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FROM: "QUESTION AND ANSWER SESSION" FOR ANGLO-JAPANESE ECONOMICS & TRADES

——BRITAIN IN THE 20TH CENTURY INTERNATIONAL ECONOMY——

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Assignment:

1. What were the major problems faced by the British economy in the early 1920's?
2. Outline briefly the main characteristics of unemployment in Britain between the wars and explain why it was so severe.
3. Why was the International Depression of the 1930's so widespread and so deep?
4. Account for the British financial crisis of 1931.
5. To what extent and why did the British economy recover from the depression of the 1930's?
6. Outline and account for changes in the size of British companies since 1920.
7. What were the major economic problems faced by Britain in 1945? How and to what extent had they been overcome by 1951?
8. Why did Britain experience full employment in the quarter century after the Second World War?
9. Why, by international standards, was the British economic growth so slow in the 1950's and 1960's?
10. Discuss briefly the principal features of the Bretton Woods system and account for its collapse in the early 1970's.
11. Discuss the causes and consequences of the oil price explosion of 1973/74.

This material is a collection of some of the responses to a "Question and Answer Session for Anglo-Japanese Economics & Trades" conducted at the University of Portsmouth on the occasion of my acceptance by the University as a researching fellow.

1. WHAT WERE THE MAJOR PROBLEMS FACED BY THE BRITISH ECONOMY IN THE EARLY 1920's?

The 1920's have been regarded as a period of stagnation as far as the British economy is concerned. Especially 1921, has been quoted as one of the worst years of depression since the industrial revolution. It was notable for its persistent high level of unemployment, stagnation export and decline in the staple industries.

During the war, the government had to finance its expenses through borrowing, and this was done by issuing Treasury Bill, which inevitably increased the fluid state of the economy. Many speculative activities occurred as banks were able to expand their credit creation and money could be borrowed easily from banks. A boom started to develop, demand for goods was stimulated, consumer expenditure rose, many companies and capital equipments were bought up and refloated at inflated prices.

The boom came to an end in April 1920 when the Bank rate was raised to 7 %. As those speculative buying of capital equipment occurred mainly in the older industries like shipbuilding textile and engineering industries which used old techniques of production and did not have potential growth, these industries were left with heavy interest liabilities because of the higher interest rate. Price level had been

rising since supply could not meet demand in the short-run because the production capacity was inefficient, and higher prices resulted is higher wages which aggravated the supply position.

After the boom, the number of the unemployed rose to over 2 million. The main feature of the employment was overdependent on the staple industries. Since the war, most of Britain exports consisted of staple products-like coal, ships, textiles. These industries accounted for not less than 75% of employment share in the economy. World trade recession in 1921 which resulted in the collapse of Britain export market in some way contributed to the rapid increase in the level of unemployment.

Exports which fell sharply in the early 1920's could be also attributed to the changes in demand for British export. Britain had been producing high quality products since the pre-war period. And she specialised in exporting staple products to primary producers or low-income countries instead of high-income elasticity products to richer countries. When commodity prices fell which in turn affected the incomes of the imported countries, these countries shifted their demand to cheaper and low quality products supplied by, for example countries like Japan and India. Also, at the end of 1920's, although protectionism became prevalent all over the world, Japan, India, Brazil, Italy, tried to invade the foreign market but protected their domestic industries. The industrialization of new countries, led to more supplies flowing in to the export market, thus resulting in Britain's export market share becoming smaller.

In addition to the external factors mentioned above there were also some internal factors which should be taken into account in explaining the decline in British staple industries which were also the

exporting industries. British staple industries at that time were too old and too weak to compete overseas with the newly developed countries which adopted new technological changes. They faced the problems of reorganization. Ownership was fragmented, equipments were a motley assembly of new and old units poorly integrated with low productivity levels and high costs. This result was partly due to the strengthen of the trade unions. After the war, trade unions were more organised for wage negotiation. Between 1919 and 1920, weekly money wages were bid up, and rose further than the cost of living. The wage rate was pushed up further in real term by general reduction in working hours, as a result, unit labor cost rose rapidly and this large increase in wages could not be compensated for by increasing productivity or passing the costs on the final products especially after 1920 when demand showed sign of decreasing. Even though wages fell sharply in 1921, real earning actually rose because of even greater fall in commodity prices and the cost of living. High costs and low productivity made British export uncompetitive in the world market. Another problem faced by the British economy was the repayment of the huge national debt left by the war. The method used by the government to finance the war was borrowing rather than obtaining money from the economy through taxation. This led to a substantial increase in national debt and the annual cost of servicing the debt was high due to the relative high rate of interest. Much of the borrowing consisted of short term floating debt which had an inflationary effect in the economy. Several attempts were made to reduce the national debt by financing it as cheap as possible. This was to reduce the cost of servicing the national debt by conversion and funding at a lower rate of interest. Also this would serve to keep the

overall debt at its existing level. Since the government failed in the first respec,t attention was drawn to the area where the goverment could have more direct control, the restraint of public spending. The deflationary budgetary policies were carried out to achieve a surplus to pay off the national debt. Spending was cut and at the same time taxes were raised, thus resulting in a fiscal year surplus.

Although the British economy experienced a boom in 1919–1920, it was merely an artificial and a speculative one rather than a substantial gain, which no doubt ended in disaster. This is well illustrated by the British staple industries. During the boom those industries were bought up with easy money created by government's borrowing after the abandonment of gold standard and refloated at inflated prices. Profits earned before the war were stuck in those second-hand assets with no future potential for growth. When interest rate was raised they were all heavily in debt. British exports were vulnerable to the shifts in patterns of world demand. The cost structure of the industries made the products uncompetitive in the world market. Trade recession in 1921 was also a part of the reason why British export was in a even worse situation. Inefficient and low productivity had always been a problem of the British industries. High levels of unemployment showed no sign of significant recovery in the early 20's. It was mainly because the power of trade unions after the war push up money wages but commodity prices fell this, together with a general reduction in the number of hours in the work week resulted in an increase in real wages. It is doubtful that firms would increase employment when demand conditions slackened. In order to reduce the massive national debt left by the war, public spending had to be cut. This undermined the growth of new indus-

tries like motor cars and electrical industries when a reinvigoration of the economy was needed.

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2. OUTLINE BRIEFLY THE MAIN CHARACTERISTICS OF UNEMPLOYMENT IN BRITAIN BETWEEN THE WARS AND EXPLAIN WHY IT WAS SO SEVERE.

Unemployment was a major problem for the British economy in the inter-war years. Immediately after the war Britain coped quite well with mobilized soldiers back into their peace time occupations. Unemployment, at this time of great changes barely rose above the half million level. At this time there was even a mini-boom, brought about by increased consumer expenditure which rose 21% from 1918 to 1919. The boom collapsed in March 1921, and by the end of June the proportion of the labour force without work was (in the insured trades) 16–17%. The great depression of the 1930's brought the level of unemployment even worse than the 1920's–23% in August 1932. Not all areas of Britain were affected the same by unemployment. It was essentially regionalised. Prior to the war Britain's staple industries such as shipbuilding, coalmining, steel manufacturing and cotton were still expanding, but after the war there was a shift of resources away from the old staple industries into the new ones. Industries such as electrical engineering and motor car manufature were industries of the future. From 1924–29 the British steel industry was operating at half capacity, world shipbuilding had doubled but Britains was hardly

growing. Coal lost out to other forms of energy and the cotton industry which accounted for 4 / 5 of output in 1914 lost many of its export markets. It was the heavily industrialised areas of Wales, the North East and The Clyde that suffered the most. Unemployment in Wales in 1932 was 2 / 3 higher than the national average. London and the South-East was relatively well off.

The majority of job losses were borne by the unskilled labourers. The census of 1931 indicated that 30. 5% of unskilled labourers were without work, and only 5 - 8 % of white collar workers were unemployed. It can also be said that the older a person was when he lost his job, the more difficulty it became for him in finding an alternative work. The same applies today, firms are reluctant to take on employees who are reaching the end of their working life. Unemployment was then somewhat age-structured.

Towards the great depression of the 1930's unemployment was showing signs of becoming a long term problem for many people. In 1929, 4. 7% of the labour force who registered for benefit had been unemployed for over a year and this figure reached 16. 4% in 1932 and 25. 6% in 1936.

The burden of unemployment between the wars was shared by many of the workforce particularly the unskilled. Its severity is attributed to many factors, some of which could have been avoided, possibly by reducing the level of unemployment.

