.

⁹ Although the Liberals recognized that the increased income of those employed on public works could lead to increased expenditure beyond that, they nevertheless restricted such secondary effects to related sectors of industry only.

¹⁰ i.e. the process whereby induced investment is called forth because an increase in capital is required to enable output to expand further.

¹¹ U. HICKS, *The Finance of British Government, 1920-1936*, Oxford: Oxford University Press, 1938, pp. 224-5.

almost totally devoid of any understanding of the necessary financial implications of a general stimulation of economic activity through a large development programme. Nor was Mosley's strident demand that public works be given more sympathetic attention as a practical means of home-market recovery matched by any ready (let alone convincing) analysis of their likely cumulative impact on demand and employment. In similar vein, Lloyd George's enunciation of the effects on jobs of his 1935 plan of national development was based essentially upon his own particular analysis of the 'real' components of demand and supply in the labour market, allowing the Government ample scope to dismiss his estimates as mere 'hopeful prophecies'.¹²

It is customary nevertheless to point, in support of the view that inadequate economic theory was a major stumbling block to the adoption of large-scale interventionist policies in aid of employment, to the extent to which Keynes changed his mind down to the mid-1930s as to the appropriate roles, methods and goals of internal monetary and fiscal policy, to how dependent he was upon Kahn's pioneering analysis of the primary and secondary employment effects of increased investment which only became available in 1931,¹³ and to how it was not until March 1933 that Keynes made his first full statement of deficit-finance, distinguishing capital and current accounts. There is evidence too of how an analytical version of the multiplier, though available to members of the Economic Advisory Council's Committee of Economists early in 1930, failed to evoke amongst them much discussion of its potential for policy.¹⁴

There are good reasons, however, for not dwelling unduly on the absence of a coherent body of economic analysis in support of radical programmes of deficit-financed public works as an acceptable excuse for the shortcomings of government policy. It is clear that there was growing support, not least within the economics profession, for policies designed to expand home investment in order to stimulate demand long before Keynes provided the full weight of his theoretical analysis. Keynes himself maintained that practically every leading economist by 1929 supported the need for an expansionist programme involving an easier monetary policy and large-scale government expenditure. Where Keynesian-type policies were adopted in other countries, moreover, it was not as a result of officials there having grasped the fundamentals of full-employment theory far in advance of their British counterparts.

It might still be argued, of course, that it was not the absence of proto-Keynesian ideas that was important so much as the speed by and the extent to which they developed an authority sufficiently persuasive to secure the sym-

¹² P.R.O. Cab 24/256, CP 150, 'Statement by His Majesty's Government on Certain Proposals Submitted to them by Mr. Lloyd George', 19 July 1935.

¹³ R.F. KAHN, 'The Relation of Home Investment to Unemployment', *Economic Journal*, 41, 1931.

¹⁴ S. HOWSON and D. WINCH, *The Economic Advisory Council 1930-1939*, Cambridge: Cambridge University Press, 1977, p. 49.

pathetic support of policy makers. Much is made in this context of recent evidence of an alleged conversion of the Treasury and the Bank of England to 'Keynesian-type' policies at least a year before the publication of the *General Theory*, following upon a supposedly more enlightened climate of economic reasoning in the mid-'thirties than had been apparent in the 'twenties.¹⁵

But this is to miss the point. The absence for most of the interwar period of any precise or comprehensive analysis of the dynamic effects of an increase in the scale of government expenditure does not mean that the authorities' opposing arguments held sway because they possessed greater intellectual strength or sounder theoretical underpinning. Nor should it imply that arguments in favour of state-sponsored investment on a national scale would have won greater respect or gained earlier acceptance as declared objectives of policy had the progressive elucidation of the concept of the multiplier or the considerable support for a positive programme of 'pump-priming' evident within informed circles by 1933¹⁶ occurred much earlier. The influences determining the official response to interventionist remedies for the reduction of unemployment have to be sought outside of the imperfections of economic knowledge. After all Keynes had an instinctive grasp of policy priorities long before the *General Theory* provided the theoretical foundations to support many of his proposals.¹⁷ It was the imperfections and injustices of the *laissez-faire* system and not the blatant inadequacies of economic theory that spurred Keynes to action. Indeed, his advocacy of loan-financed public works in May 1924 was not at the time based on any revolutionary concept of the use of fiscal policy with regard to savings and investment; it was rooted in a belief that there was a fixed volume of aggregate savings. He called nevertheless for the state to play a more positive role in the organization and distribution of the flow of that volume of savings.

III

It was not, therefore, the clash between the 'conservatives' and the 'radicals' that was important. It was the distinct absence within the political establishment of any real dissent from an economic orthodoxy which powerfully influenced the essential objectives of government policy.¹⁸ Added to this was a predisposi-

¹⁵ See for example Howson and Winch, *op. cit.* Chapter 5; R.S. SAYERS, *The Bank of England 1891-1944*, Vol. 2, Cambridge: Cambridge University Press, 1976, pp. 462f.

