1. Introduction

The 1929 world depression raises a series of issues for economic analysis and historical methodology which can perhaps be summed up most concisely in the difference of view precipitated in a television debate in May 1969 between two American economists, Milton Friedman and Paul Samuelson. Friedman insisted then, as he has done on other popular and professional occasions,[1] that the depression had a single cause: errors in carrying out monetary policy in the United States. Samuelson maintained it was the result of a series of historical accidents. The Friedman position disposes of a series of lesser analytical issues which emerge if the original question of system *v.* accident is resolved in favour of system. He finds the origin in the United States rather than in Europe or the periphery; in monetary rather than real factors; in policy rather than in the nature of institutions or in the tasks required of them; in a national economy rather than in the operation of the international system. Within the limits of United States monetary policy, moreover, which excludes the villain of many another analysis – structural dislocation in Europe after the First World War or the failure of the United States to act like a creditor nation, particularly the imposition of the Smoot-

1. See, for example, *The Balance of Payments: Free versus Fixed Exchange Rates*, American Enterprise Institute for Public Policy Research, Washington, D.C., 1967, p. 90: 'When the United States embarked on deflation and proceeded to reduce its money stock, the rest of the world was forced into a major catastrophe.' Professor Friedman's scholarly treatment of the subject is in Milton Friedman and Anna Jacobson Schwartz, *A Monetary History of the United States, 1867–1960*, Princeton University Press, 1963, esp. Chapter 7, 'The Great Contraction, 1929–33'. This is also published separately in *The Great Contraction*, Princeton University Press, Princeton, 1966.

Hawley Tariff Act of 1930 – he rules out stock-market speculation, and the delay in passing the Glass-Steagall Act of 1932 which overcame a domestic shortage of monetary gold by allowing the Federal Reserve System to substitute government securities instead of gold for the lacking eligible paper needed as backing for the central bank's liabilities. There would doubtless have been a recession or a depression with perfect monetary policy, or a money supply which grew in the United States at some optimal pace. But Friedman's explanation of the 1929 world-wide great depression is national, monetary, related to a policy decision. It is uni-causal. In my judgement it is wrong.

There is a host of similar explanations which rely mainly on a single root cause of the depression, or a single origin. President Hoover was persuaded throughout his career in the White House and in writing his memoirs on the depression twenty years later that the origin of the trouble lay in Europe, starting with the difficulties of adjusting to the consequences of the First World War and accentuated by a financial crisis in 1931.[2] The widest-held European view is that the depression started in the United States: fundamentally in that country's unwillingness to write off war debts; more precisely in the stock-market crash of 1929 or the frenzied lending of 1927 and 1928. More subtle analysts look to the failure to operate the gold standard properly, converting it to the gold-exchange standard on some showings, lowering interest rates unduly in the United States in 1927 on others.

But Samuelson's explanation of 'a series of historical accidents' is perhaps no more satisfactory. Great depressions recur. The great depression of 1873 to 1896, sometimes regarded by economic historians as *the* great depression, was perhaps different in origin, characteristics and effects, so that on these scores one can regard the period from 1929 to 1939 as unique.[3] Going further back,

2. *The Memoirs of Herbert Hoover*, vol. III: *The Great Depression, 1929–1941*, Macmillan Co., New York: Hollis & Carter, London, 1952. For a contemporary statement, see his Foreign Affairs Message to Congress, 10 December 1932, in Department of State, *Foreign Relations of the United States, 1931*, vol. I, Washington, D.C., 1946, pp. x ff.

3. But note that J. T. W. Newbold, 'The Beginnings of the World Crisis, 1873–1896', *Economic History*, vol. II, No. 7 (January 1932), pp. 437 and 439, found the origin of that depression in the 'profound unsettlement of short-

however, produces the uniformities that the social scientist searches for. Like the First World War, the Napoleonic Wars were followed by a short, sharp deflation in 1816, comparable to that of 1920–21, and a period of monetary adjustment culminating in the restoration of the pound to par in 1819 and 1821. Then came a spurt of foreign lending, from 1821 to 1825, followed by a stock-market crash in 1826 and a depression. If one subtracts 100 plus three to five years from the major economic events of the 1920s and 1930s, interesting parallels emerge. The 1826 depression was not perhaps as deep or as widespread as that of 1929, or as those of 1837 and 1848 which followed it. But the timing is disconcertingly similar.[4]