One such factor which accounted for this was the government's decision to return to the Gold Standard in 1925 at the pre-war parity of $ 4. 86. Keynes said that this level was 10% too high and others such as Redmond said that against a basket of currencies, $ 4. 86 may have been up to 20 or 25% too high. The effects of the currency over

valuation were felt in the export market. The relative prices of UK exports increased and became uncompetitive, many of the exporters (particularly in the staple industries) were begun to loose the edge anyway so this came as a double blow to them. Government monetary and fiscal policies were geared towards the Gold Standard, making any reversal in the unemployment trend even more difficult. The benefits given to persons without work may not hava helped the unemployment problem. Benefit was based on an insurance scheme where workers paid statutory contributions regularly in return for benefit at a time of unemployment. The scheme had 4 million contributors in 1918 as opposed to 15.4 million in 1938. The argument is that the higher the level of benefit the lower the opportunity cost is of being unemployed, when a family with two children were in 1930 entitled to 50% of their normal wage as a benefit payment and 60% in 1938. It can be seen that the figures for voluntary unemployment may have been quite higher. It may however, as in many cases, be true that even a payment of 60% of the working wage was not equal to the loss of pride, skill and self-respect that an unemployed person had to bare. There was obviously no shortage of labour, but there was a shortage of the correct type of labour in many of the new industries who also suffered unemployment towards the end of the period. The majority of the group of unemployed people were adult males who were skilled or were crafted e. g. shipbuilding. However the new industries did not require huge numbers of skilled craftsmen but needed semi-skilled workers, basically, the redundant workers from the old staple industries who were suffering from occupational immobility brought about by the shift in resources from the old to the new consequences.

There was also a degree of geographical immobility e. g. mass un-

employment in the North East and Wales and the possibility of more job opportunities in the Midlands and South East. People became tied to one area and were reluctant to move and break social contacts. Unfortunately for the new industries, there was not a great deal of capital available to them as much of it was still tied up in the old fast-declining staple industries. The UK was also seen as a bad investment area and capital that should have been invested in the UK went overseas where better returns were expected.

Unemployment when viewed as a function of wages, rates, may have risen due to the trade unions resistance to cut in real wages, a resistance which eventually led to the General Strike in 1926. It is however fair to say that a fall in real wages would not have vastly reduced unemployment because the competition the UK faced from Japan, China and the Near East (particularly in textiles) was just too intense. Wage rates there were a fraction of UK rates and trade barriers or changes in the rate of exchange may have been used to prevent advantage through cost reductions.

Inflation during World War I fuelled strict government monetary policy and monetary restrictions in 1920. These deflationary policies cannot be blamed directly for the level of unemployment of around 15% in 1921–22 but they were certainly a contributing factor.

Despite the fact that from 1924–1937, GDP in real terms was increasing at between 2 and 2.4% per annum and from 1920–1937, industrial production was increasing at 3.1% per annum, unemployment was still as big a problem as ever. Over the period from 1924 to 1933 shipbuilding recorded 37.4% out of work, even the so called "new" industries had (over the same period) unemployment levels of nearly 8 %.

Although the boom of 1919–1921 was fairly small in UK, the country faired better than most other countries in the 1929–32 depression, but U. K. was slowly and sorely losing its share of world trade to the USA, Germany and Russia.

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3. WHY WAS THE INTERNATIONAL DEPRESSION OF THE 1930'S SO WIDESPREAD AND SO DEEP?

Between the First World War and the "Great Depression" the world saw a period of short but a rapid unprecedented economic progress (the so-called roaring twenties). By 1925 all major countries of the world had returned to the gold standard, with exception of France. Between 1925 and 1929 world production of primary products rose by 11%., and world trade rose about 20%.

But the world economic situation in the twenties was not stable. The world war had meant that the traditional economic structure had been altered resulting in a strain of production and trade. Some of the problems were solved after the war, but others were too large to be solved by market forces and half-hearted government interference. These problems could have been covered up by international credits were concealed for a short time by the prosperity of the decade. But they re-emerged after 1929 and became part of the cause of the great depression.

One of the problems was over-production in some areas of world agriculture. The surplus in productive capacity of the large primary producing countries and the tendency for agricultural prices to fall relatively to those of manufactured goods, benefited the industrial countries: it stimulated their industrial output and led to rapid rise in their standard of living. But the export trades of the manufacturing counties suffered because a smaller volume of their goods could be bought in exchange for a given weight of primary products. The fall in agricultural prices resumed its course after the unusually large harvest in 1928, and it was one of the contributing factors in the world depression, because it upset the balance of payment of the primary producing countries, forcing them to protect their currencies which led some of the industrial countries to protect their domestic agriculture by tariff and their balance of payment by exchange control or devaluation.

Another problem was a change in international specialization. The war meant an end to the process by which the advanced industrial countries of Europe, under the leadership of Great Britain, had invested vast amounts in territories overseas for the production of their food and raw material supplies. During the war secondary industies had been developed in all the overseas primary producing countries, stimulated by the need to replace imports from Europe. After the war this trend continued.

New power resources and mechanization reinforced the tendency towards the localization of consumer's googs industries near their markets rather than near the supply of basic raw materials. These long-term trends largely account for the economic nationalism of the new non-European territories and the difficulties of the export trades

of the European industrial countries after the war. But also the peace treaties which had multiplied national frontiers and broken up larger economic units had an influence. These new nationals were all eager to build up their own industries in order to be as selfsufficient as possible by expanding exports and raising tariff barriers.

The third and probably most important cause of the economic instability before 1929 was the war debts and reparations. The USA had replaced Great Britain as the leading creditor nation, and was owed $ 12-14 billion at the end of the war. The reparations the Germans were to pay the victors, for having started and lost the war, were huge, and the repayment of this enormous international debt could only have been paid back in the form of goods. This involved a profound alternation in the direction of world trade and profound changes in the internal economic structure especially in the USA, and made Germany an economic giant. But such a change was not completed, because, in the USA, tariff was closely bound up with the internal political situation and guarded by powerful vested interests. The only alternative to accepting repayment was to relend the money to the European debtors. The debt distorted the international economy and made it vulnerable to depression. The amount borrowed were too large, the borrower's economies became highly unstable, and a large proportion of the borrowing was short term capital which was highly volatile. The post-war inflations which occured in most counties worldwide made most decision-makers want their countries to restore the gold standard, and it was restored in a lot of countries. But the gold standard broke down during the depression partly because of the way in which it had been restored in the 1920s. Whereas its predecessor had operated under conditions of equilibrium, the post-

war gold standard was restored when economies were fundamentally imbalance. The "new"gold standard did not provide stability, but was itself a source of instability.

It has often been said that it was not the Great Wall Street Crash of 1929 which caused the great Depression in the 1930s, but the measures and policies governments chose to deal with it. Perhaps this is a correct interpretation, especially in light of the evidence from the 1987 Stock Market Crash. This recent event saw the Dow Jones index fall nearly 23%-more than it dropped during the Great Crash of 1929-and yet the world has not experienced the severe economic repercussions such as widespread unemployment which characterized the Great Depression. Some scholars attribute the difference between the events of 1929 and 1987 to the so called "wise" measures taken after the 1987 market crash. Economists and politicians now know that a financial slump need not result in economic recession if the governments have the vision to act collectively in their common interest and adopt the right policies. The origins of the worldwide slump of 1929–32 must be located in the USA. The industrial production of the USA, in 1929, represented 46% of the total industrial production of the 24 most important producers in the world. Consequently, any downturn in the economy of the USA would have serious repercussions on the rest of the world. Four major mistakes were made which turned financial slump into economic depression, bringing misery to millions across the industrialized world by throwing them out of work.

1) In order to control the stock exchange boom the Federal Reserve in the USA tightened credit. The result was a succession of bank failures and bankruptcies.
2) The US Congress passed the Hawley–Smoot tariffs in 1930, which

considerably increased tarriffs on imports. This led to an immediate retaliation by foreign governments, and made matters even worse for some European nations.

3) President Hoover decided he had to balance the budget by raising taxes, in June 1932, and cutting public spending even though economic demand was slumping in the wake of falling share prices. The consequence was to make recession inevitable.

4) The world's leaders could not muster even a semblance of a coordinated international response to the crisis. Britain was a fading giant and the USA was not ready to take over the world leadership, so everybody went their own way. This abdiction of responsibility on the part of the great powers helps to explain the depth and intensive of the crisis.

One of the most important factors deepening the depression was the collapse of prices of raw materials. Between 1929 and 1933, the world price of foodstuffs fell by 55%, and raw materials by 60%-a much sharper fall than in the prices of manufactured products. Farm incomes ceased to rise after 1925, as increasing world supplies caused downward presures on the prices of most agricultural products. As a result of the depression, the total value of the world trade fell by 19% in 1930. The depression did not originate in the primary producing sector, the agricultural countries were rather a victim of declining industrial incomes, increasing trade restrictions and their own latent instability.

Before Keynes's ideas became widespread it was believed that a government should not spend more then it received in revenue and, if possible, should earn surplus to help pay off any outstanding debt. But during a depression tax revenue falls, and if unemployment

benefit schemes are in operation, expenditure on them increase. The orthodox economists claimed that it was impossible for governments to create work, because job-creating schemes only would rob other sectors of investment that could have been more productive. They hoped that recovery would come from a reduction in costs which would lead to an increase in profits, more competitive exports and consequently to an expansion in production. The element of cost most under attack was wages, and many economists believed that if workers were willing to work at a low-enough wage, their employers could afford to give all of them jobs. The unemployed were, therefore, victims of their own reluctance, especially through their trade unions, to accept wage cuts. It was not until the rate 1930s that keynesian economists were able to demonstrate that reduction in many wages could lead to a reduction in consumption and ultimately more unemployment. But during the depression years it was a popular view that wages, which naturally rose during a boom, should fall during an enclosing slump.