¹⁶ Some of the most influential economists of the day joined forces between 1932 and 1933 (at least within the pages of *The Times*) to denounce government economy measures and to advocate raising demand by organized deficit financing.

¹⁷ Keynes stressed in 1931 that the differences between those who supported schemes of state-sponsored investment and those who rejected them 'are not so much matters of theory as of the practical judgement of probabilities and of what is most prudent', *Committee on Finance and Industry*, 1931, Addendum I, para. 53.

¹⁸ For a fuller discussion see R. SKIDELSKY, 'The Reception of the Keynesian Revolution', in M. KEYNES (ed.), *Essays on John Maynard Keynes*, Cambridge: Cambridge University Press, 1979.

tion on the part of every party in power to give undue prominence to the bearers of that orthodoxy — especially in the City — thus helping to reinforce the powerful influence they wielded within the establishment.

In the period down to 1931 especially politicians remained trapped in a body of thought which gave particular prominence to Britain's unique entanglement in the world economy. From this followed an entrenched belief in economic internationalism as the foundation of nineteenth-century economic success and the justification for opposing any policies for the relief of unemployment which put the pursuit of national self-determination above the maintenance of a healthy international economy.¹⁹ This helps to explain why the efforts to remedy structural unemployment in the late 1920s placed so much emphasis upon reduced capacity and rationalization, lower unit costs and the reduction or redeployment of the labour force as a way of expanding exports. Politicians were unaware of or unwilling to accept any policy trade-offs. Labour's decisive links with nineteenth-century Liberalism made acceptance of the gold standard, free trade and the finance-capitalism of the City of London easy to equate with socialism. But by the same token it put the Party at odds with those such as Keynes who insisted in the late "twenties and early" thirties that to avoid cumulative deflation in conditions of international disequilibrium the ties between national and international economics had to be severed.²⁰

Perhaps the most notorious manifestation of economic orthodoxy was the 'Treasury View' and its repudiation of the search for economic recovery via domestically-orientated, government-financed public works on a national scale. At its crudest, the Treasury's basic objection to such state-sponsored public works was that they would be diversionary and unproductive. With a limited supply of capital available for the finance of new investment, it argued, borrowing for public works without due regard to profitability would simply reduce the supply of capital available to finance private (and more profitable) investment. Productive private investment would increasingly be replaced by less productive public investment, helping to lower efficiency and to raise costs throughout the economy. Moreover, increased government expenditure beyond the levels justified by prevailing conditions of demand would encourage price rises and an increase in wage units costs, thus adding a twist to the inflationary spiral.²¹ The 'diversionary' argument was manifestly absurd in conditions of large-scale unemployment and surplus productive capacity and

¹⁹ Skidelsky in M. Keynes, *op. cit.*

²⁰ R. SKIDELSKY, '1929-1931' Revisited,' *Bulletin of the Society for the Study of Labour History*, 21, Autumn 1970.

²¹ For a detailed statement of the Treasury's view of the effect of a development loan programme see *Memoranda on Certain Proposals Relating to Unemployment*, Cmd. 331, 1929. The nature of the contemporary fear of inflation was outlined by R.F. KAHN in 'Public Works and Inflation', *Journal of the American Statistical Association*, XXVII, March 1933.

had been rejected by practically all leading economists by 1929.²² Moreover, as Keynes and Henderson pointed out, the notion that state investment was either inflationary or diversionary could logically be applied to all private investment.²³

The official records of interwar administrations bear witness however to the powerful influence of the 'Treasury View'. Churchill, as Chancellor of the Exchequer, informed the Cabinet in November 1925 that in the opinion of the Treasury 'unemployment is more effectively assisted by National economy than by National expenditure'.²⁴ The Liberals' plans for national development, so cogently argued by the end of the 'twenties, were roundly condemned by the Treasury:

'The whole programme reflects a war mentality... without much thought of cost or consequences... The necessary road works, the necessary telephone extensions, the necessary housing etc. etc. are being undertaken by this Government as and when they are needed. The new Liberal plan consist (sic) in going beyond necessary works and spending money on things that will bring little or no return for years to come and therefore for the moment represents a dead loss of capital... Mr. Lloyd George would freeze up every dead penny into some profitless work leaving the country no reserve with which to bound forward when the opportunity at last arrives. In so far as his schemes would demand more money than... (is) held in suspense they would inevitably compete with other demands for capital'.²⁵

Sir Wilfred Eady, Principal Assistant at the Ministry of Labour, rejected the supposed benefits of government-financed public works as 'an illusion' arguing that 'all expenditure by the Government must be directed to strengthening the economic structure of the country' so enabling trade 'to give regular employment to men in the ordinary course of business'.²⁶ A Committee of the Economic Advisory Council, reporting in 1932, agreed that public works schemes involving long-term financial commitment on the part of the government would tend to 'hamper development along normal business lines' by posing a threat to the volume of available capital.²⁷

²² T.W. HUTCHISON, *Economics and Economic Policy in Britain 1946-1966*, London: Allen and Unwin, 1968, Appendix.