Moreover, the European depression of the 1840s, not deeply shared in the rest of the world, presents the same issues as the 1930s as to origin and the role of accidental factors. British historians think of the 'commercial crisis of 1847–8' as largely the result of the railway mania, with an admixture of money panic associated with the failure of a series of grain dealers. On the Continent there was considerable difference of opinion. Cameron calls it 'first and foremost a financial and banking crisis',[5] whereas other economic historians direct attention to real causes, including the smallest whęat crop in fifty years in 1846, followed in 1847 by the largest crop in fifty years. Fohlen, more or less ignoring financial aspects, calls the 'crisis of 1848 . . . in effect a series of economic and political accidents'.[6] At a deeper level, it may be possible to detect a parallel between the crisis of 1848 on the European Continent and the 1929 depression; both represented failures of the economic system at a transitional stage from one set of institutions and forms to another. But this is to anticipate.

term money markets', arising from a withdrawal of £90 million from London in twelve months. These funds had been accumulated by Germany as part of its receipts of the Franco-Prussian indemnity of 1872. See also Walter Bagehot, *Lombard Street*, new edition, John Murray, London, 1917, pp. 291 ff.

4. Alexander Dana Noyes, *The Market Place: Reminiscences of a Financial Editor*, Little Brown, Boston, 1938, pp. 338–40.

5. Rondo E. Cameron, *France and the Economic Development of Europe,* Princeton University Press, Princeton, 1961, p. 125.

6. Claude Fohlen, *Une Affaire de famille au XIX^e siècle: Méquillet Noblot*, Colin, Paris, 1955, p. 62.

Another form of 'historical accident' might be the pure fortuitousness of regularly recurring cycles of three different periodicities reaching their depression phases simultaneously. The depression of a Kondratieff long cycle covering as much as fifty years arrived simultaneously with the depressions of a Juglar intermediate nine-year cycle and of a short-range Kitchin cycle in inventories. Vastly oversimplified, this is the Schumpeter view.[7] It is difficult, however, for most economists to think of these sorts of cycle as independent of each other, like celestial bodies in orbit, and of the great depression as a random but predictable event like an eclipse.

If we reject both the single or dominant cause and the series of historical accidents as the explanation of the great depression, we are left with a host of issues. In one perspective, we may ask how and where the depression originated, why it spread so widely, why it went so deep and lasted so long. Questions about where and how it originated have an obvious interest apart from political recrimination, but in their turn they open up new conundrums about *causa proxima* and *causa remota* as well as *causa causans*. Assume that the answer to the question of where the depression originated is limited to the United States, Europe, the periphery or to the relations among any two or three of them. We then need to know, first, what happened to produce the trouble, and secondly, why the economic system failed to respond to deal with the trouble, either automatically, through the microeconomic mechanism of adjustments in supply and demand, or through macroeconomic response through monetary and fiscal systems; or through policy reactions in which the automatic economic forces set in motion are reversed or supported in the interest of stability. Take, for example, the view that the depression originated in the recovery of European production in foodstuffs, raw materials, textiles and so forth, the output of which had been expanded overseas during the First World War. This would be a real explanation instead of a monetary one, but it is not complete unless we can explain why

7. Joseph A. Schumpeter, *Business Cycles: A Theoretical, Historical and Statistical Analysis of the Capitalist Process*, 2 vols., McGraw-Hill, New York and London, 1939. Schumpeter also makes allowance for 'non-essential events which explain particular circumstances' (p. 908), and for 'incidents, accidents and policy' (pp. 937 ff.).

over-expansion in one or more lines did not produce price declines which cut back output and redirected resources. Or, if the blame is laid on the halt in United States lending to Germany and the periphery in 1928, perhaps owing to the attraction of funds into the call-money market supporting the rise in New York stock prices, it is necessary to explain not only how the halt in lending set the world economy into reverse gear, but why other forces did not move into action to offset the impact – either borrowing from a different source or in a different form through the automatic market mechanism; or why monetary or fiscal measures were not taken to offset the impact as a result of policy decision. The initial force may be contained in two ways – automatically or by policy decision – and to explain its consequences one has to account both for the failure of automatic forces in the economy to act and for the failure of decision-making machinery.