Economic policy during the depression was, as we have seen, a combination of devaluation, exchange control, default on debts, import substitution and tariff increases. The combination of these elements made it almost impossible to attract capital and consequently exports faded. It was rearmament and war which finally set the wheels of industry turning.

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4. ACCOUNT FOR THE BRITISH FINANCIAL CRISIS OF 1931.

In 1930 and 1931, the world was experiencing a recession, due mainly to the Wall Street crash of 1929. The 1920's were seen as a period for growth, and as a result, there was great optimism about the future, but unfortunately the dreams of many were only shattered illusions. Britain's depression was only modest. Incomes were rising and so was the standard of living, and if it hadn't been for high unemployment and the departure from the Gold Standard in September 1931, there probably wouldn't have been a financial crisis at all.

The crucial factor about Britain's economy at this time was that it suffered high export vulnerability. There was a dependence on staple products and markets of primary producing countries, where, in the 1930's, income weren't buoyant. As incomes went down, so did prices and therefore demand for British goods weakened. Britain relied on the fact that 40% of goods exported went into these markets, but this wasn't the case as the U. S. accelerated deflationary policies.

The Wall Street crash was caused by a tightening of policies involving credit. In the 1920's there was excessive speculation in financial circles, and many businesses, both personal and industrial, were agreed on credit. When the policy was controlled, most people sold their stocks and there was the crash. United States import demand fell sharply and this served to depress prices and incomes in the primary producing exporting countries, who then proceeded to suffer Balance of Payments problems which reduced their ability to import

from industrial countries including Britain. America called back many of the loans and this proved to be the catalyst of the financial crisis as far as Britain was concerned.

Before the suspension of gold convertibility the authorities, especially the Bank of England, sold over £ 200 million of owned or borrowed gold and foreign exchange in their attempt to defend the parity of $ 4.86 because it was the maintenance of this which they saw as their main economic policy.

In the 1920's, foreigners, spurred on by high returns, increased their sterling balance. As a result the Bank of England saw its gold and hidden foreign exchange reserves rise in 14 of the 19 quarters between March 1925 and December 1929. In 1930/31 the proto-overseas sterling area countries were themselves in severe balance of payment difficulties and were reducing their sterling balance, which, when transferred to foreigners were often taken from London in gold. In addition to this, the French Government was drawing on its large London funds to meet a budget deficit. French banks were drawing down their sterling secondary reserves to increase their cash reserves and allow for deposit and currency expansion and as interest rates fell to low levels, foreigners often anticipating liquidity problems at home, found it prudent either to reduce their sterling balances or, at best, not to increase them. The result was that Britain, without any abnormal international events, faced a substantial balance of payments problem in 1931.

To meet the deficit, the Bank of England had reserves of roughly £150 million plus an exchange reserve of £30 million, although not all was available for exchange defence, £100 million was needed to cover the domestic note issue.

A choice that the Bank had was to borrow from other central banks as it had before but these banks were becoming less willing to lend, and although there wasn't much choice, the Bank of England was less willing to borrow. The decision was taken by the government in the spring to deflate the economy. Reflation, devaluation and protection were all dismissed as politically difficult, therefore deflationary policies were assumed by a process of elimination, even though unemployment at the time exceeded 20%.

Throughout the spring of 1931, the labour government stalled, speaking of future disasters while merely attempting to hold the existing position until the autumn, thus Montagu Norman, the Governor of the Bank of England, said "The future here depends more on politics than on finance." That was still the position when Britain's difficulties were compounded by an international liquidity crisis. The beginning of pressure on international liquidity really began in the late 1920's when primary producing countries were faced with falling prices and incomes due to over-production and stock piling. These countries became debtors and were faced with large payments deficits and an outflow of funds, therefore many, including Canada, Australia and New Zealand were forced to leave the Gold Standard and devalue their currencies.

The deflationary process, exacerbated by the world recession and the Wall Street crash, led to many institutional weaknesses as a wave of bank failures spread across both the U. S. and Europe.

The banking crisis, which led to 2, 000 banks in the U. S. collapsing in eighteen months soon spread to Europe. The crisis began with the announcement of the difficulties of the Credit Anstalt of Vienna on 11 May, which partially resulted from politically inspired French with-

drawals. They had found some of their supposedly liquid assets frozen, so tired to improve their positions by recalling funds from other banks or financial centres, starting with those most likely to be in future difficulty. This move quickly spread to London as the premier money market in Europe, because Dutch, Belgian, French and Swiss banks kept most of their liquid reserves there and would want them for their own funding. This came at a time when fresh inflows of funds were needed to finance balance of payments deficit.

Between June 1930 and December 1931, London lost £350 million of foreign funds and this outflow reached panic proportions in the summer of 1931 when approximately £200 million left the country. The rapid rate of withdrawal and the continental financial panic diminished Britain's ability to sustain her external payments and therefore her ability to remain solvent. With the unfavourable short term liquidity position, there seemed little else to do but to release the sterling parity and so on 21 September, 1931. Britain finally abandoned the gold standard and devalued her currency.

It had become apparent that London could not withstand the strain for long without soon depleting reserves by realizing her short term assets, and the alternatives presented problems. Devaluation, however distasteful to the authorities, was preferable to further doses of domestic deflation.

At the bottom of Britain's 1931 difficulties lay a weakened international financial position and a large payments deficit, both of which stemmed from previous policy decisions and the current economic conditions. Many of Britain's short term assets abroad were rendered difficult to resolve owing to the fact that many were locked up in European financial centres which were themselves in a non-liquid

state.

It was the inability to either retain previously invested funds in London or to attract further investment by foreigners that was the root cause of London's short term difficulties.

The report of the May Committee which was commissioned by the government, did not help the financial situation of 1931 when they "painted the budgetary picture in the blackest possible terms and recommended large, politically impossible cuts in unemployment expenditure." It was this report that the labour government had been waiting for in the spring, hoping that they might encourage investment, but this was not to be the case, and Britain plunged into the world financial crisis of 1931.

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5. TO WHAT EXTENT AND WHY DID THE BRITISH ECONOMY RECOVER FROM THE DEPRESSION OF THE 1930'S?

The financial crisis of 1931, compounded by the depressed state of economic activity from 1929 together resulted in a depression of the severest intensity. Recovery from such a trough was therefore inevitable if only on the rebound. Throughout the whole economy, there were high unemployment levels and high wage rates together with a lack of business confidence. Desperately needed was an increase in Aggregate Demand in the home market and in especially

foreign markets. Government action was therfore needed if not to directly attack any particular problem, but to at least set the stage for an economic upturn.

By September of 1931 with the Pound devalued to $ 3. 40 and the Gold Standard abandoned, conditions in the economy started to change. The sterling had been devastatingly overvalued making British goods uncompetitive on international markets. Now with a floating exchange rate, the sterling could perhaps attain its true value resulting in increased exports. Despite a floating exchange rate, the sterling remained overvalued by between four and five percent in 1934 and by 1937 was more overvalued then when on the Gold Standard. The effect of exchange rates becoming favourable to Britain never surfaced and by 1933 exports going to countries outside the sterling area were 37. 9% of total exports, compared with the 1929 figure of 43. 8%.

A change in policy by the National Government towards the sterling was accompanied by a more active role to improve economic conditions. The situation could hardly have been worse. High unemployment rates were due to the decline in the traditional staple exporting industries which were all centered in specific areas. There was the cotton industry in North West England; coal mining in Wales; shipbuilding, iron and steel in Scotland and the North East of England. Between 1929 and 1932 these industries had lost over 310, 000 jobs. Their decline and reducing exports went hand in hand and so any increase in demand by the home market did not affect these industries. Therefore by 1937 when the economy was burning these industries still had 330, 000 less employees than in 1929. The coal industry had lost export orders of 20 million tonnes between 1929 and

1937 which accounted for the drop of 17.5 million tonnes in output. The cotton industry was also in a poor state with only 75% of spinning capacity being used and only 68% of weaving capacity in production.

Although recovery of the economy did take place it was concentrated on the newer industries which had the potential for expansion already seen in the traditional industries. The electricity industry and the manufacture of associated goods; motor vehicle manufacturing; the aircraft industry; chemical industries and the construction industry were just some of those industries which shared unprecedented growth throughout the recovery period. The demand for such goods centered on the salaried workforce which was based in the South East of England. Salaried workers were much less susceptible to unemployment which meant demand for the new commodities was elastic. The electricity industry increased supply to nearly nine million consumers in 1939 as against only three million in 1929, and even at the lowest point of depression employed over 100,000 workers. The number of electrical engineers rose from 173, 600 in 1924 to 367, 000 in 1937. The motor industry supplied over half a million vehicles by 1937, a five fold increase in fourteen years.