²³ J.M. KEYNES and H. HENDERSON, *Can Lloyd George Do It?*, London, 1929, pp. 34-5.

²⁴ PRO Cab 24/175, CP 487, Cabinet Education and Unemployment Relief Expenditure, 23 November 1925.

²⁵ P.R.O. T161/303, S40504, 'Some Comments on "We Can Conquer Unemployment"', 1929/30.

²⁶ Lansbury Papers, L.S.E., Section II, Vol. 19 (d), Unemployment, Letter from Sir Wilfred Eady, 10 September 1929.

²⁷ PRO Cab 58/12, Economic Advisory Council, Sub-Committee on the Limits of Economic Policy, Report, 18 March 1932.

The resistance to the 'Treasury View' was not confined solely to economists and others outside of government. Early in 1929, Joynson-Hicks (Home Secretary), Steel-Maitland (Minister of Labour), and Amery (Secretary of State for Dominion Affairs), called for an extensive trunk road reconstruction programme to be financed entirely by the government, irrespective of Treasury objections that any credit advanced would divert funds from ordinary business.²⁸ 'After 8 years of financial orthodoxy and 8 years of unabating unemployment', Steel-Maitland pleaded in Cabinet, 'ought we not to ask for a reasoned proof, for some foundations of belief that the financial policy by which we guide our steps is right?'²⁹ At the Ministry of Labour Hilton called for the appointment of a mixed official and non-official committee to examine the 'theory and practice' of the Treasury view that capital raised by the state diminished that which would otherwise have gone to employment-creating investment.³⁰

The inherent strength and influence of the 'Treasury View' did not ultimately depend, however, upon its theoretical soundness and it is doubtful whether attacks from within or outside government on the supply of capital thesis, even if they had been more successful,³¹ would have necessarily called forth more positive action. The objections of the Treasury and of other government departments to public works proposals embraced a range of practical and administrative considerations which were pressed with particular conviction after 1929. Road schemes, ministers were keen to point out, were a singularly inappropriate method of dealing with an immediate crisis given the need for adequate planning, technical and legal consultations and after allowing for the multifarious problems associated with the acquisition of suitable land, labour and materials.³² Any trunk road programme that could be launched quickly could

²⁸ PRO, Cab. 24/201, CP37, Unemployment. Memorandum by the Minister of Labour, 16 February 1929; Cab 24/201, CP27, Memorandum by the Home Secretary, 7 February 1929; Cab 24/202, CP87, An Employment Policy for the Election. Memorandum by the Secretary of State for Dominion Affairs, 18 March 1929.

²⁹ PRO Cab 24/201, CP37, *loc. cit.*

³⁰ PRO Lab. 2/1361, Ed. 9885, *The Liberal Pamphlet and the Melchett-Turner Report*. Note by Mr. Hilton, 22 March 1929.

³¹ Kahn's pioneering work on investment and employment in the early 'thirties is interesting in this context. Keynes' attack on the 'crowding-out' view of the Treasury was based in 1929 on the view that the savings employed would not need to be diverted from private sources since they would be readily available from those generated on the unemployment fund, from those running to waste through lack of adequate credit machinery, and from those obtained by a redirection of funds from overseas. It was Kahn, however, who first demonstrated that not only could investment increase savings but that the increase in savings would be sufficient to finance the additional government expenditure involved, thus refuting the Treasury view. See D. PATINKEN, 'Keynes and the Multiplier', *Manchester School*, 3, September 1978.

³² In this context see the celebrated evidence of Sir Richard Hopkins, Controller of the Finance and Supply Department at the Treasury, before the Macmillan Committee in 1930. Hopkins was far more concerned to outline the practical difficulties of swiftly adopting the Liberals' plans than he was to defend the theoretical justification for Treasury opposition to public works.

have only a minor effect on registered unemployment it was argued; more extensive proposals on the other hand would take so long to plan and to execute that it would be almost impossible to synchronize the peak of expenditure with the appropriate point of the trade cycle.³³ Ministers seriously doubted whether the number of worthwhile public works schemes forthcoming during a depression would justify the faith placed in them. J.H. Thomas told the Cabinet in May 1930:

'It is one thing to construct a paper programme and to quote it as evidence that you have a policy; quite another to work out the details of concrete schemes which will give an economic return, obtain the necessary powers, and get the work put in hand... The idea that when we took Office there were, and still are, countless projects of economic development all ready and awaiting only the genial influence of a substantial Exchequer grant to set them in instant motion, is a myth'.³⁴

