

***Monetary Reformers, Amateur Idealists and  
Keynesian Crusaders***

**Australian Economists' International Advocacy,  
1925-1950**

by

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## **Abstract**

Between 1925 and 1950, Australian economists embarked on a series of campaigns to influence international policy-making. The three distinct episodes of these campaigns were unified by the conviction that ‘expansionary’ economic policies by all countries could solve the world’s economic problems. As well as being driven by self-interest (given Australia’s dependence on commodity exports), the campaigns were motivated by the desire to promote economic and social reform on the world stage. They also demonstrated the theoretical skills of Australian economists during a period in which the conceptual instruments of economic analysis came under increasing pressure.

The purpose of this study is to document these campaigns, to analyse their theoretical and policy implications, and to relate them to current issues. Beginning with the efforts of Australian economists to persuade creditor nations to enact ‘cheap money’ policies in the early 1930s, the study then explores the advocacy of F.L. McDougall to reconstruct agricultural trade on the basis of nutrition. Finally, it examines the efforts of Australian economists to promote an international agreement binding the major economic powers to the pursuit of full employment.

The main theses advanced in the dissertation are as follows:

Firstly, it is argued that these campaigns are important, neglected indicators of the theoretical positions of Australian economists in the period. Hitherto, the evolution of Australian economic thought has been interpreted almost entirely on the basis of *domestic* policy advocacy, which gave rise to the view that Australian economists before 1939 were predominantly orthodox in theoretical outlook and policy prescriptions. However, when their *international* policy advocacy is included, a quite different picture emerges. Their efforts to achieve an expansion in global demand were aimed at alleviating Australia’s position as a small open economy with perennial external sector problems, but until such international policies were in place, they were forced by existing circumstances to confine their domestic policy advice to orthodox, deflationary measures.

Secondly, the campaigns make much more explicable the arrival and dissemination of the Keynesian revolution in Australian economic thought. A predilection for expansionary and proto-Keynesian policies, present within the profession for some time, provided fertile ground for the Keynesian revolution when it finally arrived. Thirdly, by supplying evidence of expansionary international policies, the study provides a corrective to the view that Australia’s economic interaction with the rest of the world has largely been one of excessive defensiveness.

Originality is claimed for the study in several areas. It provides the first comprehensive study of all three campaigns and their unifying themes. It demonstrates the importance to an adequate account of the period of the large amount of unpublished material available in Australian archives. It advances ideas and policy initiatives that have hitherto been ignored, or only partially examined, in the existing literature. And it provides a new perspective on Australian economic thought and policy in the inter-war years.

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**This work is dedicated to**

**Peter and Diana Turnell**

**and to the memory of**

**William and Jessie Turnell**

**and**

**Reginald and Dulcie Fraser**

*The belief that we have come from somewhere is closely linked with the belief that we are going somewhere. A society which has lost belief in its capacity to progress in the future will quickly cease to concern itself with its progress in the past.*

E.H. Carr, 1961



## INTRODUCTION

### **1.0 Introductory Comments**

On 30 May 1945, Australia's Minister for Post-War Reconstruction, J.J. Dedman, tabled *Full Employment in Australia* before the Commonwealth Parliament. The product of countless drafts and compromises, this 'White Paper' was an extraordinary testimony to the extent to which 'Keynesian economics' had taken root in Australia. Declaring that it was the responsibility of governments to stimulate spending on 'goods and services to the extent necessary to sustain full employment', the White Paper explicitly recognised Keynes's central point that aggregate demand was the primary determinant of employment. Breaking aggregate demand into the components familiar to any modern student of introductory macroeconomics - private consumption, private capital expenditure, government spending and net exports - the White Paper identified private capital expenditure as one of the chief sources of instability of demand and employment. This was consistent with Keynes's prognostications and with similar documents issued overseas, as was its solution to the problem of deficient demand by both compensatory public expenditure and monetary measures to encourage private spending.

In contrast to its overseas counterparts, however, private capital expenditure was not identified by the White Paper as the *chief* source of fluctuations in demand and employment. The chief source of unstable demand in Australia, rather, was instability in export income. Unstable export income was, indeed, doubly cursed - for not only was it a source of demand instability itself, but it was also an important constraint on government policies designed to alleviate other sources of deficient demand. Of course, the White Paper's identification of the external sector as the principal constraint on the domestic economy was hardly new. A preoccupation with external balance and a 'brooding pessimism' about its prospects has been a defining feature of Australian economic thought for many years (Corden 1968, p.15). It was also the motivation for the relatively numerous contributions of Australian economists to the literature devoted to trade and protection, perhaps the area in which they have made their greatest additions to the sum of economic knowledge.

The preoccupation with external balance had previously produced a number of devices designed to manage it, but almost all of these (captured under the guiding philosophy of 'New Protection') involved the restriction of imports in some way. In the White Paper, 'protection' was not disavowed, but it took a back seat to a complementary policy which its authors regarded as much more in keeping with the spirit of its times.

This policy took the form of a proposal that the Commonwealth Government seek agreement with other nations to enter into a binding commitment with each other 'to do all in their power to maintain employment within their own territories, and thereby expand demand for internationally-traded goods'. Called variously by Dr. H.C.

(Nugget) Coombs, one of the principal authors of the White Paper, the ‘positive approach’, ‘Australia’s international Keynesian crusade’ or, most popularly of all, the ‘employment approach’, it was a policy which informed Australia’s positions to all the conferences concerned with the reconstruction of the world economy during, and immediately after, the Second World War (Coombs 1981, p.35). Devised by Coombs, Giblin, Melville and other influential economists from the ‘golden age of Australian economics’, the ‘employment approach’ was motivated by the concerns for external balance (Groenewegen and McFarlane 1990, p.118). It was also self-consciously an attempt to apply what its authors believed to be Keynesian economics on a global scale. Self-interested and theoretically innovative, the employment approach was the product of a generation impressed by Marshall’s dictum that it was with ‘cool heads but warm hearts’ that economists should go out into the world.<sup>1</sup>

This ‘radical and distinctly Australian’ approach was not, however, the first time Australian economists had embarked upon a programme which combined the traditional anxieties for external balance with theoretical innovation and a Marshallian sense of mission. Two earlier campaigns, shorn of the model fully developed by Keynes in the *General Theory*, but inclusive nevertheless of many of the ideas which led to it, had been initiated by Australians in the previous two decades. The first of these, the product of Giblin, Melville and the ‘older’ group of professional economists in the vanguard of the employment approach, was concerned with attempts to convince the world’s creditor nations of the efficacy of expansionary monetary policies as the solution to the global Depression. These efforts, which were the basis of Australia’s approach to the Imperial Economic Conference at Ottawa in 1932, and to the World Monetary and Economic Conference in London in 1933, ultimately foundered upon the breakdown of the latter. With it went the last hope of a multilateral solution to the problems of the global economy before the Second World War.

The second campaign began after the failure of the World Monetary and Economic Conference. Advanced by F.L. McDougall, an influential amateur in a long tradition of Australian economics, the ‘nutrition approach’ was hawked around creditor nations throughout the latter half of the 1930s. It called for a reorganisation of world agriculture along lines of comparative advantage through the elimination of agricultural protection, with simultaneous public spending initiatives designed to improve living standards. These ideas were an intellectual extension of earlier efforts by McDougall, in company with the then Prime Minister of Australia, S.M. Bruce, to build a prosperous and well-populated Australia within a reforming British Empire. Broadened into a campaign of ‘economic appeasement’, McDougall’s propagation of his nutrition ideas continued into the war years where it interconnected with the employment approach - completing a neat circularity of ideas which seemed to foreign observers as something quite distinctively Australian.

This perception of foreign observers was a real one. It is a proposition of this thesis that the approaches outlined above represented a consistent line of advocacy, one which should be considered as a counter to the protectionist and syndicalist themes traditionally associated with Australia’s interaction with the world.

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<sup>1</sup> Marshall cited in Smyth (1994), p.26.