However due to increased mass production through increasing technology, only 160, 000 jobs were created. Decreasing cost were enjoyed by many of these new industries which meant markets could be expanded and output raised. The construction industry experienced a boom period with residential construction 40% higher in 1933 than in 1929. The reduction of the mortgage rate from 6 to 4 % and the ability of contractors to obtain cheap credit stimulated the industry in a very positive way.

Cheap credit was very much a culmination of events starting with the abandoning of the Gold Standard in 1931. Foreign money was no longer needed to bolster the resources to find the Gold Standard and so the bank rate was reduced from six to two percent. Interest rates throughout the system fell, a situation which the government hoped would increase private investment and thus reducing unemployment and increasing production. With cheap interest rates the burden of the National Debt reduced, enabling a balanced budget easier to attain, because the interest on the National Debt was the single largest payment paid by the Treasury.

The cheap money policy kept recovery going once prices began to rise and by 1934 investment was back at the 1929 levels. The contribution by the influx cheap money towards economic recovery had less foundation than a fixed bank rate may have had. The main aim of National Governments fiscal policy remained consistent with that of previous government spending; however in 1931, government spending was at an unprecedented level. Rapidly increasing unemployment forced the Treasury to lend to the Unemployment Insurance Fund whose deficit was £100 million by mid 1931. The Treasury therefore showed that borrowing to pay benifits unbalanced budgets and was the main factor behind the reductions in unemployment that followed. Fiscal policy remained deflationary until 1933 at least when rearmament began, and thus played little part in the recovery.

Government policy to induce recovery also changed in other areas. Tariffs were introduced to protect industry from foreign competition. Some industries, such as cotton and chemicals, benefited from protection, while others suffered because of the increase in prices of the imported raw materials. Tariffs as means of protecting industries

were rather unsuccessful because the industries mainly in the decline suffered export losses when other countries retaliated their own tariffs. During the period 1929 to 1936 regional government policies resulted in 270,000 workes given advance wages and Layoff benefits to assist in finding new employment. Meanwhile, the South East and London, in particular, became increasingly congested due to the decline in industry and by 1937 radical changes in government policy were being called for.

By 1937 there had been a definite recovery and the economy was booming. By mid summer the Board of Trade estimated that industrial output was up 64% from 1932, even 30% above the peak level of 1929. During the following twelve months, however, 10% dropped off this index in a crash half as bad as that between 1929 and 1932. Unemployment was still high at 8.5% in 1937 despite the ongoing process of rearmament. Manufacturing growth between 1932 and 1937 was unpredicted which was probably due to a combination of the effects of increased protection from tariffs and the short term effects of sterling depreciation. However from 1935 the process of rearmament greatly exaggerated this boom. The steel industry despite its uncompetitiveness actually increased production from eleven million tons in 1929 to fourteen million tons in 1939, as a result of rearmament. There had been rapid growth in economic activity in the 1939's after the trough of 1931. This growth did not spread equally throughout all the industries or the country, and so high levels of unemployment continued until the outbreak of the war. The new industries which emerged were capital rather than labour intensive and so the traditional industries continued to decline, and unemployment remained at high levels. Government policy helped to alter the problem of eco-

nomic slump through orthodoxy and innovation. For the salaried worker the 1930's became an increasingly affluent time, but for the ordinary worker unemployment and the fear of it remained a fact of life.

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6. OUTLINE & ACCOUNT FOR CHANGES IN THE SIZE OF BRITISH COMPANIES SINCE 1920.

Our indication of the size of British companies is usually measured using the concentration ratio. This is the share of the largest one hundred firms in the total sales or output of the economy. Other measures of size have also been used, such as profits, assets, market valuation of capital and the number of employees.

In the late nineteenth and twentieth century, there were strong inducement making for larger scale enterprise. During the First World War the Government planned, financed and directed the activities of manufacturing firms. Firms were induced to adopt the most economical methods. This lead to some increased merger activity in order to expand capacity. However after the war the situation was far from that of prosperity; in fact Britain suffered a fierce slump. Rationalization was seen to be the solution to the problem experienced by the British economy, although Lyndall Urwich urged that:

> The mere financial combination of businesses or the wider application of scientific methods of management to existing units of

control, can neither of them by themselves contribute effectively towards equipping Great Britain with that reorganised national economy which is essential if she is to retain her place among the industrialised nations.

The failure of the market economy to produce prosperity and full employment lead to call for very large scale merging of intersts.

The major changes in the size of British companies began in the 1920's, with this period appearing as the first merger intensive decade, corresponding to a period of increased shape of output accounted for by the one hundred largest firms. Fig. 1 below, shows how the concentration of British firms has increased.

FIG 1

YEAR	SHARE OF OUTPUT ACCOUNTED FOR BY 100 LARGEST FIRMS (in %)
1909	16
1924	21
1935	24
1949	21
1953	26
1958	33
1963	38
1968	42
1970	40
1978	41

Official policy towards mergers was at that time favourable; with them being considered as necessary in order to improve efficiency and ensure competitiveness abroad. In 1921 the Profiteering Act was abolished. It had up until then, made the earning of a profit which to, in view of all the circumstances unreasonable, a punishable offence. Now, this lead the way for firms to increase their control of the market, and profits without fear of punishment.

During the first half of this century, many smaller family firms coed to larger quoted firms, thus decreasing the number of small firms. The advantages of this were considered to be an increase in efficiency, and increasing returns to capital. It was felt at the time that the returns from economies of scale and monopoly could be maintained if firms were prepared to consolidate their assets into larger units. Up to 1965, most capital gains were free from taxation and therefore most of the proceeds from the sales of a firm went directly to the owners.

The growth of giant companies was usually the result of the pooling of assets, which had previously been controlled by many firms. Reseach and development could be carried out on a much larger scale by large companies; so increasing the size of firms was considered to be beneficial to future technical progress, through the bringing together of ideas from various sources. For large firms such projects laid the basis for future corporate growth and diversification, adding further to the pressures toward large firms.

The setting up of the Banker's Industrial Development company (BIDC) in 1929 encouraged the formation of largest firms. It was intended to devise schemes to re-equip and where necessary merger companies in the staple industries which were suffering financial problems. One large firm formed under the guidance of BIDC was the Lancashire Cotton Corporation which between 1929 and 1932 absorbed almost one hundred firms.

The larger scale merger activity of the 1920's increased the rate of growth of leading firms over a wide range of industry groups eg, 82% of the growth in the food industry was due to mergers, the corresponding figures for Chemicals and Building materials being 91% and 93% respectively. All but three of fifteen industries showed mergers

as being more important than internal growth in increasing the level of concentration. Fig. 2 shows the number of firms decreasing through mergers.

FIG 2	YEAR	NO OF FIRMS DISAPPEARING THROUGH MERGERS.
	1910–19	750
	1920–29	1884
	1930–39	1414
	1940–49	778
	1950–59	1967
	1960–69	5635
	1970–79	3166

During the inter-war years no pressure groups emerged that were strong enough to have an effect on the imposition of a monopoly policy even the Labour Party failed to gain acceptance for their proposals for the investigation of monopolies. Mergers were generally welcomed as a sign of industrial vigour and only in the late thirties were doubts raised and popular opinion turned against schemes of rationalization which showed no regard for the public interest.

Between 1930 and 1948 there was a decline in the share of the market held by the one hundred largest firms from 66% to 57%. Declines were shown in thirteen out of seventeen industries with the increases in the others being very small. Expenditure on mergers fell to half its 1920's value in the thirties and fell further in the 1940's. There was a decrease in the numbers of small firms (employing less than two hundred peoples), from 38% of total employment and 35% of total output in 1935 to 24% and 20% respectively in 1958. Evidence of increased concentration outside manufacturing is however less satisfactory, although, for grocery retailing in particulars the concentration has dramatically increased.

From the 1940's goverment interest in merger activity increased and many policies were implimented after this date. The rise to power of the Labour Party brought about the monopolies and restrictive practices commission's formation in 1948. Following the reports of the commission, mergers no longer received such strong support. In 1956 the conservative government established the Restrictive Practice's Court to act as a futher deterrent. The Restrictive Trade Practices Act assumed that restrictive practices were harmful until proven otherwise, and the court found that only 1 % of the agreements registered were in fact in the public's interest. The act was successful in increasing competition in a significant number of industries.

Competition was also increased by the General Agreement on Tariffs and Trade (GATT), as barriers were reduced, an influx of capital into the UK economy from overseas lead to increased competition, although merger activity offset this to certain extent.

The 1948 Companies act made takeover bids much easier as firms were forced to disclose more details of their assets and profits. This added to the ways in which firms could become larger. Bids could now be made directly to the shareholders instead of via the directors of the firm. In the fifteen years after 1948 a quarter of quoted companies were acquired by other quoted companies. This figure rose to thirty - eight per cent between 1957 and 1967.