Even if *bonafide* schemes were available, claimed the Ministry of Labour, they were unlikely to provide much beneficial employment for men in their normal trades or in areas where they were most needed — indeed indiscriminate public works which failed to improve directly the structural problems of basic industries such as coal, textiles and ship-building were regarded as positively harmful.³⁵ The Ministry doubted moreover whether many more than 250,000 men of the type normally required for public works would actually be forthcoming given the wide variation in the age, sex and physical suitability of the registered unemployed and the natural inclination among adult males to await reabsorption into their former occupations rather than take up new work (especially if they were older men with dependants).

There were real fears that state-sponsored investment would actually increase unemployment by encouraging private firms to delay their plans for industrial expansion in the hope of securing government financial aid. 'It is to the normal working of ordinary industry that the employable population must look for its livelihood', stated a Ministry of Labour memorandum, 'Unless this is made clear... the institution... of a big programme of public works will create

³³ PRO Cab 24/202, CP53, Unemployment. Memorandum by the Chancellor of the Exchequer Covering Treasury Memorandum. 23 February 1929. Experience of road schemes during the period 1920/1-1924/5 had suggested that each year's programme took at least six years to complete and that the peak of expenditure on and the employment provided by each scheme was reached only in the second and third years from the date of starting. Cab 27/440, CP293, Unemployment Policy. Memorandum by the Lord Privy Seal, 18 August 1930.

³⁴ PRO, Cab 24/212, CP178, Unemployment Policy. Memorandum by the Lord Privy Seal, 26 May 1930.

³⁵ PRO, Prem. I/183, Unemployment, 1935. The question of whether there were public works schemes available which could have had such a positive discriminatory influence was never seriously examined.

an appetite that will be satisfied only with increasing difficulty'.³⁶ Traditional arguments in support of public works received an increasingly cool reception from the early 'thirties. There was not much evidence, according to government officials, that public works in the past had done much either to reduce registered unemployment significantly or to improve efficiency and industrial competitiveness. Nor did they necessarily increase confidence. 'There can be no doubt that a heavy rate of expenditure, stimulated by generous state assistance, has a strong contrary tendency', reported the Cabinet Employment Policy Committee in 1932. For the individual 'the moral effect of a spell of employment on relief works is small compared with the inspiration given by a revival of hope of a return to normal work'.³⁷

The authorities' narrow views as to what constituted 'acceptable' and 'worthwhile' public works virtually ensured that any development programme would have limited potential impact, almost irrespective of Treasury control over expenditure. Treasury prerogatives after all were occasionally breached as when Morrison, Minister of Transport in 1929, won approval for an expanded trunk road programme. The determinant factor was not so much formal Treasury control as the determination of the Chancellor of the Exchequer and his officials to use their financial control over particular expenditures to ensure that the parameters of policy were met both in practice and in principle. Public works, for example, had to be capable of being speedily implemented and yet yield an economic return sufficient to pay the interest on the sinking fund of any loan. In addition they had to be directly instrumental in improving trade and reducing industrial costs, involve no 'demobilisation' problems on their cessation, guard against upsetting traditional wage differentials and prevent labour being drawn away from sectors likely to provide secure employment in more normal times.³⁸ 'However much we may be criticized', a Cabinet committee reported in 1930, 'we must not be rushed into shovelling out public money merely for the purpose of taking what must inevitably be a comparatively small number of people off the unemployment register to do work which is no more remunerative and much more expensive even than unemployment'.³⁹

Attitudes such as these were more powerful in limiting the development of an active public works policy than were theoretical disagreements over the

³⁶ PRO, Cab 24/203, CP 104, Inter-Departmental Committee on Unemployment. Report on "We can Conquer Unemployment", 1929.

³⁷ PRO, Cab 24/227, CP 36, Cabinet. Employment Policy Committee, Report, 25 January 1932.

³⁸ See W. JANEWAY, 'The Economic Policy of the Second Labour Government, 1929-31', Unpublished Ph.D Thesis, University of Cambridge, 1971. Although the Committee of Economists attached to the Economic Advisory Council rejected the 'diversionary' argument of the Treasury regarding public works it was prepared to support public works only if they fulfilled such strict criteria. PRO, Cab 58/11, Economic Advisory Council, Committee of Economists, Report, 24 October 1930.