## **1.1 Aims and Significance of this Research**

The first and most basic aim of this research is to document, and critically examine, Australia's posture to the international economy as encapsulated by the campaigns above. With the exception of the 'employment approach', these have not been examined in the existing literature in any systematic way. The possible links between them has not been examined at all. The descriptions of the employment approach, the best known of the campaigns, are largely confined to relatively brief accounts in the memoirs of the protagonists and in works concerned with Australian economic thought and policy in the war years more generally. And finally, the *economic* ideas of McDougall, and the monetary campaigns of Australian economists at the Ottawa and World Monetary and Economic Conferences, have not been examined at all.

This would not matter if these approaches were merely trivial extensions to the corpus of Australian economic thought that was already in the public domain. It is a proposition of this thesis, however, that these approaches are vitally important. In a country whose economic history has been so dominated by the concern for external balance, an exclusive concentration on the domestic advocacy of Australian economists will present a distorted picture of the understanding of the economic *theory* that lay behind such advocacy. The advocacy of Australian economists internationally, by contrast, was made in a scenario in which the special constraints of Australia's particular circumstances were removed. This, it will be argued, is especially important when considering the period under examination, a period which included the most severe balance of payments crisis ever experienced by Australia. In this context, the deflationary stances implied by the 'Premier's Plan' and related proposals have come to be regarded as constituting the *leitmotif* of economic policy in Australia between the wars. Such policies should *not* be regarded, however, as indicative of the *theoretical* understanding of Australian economists, whose overseas advocacy revealed them to be less the slaves of economic orthodoxy, than informed users of an alternative discourse which would reach fruition with the publication of Keynes's *General Theory* in 1936.

By extension, a further aim of this study is to examine the extent to which the international advocacy of Australian economists sheds light on the existence, and propagation, of a 'Keynesian revolution' in Australian economic thought. A growing literature on this topic has tended to tell a story in which a rapid conversion of Australian economic thought took place in Australia via the infiltration of the profession of primarily 'young' economists during the war years, zealously convinced of the correctness of Keynes's prescriptions and making their way into positions of influence opened up by the exigencies of war. True up to a point, such a story ignores the extent to which Australian economists had been in the vanguard of developments throughout the inter-war years, developments that this thesis labels 'proto-Keynesian'. Less evident in their domestic and published writings, such theoretical positions are clearly apparent in the writings of Australian economists concerned with the international economy.

One major reason for the over-emphasis on a 'revelatory' or 'messianic' approach to the influence of Keynes in Australia is that a great many of the existing works concerned with the history of Australian economic thought rely upon the *published*

writings of Australian economists. This reliance, and because the work done by Australian economists on international matters tended to be for the Government and therefore generally *unpublished*, means that a disproportionate weight is attached to their domestic advocacy. Such a weighting paints a picture of Australian economic thought that is much more orthodox, much more restrictive and ‘deflationary’, and much less open to new ideas than is the case when the *unpublished* writings of Australian economists on international matters are given their due. Without these unpublished writings, there is, indeed, a yawning gap between the writings of Australian economists pre-*General Theory* and those of the wartime and postwar period. Once they are included, however, the gap narrows remarkably, and the rapid take-up of *General Theory* Keynesianism in Australia becomes far more explicable. In this present study therefore, great reliance is placed upon the unpublished writings of Australian economists on Australia’s prospects within a global economy. This allows for an explanation of the Keynesian revolution in Australia which, while noting the importance of the changes in thought instigated by Keynes’s most important work, is not one of a sudden meeting on the road to Jerusalem. It also leads to a substantial reappraisal of the roles and theoretical positions of some of the most prominent Australian economists of the period.

The period in question was a time of extreme instability in the international economy. The financial domination of the United Kingdom was fast receding, that of the United States was only just beginning. This was made more unsettling in Australia because the Australian economy was undergoing substantial structural change. Its evolution from a largely agricultural producer to an industrialised one had been underway for some time, but in the period under examination the process greatly accelerated. This structural change was also reflected in the international advocacy of Australian economists. The efforts of McDougall were directed to a largely static role for Australia as an agricultural producer in the international division of labour. For the economists behind the employment approach, Australia’s agricultural interests were never far away, but the new realities of Australia as an industrial country were central. This meant there was a subtle difference in the motivation behind the earlier and later international campaigns. The advocacy of McDougall was about maximising Australia’s national income by maximising global demand for primary commodities. For the employment approach, global demand was conceived not so much as *the* source of national income, but as a potential source of disturbance to domestic full employment.

The structural evolution in the Australian economy was reflected in a changing economic relationship with the United Kingdom. This relationship, initially based on the classic pattern of an agricultural periphery and an industrial and financial metropolitan centre, had been in long term decline. It is one of the surprising findings of this research that this declining economic relationship was not matched by a concurrent decline in the role of the United Kingdom in the imagination of either Australia’s economists or policy makers. Though this was most obviously apparent in the advocacy of McDougall and the Australian economists at Ottawa and the World Monetary and Economic Conference (all of whom sought to exploit the economic power of the United Kingdom directly), its role in the schemes of Australian economists right through the war years and beyond continued a filial relationship that is surprising to modern eyes. A subsidiary aim of this research is to highlight this

changing role, and to present Australia's economic diplomacy in a way which could help shed light upon the process by which its place in the world at large was evolving during these seminal years.

## **1.2 Limitations of this Research**

This thesis is concerned with an aspect in the history of Australian economic thought, and not with economic history more generally. This means that economic *policy* will be dealt with only to the extent that it affected, or was affected by, the advocacy of the economists. Detailed examination of policy relevant to Australia's external relations, but not related to the campaigns under examination, will not feature. Thus, for example, the thesis does not deal with the trade diversion policies against Japan and the United States in the late 1930s, nor the interminable bilateral trade negotiations that are the bread-and-butter of economic diplomacy. This same methodology will be employed when examining the policy responses of other governments to the Australian approaches. To the extent that they reflect either conflict or congruence with the theoretical positions of the Australian economists, such responses will be examined, but when they are not, a passing reference will suffice.

Australian Government policy enters into this research, therefore, according to the way in which its imperatives shaped the advocacy of the economists. Matters of government policy were of the least importance to the advocacy of the economists at Ottawa and the World Economic Conference because there was little government involvement. Similarly, the work of McDougall on nutrition had very little to do with the Australian Government. The source of this lack of government involvement was the same for both episodes - the Lyons Government in Canberra. This was a 'do little' administration whose economic philosophy constituted hardly more than a desire to ride out the storm before the arrival of an international recovery. By contrast, the employment approach was very much in keeping with the broader political objectives of the Curtin and Chifley Governments of the 1940s and was very much shaped by them. This became increasingly apparent as the campaign advanced and the mercurial Dr. H.V. Evatt, the Minister for External Affairs in both these Governments, exerted his influence. Even here, though, the role of the Government was not great beyond key individuals. As late as 1947, Chifley observed in relation to the employment approach that the 'proposals are still extremely vague so far as the public, the labour movement, caucus and even the majority of Cabinet are concerned, not to mention opposition parties'.<sup>2</sup>

A related limitation of this study is that it does not attempt to include all the work of the various economists who enter its narrative, even that which might constitute their most notable. This exclusion also involves works related to Australia's economic relationships with the outside world that were primarily concerned with domestic policy rather than being attempts to influence international affairs. Prominent examples of such work, which are mentioned only in passing, are the deliberations of the 'Brigden Report', commentaries on protection policy and organised marketing, and criticisms of trade diversion policy. Such work was often important, but in the

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<sup>2</sup> Prime Minister Chifley to J.J. Dedman, Minister for Post-War Reconstruction, 22 July 1947, National Archives of Australia (NAA), CP855/1/1, S1-BUN1, 1.

end it was guided by the constraints that influenced their domestic policy advice. It contained, therefore, the same limitations as the purely domestic efforts in serving as indicators of the economists' theoretical positions.