The failure of economic policy is relatively easy. Throughout the chronological account of the depression which follows, we shall cite instance after instance of what, with hindsight, appears as economic illiteracy. There is no monopoly. Deflationists are found everywhere – Hoover, Brüning, Snowden, Laval. Examples abound of bad judgement – the British decision to return to the gold standard at par in 1925, and the similar Japanese decision taken in July 1929 and carried out in January 1930; of ill-conceived nostrums – the Roosevelt-Morgenthau-Warren attempt to raise commodity prices by changing the price at which the Reconstruction Finance Corporation bought newly mined gold in the United States, and the Blum experiment with the forty-hour week in France in 1936; of too little and too late, such as the 50 million schilling ($7 million) loan for Austria on 16 June 1931 which the Bank of England made for a week (but was forced to renew many times). Often no one in authority had any positive idea of what to do, and responded to disaster in the policy clichés of balancing budgets, restoring the gold standard and reducing tariffs. Hobsbawm puts it too strongly perhaps: 'Never did a ship founder with a captain and a crew more ignorant of the reasons for its misfortune or more impotent to do anything about it.'[8]

8. E. J. Hobsbawm, *Industry and Empire· an Economic History of Britain.*

There were many economists and a few public figures in Britain (Keynes, H. D. Henderson, Mosley), in France (Reynaud), in Germany (Lautenbach, Woytinsky), and perhaps in the United States, who had domestic remedies which made sense in modern terms; and a number of suggestions put forward for the World Economic Conference of 1933 anticipated the decisions of Bretton Woods a calendar decade and intellectual light-years later. Roosevelt frequently confessed to his ignorance, but had the virtue of not being doctrinaire and, more positively, of insisting on trying one thing after another until he found something which would help.[9]

The emphasis on doctrine in policy formation may be too simple. In many instances, policy was constrained not by official understanding of economic principles but by public attitudes. The classic example was perhaps war debts, the American public being 'more unanimous on this one question of foreign policy than on any other'[10] in wanting debts collected; even if Hoover and Roosevelt had wanted to cancel the debt – which they did not –

since 1750, Weidenfeld & Nicolson, London: Pantheon, New York, 1968, p. 179.

9. See Raymond Moley, with the assistance of Elliott Rosen, *The First New Deal*, Harcourt Brace & World, New York, 1966, p. 6: 'Roosevelt's knowledge of economics was limited'; and p. 244: 'I doubt that Roosevelt or I could have passed an examination such as is required of college students in elementary economics. . . . We were rank amateurs in the very domain of knowledge that was of paramount importance.' See also John Morton Blum, *From the Morgenthau Diaries*, vol. I: *Years of Crisis, 1928–38*, Houghton Mifflin, Boston, 1959, p. 141: 'Roosevelt said [to Morgenthau]: "You and I, of course, started with no knowledge of this subject, but the two of us have done well and have been able to more than hold up our end."' Schlesinger quotes Roosevelt as likening himself to a quarter-back who would try a variety of plays to find one that succeeded. See Arthur M. Schlesinger, Jr, *The Age of Roosevelt*, vol. II: *The Coming of the New Deal*, Houghton Mifflin, Boston, 1959; Heinemann, London, 1960, p. 193. But see Rexford G. Tugwell, *The Brains Trust*, Viking Press, New York, 1968, p. 73, who insists that Roosevelt had had courses in economics, 'not only in such specialties as finance, transportation, taxation and insurance, [but] he was far from a beginner in economic theory'.

10. See Robert H. Ferrell, *American Diplomacy in the Great Depression: Hoover-Stimson Foreign Policy, 1929–1933*, Yale University Press, New Haven, 1957, p. 33.

they would have had no easy time doing it. (Hoover's failure to understand is reflected in his insistence that, because the French had deposits in New York in excess of the amount due in, say, December 1932, they were able to pay, thus ignoring the distinction between capital and income or how the French Treasury was to gain command of the dollars or gold from the Bank of France without violating its statutes or the budgetary process.)[11] Equally adamant in its unwillingness to pay in December 1932 was the French Chamber, as was evidenced by Herriot's fall from power on 14 December 1932, when he proposed the payment of the instalment due the next day.[12]

The failure of automatic forces to offset events which pushed the system in the direction of depression has received some attention with regard to the gold standard, but less in other respects. The claim is widely made that it was not the gold standard which failed, but the way it was operated.[13] Countries which lost gold did not always deflate, and those which gained it, notably France and the United States, expanded too much or too little. It is not so universally recognized that other aspects of the international monetary mechanism are supposed to work symmetrically; if the

11. *The Memoirs of Herbert Hoover*, vol. III, p. 185. Hoover claims that the French would have paid in December 1932 had it not been for an unfortunate statement by Roosevelt at Warm Springs to the effect that he did not regard payment of the 15 December instalment as a necessary condition for opening further negotiations. The amount due was $50 million and French holdings in New York were $500 million.