³⁹ PRO, Cab 27/418, CP 134, Unemployment Policy Committee, Report, 29 March 1930.

operation of the money and labour markets, if only because they were self fulfilling. As long as the Cabinet insisted that state aid for public works had to come from current revenue, that the origin and execution of any programme had to remain the initiative of local authorities, and that the works themselves had to be directly 'useful', 'remunerative' and be likely to improve industrial efficiency, then the scale by which they could be mounted inevitably meant that they could only be of limited practical value, incapable of effecting a substantial reduction in recorded unemployment.⁴⁰ Given the contemporary predilection to judge public works by only the narrowest business-like measures of 'economic' as against 'social' utility, there was a natural tendency to oppose large-scale programmes which did not offer an immediate prospect of profitable return. The Economic Advisory Council, for example, though opposed to a large-scale policy of public works nevertheless called upon the government in 1932 to encourage public utilities and local authorities to undertake works of an essentially commercial character on a remunerative basis.⁴¹

The official attitude towards public works in depressed areas, moreover, actually retarded positive developments in this field. Until mid-1930, for example, regions with a rate of insured unemployment of 10 per cent or more were offered aid for works programmes on terms distinctly less attractive than the more prosperous areas, providing the latter employed transferred labour. This held up work both in those areas reluctant to accept greater imports of unemployed men and in the needy areas where the lower grant required to sustain the premium elsewhere stifled initiative.⁴² The administrative organization for sanctioning and initiating public works (as conventionally defined) was, furthermore, extremely cumbersome and slow to operate. The prospect of overriding the whole machinery of local government or at least of contemplating a new series of legal, practical and constitutional arrangements to accommodate an active public works policy was never seriously entertained within Whitehall. Mosley came close to recognizing the necessity of linking economic initiative with an effective administrative machinery charged with the required executive authority. But if the Treasury was unmoved and unmovable in its resistance to 'radical' pleas for national reconstruction it was motivated not just by a tradition

⁴⁰ Keynes had anticipated such arguments. He called in 1931 for work to proceed on well-conceived projects irrespective of the speed by which they could be executed, confessing that 'the main obstacle in the way of reducing unemployment by such schemes is... to be found... in the practical difficulties of initiation and organisation... It is difficult to *improvise* good schemes'. *Committee on Finance and Industry*, Addendum I, *op. cit.*, para. 48.

⁴¹ PRO, Cab 58/12, Economic Advisory Council, Sub-Committee on the Limits of Economic Policy, Report, 18 March 1932.

⁴² Mosley's demand for national road schemes was a direct recognition of the need to cater for transferred labour from the depressed areas by an alternative means to the prevailing 'long manœuvre between local authority and government, each striving to beat the other'. PRO, Cab 24/209, CP31, Unemployment Policy, 23 January 1930.

of financial parsimony but by a belief prevalent within a wide range of government departments that such proposals were both unwieldy in practice and inappropriate in the prevailing circumstances.

There is evidence, it is true, that by the mid-thirties some influential officials within both the Treasury and the Bank of England were more positively inclined towards public works than they had been hitherto.⁴³ The growing awareness of the need for macroeconomic management was such, according to Howson and Winch, that 'by 1937 the... position which we associate with Keynes's *General Theory* had altered the thinking of the most important policy-making civil servants in the Treasury',⁴⁴ not least in the acceptance of an expansion of public borrowing as a means of sustaining economic recovery. But it is easy to exaggerate the drift from orthodoxy towards 'Keynesianism' especially with regard to public works. Prior to the war at least the Treasury remained sceptical as to the employment-generating effects of public works, convinced of their delayed impact and of their potential merely for shifting unemployment from one period to another rather than in effecting a substantial reduction in the number recorded as out of work.⁴⁵ The stimulus to increased government expenditure in the late 1930s came from rearmament and not from any Damascus-like conversion to state-sponsored works. Keynes himself was clearly aware of this, writing in August 1938:

'We are at this moment allowing war expenditure for defence to help solve our problem of unemployment as a by-product of such spending, whereas if disarmament had prevailed we might have allowed a serious recession to have developed by now before introducing loan-expenditure on a comparable scale for the productive purposes of peace'.⁴⁶

There were other formidable constraints on the pursuit of national domestic economic recovery via deficit-financed public works not least an entrenched belief within government in 'sound finance' as the champion of confidence and stability both at home and abroad. Alternative monetary and fiscal policies were ruled out by the decision to return to and subsequently to manage the gold standard at the pre-war parity. There was little chance before 1931 of any proposal to increase state expenditure receiving sympathetic support, whatever its justification in theory or practice, if it threatened the stability of the exchange rate. Hubert Henderson, for example, was only prepared to support reflation by public works programmes if it was linked to an import duty on manufactured

⁴³ See above pp. 9.

⁴⁴ Howson and Winch, *op. cit.*, pp. 109, 130. By 1935, according to Howson and Winch, the Treasury had come to regard the multiplier, 'as a possibly true, but as yet unconfirmed theory, rather than one that was definitely false'. *Ibid.*, p. 131.

⁴⁵ G.C. PEDEN, 'Keynes, The Treasury and Unemployment in the Later Nineteen-Thirties', *Oxford Economic Papers*, 32, March 1980.