The study devotes a chapter to the implications of its theses to the Keynesian revolution in Australian economics. This chapter is limited, however, in two ways. Firstly, the 'revolution' with which it is concerned is an intellectual one confined to economists and their advice, and not to policy-making more broadly. Secondly, it does not attempt to construct an alternative holistic explanation for the rise of Keynesian ideas in Australia. Rather, it is concerned to suggest ways in which the existing literature on this subject should be recast in the light of the international advocacy of Australian economists. New ways in which this subject might be addressed using 'new institutional' models of intellectual change are examined, but this is also subject to the constraint of being limited solely to the economists' international advice.

One of the great problems of historical writing is in knowing where to begin and where to end. Although the time period chosen necessarily restricts the field of vision, in this case it is sufficiently broad to cover all that is necessary for the central ideas. The beginning date, 1925, has been chosen since it was in this year that McDougall published the most comprehensive account of his 'sheltered markets' concept. This year also saw the return of the United Kingdom, and therefore Australia, to the gold standard. In so doing, it exacerbated the divergence between official policy and 'monetary reform'. The concluding date, 1950, has been chosen since it was in this year, with the failure of the United States Congress to ratify membership of the International Trade Organisation, that Australia's efforts to secure an international agreement on full employment were effectively brought to an end. These dates are not cast in stone, though, and where necessary the study will venture beyond them.

There is no existing literature for the topic matter of the thesis as a whole. For this reason, there is not a single omnibus chapter devoted to reviewing the literature. Instead, the existing literature is referred to at relevant points in each chapter.

### **1.3 Outline of the Study**

The thesis is divided thematically into five sections, and divided either chronologically or by subject matter into 11 chapters.

Sections I and II examine the advocacy of Australian economists, and their amateur colleagues, before the Second World War.

Section I takes up the story of what this study has called the 'monetary reformers'. Extending out of that broad movement of economists dissatisfied with the workings of the gold standard in the early years of the twentieth century, it was a tag self-consciously taken up by Keynes, Ralph Hawtrey and Gustav Cassel (amongst the most prominent) after the First World War in reference to their advocacy of *discretionary* monetary policies and price stability. Their ideas, especially those of Keynes, were immensely influential amongst a group of Australian economists, led by

Douglas Copland (in monetary matters) but also including L.F. Giblin, Edward Shann and Leslie Melville.

For the purposes of this study, the label ‘monetary reformers’ has been appropriated to refer to the efforts of these Australian economists to convince the world’s leading creditor nations to adopt expansionary monetary policies as the solution to the global Depression. Based on the writings of Keynes and the other postwar monetary reformers, this advocacy was undertaken in the context of two chronologically distinct episodes. These episodes, the Imperial Economic Conference at Ottawa in 1932, and the World Monetary and Economic Conference in London in 1933, are examined in Chapters Two and Three.

Chapter Two is concerned with the Ottawa Conference. In the existing historical literature, Ottawa has been examined as a watershed event in the collapse of international trade between the wars, but not as the venue for the argumentation of monetary policy. The Chapter will provide an examination of the Australian economists’ understanding of monetary theory and some brief biographical details of each. The Chapter will then detail the preparation for the Ottawa Conference and the development of the monetary line adopted by the Australian economists. The Conference and its outcome will then come under the spotlight. The Chapter will document, for the first time, a most remarkable theoretical debate that opened, on conclusion of the Conference, between Leslie Melville and Lionel Robbins. An assessment of the efficacy or otherwise of the Australian strategy is then made.

Chapter Three is concerned with the World Monetary and Economic Conference of 1933. Representing Australia at this Conference was roughly the same group of economists present at Ottawa, providing them with another opportunity to advance their monetary line. The months before the Conference was a period spent in refining the approach taken at Ottawa and, accordingly, was one which was relatively rich in the discussion of theoretical matters. These discussions, very revealing of the economists’ theoretical positions, have hitherto been ignored in the literature. The Chapter will then document the Conference and its collapse in the wake of the inability of the ‘gold bloc’, the ‘sterling area’ and a confused United States’ leadership to agree on a common approach to reconstructing the world monetary system. Finally, the Chapter concludes by noting the despondency which thereafter prevailed amongst the Australian economists with regard to the global economy, and the chances for Australian recovery within it.

Section II breaks strict chronology to take up the great tradition of the ‘amateur’ in Australian economics, but extends this to the area of international economic diplomacy by examining the role of F.L. McDougall in advancing what he perceived to be Australia’s interests. McDougall’s ideas were sometimes ill-formed, sometimes anachronistic and something short of rigorous economic theory, but were, nevertheless, widely disseminated throughout the inter-war years and taken to be most representative of Australia’s positions.

Section II is divided into two historical episodes, beginning with McDougall’s conception of ‘sheltered markets’. A revisit of the Chamberlainite imperial economic model, sheltered markets is examined as an example of but one of the many amateur

‘proto-Keynesian’ movements which littered the inter-war period. The propagation of the concept will be noted, as will its relationship to similar movements and the position they occupied relative to contemporary trade theory.

The examination of McDougall and his ideas continues with what became known as the ‘nutrition approach’. This was an ‘underconsumptionist’ diagnosis of the global Depression. Much more identifiably proto-Keynesian than sheltered markets, the nutrition approach was a mixture of self-interest with an eye to selling more of Australia’s primary products, together with a broader agenda with ambitions of economic and social reform. The Section will examine the launch of the nutrition approach, the extension of the concept into a programme for improving living standards and ‘economic appeasement’, and its propagation around the global power centres. It concludes by examining the achievements of the approach and its relationship to underconsumptionist economic theories.

Section III takes the narrative through the Second World War, and the culmination of the ‘expansionist’ advocacy of Australian economists via the employment approach. Linked in terms of personnel and theoretical underpinnings to the two approaches outlined in Sections I and II, the employment approach was instigated after the revolution in macroeconomic theory following Keynes’s *General Theory* in 1936.

The largest component of this study, Section III contains five chapters concerned with the evolution and propagation of the employment approach from 1942 to 1950. Chapter Five begins the story with an examination of Article VII of the Mutual Aid Agreement - the United States’ desired ‘consideration’ for Lend-Lease aid during World War Two. Article VII presented Australian economists with the traditional dilemma of Australian economics - internal *or* external balance - unusually starkly, and the employment approach, born out of this sudden requirement for a considered reconciliation, was the result. The Chapter examines the beginnings of the employment approach out of the deliberations of the Financial and Economic Committee headed by Giblin, its emergence as the product of the interaction between an older and younger generation of Australian economists, and its initial advocacy in London in 1942. Chapter Five also introduces the competing plans for the reconstruction of the international monetary system - Keynes’s ‘International Clearing Union’, and the ‘Stabilisation Fund’ of Harry Dexter White.

Chapter Six takes the employment approach into 1943, and its consolidation under Dr H.C. Coombs. It details the ongoing discussions over the Clearing Union and the Stabilisation Fund, and takes something of a diversion to document the creation of the first of the United Nations’ autonomous bodies, the Food and Agriculture Organisation (FAO). The FAO was the culmination of the efforts of McDougall, who continued his advocacy during the war but was joined, at the ‘Hot Springs’ Food and Agricultural Conference in 1943, by Coombs and other Australian officials. Their joint efforts were at least partially responsible for the creation of the FAO, forming in this institution a unique achievement that blended the older and younger Australian approaches. The Chapter then takes the employment approach into 1944, and documents further interactions with Keynes. The Chapter concludes with the



diversion of the approach at the hands of Dr Evatt at the Conference of the International Labour Organisation (ILO) later that year.

Chapter Seven examines Australia's attempts to have the employment approach adopted at the Bretton Woods Conference in 1944. Bretton Woods saw a one-sided compromise emerge between the Clearing Union and the Stabilisation Fund in the creation of the International Monetary Fund and the World Bank. In many ways Bretton Woods was the climax of the conflict of ideologies between orthodoxy and the new macroeconomics of Keynes. The failure of Australia's efforts at Bretton Woods to have the employment approach written into the articles of the two new institutions is fully documented in this Chapter, as is the soul-searching and recriminations which followed.