There were two important requirements on movement towards higher concentration which were removed in the fifties. They were the absence of strong competitive firms and restrains on takeover bids. The government was moving way from policies of non-intervention, in merger activity. The policy of intervention in private industries were further increased by the labour government of 1964-

1970. Previous fears that mergers could create unemployment had been dropped and replaced with the theory that larger units would in the long run be beneficial to future employment.

Internal growth has played a more important part in the increase in the size of firms in recent years. This is the growth due to investment in new factories etc. In recent rears it has become more predominant as there is now a greater emphasis on ploughing profits back into the firm, rather than removing them. Now capital issues also increased the size of firms. The stock market offererd this facility and it was particularly useful to companies which did't have the cash flow to finance large investments since without this facility they could not easily have gained access to scale economies.

Diversification increased throughout the 1960's with 45% of companies being diversified in 1960. This figure rose to 60% by 1930. Much of this diversification seems to have been the result of earlier mergers. Between 1957 and 1968, 39% of acquisitions by quoted firms were of firms from other industries. Many firms also expanded through the acquisition of overseas subsidiaries. In 1950 only 29% of large firms held overseas subsidiaries. By 1970 this figure had risen to 58%.

Merger activity remained relatively high in the 1970's, but after the oil crisis of 1973 and with a sluggish stock market, the number of mergers declined, accounting for a smaller proportion of total investment expenditure than had occured during recent decades. In 1973 the Fair Trade Act redefined monopoly as occurring when a firm controls 25% of the market (it had previously been a third) was enacted. This lead to more mergers being reported to the commission, and the share of the market controlled by the one hundred largest firms remaining fairly consistent.

Improved technology and the wider use of computers has made the management of large firms much easier in recent years. Consequently, firms can become much larger before problems arise with administration etc.

In conclusion it appears that there has been a long term tendency for the concentration of UK firms in the merket. This rate of increase has accelerated in proportionate terms since the end of the war. The rate of increase for 1950–70 being double that of 1901–1935. Important factors in recent years being changes in personal and company taxation, the distribution of personal wealth. The operations of insurance and pension companies have also played an important part in the change in the size of UK companies. They direct the publics savings into large quoted companies. The market for industrial capital has therefore favoured large quoted companies, and brought about lower capital costs encouraging the creation of large financial units, by means of mergers etc.

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7. WHAT WERE THE MAJOR ECONOMIC PROBLEMS FACED BY BRITAIN IN 1945? HOW AND TO WHAT EXTENT HAD THEY BEEN OVERCOME BY 1951?

After the end of the war in Europe a general election was called almost immediately afterwards. The election returned a Labour government to power with clearly an overwhelming majority.

The Labour government of 1945 was in a way the delayed results of the bitter experiences of the interwar years. Labour's ideology was based on J. M. Keynes' radical ideas, but many of the policy changes, which took place under this governments, were no revolutionary at all but were to a certain degree, based on the preparatory work initiated during the war.

The national disasters and sharing of hardships during the war had created a new spirit of national consciousness which made a new approach to the country's future a necessity. In order to meet the demands from the trade unions the Churchill Coalition Government worked out plans for postwar social security; and full employment. Plans for unscrambling the war machine and for international relations were also prepared.

Keynes was the mastermind behind a treasury submitted proposal for the establishment of an International Clearing Union for discussion at the Bretton Woods Conference in 1944 in the USA. The aggreement resulting from this conference led to the establishment of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD).

Bank Rate was held steady at 2 % during the war and this policy, combined with direction of labour, and other physical controls, a saving campaign, became successful. Investment declined and the net additions to the capital stock were negative but most losses on the domestic side were made good in a couple of years after the war.

The most serious economic problems the new Labour Government was confronted with occurred on the financial side. During the war Britain had been transformed from the world's largest creditor to the world's largest debtor.

The country had for years lived beyond means by consuming its capital, by borrowing and on gifts from abroad. Another problem was the disruption and diversion of the British productive capacity, and in the immediate postwar years the primary need was to replenish the devastated stock of capital assets and raw materials. But in order to restore its economy Britain had, it was estimated, to raise her exports to 75% above the prewar level. The balance of payments was seen, therefore, as the central problem of the economy, and the core of this problem was the shortage of hard currency resulting in the so-called dollar gap. The situation was aggravated by the large accumulation of purchasing power. Consumers emerged from the war years with substantial money balance which they had been prevented from spending, thus creating a dangerous inflatory potential.

Dalton, the new Chancellor of Exchequer, introduced aimost immediately a policy of still, cheaper money, which separately and also alongside with continuing physical controls like building licences and control on imports. But the accumulated purchasing power combined with the government's policy of forcing down interest rates could not, due to price controls, be used by consumers to bid up prices and so attract resources into the promotion of the most desired commodities. Instead resources went into the production of goods of secondary attractiveness where prices were not controlled raising the overall cost and therefore the prices of British exports.

The problems with the balance of payment became really acute and gold and dollar reserves were rapidly exhausted in spite of restrictions on imports. Only the USA had the necessary productive capacity to make good the losses experienced by other countries. In 1946, in order to alleviate the shortage of dollars, the USA and Canada made sub-

stantial loans including 1,000 million to Britain. It was expected that these loans would be sufficient to cover requirements over the short period which was all that was expected and seen necessary for the world economies to recover. But in 1947 the situation deteriorated. It was officially admitted that the loan was drawn on much more rapidly than was safe and on top of that came, in March, coal was reckoned to have cost the country about 200 million in exports. In July the sterling became convertible but that lasted for only few weeks because the size of the dollar deficit increased immediately.

In 1948 a general liquidity crisis was only avoided by further loans made under the European Recovery Programme, through which Britain received loans amounting to 1,500 million between 1948 and 1950. The programme was called Marshall Aid, after the American Secretary of State, General Marshall. The loans were allocated under the directon of Organisation for European Economic Coorperation (OEEC). Without this aid the prospects for British economy would have been very bleak.

Despite the periodic crisis the overall performance of the Britsh economy, the period after 1945, was quite impressive. There was a strong and steady expansion in output and exports, while controls kept inflation and consumption in check and employment remained high. Exports grew at and average rate of 11.9% a year between 1946 and 1951, while industrial production grew 5.75% on average. GDP rose only by 2.5% a year, largely because the service sector was held back. Unemployment fell from 3.1% in 1947 to 1.2% by 1951. The balance of payment, boosted by the Marshall Aid, showed signs of stability by 1950. But in the latter part of the period there were signs that other countries were beginning to pull ahead of Britain.

Britain continued to concentrate on the markets of the sterling area (the former Empire) because it was found easier to push exports to these markets than to North America and Western Europe, but, unfortunately, it was not here that the valuable dollars, so much needed to improve the balance of payment, were found. Britain had it within its grasp to participate in the reshaping of Europe and its recovery, but the country missed the opportunity and failed to participate in the trade boom within Western Europe between 1948–1951.

Labour Government laid the foundations for the Welfare State, but was unable to give a new sense of purpose and direction on economic matters to the British public. Britain, the first of all "developed" economies, found it hard to think in the terms which came so naturally to backward nations trying to catch up with advanced ones and consequently little was done to show how growth, productivity, technological change and the need to export could contribute to real income gains and economic wall-being of the country.

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8. WHY DID BRITAIN EXPERIENCE FULL EMPLOYMENT IN THE QUARTER CENTURY AFTER THE SECOND WORLD WAR?

If the inter war years were characterised by mass unemployment, the post war years were marked by a sharp reversal in employment trends to the extent that labour was brought from abroad to satisfy

the demand.

Between 1952–73 the number of people in civilian employment rose by 29%. Lord Beveridge had assumed an unemployment rate of 8.5%, but in 1944 stated that 3 % was a reasonable definition of full employment. Britain's unemployment level remained below 3 % for almost 25 years and remained below one million.

The popular explanation for the dramatic turn about in unemployment between the interwar and post war period is the implementation of the Keynesian demand management policies. This identified the main problem of the 1930's as demand deficiency. This restricted consumption and in turn production, exports and employment were promoted. Demand management relied on the government to increase the demand in the economy by increased spending which, through the multiple effect would increase general activity in the economy and this rectify output and employment problems.

There is little doubt that in the post war years there was an increase in demand in the economy. R. C. Matthews questions the governments role in this process as to "whether the high level of demand that actually occured was due to government action or whether it was due to other forces as a result of which government action was not needed."

Matthews argues that government policy was, if anything, having a restraining effect on the economy. This is because there was a government surplus of 3 % (average per annum) and so rather than increasing demand by borrowing the governments surplus created a deflationary pressure. The success of the post war period according to Matthews was the level of investment and export increases.

There was an increase both in the demand for, and willingness to

supply as well as investment. Demand was caused by the reconstruction and reallocation of resources lost in the war effort, the neglect of investment during the war years and indeed during the slump of the 1930's.