⁴⁶ *Economic Journal*, Vol. XLVIII, 1938, cited in Peden, *loc. cit.*, p. 6.

goods to provide the necessary finance and maintain balance-of-payments equilibrium.⁴⁷

Domestically, the principle of 'sound finance' ensured a resistance to virtually all demands for increased expenditure or at least the limitation of concessions to the barest point of acceptance until such time as normality was resumed (whatever that meant). Balanced budgets (or budget surpluses) and the reduction of the National Debt were central to this objective but, although viewed ultimately as means of maximizing prosperity, they became ends in themselves used to block more specific and unorthodox policies to revive domestic activity and employment. The Chancellor of the Exchequer warned the Cabinet as early as 1922 that the effects of public works on unemployment were more psychological than real and 'could be bought at too dear a price if the equilibrium of the country's finances is upset by excessive burdens being imposed on the Exchequer'.⁴⁸ Not only did 'unsound' finance threaten the exchange rate, trade, and international financial transactions, it raised the fearful prospect of inflation, the arch enemy of thrift and national solvency. The Treasury recognized that so long as the government could borrow from the public to finance a budget deficit there was no *automatic* link between unbalanced budgets and inflation; but a regular or permanent recourse to deficit finance was likely to raise the long-term rate of interest and reduce confidence and private investment as individuals came to expect a fall in the price of bonds, thus eventually forcing the government to monetarize the debt.

The power of budgetary orthodoxy in severely limiting the scope of alternative economic policy should not therefore be underestimated. It is customary nevertheless to stress the beneficial effect which balanced budgets had on confidence, especially during 1929-31. Aldcroft has argued, too, that the offsetting nature of different fiscal measures and the timelag between decision-making and implementation tended to neutralise the aggravating effects of budgetary policy.⁴⁹ In addition, extra-budgetary outlays in the form of public and semi-public investment and local authority expenditure are often alleged to have been a stabilizing influence, especially during 1929-31, acting as 'a sea-anchor against the drift of national income to lower levels'.⁵⁰ But as recent research has shown fiscal 'window-dressing' disguised the extent to which budgets in the early 'thirties were draconian in their effect; high unemployment merely intensified orthodoxy in the extreme, giving full reign to a discretionary destabilizing budgetary policy probably sufficient to have outweighed any positive influence

⁴⁷ PRO, Cab 24/212, CP 196, 'Unemployment Policy - Industrial Reconstruction Scheme', 3 June 1930.

⁴⁸ PRO, Cab 24/138, CP 4136, Memorandum by the Chancellor of the Exchequer, 31 July 1922.

⁴⁹ D.H. ALDROFT, *The Inter-War Economy, Britain 1919-1939*, London, Batsford, 1970, pp. 302-14.

⁵⁰ International Labour Office, *Public Investment and Full Employment*, Studies and Reports, New Series No. 3, 1946, p. 173.

upon business confidence and certainly the death knell of any expansionary public works programme.⁵¹ Much of the increased capital expenditure outside strict central government budgetary outlays, moreover, 'was financed out of additional current revenue and new borrowing was partially offset by simultaneous repayment of debt, while, in addition, expenditure was lowest in those areas with the highest unemployment'.⁵²

There is no doubt, however, that to the majority of contemporary politicians, civil servants, city financiers and industrialists, a policy of deliberately unbalancing the budget in the hope of expanding employment was a fearful prospect, not least in its potential for encouraging repeated demands for yet further increases in public expenditure. Keynes may have believed that once economic priorities became increasingly dependent upon continuous political decisions the authorities would act intelligently and responsibly; contemporaries feared, perhaps more realistically, that the political pressures towards even greater expenditure to cure the economic malaise would merely intensify. More importantly, such reactions were instinctive, part of the political culture of the time and ones which were unlikely to be compromised by the subtleties of the opponents' case. The prevailing misgivings within official circles as to the damage to confidence and initiative from any government-financed works programme were never entirely or even substantially overcome by claims that it would lead to multiple rises in income and employment and would generate further investment via the accelerator. The fact that there were few readily available or generally accepted estimates of the scale of government expenditure required to have a substantial impact upon employment via the multiplier⁵³ is not in itself critical since the arguments for or against a counter-cyclical budgetary policy did not rest essentially upon precise orders of magnitude nor were such data systematically sought after by policy makers.

The other major barrier to the adoption of a more positive public works policy was the fear of increasing state intervention. The rules of 'sound finance' were, as one writer has pointed out, a defence not only against economic catastrophe but also against state socialism.⁵⁴ Indeed, in calling for a more drastic remedy for unemployment via loan-financed public works Keynes remarked in May 1924 that 'the next development of politico-economic evolu-

⁵¹ R.F. MIDDLETON, 'The Constant Employment Budget Balance and British Budgetary Policy, 1929-39', *Economic History Review*, Second Series, XXXIV, May 1981.