Following its failure at Bretton Woods, Australia pressed strongly for a stand-alone conference on employment at which it could press for an international agreement binding countries to the use of policies to promote full employment. Chapter Eight details these efforts, which seemed to yield success when, in 1946, the United States agreed to sponsor an International Trade and Employment Conference. Held in 1947 in Havana, Cuba, this conference resulted in a proposal for an International Trade Organisation (ITO) which incorporated in its charter many of the measures sought by Australia under the employment approach. A seeming victory was taken away, however, with the failure of the US Congress to ratify the ITO. Chapter Eight will fully document these twists and turns, together with an account of Australia's parallel efforts to have the employment approach incorporated into the charter of the United Nations.

Chapter Nine concludes Section III by reconsidering the employment approach in terms of economic theory and in terms of the *geo*-political economy of its times. Finding in favour of the approach in both these aspects, it speculates that in the Marshall Plan and the military spending of the 'Cold War' there emerged a policy framework from the world's leading creditor nation that was equivalent, in terms of the maintenance of aggregate demand, to the employment approach.

Section IV examines a theme implicit through all three of the previous sections - the growing influence of Keynes and the subsequent 'revolution' in macroeconomics in Australia. Beginning with a survey of the existing literature concerned with the influence of Keynes in Australian economics, its finding is that this literature is made less convincing by its failure to document the *international* advocacy of Australian economists. It is this advocacy, shorn of the constraining special circumstances of Australia's external position, which is a much better indicator of the theoretical positions of Australian economists of the era than that which may be distilled from their domestic advocacy alone.

Section V concludes the work by drawing its general themes together, and makes some suggestions for further research.

### Archives Consulted

Though secondary works are used from time to time, the bulk of this thesis has been constructed via source documents at a number of repositories. These include the National Archives of Australia, the Australian National Library, the archives of the Reserve Bank of Australia, the State Library of New South Wales, the Public Record Office in the United Kingdom and the archives of the Food and Agriculture Organisation of the United Nations (Rome).

This thesis has also benefitted from the recollections of a number of the surviving participants of the events it portrays. During the course of the study the author interviewed (in alphabetical order), Dr John Burton, Dr. H.C. Coombs, Mr Reginald Holder, Miss Elizabeth McDougall, Professor James Meade, Sir Leslie Melville, Sir Arthur Tange, Mr W.C. Wentworth and Sir Frederick Wheeler.

## **SECTION I**

### ***Monetary Reformers***

## **Introduction**

The Imperial Economic Conference that met in Ottawa in July 1932, and the World Monetary and Economic Conference (WMEC) that met in London the following year, were watershed events in the conduct of international trade between the world wars. The most prominent attempts to salvage order from the collapse of the global economy, the conventional historical accounts of the retreat at Ottawa of the United Kingdom into protectionism, and of the subsequent collapse of the WMEC, have become totems of the bankruptcy of international economic co-operation in the inter-war years. Less well known is the fact that both these conferences were also the venues for a range of fertile schemes originating outside the economic orthodoxy. Many of these concerned monetary policy, and it was in this field that Australia was to play a prominent role.

Ottawa came less than a year after the United Kingdom's historic break with free trade, and the agreements reached there were an attempt by the members of the British Empire to construct (via tariff preferences) an *imperial* division of labour. But Ottawa was about more than trade, it was also about money. More specifically, Ottawa was a venue for the countries attached to sterling to attempt to affect British monetary policy - policy which greatly impacted upon their own economies. Given Britain's break with the gold standard in 1931, it was also an area in which there was perceived room for influence.

The WMEC met in London in June-July 1933. Convened by the League of Nations, sixty-four nations met to 'decide upon the measures necessary to solve the economic and financial difficulties which are responsible for, and may prolong, the present world crises' (Australia, Parliament 1933, p.1). It was a dismal failure. Mistakenly believing that he was being called upon to fix the value of the dollar in terms of gold, President Roosevelt made public his famous mid-Conference 'bombshell' that he was not willing to surrender domestic action for the 'old fetishes of so-called international bankers'.<sup>3</sup> His pronouncement effectively rendered the Conference moribund and it was adjourned shortly after. The WMEC was the last time a multilateral solution to the depression was attempted before the Second World War. If it is remembered for anything today, it is usually for the nature of its demise and the theoretical divisions which it exposed between gold standard orthodoxy and an alternative approach that had its roots in monetary reform.

Australia's position on monetary matters at Ottawa and at the WMEC was the product of four of its most distinguished economists - Douglas Copland, who then held the chair in economics at the University of Tasmania, Leslie Melville, the first ever economist for the Commonwealth Bank, Edward Shann, the foundation professor of history and economics at the University of Western Australia, and L.F. Giblin, who then held the Ritchie Chair in economics at the University of Melbourne. All four were involved in the deliberations of economists which led up to the so-called 'Premiers' Plan', that compromise between the advice of the economists and the powerful advocates of deflation such as the Commonwealth Bank.

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<sup>3</sup> Roosevelt cited in Skidelsky (1992), p.481.

Trade issues apart, the Conferences have been largely ignored by historians of economic thought in Australia who have generally been concerned with the advice and activities of economists domestically, and for whom the Premiers' Plan has become the *leitmotif* of their theoretical positions. Such an omission is unfortunate and misleading. As will be argued below, it is the approach taken by Australian economists to *international* questions which provides a much better indicator of their theoretical positions and development.

In this context the two conferences are extremely important. Australia's representatives advanced the line that Australia's (and the world's) best hope for economic recovery lay in expansionary monetary policies carried out by the principal creditor nations. A line consistent with that long advocated by Keynes and other monetary reformers, it had been evident in the individual writings of the Australian economists for some time, but was brought together with the Conferences in mind. Using archival sources hitherto unexplored, it is concluded that key members of the Australian economics profession in the interwar years were theoretically much less deflationary than conventional studies, confined to domestic policy, have allowed.

The argument thus outlined proceeds as follows. Chapter Two examines the monetary side of the Ottawa Conference. Taking Copland, Shann, Melville and Giblin in turn, it explores the international implications of monetary reform and examines the degree to which such ideas were present in their writings up to 1932. The Chapter then takes up the issue of the 'Wallace Bruce Report', and an interesting discussion with Keynes that was to inform much of which followed. It then looks at the Conference itself - the preparations, the resolutions and its aftermath. A hitherto completely overlooked theoretical debate which occurred in its wake between Melville and Lionel Robbins will be outlined in detail. The Chapter concludes with an analysis of the efficacy of the Australian efforts.

Chapter Three is devoted to the WMEC. Examining first the background to its convening, it will move on to document the evolving monetary thought of the Australian economists since Ottawa, and their objectives for the WMEC. The Conference itself will then be reviewed, highlighting the controversies over quantitative restrictions, international public works and the question of exchange stability that was to bring about its undoing. The Chapter concludes by noting the extraordinary theoretical journey some of the Australian economists had made during the 1930s in the course of their international advocacy.

## **Chapter Two**

### **Cheap Money and Ottawa**

#### **2.0 Australian Economists and Monetary Reform**

Douglas Copland, Edward Shann, Leslie Melville and L.F. Giblin were among the most prominent Australian economists of the inter-war years. Members of the first generation of the economics profession in Australia, they were formative in establishing economics as an academic discipline and were also highly influential as advisers to government on an *ad hoc* basis. Most famous as the core group of economists behind the Premiers' Plan in 1931, their advice was informed throughout by an overriding concern for Australia's external position - and an implicit assumption that Australia would always honour its external debt. These concerns meant that the Premiers' Plan, though supposedly a mix of deflation (cuts to money wages, deficit reduction, tariff cuts) matched by reflation (exchange depreciation, bond rate cuts) was, in fact, decidedly deflationary in its effects.<sup>4</sup> The Premiers' Plan has come to dominate the way we think about the response of Australian economists to the onset of the Depression, but it was not actually representative of their larger theoretical positions. This was especially the case with regard to monetary policy. Remove the special circumstances of Australia's dire external circumstances in the 1930s, as was the case in their advocacy of monetary action in the major creditor countries, and a quite different picture emerges. This is what Ottawa was about, and this is why it is important to this study.