Coupled with the demand for investment was the increase in supply. There was a change in entrepreneurial attitudes caused by the feeling that the government would support demand if a slump occurred. Money was relatively cheap as interest rates were low and there were tax incentives to invest. There was an inflation rate of approximately 4 % which was perceived as being good for business and demand was supported by inflexible wages in downward direction.

Thus investment levels were very high during this period. Inevitably employment levels increased. A good example was the house building industry which employed many people. Matthews argues that investment during this period was increasingly concentrated private sector (although both public and private were increasing). There was very fast growth of capital stock which was low immediately after the war with investment ratios averaged at 12. 9% between 1950–70 (compared with 5. 6% 1928–38). Investment returns too were high averaging 13% per annum. This investment thus created increasing activity in the economy and employment increased.

Technical advances were also made during this period. New capital was often far superior to pre-war capital. New efficient machines made productivity per worker increasingly higher and made workers a more attractive commodity. Coupled with this was an increase in the efficiency of the allocation of resources, further aiding productivity.

Exports also increased in this period. This was aided by a massive

devaluation of 30.5% in 1949 due to an American recession. The introduction of fixed exchange rates also improved business confidence.

EXPORTS	1958=100
1913	91
1929	74
1933	59
1950	91
1958	100
1960	109
1970	170

Source : Gower "Key Economic Statistics 1900–66"

The growth in the economy was the great. Production increased in the advanced capitalist countries to levels 180% higher than the 1930's. Output per head increased. The economy grew at a rate of nearly 3 % per annum between 1950–70. Armstrong wrote, "The fifties and sixties were capitalisms golden age. 1" Immediately after the war there was increased spending power as people had savings from the war. Youngson argues that these things helped to create a boom to rectify the war years and after that was completed there was a largely self-propelling maintenance of high levels of activity.

The increased demand wasn't solely British phenomena. Throughout Europe the general level of trade and growth occured. Thus Britain was helped substantially by a general world boom. This was helped by better marking relations created by Bretton woods, Gatt and later the E. E. C., who all worked towards lowering the barriers to trade. There were no reflections or war debts between any of the war countries which hindered growth after the first world war and America's Marshall and assisted the upturn in international trade.

Wiedleburger suggests employment levels were determined largely

by the Two Sector move up of the economy. There was a shift from the Agricultural sector, where marginal product is near 0 and wages are barely above subsistance levels, to the industrial (and particularly manufacturing sector). Here people were drawn into the latter by pay above subsistance levels but replace the marginal product. Thus profit was increased and the demand for labour increased. This theory has been criticised as it does not seem to hold true for the 1920's and 1930's.

Thus it is difficult to say conclusively that any one factor was solely responsible for employment levels in the post war period. Most would agree that it was probably a combination of many of the aforementioned factors, which increased the levels of activity and through multiple processes the level of employment.

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9. WHY, BY INTERNATIONAL STANDARDS, WAS THE BRITISH ECONOMIC GROWTH SO SLOW IN THE 1950'S AND 1960'S?

In historical terms many of Britain's growth statistics were impressive after 1945. Between 1945 and 1950 industrial production increased by 30–40% and the rate of real growth in total industrial output increased by 3.7% between 1945 and 1960. Britain's international trade per-

formance improved dramatically; with visible exports increased by 75% over pre-war levels, and no increase in imports. However, these figures are depressing when compared with the achievements of other countries, expecially the founder members of the E. E. C., Japan and the partners of the European Free Trade Association (E. F. T. A.). Britain had internal constraints which inhibited economic growth and modernisation on the same scale as those of other countries. There was inefficient organisation of industry, dated capital, a low level of capital goods replacement, widespread trades union power and general mismanagement. The external constraints related to Britain's vulnerable financial system, which in itself was a function of limited resources, unfavourable balance of payments and Britain's financial and economic commitments, such as her involvement in the Suez and with the Colonies.

The Government was largely to blame for the economic decline in the 1950's and 1960's. To achieve traditional goals, foremost prestige, the government sacrificed the economy mainly by protecting the most cherished symbol of Britain's international position-the value of the Sterling. Expensive British goods were no attractive to foreign markets, which probably produce superior quality ones themselves. By the end of the 1950's a vicious cycle had evolved where the effort of maintaining Britain's international position had become the cause of here international vulnerability. The Government made few attempts to enhance trade; the Foreign office did not have the economic expertise and the Board of Trade at the time played a far less central role in the international economy. Twice in the post-war years were special government offices opened to deal with the domestic economy, the first being the Ministry of Economic Affairs in 1947 under Cripps

and the second being the Department of economic Affairs in 1964 with George Brown as the Minister in charge. In both cases the Treasury re-asserted its traditional control over the entire scope of the domestic economy within a short while.

Investement in Britain was low due to the whole panoply of government power, mainly exercised by the Treasury, which was keen to keep it that way. The Treasury was obsessed with the balance of payments, a balanced budget, the external value of sterling and inflation, but certainly not industry. Hence the Treasury was obstructive to investment in industry as it had always been wedded to a narrow segment of the economy – foreign exchange and currency balance. The strain of single-faceted responsibility, but multi-faceted power, led unsurprisingly to the Treasury putting its own interest first over the long-term interest of the country. Also, the traditional job of the Treasury was to minimise the expenditure of other government departments, expenditure being seen as the ultimate evil. It must be mentioned that many of the treasury employees were unprepared for the task of administrating a complex economy, most having had a training in the Classics. Also the tradition of reposting people to new positions every two or three year did no provide a basis of stability.

The Treasury, therefore, ignored the cries of the industries whilst listening to those of the banks and, inparticular, the Bank of England. Elsewhere in the world, central banks acted as economic policy-makers and planners for the whole nation. United Kingdom banks on the other hand did not acknowledge the need to be integrated with industry. This led to the phenomenon of the "Stop-Go" cycle. As the government sought to restrain balance of payments, it place restric-

tions on domestic consumers' purchasing power by manipulating hire purchase rates, all of which disrupted and discouraged long-term investment programmes in the consumer durables industries. City and Merchant banks placed their main interest in trade and overseas investment, whilst industries were sacrificed, as always, to the altar of the City's financial system.

A further cause of Britain's international decline was the fact that it did not exploit its strong position at the end of the Second World War. German and Japanese power had been greatly eroded whilst Britain stood as the victor. People in Britain had saved money during the war and in the first 10 years after 1945 the release of this pent-up demand made it very easy for producers to sell their products. They lacked the aggressive nationalism so vitally necessary to industrialists, whilst other countries, which were ruined during the war, worked hard to restore national pride in the form of fortifying their economy. British Industrialists were hostile to showing openness towards the foreign expertise that was emerging. There was no modernisation, nor thought for the future as they seemed content to rest on their laurels. It took until 1965 for an organisation providing expertise and industrial capital to be created-the Confederation of British Industries (CBI). Once again Britain waited for a crisis before acting.

The money that Britain did make in the post-war boom was not reinvested in industries; in fact, general de-industrialisation occurred. For example, the National Health Service was created so that human suffering and deprivation of the interwar years would not be repeated at any cost. Although the N. H. S. was a phenomenal achievement in itself, this was no consolation to the industrial sector. Scarce investment resources were mis-allocated to research and developments,

which was an unproductive absorption of surplus at excessive levels and took over 40% of all research scientists and engineers. In 1955 total research and development expenditure in the UK amounted to 187 million, the highest figure for any country in Western Europe, yet 63% of this total was spent on defense and less than one-third funded by private industry. It was noticeable that Japan and West Germany, who were denied the right to sustain a large national army, had the most technically and competitively efficient economies.

Trades unions were also a cause of industrial retardation. The most extreme criticism of British Trades Unions in comparison with foreign counterparts is that they were politically motivated organisations, prepared to use their considerable power to secure a privileged position in society. Until 1945 Unions had been mainly amongst craft workers, but after 1945 the balance of class forces changed and Unions emerged amongst semi-skilled workers in the new industries of engineering, vehicle construction and chemicals. Certainly UK exporters and industrialists found it to their advantage to avoid conflict with workers, hence redirected sales to new or protected markets rather than compete, which, in the end, stifled economic growth. Again, it must be stressed that the lack of competition amongst industrials in the early post-war years also enhanced the strength of the Unions.

Abroad unions were less militant and disunited as they were usually and internally, religiously or politically divided, whereas the British T. U. C. was not. Foreign competitors concentrated on producing, not quarrelling, hence Britain's profits were comparably eroded. Successive governments found themselves unable to tackle Union strength as they lacked the legal means to alter class practices at factory level and because the Labour movement was willing to strike against the

introduction of legal changes.

On the management side there was an almost equal volume of criticism. Brooking's Institution Study of the British Economy published in 1968 castigates British management for its poor overall quality. It lacked professionalism and qualifications due to nepotism and the extensive "Old Boys" network.