12. See Henry L. Stimson and MacGeorge Bundy, *On Active Service in Peace and War*, Harper & Brothers, New York, 1947, p. 217. Herriot was a real hero to Stimson for opposing his own people in the interests of international understanding – much bigger than anyone on the United States side of the Atlantic. Stimson was one of the few cancellationists in the United States government. See Elting E. Morison, *Turmoil and Tradition: A Study of the Life and Times of Henry L. Stimson*, Houghton Mifflin, Boston, 1960, p. 433, when Stimson and Mills went to the White House in January 1933 to ask President Hoover to take some bold step. 'For a time the President was roused by the possibility of a "great state paper", but then he changed his mind. Stimson, he said, was "ten million miles away from his position" – the "debts were merely a chip on the current of ordinary prosperity".'

13. See Lionel Robbins, *The Great Depression*, Macmillan, London, 1934, esp. pp. 97 ff.

flow of capital stops, for example, it may be deflationary for the countries which cease to import capital, though it should be expansionary for those which no longer send savings abroad. Equally, the imposition of tariffs should be expansionary for the importing country if contractive for the countries losing export markets. If prices of particular internationally traded commodities fall, the income and spending of countries specialized in these goods evidently also fall, but those of countries which regularly buy them should rise. Again, currency appreciation is deflationary, but the counterpart of depreciation in other countries pushes in the opposite direction. It is therefore inadequate to explain world depression by referring to losses of gold or markets, a fall of prices, or currency appreciation, without specifying why the expansionary force, which is a counterpart to the depressive factor specified, did not function properly. There are a number of factors which can be pointed to, which will be explained as the occasions arise: accelerators, money illusion, elastic expectations, the dynamic spread of deflation to the banking system and the like. Without some such asymmetry or positive feedback, however, no substantial depression is possible.

A symmetrical system with rules for counterbalancing, such as the gold standard is supposed to provide, may give way to a system with each participant seeking to maximize its short-run gain. This is the competitive system envisaged by Adam Smith where each man (or country), in advancing his own welfare, advances that of the total, either because of an absence of interactions or because of external economies. But a world system of a few actors (countries) is not like this, and the fallacy of composition – that the total often differs from the sum of the parts – enters to affect the outcome. In advancing its own economic good by a tariff, currency depreciation or foreign-exchange control, a country may worsen the welfare of its partners by more than its own gain. Beggar-thy-neighbour tactics may lead to retaliation, so that each country ends up in a worse position from having pursued its own gain.[14] National economic interests are some-

14. See President Roosevelt's First Inaugural Speech: 'Our international trade relations, though vastly important, are in point of time and necessity secondary to the establishment of a sound national economy. I favour as a

times complementary, sometimes opposed, with no one or two countries controlling the outcome, which rather depends upon the actions of them all.[15]

This is a typical non-zero sum game, in which any player undertaking to adopt a long-range solution by itself will find other countries taking advantage of it. Agreement that all should adopt a long-range strategy may be conceptually satisfactory, but is likely to involve different degrees of sacrifice from different players at a given moment in time. Britain wants to stabilize currencies at $3·40 to the pound, while the United States lacks interest in the subject until the rate is nearer $4·86. Or postulate a network of reparations, war debts and commercial loans in which Germany owes reparations to Britain and France and commercial debts to the United States; Britain owes to the United States about what it receives from Germany, and is owed in war debts from France; France is to receive the lion's share of reparations, well in excess of its war debts to Britain and the United States. In this circumstance, Germany is more ready to cancel reparations than to default on commercial debts, since it owns some assets abroad and is interested in maintaining its credit. Britain is willing to cancel reparations, but only if war debts are excused. France insists on receiving reparations, wants war debts cancelled, and is relatively indifferent to commercial loans. The United States can see no connection between war debts and reparations, is

practical policy the putting of first things first. I shall spare no effort to restore world trade by international economic adjustment; but the emergency at home cannot wait on that accomplishment' – *The Papers and Addresses of Franklin D. Roosevelt*, vol. II: *The Years of Crisis*, Random House, New York, 1938, p. 14. See also Blum in *From the Morgenthau Diaries*, vol. I, p. 75: 'European nations on the whole resented the gold-buying policy, but no nation had for several years shown much regard for the economic convenience of others, and in 1933 the pressure on the President was such that he had to do something'; and Hugh T. Patrick, 'Some Aspects of the Interwar Economy', prepared for Sixth Conference on Modern Japan: 'Dilemmas of Growth in Prewar Japan', a conference held in Puerto Rico, 2–7 January 1968 (mimeographed), p. 43: 'There is some merit to criticism that Japan pursued a beggar-thy-neighbour policy; in the world economy at that time though, neighbours had to look out for themselves.'