Given their different approaches to monetary matters, the ideas of each of the four economists are examined separately. These are subsequently brought together to examine their joint advice for the Wallace Bruce Committee in 1932, and for the Ottawa Conference itself.

#### *Copland*

Douglas Copland was the most prominent writer on monetary theory and policy in Australia during the interwar years, a position aided by his editorship of *The Economic Record* from its inception in 1925. A firm adherent of a strictly 'classical' conception of the quantity theory of money in his earliest writings, by the early 1920s Copland became enamoured of the work of 'monetary reformers' such as Irving Fisher, Ralph Hawtrey and J.M. Keynes. Keynes's *Tract on Monetary Reform* was particularly influential and its central theoretical claim, that fluctuations in the general price level were a function of the demand for, rather than the supply of, money, was quickly absorbed by Copland. Copland also adopted Keynes's revised quantity

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<sup>4</sup> A vast amount has been written on the Premiers' Plan. For more details see Schedvin (1970), *passim*. For its ultimately deflationary effects, see Groenewegen and McFarlane (1990), pp.126-129.

formula in all his subsequent writings. The formula stressed that the velocity of circulation of money could respond to changes in money demand. This implicitly recognised the ability of a modern banking system to create credit and thus influence prices and output without the stock of (base) money actually changing.<sup>5</sup>

An important feature of this pre-*General Theory* reasoning was that price changes were the motive force behind changes in output. This meant that although the story was more complicated, the quantity equation remained central to the determination of output (via prices) and hence to monetary policy. With the money supply dethroned as the determinant of prices, however, monetary policy was now directed towards stabilising the demand for credit. How this should be done, according to Keynes, was to vary the rate of interest to offset changes in the velocity of circulation. When it should be done would depend upon movements in the price of some 'standard composite commodity'. Why it should be done was because stable prices were consistent with the needs of contemporary capitalism - 'unemployment, the precarious life of the worker, the disappointment of expectation, the sudden loss of savings, the excessive windfalls to individuals, the speculator, the profiteer - all proceed, in large measure, from the instability of the standard of value' (Keynes 1923, p.5). It should be noted that at this stage, and up to and including his later *Treatise on Money*, what was missing from Keynes's money story was a story of effective demand.

Copland took up monetary reform ideas with extraordinary speed. In August 1924, nine months after the appearance of Keynes's *Tract* (in England), Copland was declaring to the Australasian Association for the Advancement of Science that 'we may overlook the teachings of the classical economists regarding money' (Copland 1932a, p.33). Advances in both the practice of central banking and in monetary theory - especially 'the more adequate expression of the quantity theory of money, with particular reference to the factor "rapidity or velocity of circulation"' - all seemed to prove to Copland the essential truth of the monetary reform position (Copland 1932a, p.33). Taking his pick of Fisher, Hawtrey and Keynes, Copland ventured 'the main objectives of monetary reform', and the 'fundamental conditions of future policy', to be:

- (i) Stability of prices;
  - (ii) Control of credit rather than control of currency;
  - (iii) Regulation of the credit cycle, with a view to eliminating short period fluctuations;
  - (iv) The use of the central bank as a means of controlling credit and prices; and
  - (v) A new place for gold as an international currency, and not the basis of domestic credit and currency nor the ultimate determinant of prices.
- (Copland 1932a, p.73)

But having dictated the terms of what a modern monetary policy should look like, Copland determined that it was not yet within Australia's reach. Australia was a 'small dependent economy' whose national income was determined by export prices 'not dependent upon any conditions under political control in Australia', but moving in accordance with 'financial policy abroad, the purchasing power of our customers,

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<sup>5</sup> The development of Copland's conception of monetary theory can be seen in Copland (1932a).

and the international situation' (Copland 1932a, p.62). Copland also did not believe that Australia as yet had a monetary system up to the task of maintaining domestic price stability. Until the Commonwealth Bank Act (1924), Australia did not have a central bank even in name. The 1924 Act provided the Commonwealth Bank with the power to rediscount bills of exchange and to publish a rediscount rate, but there was no obligation for the trading banks to keep reserves with it, nor were there any powers granted to the Bank for acquiring external reserves. After the 1924 Act, central banking in Australia evolved exceptionally slowly and, up until the onset of the Depression, the only real central banking function undertaken by the Commonwealth Bank was to control the note issue.<sup>6</sup>

This slow evolution in central banking in Australia was accompanied by an even slower evolution in the thinking of those in charge of it. The Commonwealth Bank's Board and its all powerful Chairman, Sir Robert Gibson, had little experience of banking and could be relied upon to fall back upon conservative doctrines of 'sound finance' at every available opportunity. As the Bank's first official historian identified, the Board did not really understand that the creation of credit could extend beyond the note issue, resulting in 'an exaggerated importance attached to currency' (Giblin 1951, p.11).<sup>7</sup>

For all of these reasons, Australia was not in a position to run a truly independent monetary policy. The solution to price stability in Australia was, rather, up to the monetary authorities in those countries whose activities had most bearing upon Australian export prices. For Australia this meant, as it had always meant, the United Kingdom. 'Deflation in England...means deflation in Australia' and, as such, 'it would be in the best interests of this country to set up machinery for maintaining stability of exchange on London' (Copland 1924, p.58). What was required, therefore, was 'enlightened' policy *in the United Kingdom* so as to achieve stability in the British price level. In this way, and in contrast to what monetary reform meant for countries which had the *means* to maintain a stable domestic price level, Australia's interests were best served by its traditional fixed link with sterling.

In advocating such a framework for Australia, Copland was consistent with other monetary reformers. This was especially the case with regard to Keynes - who envisaged such a general system in which one or two countries would direct monetary policy to achieve price stability, and against which other countries could attach their own currencies via a gold exchange standard. Such a global scheme offered countries, according to Copland (in reasoning faithful to Keynes's *Tract*);

a means of escape from the gold standard...it may be used to promote stability of exchange in all countries that find it convenient to establish a definite link with the currency of a more powerful creditor nation...Other countries may then tie their currencies to those of the creditor nation by setting up the machinery of the gold exchange standard. We may therefore expect to see a new grouping of central banks according to the position of the countries. In

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<sup>6</sup> For more on the early history of central banking in Australia, see Giblin (1951).

<sup>7</sup> The Bank's second official historian, C.B Schedvin, wrote that the Board's obsession with the note issue was to a degree to which 'even the crude quantity theorists would have shuddered' (Schedvin, 1970, p.85).



practice the heavier international responsibilities will fall upon the Federal Reserve Banks and the Bank of England...(Copland 1924, pp.43-44)<sup>8</sup>.

Copland's faith in the ability of the Bank of England to maintain a stable price level in the United Kingdom and, by extension, to grant Australia price stability, was shattered by what Giblin (1951, p.64) described as a fall in Australia's export prices in 1929 of 'another order, both of magnitude and persistence' to anything which had gone before. Export prices had been weak in 1928, but were not too far outside the decade's average. The collapse of prices which began in 1929, however, was altogether different. By the end of 1930 the prices of Australia's primary exports had fallen to less than half of those prevailing in 1928, and by 1931 were only 40 per cent of the 1928 levels. Reflecting this collapse, Australia's balance of payments sharply deteriorated from a relatively modest deficit of £2 million in 1928-29 to £30 million (or 10 per cent of GDP) in 1929-30. This, coupled with a complete cessation of capital imports, meant an almost complete exhaustion of the nation's external reserves (Giblin 1951, pp.63-66).

It was the loss of these reserves, primarily in the form of the London funds of the private trading banks, that brought the issue of Australia's monetary arrangements to a head. Under the rules of the gold standard, restoration of external balance would come via domestic deflation - an automatic reduction in bank credit which would lead ultimately, assuming price and wage flexibility, to a reduction in domestic costs and a restoration of trade balance. Of course, to the extent that there was price and/or wage rigidity, such deflation would also be represented by an increase in unemployment. Australia's gold exchange standard was somewhat more flexible than a strict gold standard, but it was just this form of deflation that occurred during 1929 and early 1930. In response to the reduction in London funds, the trading banks liquidated assets and reduced lending, thereby increasing nominal interest rates substantially and (since prices were still falling), increasing real interest rates by an even larger amount (Butlin and Boyce 1988, p.199).