⁵² *Ibid.*, p. 283.

⁵³ Kahn had suggested in 1931 that the value of the multiplier in relation to public works spending was within a range of 1.56 to 1.94. More refined calculations only became available in the late 1930s and early 1940s and suggested an order of magnitude varying between 2.07 and 3.22 for different periods of the 'thirties.

⁵⁴ R. SKIDELSKY, 'Keynes and the Treasury View: The Case For and Against An Active Unemployment Policy 1920-1939', in W.J. MOMMSEN (ed.), *The Emergence of the Welfare State in Britain and Germany*, London, Macmillan, 1981.

tion will emerge from new experiments directed towards determining the appropriate spheres of individual and of government action'.⁵⁵ And behind the Treasury's notorious rejection of increased government expenditure for such purposes lay the powerful conviction that it would undermine the democratic structure of local government and threaten private property rights.⁵⁶ What worried contemporary politicians (not least within the Labour Party) about the development programmes of Lloyd George and Oswald Mosley was their implicit assumption of a powerful central executive, their rejection of the inherent efficacy of market forces in favour of some form of 'managed capitalism', and a suggested timetable of action which smacked of bureaucratic dictatorship.

The role of the TUC is interesting in this context. Its campaign in 1933 for the 'right to work' and not merely the 'right to maintenance' incorporated the first explicit endorsement of deficit-financed public works, suggesting that the majority of its members had become converted to an unorthodox expansionary policy.⁵⁷ The vigour and novelty of Roosevelt's New Deal supposedly tipped the balance in favour of initiating public works 'financed by the use of the national credit'⁵⁸ for the sake of increasing employment. But in fact such a policy prescription appears in no other resolution or statement of the TUC for the rest of the decade. In reality Congress was more inclined in the 1930s towards remedies for structural unemployment — 'reorganising industry under capitalism'⁵⁹ — and was fearful of any extension of state influence in the management of industrial and economic affairs, not least in the area of free collective bargaining.⁶⁰ Support for Keynesian-type policies within the TUC was compromised in other words by a more determined search for the restoration of capitalism via 'collective *laissez-faire*'.

IV

Although these various constraints on the evolution of a more positive unemployment policy were reduced somewhat after 1931 with the abandonment of the gold standard, the reduction of interest rates and the break with free trade, neither the doctrine of minimum government interference nor the innate

⁵⁵ J.M. KEYNES, 'A Drastic Remedy for Unemployment: Reply to Critics', *The Nation and the Athenaeum*, 7 June 1924.

⁵⁶ Skidelsky in Milo Keynes, *op. cit.*, p. 99.

⁵⁷ Cf. Pollard's view that the effect of the 1931 crisis on the TUC was 'to have converted its majority to Keynes rather than to Marx'. S. Pollard, 'Trade Union Reactions to the Economic Crisis', *Journal of Contemporary History*, 4, 1969, p. 115.

⁵⁸ TUC, *Annual Report*, 1933, pp. 261-2.

⁵⁹ *Ibid.*, pp. 263-4.

⁶⁰ For fuller discussion see Barbara Malament, 'British Labour and Roosevelt's New Deal. The Response of the Left and the Unions', *Journal of British Studies*, XVII, Spring 1978.

hostility towards unorthodox economic policy was seriously challenged. Phillips at the Treasury was clear as to the parameters of policy, writing in 1934:

'If we can hold out to industry a prospect of stable rising prices, a reasonable stability in exchange, cheap capital and money, a check on the rise in taxation and possibly some reduction, *and a guarantee against revolutionary and dislocating departures in public enterprise*, confidence will revive, enterprise will quicken and employment will expand'.⁶¹ (My italics)

Public works, to be acceptable, still had to fulfill the strictest criteria of utility. MacDonald warned his General Purposes Committee in April 1935 that he would only look favourably upon schemes of work that could be 'put in force speedily and effectively' and urged 'the necessity of maintaining a most careful and continuous watch on the reactions of the intervention of the State on private and local enterprise and initiative'.⁶² This fear of increased state involvement was not entirely unfounded. The local authorities in the 1930s were in aggregate a far more important source of domestic capital formation than was central government. An expanded public works programme, therefore, would have entailed either a very generous system of grants to the authorities (with all the attendant risks to controlled expenditure and without any firm guarantee that the authorities would respond positively) or a greater concentration of public investment under direct control. The General Purposes Committee's own assessment of the efficacy of public works was characteristically circumspect noting that:

'Not only is the volume of extra employment to be anticipated trifling ... but it is inevitably located largely in the areas where unemployment is least severe, while it is apt to be offset by delay in other projects arising out of the hopes of their promoters that they may presently share in the bounty of the State'.⁶³

The Economic Advisory Council was advised in 1935 that public works policy should under no circumstances involve an increase in the *general* level of public capital expenditure 'over the average of good years and bad together, but only a concentration of expenditure in the bad years' and then only on schemes not competitive with ordinary industrial expenditure.⁶⁴ Part of the reason for the almost deliberate absence of action by the National Government in the early 'thirties was that there was never much persistent pressure from the unemployed themselves for an alternative and more radical economic strategy. If anything,

⁶¹ PRO, T172/1821, Gold Standard: Conditions Required for Return to Gold, 1934.