It is not surprising, under the general spectrum of British decline, that Britain applied to join the E. E. C. Although political considerations were foremost in the mind of the government in 1961, Ministers were not neglectful of the economic benefit which would include economies of large-scale production, specialisation and an increase in industrial efficiency as a result of exposure to the vigours of international competition and general stimulation to growth due to close association with a group of countries experiencing rapid economic expansion. In fact it was a means of assuring that Britain would catch up with the West.

The missed opportunities of the 1950's were difficult to recapture. Many industries were forced to collude which in itself was regressive to competitive growth. The struggle to maintain financial prestige in the City caused large-scale dis-investment which led to an absence of economic growth and hardened worker resistance. Sluggish markets meant that labour-saving techniques brought redundancies, which added to the crisis; low investment and high government expenditure resulted in inflation. What the UK economy needed during the 1950's and 1960's was general restructuring and modernisation.

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10. DISCUSS BRIEFLY THE PRINCIPAL FEATURES OF THE BRETTON WOODS SYSTEM AND ACCOUNT FOR ITS COLLAPSE IN THE EARLY 1970'S.

By the end of the World War II it was clear that the international monetary system needed completely reorganising and that multilateral trade needed to be re-established. To this end there were a number of discussions held in both Washington and London, between the U. S. and UK governments. The aim was to produce a set of rules or code of conduct for international monetary affairs. These talles culminated with an international conference held at Bretton Woods, New Hampshire in July 1944.

It was at this conference that the International Monetary Fund (IMF) was set up and the idea of the Gold Exchange Standard was introduced. The IMF was to be the organisation that had the job of creating the conditions, under which the transfer of goods from one country to another could take place unfettened by restrictions on trade or controls over international payments. The IMF had 3 main objectives. They were:

i) To extablish a multilateral system of payments based on world wide convertibility of currencies.

ii) To establish exchange rate stability well competitive devaluations avoided

iii) To allow member nations to pursue domestic policies such as full employment without worrying about the exchange rate.

In order to achieve these objectives the Gold Exchange Standard or Bretton Woods system was introduced. It was supposed to combine the best of both the old Gold Standard and free floating exchange rates. The dollar was given a face value against Gold of $ 35 per ounce. The currencies of other countries were then pegged against the dollar and therefore indirectly against gold. The dollar could only be converted into gold internationally and not domestically. The dollar was therefore as good as gold. There was also some flexibility. The exchange rates of countries could be pegged 1 % of their par value, and also the currencies were allowed to change in value but only by 10%. If any higher a change was necessary permission had to be sought from the IMF . The dollar was therefore to be the key currency backed by Sterling.

The IMF had a pool of funds made up of the currencies of all the member countries. The amount of currency each member country had to subscribe to the fund depended on the countries G. N. P. The amount of the countries subscription also decided it's voting quota on the IMF and how much it was allowed to withdraw from the pool. 25% of the money subscribed was in the form of gold and 75% in the form of the countries own currency. In this way it was hoped that the pool would contain sufficient funds. The largest quotes and therefore the countries with the most power were the USA, India, France, and UK. If a country had a short run balance of payments deficits it was allowed to withdraw foreign currency from the IMF pool. The country was expected to surrender the equivalent value of its own currency and was also expected to repurchase it, in the near future, with either gold or a convertible currency. The maximum that was automatically allowed to be withdrawn was the equivalent of the

value of gold it had subscribed to the fund. If a currency became scarce the fund had 2 options. The first option would be to either exchange gold with the country or borrow the currency from a member country. The second option was to declare the currency scarce and use exchange controls to ration the currnency. These measures would be continued until the surplus in the country was controlled . These policies were only meant to be for short term deficits and surpluses since it was assumed that over time, surpluses would cancel out deficits. If this did not happen devaluation or revaluation was acceptable with consultation with the IMF.

The Bretton Woods system did by no reasons get off to a good start. Between 1945 and 1955 there was a severe shortage of dollars. The problem was most acute between 1945 and 1948 when there was a large trading gap between Europe and the USA. Dollars were needed by Europe in order to buy much needed US goods, but it sold nothing in order to pay for these goods. It was not until 1948 when the Marshall plan was introduced that dollars became available. Marshall aid was a gift from the Americans to Europe . Its main objective was to keep the markets for its goods open by stopping any spread of communism into Europe . It also allowed European countries to yet, hold off much needed dollars . Without Marshal aid it would have been impossible, for the IMF to cope with the situation. It, therefore, took a back seat until 1955 .

It was not until 1958 that all W. European currencies were convertible into dollars. The Bretton Woods system did not function fully therefore until 1959. Its main period of operation was between 1959 and 1971. In 1958 however US exports fell dramatically and imports rose slightly. This meant the trade balance was no longer sufficient to

meet the needs of the huge amounts of external capital and military spending that the USA was commited to. The result was an outflow of gold from the USA. Although this loss was only $ 176 million from a total of $ 19.5 billion in 1959 it was the beginning of a rising trend that continued throughout the 1960's. The dollar problem had thus reversed by the end of the 1950's from a scarcity of dollars to a glut of dollars.

This showed up the difference between the gold standard and the gold exchange standard . With the gold standard the UK's gold was convertible domestically, there was therefore an automatic constraint on the domestic money supply and thus the balance of payments of deficits. With the US system, there was no such constraint on the money supply since gold was not domestically convertible and indefinate expansion was possible. In 1952 US liabilities passed reserves and by 1968 liabilities were more than 2 times greater than the gold and foreign currency reserves. In order for the US to continue to have balance of payments deficits, European banks were forced to hold dollars. As these holdings increased there became a conflict of interests between Europe and the US. The countries which held dollars did not need them since they were the most economically strong and not so reliant on US goods. Dollars were therefore worthless to them. But countries short of dollars couldn't afford them. Unlike gold, the dollar was no longer an objective form of money.

In the short term therefore the US was illiquid due to its high military spending, especially in Vietnam, and its high overseas investment. In the long run however its overseas assets were much greater than its debt. The US needed to cut back on its foreign investment or its military spending. The US was reluctant to do this because it feared it

might lose the markets it was exporting too and also its influence in world affairs.

By the end of the 1960's a major international crisis was inevitable. This was accelerated by the Vietnam War and the Keynesian policies of the US which it pursued in order to achieve full employment. In this it was very successfull and the US experienced its longest preiod of growth in its history. Unfortunately it meant an increase in the money supply and a rising budget deficit and this lead to inflation as costs outstripped productivity. This inflation was transmitted to other countries in the form of higher costs and interest rates. All this put a great strain on the monetary system. The problems of the fixed exchange rate were shown up as the system found out that had to cope with countries inflating at different speeds. The deficits and surplusses were also larger than the IMF could cope with.

The beginning of the end was in 1967 when the Sterling was forced to devalue by 14% despite considerable efforts from the US and other countries to try and prevent it from happening. Ever since 1957 Kenedy had been concerned with Sterling crisis as the Sterling had been unable to fulfill its role as the second key currency. The UK's major problem was that it wanted to maintain a similarly high role in economic affairs as it had done in the past. Unfortunately its industries were not strong enough to support overseas investments and military expenditure that was required to achieve this status. These problems led to the stop go cycle and deflation. This caused large UK firms to divert funds overseas and this continued the decline in Britains competitiveness. The US was desperate for the UK not to devalue its currency. This was because if the sterling was devalued there would be a lack of confidence in the system and consequently it

may break down. The Bretton Woods system was dependent on the assumption that the key currencies were as good as gold.
The US's fears became reality the following year when the dollar suffered a confidence crisis. As the dollar was the key currency it could not use exchange rates as a weapon to influence the balance of payments. Therefore in 1968 the price of gold rose to $ 40 per ounce and by 1969, 46 countries had converted their dollars to gold. By 1971 the US gold reserves had fallen from $ 17.8 billion in 1960 to $ 11 billion. At that rate of withdrawal it was calculated that with speculative acceleration there was only 5 years supply of gold.
Wherever there is a trade deficit in one country, it means there is a surplus in another country. In this case the surplus was in Japan and W. Germany. It was clear that equilibrium needed to be restored. There were 4 ways of doing this. The first option was for countries with surpluses to devalue their currencies, this was what was favoured by the US but neglected by these countries. The second option was for the US to deflate, but this was not politically feasible with the government going into an election. The third option was for the countries with surpluses to take up expansionary policies, but this was neglected by the inflation fearing Germans. The final option was to use suppression methods such as tariffs and controls on the US deficit. This was however against the Bretton Woods rules.
In order to get some action, the so called "Nixon shock" were introduced in August 1971. First of all, gold price was raised effectively devaluing the dollar by 8 % in terms of gold. Secondly the dollar was made unconvertable and thirdly an import surcharge of 10% was introduced. These had the desired effect and exchange rates were adjusted mutilaterally with the Smithonian agreement on 18th De-

cember 1971. Great flexibility in the pegging margins was introduced allowing differences of 2. 25% and the gold price rose from $ 35 to $ 38 an ounce. Unfortunately nobody believed the Smithonian agreement would work. This led to lack of confidence which in turn led to a speculative run on the dollar.