The price deflation that Copland had argued was the proper concern of monetary policy had now dramatically arrived, and it was the reason he finally broke with his belief that Australia's best interests were served by parity with sterling. Australia now manifestly required an exchange rate devaluation, and preferably be off gold altogether. But even this would not likely be enough to stave off deflation for debtor countries like Australia. Exchange depreciation could, on the one hand, improve matters to the extent that export income rose, but this would be partially countered by the increase in the Australian pound value of the (largely) sterling denominated debt. On the trade side of the story much would depend upon the respective price elasticities of Australia's exports and imports. But for Copland the situation did not look good. Australian exports were being sold into already glutted markets while imports were, as a consequence of the Scullin Government's emergency tariff increases of 1930, about as low as they could go.

Copland's solution to this problem was given expression in the Premiers' Plan. This recognised that Australia had suffered a shock to real national income which could only be offset by measures which would not further prejudice the balance of payments

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<sup>8</sup> See also Keynes (1923), pp.204-205.

- proposals which thus contained a mixture of inflation (a depreciation of the exchange rate and reduction in interest rates) and deflation (the reduction in wages, salaries and government spending).<sup>9</sup> But there was another way of looking at the issue that returned Copland to earlier and more optimistic themes. That is, rather than Australia engaging in a process of deflation to move costs in line with lower prices, would it not be better for the world's central banks to engage in a process of lifting world prices to remunerative levels? The fall in Australia's national income had come from unenlightened monetary policies in the *rest of the world*, and it was 'the task of central banks throughout the world' to negate a process they had themselves set in motion. This was the only long-term solution available to what Copland believed in 1930 to be 'perhaps the most important international issue at the moment. A fall in the world's price level can cause more social disturbance and greater injustice than any major political event' (Copland 1932a, p.126).

### *E.O.G Shann*

Influential historian as well as economist, Shann's historical writings have been described as depicting 'the struggle of enterprising groups against the forces, largely public, of restriction' (Snooks 1988, p.575). This theme was apparent up to, and including, his early economic writings on the Depression. Thus Shann's initial reaction to the falling world prices for Australia's exports was to press for a large and rapid reduction in costs. Fitting in generally with his view of a profligate Australia living beyond its means, this meant 'a radical revision of individual incomes all round... so radical as to enable the local manufacturer to compete at lowered prices for the impoverished exporters' custom' (Shann 1930, p.2). Shann expected that Australia would continue to meet all its debt obligations, and in the long run maintain the gold standard.

Remarkably, it was in the context of the exchange rate though that the influence of Shann on Australian monetary policy was to be most apparent. In 1930 the exchange rate was for all practical purposes not a policy instrument available to the government or the Commonwealth Bank. Historically set at a rate marginally short of sterling (and in the absence of any foreign exchange holdings of the Commonwealth Bank), Australia's exchange rate relied for its maintenance upon the co-operation of the Australian trading banks and their London funds.

In January 1930, Shann was appointed by the largest of these, the Bank of New South Wales, as its 'consultant economist' - the first such position at an Australian bank. Shann had been in contact with the Bank's general manager, A.C. Davidson, for some time and it was Shann who encouraged Davidson's interest in economics (Holder 1970, p.642). It was also through Shann that Davidson established contact with other academic economists, most especially Copland, Melville and R.C. Mills, collectively forming the nucleus of a coherent centre of economic advice at a time when there were exceedingly few economists in the service of government.<sup>10</sup> Shann's most

<sup>9</sup> The early submissions of Copland, Giblin and others of the so-called 'Melbourne School' to the Premiers were much more disposed towards an expansionary monetary policy by the sale of treasury bills to the Commonwealth Bank. For the twists and turns of this advocacy, see Schedvin (1970), pp.218-225.

<sup>10</sup> These arrangements were soon formalised by the creation of an economics department headed by Shann, again the first of its kind for Australia.

important influence on Davidson came in his advice that the Bank take a lead in moving the Australian currency off parity with sterling, and in February 1930 he wrote to Davidson that 'I cannot help feeling that the banks could lend great weight to their counsel in favour of free enterprise if they would, at some immediate sacrifice of tradition and profit, facilitate the establishment of a free market for the exchange'.<sup>11</sup> The market leader in Australia's rural sector, Davidson was keenly aware of the suffering caused by the collapse in commodity prices, and was coming around to this view in any case.<sup>12</sup> Needing to convince the other banks that such a move was not just about protecting his commercial interests, Davidson circulated memoranda written by Shann to the other private banks, the Commonwealth Bank, and to the Scullin government.

The process by which the actions of the Bank of New South Wales eased the Australian pound from sterling parity has been described in much detail elsewhere and need not concern us unduly here.<sup>13</sup> Suffice to say, that Davidson's actions to move the currency (which began in September 1930) were made in close consultation with Shann, Copland and Melville in a series of meetings over the course of the year.<sup>14</sup> Despite the wavering resistance of the Commonwealth Bank, which had declared in 1929 its view that 'the last resource which should be adopted would be any course which meant even temporary departure from the operation of the gold standard', devaluation to £A130/£stg100 was achieved in January 1931 (Giblin 1951, p.78). The actions of the private banks and the then desires of the Scullin government having forced its hand, the Commonwealth Bank in December 1931 finally assumed responsibility for the exchange rate, though it also took the opportunity to revalue it at a fixed £A125/£stg100.<sup>15</sup>

Over the course of 1931 and 1932, Shann ventured further along the lines of the monetary reformers. Influenced by the proceedings of the Macmillan Committee in the United Kingdom, at which Keynes was able to articulate much of the reasoning of his recently completed *Treatise on Money*, Shann came around to favour a much more activist monetary policy. In an article entitled 'Monetary Policy', which he wrote for *The Australian Quarterly* in March 1932, Shann quoted at length a passage of the First Addendum to the Committee's report, of which Keynes was the principal author and signatory. This pointed out what he regarded as the 'fallacy'

that 'surplus' financial resources can be gradually built up, unembodied in any physical form. It is supposed that if we 'save' a part of our current income and do not 'use up' these savings in capital schemes, we can in some way hoard them up for use at a later date and that these 'accumulated' savings will gradually strengthen our 'financial' position. These ideas are probably derived from a false analogy between the position of a particular individual or firm

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<sup>11</sup> Shann, cited in Holder (1970), p.671.

<sup>12</sup> Schedvin (1970, p.159) maintained that Shann was the 'catalyst' rather than the 'father' of Davidson's views and subsequent actions with regard to the exchange rate. It was, therefore, 'more accurate to say that the ideas of the two grew together'.

<sup>13</sup> For more on this though, see Giblin (1951), Holder (1970), and Schedvin (1970).

<sup>14</sup> The most important of which took place in Davidson's home at Leura in December 1930, during which time the issue of the exchange rate was 'boiling over' (Holder 1970, p.647).

<sup>15</sup> For the reaction of Australian economists to this development, see the 'Economists' statement on devaluation' in Shann and Copland (1933), pp.85-87. The signatories included Copland and Shann.

and that of the community as a whole... But a little reflection will show that the community as a whole cannot increase its 'liquid' resources by the various members of it building up claims against one another'.<sup>16</sup>

As the passage cited indicates, Shann recognised the core message of the *Treatise*; that it was the equality of saving and investment which was the equilibrium condition of the economic system. The trouble, according to the *Treatise*, was that Britain's return to the gold standard ensured that such an equality was unlikely to occur. The 'natural' interest rate which would equate saving and investment could not be arrived at so long as the rate of interest was also the vehicle through which stability of the exchange rate was to be maintained.<sup>17</sup> In the United Kingdom this meant a rate of interest which was too high (since sterling was overvalued) for the level of investment demand corresponding to a given level of entrepreneurial expectations. At such a rate, the resultant 'hoarding' did not deliver an equivalent level of investment, but merely fluctuations first in price, then output and employment.