15. See Oskar Morgenstern, *International Financial Transactions and Business Cycles*, Princeton University Press, Princeton, 1959, p. 572.

prepared *in extremis* to accept a moratorium on reparations and war debts, but seeks to safeguard the sanctity of commercial debts and wants to revive war-debt payments after the year's moratorium is over. No equitable solution is possible. Inevitably the system runs down to wipe the slate clean of reparations, debts and service on commercial lending. In exactly the same way, the attempt of a system of countries with interlocking multilateral trade to achieve export surpluses tends to wipe out all trade as successive trading partners cut imports from the next country.

In these circumstances, the international economic and monetary system needs leadership, a country which is prepared, consciously or unconsciously, under some system of rules that it has internalized, to set standards of conduct for other countries; and to seek to get others to follow them, to take on an undue share of the burdens of the system, and in particular to take on its support in adversity by accepting its redundant commodities, maintaining a flow of investment capital and discounting its paper. Britain performed this role in the century to 1913; the United States in the period after the Second World War to, say, the Interest Equalization Tax in 1963. It is the theme of this book that part of the reason for the length, and most of the explanation for the depth of the world depression, was the inability of the British to continue their role of underwriter to the system and the reluctance of the United States to take it on until 1936.

This game-theoretic interpretation of the international economic and monetary system, plus the insistence on an asymmetry in the operation of the system, also contributes to the general conclusion that the conventional wisdom of the period was not as wrong as most modern economists believe in its concern with the dangers of speculation, the necessity to raise prices, the desirability of lowering tariffs and the need to stabilize exchange rates. It is true that stock-market speculation was no longer a problem after 1929, and that no one knew how to raise world prices, or even to raise national prices through exchange depreciation which might only lower gold prices abroad. Programmes for tariff truce or halting competitive exchange depreciation were purely negative, stopping forces which were making the world economy continue to run down, without doing anything positive to reverse the positive-feedback mechanism. It is clear that the leading theorists and practitioners of the 1930s were wrong on a number of issues, such as budget-balancing, and poor on therapy, but their diagnosis was not as weak as is widely believed.

In the inescapable choice between chronological and functional organization, the book adopts mainly the former but associates each year or pair of years with a particular set of problems or occurrences. Chapter 2 sets the stage by discussing the recovery from the First World War to about 1926 and the position of war debts, reparations, stabilization of exchange rates and foreign lending. Chapter 3 concentrates on 1927 and the approach of difficulties in central-bank cooperation, the international capital market, the rise in New York stock prices. The fourth chapter looks at the position in major foodstuffs and raw materials, which can be said to have turned between 1925 and 1928. And 1929 is, of course, the year of the stock-market crash, the title of Chapter 5.

The years from 1930 to 1933 are each the subject of separate chapters dealing with 'The Slide to the Abyss' (Chapter 6), '1931' (Chapter 7), 'More Deflation' (Chapter 8), and 'The World Economic Conference' (Chapter 9) respectively. Thereafter the chronological pace speeds up. Chapter 10 deals with 1934 and 1935 and is entitled 'The Beginnings of Recovery'. In 1936, and Chapter 11, 'The Gold Bloc Yields'. Chapter 12 deals with 1937 and the recession. 'Rearmament in a Disintegrating World Economy' covers the final period of 1938 and 1939 and Chapter 13. A final chapter, 'An Explanation of the 1929 Depression' (Chapter 14), brings the threads of the analysis together into conclusions.

To the extent that the organization is analytical rather than chronological, there are difficulties in following issues in the years before and after their holding of the centre stage. Less developed countries are treated mainly in Chapter 4 on primary product prices, for example, but must not be lost sight of either at the depths of the depression in 1932 and 1934 or in the later stages of recovery.

In this chronological treatment a number of turning-points deserve emphasis: 1929, 1930, 1931 and 1933 – the stock-market crash, the financial crisis, the failure of revival in the spring of

1930 and the missed opportunity of the World Economic Conference to organize recovery. Most analysis concentrates on October 1929 and May–June 1931.[16] The baffling second quarter of 1930 and June–July 1933, covering the World Economic Conference, are, however, important in explaining why the depression went so deep, lasted so long and why recovery was so incomplete.

16. See, for example, Herbert Hoover's division of the depression into five phases: (1) October 1929 to April 1931; (2) April 1931 to July 1931 (the quake from Europe); (3) August 1931 to December 1931 (the collapse of sterling); (4) December 1931 to July 1932 (reaching bottom); (5) the electoral campaign in the United States, leading to the bankers' panic of March 1933 – *The Memoirs of Herbert Hoover*, vol. III, p. 38.