⁶² PRO, 30/69/615, General Purposes Committee... Introductory Statement by the Prime Minister, 18 April 1935.

⁶³ *Ibid.*

⁶⁴ PRO, Prem 30/69/471, Economic Advisory Council. Memorandum on 'The Causes of Unemployment and the Effects of Public Works Expenditure', 5 April 1935.

the depression had blunted rather than sharpened the edge of social discontent. The TUC proved especially reluctant to mobilize working class support for a reflationary policy and stood little chance of securing the backing or winning the support of progressive industrialists so long as it campaigned primarily for more liberal unemployment provision and the eventual socialisation of the economy. But the more fundamental reason was that the government was determined not to upset the 'natural' forces of recovery. Expansionist and interventionist policies threatened to weaken the restorative influence of the slump in purging the system of 'unsound' investment and unproductive practices. Acutely conscious of the interests which supported it politically and financially, the National Government vigorously pursued orthodox policies in order to retain confidence and to avoid the further economic crisis it felt was forever imminent.⁶⁵ Isolating unemployment and containing it with a flexible unemployment insurance scheme and with microeconomic measures of industrial reorganization and rationalization posed a far less serious challenge to the existing social and economic structure than did proposals for unbalanced budgets; they not only ran the risk of balance of payments crises and increased state control but threatened confidence, the value of the pound as a medium of international exchange,⁶⁶ and the trend level of interest rates. As for the latter, Hawtrey, among all contemporary British economists, had long argued in favour of credit relaxation rather than loan-financed public works as a cure for unemployment⁶⁷ but Keynes himself was insistent by the mid-'thirties that the major importance of public works would be their effect in raising the level of aggregate demand to a point where a deliberate policy of cheap (and perhaps continually cheaper) money could operate positively to sustain private investment. The Treasury, however, remained convinced that borrowing to finance public works would increase interest rates and thereby damage economic recovery.

The argument between the expansionists and the contractionists, therefore, was essentially one about political priorities; about the priority of 'short-run' solutions to unemployment against those directed towards external stability and to 'sound finance' and about the priority which was to be accorded to the state as an active agent in the determination of the level of employment. As Winch has

⁶⁵ The government's Unemployment Insurance Statutory Committee predicted in 1934 that unemployment in 1940 would average 27 per cent. For further discussion see F. MILLER 'The Unemployment Policy of the National Government, 1931-36', *Historical Journal*, 19, 1976.

⁶⁶ The orthodoxy of internationalism was by no means dead even in an era generally noted for its lurch towards national self sufficiency. After 1932, for example, British exchange rate policy was determined partly with a view to aligning the pound on the dollar in order to preserve friendly relations with the American authorities even when short-run British economic or monetary interests might have suggested a more flexible policy.

⁶⁷ See for example, R.G. HAWTREY, 'Public Expenditure and Trade Depression', *Journal of the Royal Statistical Society*, III, 1933; 'Public Expenditure and the Demand for Labour', *Economica*, 5/6, 1925-26 and his *Trade and Credit*, London 1928, Chapter 6.

observed: 'That logic alone did not determine the Treasury position is borne out by the fact that long after these objections (to increased state capital outlay) had been met by argument and by altered circumstance, orthodoxy in matters of government expenditure remained the rule in Britain'.⁶⁸ Whether, had these objections been overcome or had not been so firmly entrenched within and without government circles, the 'Keynesian' solution would have proved a practical remedy for Britain's particular unemployment problem, given her precarious financial and trading position, is another story.⁶⁹

⁶⁸ Winch, *op. cit.*, p. 113.

⁶⁹ This is one of the subjects of my current research. Some relevant observations can already be found in S. GLYNN and P. HOWELLS, 'Unemployment in the 1930s: the 'Keynesian Solution' Reconsidered', *Australian Economic History Review*, XX, March 1980; T.J. THOMAS, 'Aspects of U.K. Macro-Economic Policy During the Inter-War Period: A Study in Economic History', Unpublished Ph.D. thesis, University of Cambridge, 1975; W. R. GARSIDE and T. J. HATTON, 'Keynesian Policy and British Unemployment in the 1930s', *Economic History Review*, Second Series, XXXVIII, February 1985.