The policy prescription that emerged from the *Treatise* was much the same as the *Tract*, even if Keynes's identification of the saving/investment dichotomy had, theoretically speaking, been an advance. An enlightened monetary system was still the vehicle by which an interest rate equating saving and investment had to be found. This rate would not be arrived at automatically. Accordingly, and with the 'loosening of the links between Australian and British currencies and between both and gold' (Britain had abandoned the gold standard in September 1931), monetary policy should be used to ensure 'stability in purchasing power' (Shann 1932a, p.98). Shann even wrote that he agreed with J.T. Lang, the Premier of New South Wales who advocated debt repudiation, even if he did not believe Lang's style was appropriate. What was required in Australia was the 'management of our money so that contracts in terms of it may be carried through as they stand'. To 'attempt all-round deflation would be too difficult and almost as destructive as Mr Lang's lop-sided exaggeration of it in the class-war style' (Shann 1932a, p.100).

In his evidence before the Macmillan Committee, Keynes also put forward a number of policy options that were either necessary for, or complementary to, the general policy of 'cheap money'. These included devaluation, a 'national treaty' (an all-round reduction in incomes), protection, public works, and action by central banks around the world to act together to raise prices. The first two of these Australia had already attempted (via the Premiers' Plan). In the cases of protection and public works, Shann was of the view that Australia had over-indulged in both these areas in the 1920s (Shann 1931, p.2). He was impressed, however, with the idea of concerted central bank action to raise prices. Indeed, Shann saw such a move as integral to the whole new conception of monetary policy as envisaged by Keynes, retaining his earlier concerns as to how far countries like Australia could venture on their own. In this Shann noted the important role of the Bank of England:

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<sup>16</sup> Macmillan Committee, Report on Finance and Industry, Addendum 1, cited in Shann (1932a), pp.100-101.

<sup>17</sup> In *The General Theory*, of course, Keynes abandoned the Wicksellian concept of a 'natural' rate of interest equating saving and investment.

The first step towards the conscious management of all rates of interest so that they should maintain a moving equilibrium between capital supplies and demands came with the recognition of the Bank of England *as the other banks' bank* in what was easily the most important of the world's money markets. (Shann 1931, p.3, emphasis added)

Shann was pleased to point out to his readers that the authors of the Macmillan Report seemed to share this view, noting approvingly the Report's conclusion that;

the first measure towards the restoration of the international price level must necessarily be taken on the initiative of creditor countries and that it must consist partly in a greater willingness to buy and partly in a greater willingness to lend...<sup>18</sup>

### *L.G. Melville*

Of all the Australian economists active in policy debate in the early 1930s, Melville was the most publicly deflationist. Comfortable with the message delivered by Niemeyer and Gregory on their visit to Australia in 1930, Melville wrote later that same year that deflation 'will not make us poorer as a nation' (Melville 1930, p.48).<sup>19</sup> Most importantly, deflation was the policy by which the costs of falling world prices could be redistributed across the community, and not just borne by exporters, the sector essential to Australia's avoidance of the 'calamity' of default (Melville 1930, p.52).

By contrast, 'monetary inflation' was anathema to Melville. While this applied especially to numerous populist monetary schemes, his criticism extended equally to the schemes of 'managed inflation' put forward by his colleagues such as those of Copland, Giblin and others of the 'Melbourne' school in their early Premiers' Plan submissions (Cain 1980, pp.22-23). Arguing that local action was not likely to be effective in any case, Melville targeted the plans of his fellow economists:

It has been suggested that there is a middle road between inflation and deflation. Provided budgets are balanced and real wages reduced, then, we are told, we can stabilise our price level and ignore that of the world, allowing the rates of exchange to be determined as in a free market. It is suggested that price levels can be stabilised by the Commonwealth Bank acting as a central bank and buying and selling Government securities. To pretend that price levels can be stabilised, however, is affectation. (Melville 1930, p.50)

Melville's appointment to the Commonwealth Bank in January 1931 curtailed his public commentary on economic policy, but his collaboration with the other economists via Davidson and the Bank of New South Wales over the exchange rate

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<sup>18</sup> Macmillan Report cited in Shann (1931), p.4.

<sup>19</sup> Niemeyer and Gregory had been invited to Australia by the Bruce Government to assess Australia's prospects in the early stages of the Depression. Their message was simple - Australia had to adopt an austerity package which included the elimination of the budget deficits of the state and Federal governments. At the time, Sir Otto Niemeyer was Chief adviser to the Bank of England, and T.E. Gregory was the Cassel Professor of Economics at the London School of Economics. For more on the visit, see Groenewegen and McFarlane (1990), p.126.

revealed the beginnings of what would be a slow but extraordinary journey from orthodoxy to a new position. Even before this movement, though, Melville was not opposed to expansionary monetary policies applied elsewhere, especially in the United Kingdom. Commenting upon this later, Melville explained that there was no inconsistency:

We were bothered by a balance of payments problem in Australia. When we turned to expansion on a world scale, of course, this was a very different problem from our point of view. We saw our salvation in Australia coming from expansionary policies applied in the rest of the world and if we could have persuaded England and the rest of the Commonwealth and later the United States and Europe to develop an expansionary policy, of course this would be very much in our interests.<sup>20</sup>

### *L.F. Giblin*

A fourth important member of the group of economists who would determine Australia's approach to both Ottawa and the WMEC, though he did not attend either in person, was L.F. Giblin. The 'doyen of Australian economists in the 1930s', Giblin's extraordinary career had culminated in 1926 with his appointment to the Ritchie Chair of Economics at the University of Melbourne (Cain 1983, p.193).<sup>21</sup> Giblin had initially advocated 'relative cost adjustment' and 'expenditure switching' as the most appropriate response to the collapse in Australia's export income in the Depression (Cain 1983, pp.193-200, Hytten 1960, pp.153-163). This advice was informed by what was then a relatively orthodox approach to economics, including a belief that Australia should remain on the gold standard. It was also informed by Giblin's pioneering work on a 'multiplier' concept. Conceptually less sophisticated than Kahn's (there were, for example, no internal leakages and as such, *ex ante* savings always equalled investment), it nevertheless preceded Kahn's innovation by a year.<sup>22</sup> Giblin's multiplier was stimulated by his attempts to account for the consequences to Australia of the falls in export income and the cessation of capital inflow with the coming of the Depression (Karmel 1960, pp.164-174). This stimulus was characteristic, a concern for Australia's balance of payments position being never far from Giblin's thoughts. Giblin wrote very little on monetary policy, but by 1931 he was in favour of a much greater degree of credit expansion than that envisaged under the Premiers' Plan. He had also joined Shann, Copland and others in advocating a devaluation of the exchange rate (Hytten 1960, pp.154-155). In September 1931, not long after the Premiers' Plan, he declared before another premiers' conference that

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<sup>20</sup> L.G. Melville, interview with Alan Hodgett, National Library of Australia (NLA), Oral History Transcript, TRC-182.

<sup>21</sup> For more details of Giblin's extraordinary life, see Copland (1960).

<sup>22</sup> According to Cain (1983, p.195), Giblin's first allusion to a multiplier concept was contained in a submission he made to Australia's Development and Migration Commission in August 1929. Richard Kahn published his first account of the multiplier in the *Economic Journal* in June 1931, though he was certainly working on the concept through 1930. The very different purposes to which Giblin and Kahn used the concept means the issue of primacy is probably meaningless in any case, and remains hotly debated (Skidelsky 1992, pp.449-452).

the banking resources of the country must be used to the limit - (a) to *maintain* the wheat grower in production. (b) To *maintain* the existing volume of employment on public works. (c) To provide or stimulate enough *additional* employment to set moving the gradual revival in business and enterprise for which the conditions appear to be nearly ripe (emphasis in original).<sup>23</sup>

With a certain convergence of their thoughts on monetary matters apparent by 1932, the ideas of all four of the above economists were to be brought together in devising plans for an imperial monetary policy for the Ottawa Conference. Before this, however, each was asked once more to serve on a committee to advise the government on economic policy more generally. This work, as the account below testifies, was to shape significantly the approach taken at Ottawa.