On June 23rd 1972, Britain floated the Sterling and all through 1972, dollars relieve accumulated at an alarming rate in surplus countries. The US tried to the downward pressure on the dollar by buying dollars and selling D. M. through the foreign exchange markets. This intervention continued until 1973, but to no avail. On the 12th of February, 1973, the dollar was devaluated by 10% as the official price of gold was raised from $ 38 to $ 42. 2 an ounce. This was virtually the end of the Bretton Woods system, especially if they were in the ad-hoc form of the 1971-72 readjustments. There then followed the European scales where European Countries all floated their currencies relative to gold.

Over the period of the Bretton Woods operation several weaknesses were shown. The first was the difficulty of adjusting balance of payment deficits when fixed exchange rates were in force. This was especially true for the US dollar since it was the key currency and the country could not use the exchange rate as the weapon to influence the balance of payments. The second problem was preserving confidence in the key currencies when their economies were in difficulty. The third problem was the large amount of money allowed to flow from one center to another in the international capital market. This led to distabilizing effect. Gold production also could not keep up with its demand. This meant dollars were held and did not help world liquidity. The reason for the gold shortage was that with its fixed

price it was umprofitable to mine it in certain areas.
The main criticism of the system however was its inability to force surplus countries to expand their economy in order to reduce their surplus. This was shown when Japan and W. Germany refused to do anything about their surplusses. The US was also unwilling to do anything about its deficit and it was this lack of cooperation which was the main reason for the collapse of the system. The IMF could also have been blamed since it never even considered using the scarce currency choice in order to force suplusses to be reduced, and instead prefered to lend the currency of the member country. The IMF was also not prepared for the growth in the world economy and had insufficient funds to cope with the deficits that occurred. It had proved itself capable of dealing with short term disequilibrium but had not really kept countries to the rules of the monetary system, as many deliberately manipulated their obligations to the fund.

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11. DISCUSS THE CAUSES AND CONSEQUENCES OF THE OIL PRICE EXPLOSION OF 1973/74.

In October 1973, war broke out in the Middle East. The effects of the war put immense pressure on world economies, and the "oil crisis" which ensued brought an end to the steady and long postwar boom.

As Armstrong says, "The mini boom of 72/73 proved to be the final and most feverish phase of the long post-war boon. The "oil crisis" of winter 1973/74 and an internatonal crash in the summer of 1974 brought the golden year to an abrupt and painful halt."

Conflict in the Middle East bred solidarity among Arab oil states and gave a new impetus to the Organisation of Petroleum Exporting Countries (OPEC). This was a cartel of the major non-US, oil producers, whose aim was to reduce the power of the big oil companies and raise incomes of the member countries. In an attempt to reduce support for Israel, OPEC announced a 10% across-the-board cut in oil exports and a selective embargo, directed chiefly at the US. The oil companies dutifully followed OPEC instruction to the latter. The companies tended to do what they were told. The Saudis dictated, controlled and ran the highest percentage of the OPEC markets. One company even acceded to a Saudi request to provide information on their supplies to the US military bases worldwide.

The selective embargo proved ineffective because the companies transhipped oil from one destination to another, spreading the cutbacks equally. The reduction in supplies of some 5 million barrels a day, or 9 % of non-Eastern block output caused few lasting problems. But its effect on spot oil prices, which rose considerably, was used by the producers to justify a general price rise. In the short term, demand for oil appeared insensitive to changes in price so the world could do nothing but accept them.

OPEC succeeded in imposing and maintaining a major increase: oil prices quadrupled during the winter of 1973/74, raising the producers' annual revenue by around $ 64 billion.

Some of the exporting countries would not instantly convert their

higher revenues into demand for Western industrial products. This resulted in their building up of substantial balance of payments surpluses. In Western Europe and Japan, measures were taken at once to narrow a yawning deficit in energy balances and to reduce dependence on OPEC countries. For instance, driving was banned on a Sunday. Restrictive policies were introduced in all major countries in 1973 in response to the price acceleration of the mini boom and the large wage claims that were beginning to be submitted in its wake. Materials and food prices began to drift downward from the summer of 1973, but world inflation rose to an annual rate of 10% in the second half of the year as previous materials price rises fed through to the final goods markets.

There were four developments in the early 1970's which led to the "oil crisis". The first was an acceleration of various rates of inflation on a world scale. Secondly there was a rapid increase in the dependence of the United States on imported oil due to declining domestic reserves, and that is as well as a mismanagement of its own domestic energy affairs. The third point is that there was a shift of control in the oil industry of the Middle East from the hands of seven major international companies to the governments of the exporting countries. Lastly, and perhaps the most important is the implantation and expansion of Israel in the Middle East against bitter Arab opposition. The oil price rise worsened the conditions both for producing surplus and for realising it. It raised input costs, thereby tending to decrease profitability and intensifying the pressure on industries to raise prices because fixed capital could no longer be operated profitably at existing output prices. It also transferred, at a stroke, 1.5 of the world purchasing power to OPEC. The recipients did not, and in the short

run could not, spend the majority of their extra revenue, so world demand fell.

Pressures were intensified still further by the introduction of yet more restrictive policies. Monetary condition were further tightened in most economies in the spring of 1974. Nevertheless, inflation rose for some months, and production continued to grow in all major economies except the US during the first half of 1974. The commodities boom had increased many less developed countries' export earnings, and import rose with some lag. The oil price rise reactivated the boom in commodity prices and boosted inflation, which reached an annual rate of 15% in the spring of 1974.

The war in the Middle East had prompted the OPEC to take such actions. It is doubtfull if OPEC could have successfully imposed the price increase at the time it did in the absence of the high levels of demand that accompanied the mini boom. In addition, dollar devaluations worked to encourage a rise in price, because most oil products were priced in dollar which was being eroded in value.

OPEC would almost certainly have been unable to sustain massively higher prices in the context of the subsequent crash had United States policy toward oil imports not changed dramatically in the 1970's.

The price rise was a product of the boom in a more general and fundamental sense. A tremendous increase in oil consumption which accompanied the great burst of accumulation threatened to deplete reserves. Some possible pessimistic view were expressed as to a "depletion horizon", therefore a major price adjustment was needed to encourage both energy-saving and exploration activities.

The impact of this crisis in 1973/74 varied considerably across industries and countries. The bulk of industries faced higher costs and a

squeeze on profits whereas the major oil producers had a profit bonanza. Returns on their operations rose from $ 3. 9 billion in 1972 to 12. 1 billion in 1974. Those on investments in OPEC increased from $ 2. 6 billion to $ 6. 1 billion over the same period.

Although the majors oil producers enjoyed vastly improved profits and the oil price rise appears more of a mixed blessing when viewed in the context of other changes in the industry. The rise of OPEC brought changes in ownership and operations as well as price.

Direct exports by OPEC national oil companies rose from a negligible proportion of production within the area to some 50–55% over the course of the 1970's. Host government ownership of oil production in OPEC rose from some 2 % in 1970 to 60% in 1974 and 80–90% in 1980. By the end of the decade the major oil producers had secure ownership rights for crude oil only within the OECD area. Despite price boosts, exploration and production, OECD oil output only rose by 1. 3 million barrels a day between 1973 and 1980.

Japan experienced a greatly increased import bill. The country had no fossil fuels of her own, and thus there was a great drain on domestic incomes. This increased her balance of payments constraints and reduced any room available for manoevre over domestic economic policies. For Japan, therefore, the "oil shock" was a major blow without mitigating benefits. For the United States, the crisis brought a completely different reaction. Its large oil reserves allowed it to be self sufficient in oil. It runs a two tier pricing system which allows the US domestic industries to gain a competitive advantage by purchasing oil well below world market prices.

For a long time the US had known about reserves of shale oil and bituminous schists, which are other forms of fuel, but it just had not

been economically viable to extract them at pre-1974 prices. It was the extraction of these which would make the US self-sufficient in oil in the foreseeable future and would eliminate any dependence on foreign reserve supplies, a problem which the Pentagon had started to worry about.

So while the oil crisis caused major difficulties for the world systems as a whole, its impact, like that of the commodity boom and the dollar crisis was uneven. The US had suffered less than all of its major rivals.

Post 1973/74, nuclear energy attracted much attention. By 1977, EEC countries and Japan were importing less oil. Even during the economic revival which came at the end of the '70's, France and Italy were still able to reduce their dependence on OPEC countries.

Oil still remains a central problem in international affairs. Most of the world will almost surely demand on the Middle East for the greater part of its supplies of oil. It is clear that the stability of such a heavy dependence on such a limited base can only be ensured by extensive international co-operation. OPEC tried to reduce the oligopolistic power of the seven major companies and in many ways succeeded. But at the same time the companies increased their profits quite considerably.

OPEC is often cast as a super villain, holding the world economy to ransom for political motives. The price rise came like a bolt from the blue, damaging growth which had previously been performing well. The "oil crisis" was the trigger for the crash and separates the period of overheating from the subsequent one of mass unemployment and stagnation.

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