## **2.1 The Wallace Bruce Report and Keynes**

In March 1932 the newly commissioned Lyons Government appointed an expert committee to make ‘a preliminary survey of the economic problem’ and review the findings of the Premiers’ Plan in the light of subsequent events.<sup>24</sup> The committee comprised Adelaide businessman, Sir Wallace Bruce, together with the four economists above. As matters turned out, Copland did not serve on the committee since he was engaged in preparing a similar report in his home country of New Zealand. He was replaced by R.C. Mills but, since Copland’s Economic Report for New Zealand was philosophically little different from that which ultimately emerged as the Wallace Bruce Report, it could be reasonably supposed that his absence did not change the Committee’s findings in any material way. The Report was publicly released in June 1932 (Cain 1985, pp.2-3).

The Wallace Bruce Committee found that Australia’s economic position had continued to deteriorate since the Premiers’ Plan less than a year earlier. National income, which had fallen almost 30 per cent from 1926-27 to 1930-31, was predicted to fall another 6 per cent by 1931-32. Unemployment, at 24 per cent of trade union members in 1930-31, was expected to rise to 28 per cent, while export prices (down 43 per cent from 1926-27 at the time of the Premiers’ Plan) were expected to fall a further 26 per cent by 1931-32. In 1927-28 public borrowing overseas amounted to 9 per cent of national income, for 1931-32 it was expected to be zero.<sup>25</sup> The Report declared that its objective was ‘to find a way to restore employment’, an objective that, given Australia’s external constraints, could only ‘be found in bringing into harmony the costs and prices of export industry’.<sup>26</sup> Over the past year or so, the Report noted, Australia had ‘only just hung on’ despite ‘two remarkable export seasons’, but export production had become ‘so unprofitable that the volume of

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<sup>23</sup> Giblin’s advice, which was contained in *Employment and Production: Report to the Premiers’ Conference by the Secretariat Committee, 3 September 1931*, is here cited from Cain (1983), p.206.

<sup>24</sup> ‘Report of the Committee Appointed to make a Preliminary Survey of the Economic Problem’ (the official name of the Wallace Bruce Report), 12 April 1932, cited from Cain (1985), p.2

<sup>25</sup> Statistics as presented in the Report of the Wallace Bruce Committee and cited in Shann and Copland (1932), pp.43-46. Because of falling prices, *real* national income had fallen by about 18 per cent from 1926-27 to 1931-32 (Shann and Copland 1932, p.44).

<sup>26</sup> Cited in Shann and Copland (1932), pp.38-39.

exports could not be maintained even with similar seasons'.<sup>27</sup> The Premiers' Plan and the devaluation had done much already to restore this balance, but much more could be done. The Report noted that the Premiers' Plan had only been partially carried out, and that the cut in real wages had not been carried out in New South Wales.

To a much greater extent than the Premiers' Plan, the Wallace Bruce Report advocated a 'middle way' solution of both cutting costs *and* raising prices to restore profitability to the export sector. Cutting costs on its own would require reductions in nominal wages and returns to bond holders of the order of 50 per cent, and 'the attempt to do this would threaten social and financial stability'. Attempting to restore export prices by simply devaluing the exchange rate 'would end in loss of control of the currency and general collapse'.<sup>28</sup> The Committee, therefore, found that some middle course between deflation and reflation was the best course for Australia, and to this end came up with the recommendations:

1. That equilibrium between costs and prices be sought as a basis for the restoration of employment.
2. That Parliament authorise the Commonwealth Bank to manage the exchange rate to this end...
3. That the State Parliaments take the necessary action to empower Arbitration Courts and Wages Boards to fix wages in accordance with economic conditions.
4. That all wage-fixing authorities complete the reduction of real wages by 10 per cent below the level of 1928 where this has not already been done.
5. That the State Governments take action to complete the reductions in rates of interest contemplated in the Premiers' Plan...<sup>29</sup>

The report advised that all of these should be accompanied by moves towards the balancing of government budgets (though it acknowledged these were as much a function of recovery as a factor promoting it), and reductions in tariffs in line with movements in exchange rates (for allocative efficiency). The scope for public works would widen with the reduction in costs, but could not be considered as anything other than a short-term palliative.<sup>30</sup> Finally, and rather fatalistically, the Report concluded that 'the re-absorption of all the unemployed is unattainable until prosperity is regained over a large part of the world'.<sup>31</sup>

### *Keynes*

In April 1932 draft copies of the Report were separately sent to Keynes by Giblin (an old acquaintance of Keynes's from the time when both had been students at King's College) and C.L. Baillieu, a Melbourne business figure who represented Australia on the Imperial Economic Advisory Council. Keynes's comments on the Report were subsequently published in *The Melbourne Herald* on 27 June.<sup>32</sup>

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<sup>27</sup> *ibid*, p.39.

<sup>28</sup> Wallace Bruce Report cited in Cain (1985), p.9.

<sup>29</sup> Cited in Shann and Copland (1932), p.42.

<sup>30</sup> *ibid*, pp.42-43.

<sup>31</sup> *ibid*. pp.40-41.

<sup>32</sup> This letter has been republished in full in *The Collected Writings of John Maynard Keynes*. See Keynes (1982), pp.94-100.



Keynes's comments began with the qualification that it was 'a rash thing to write from a great distance on a matter which demands practical judgement more than theory'. To this he then nevertheless appended that someone far away had the advantage of knowing 'the forest and the jungle outside, which those dwelling amongst their own trees can scarcely hope to see'(Keynes 1982, p.94). He sympathised with the sentiment of the Report, but disagreed with it on two points. The first, concerning the reduction in costs, was a point of theory. The second, in relation to the exchange rate, was one of degree.

On the question of cost reduction, Keynes wrote that it would be a mistake for any country to attempt to adjust to the current level of world prices:

The long continuance of this level of prices is not a practical working hypothesis. It is one of those things like the end of the world, against which, though it is possible, it is not sensible to insure. For unless prices rise, the existing financial structure between nations cannot possibly survive (Keynes 1982, p.95).

To the extent that there had been inequality in wage cuts under the Premiers' Plan across the different states, then wage cuts in the recalcitrant states should proceed. But Keynes was against further reductions in the general level of money wages. Such cuts would reduce purchasing power as much as they would cut costs. In this they would also as likely as not exacerbate problems with the government budget. Acknowledging that he had proposed a 'National Treaty' in the United Kingdom, which was in many ways similar to the philosophy at the heart of both the Premiers' Plan and the Wallace Bruce Report, Keynes declared that he 'proposed this as an alternative to exchange depreciation...I do not believe that a further cut in money wages could do anything which a further exchange depreciation could not do better' (Keynes 1982, p.97). Keynes regarded the Australian economists' reluctance to advocate cost cutting alone as being based on its impracticability, whereas *his* objection was that it was dubious theory in any case because 'unless fresh purchasing power is released, it may be that prices are related to costs after the same fashion as her tail to a cat'(Keynes 1982, p.99).

Keynes's reservations about the Report's suggested use of the exchange rate, on the other hand, was entirely of degree. He regarded Australia's trade balance as 'adequate to meet pressing requirements'. This was an area in which 'Australia has done so much already and has been relatively so successful'(Keynes 1982, p.96). It was, in any case, not clear that a further devaluation would do anything to improve the trade balance since 'the aggregate sterling value of Australia's exports would only be increased if the effect was to increase their physical *volume*, for which there may not be much scope' (Keynes 1982, pp.97-98). Of course, devaluation increased the Australian currency value of the external debt too. There was also the issue of confidence. At what point, Keynes asked, would a lower exchange rate maintain confidence in the currency or lead to capital flight? According to Keynes, the exchange rate was best left where it was, unless it was accompanied by 'a corresponding rectification of tariffs' (Keynes 1982, p.98). Keynes's main piece of

advice on the exchange rate, however, came from what he regarded as the benefits of a broader picture:

I hope the Australian authorities will not overlook the fact that what would really suit them is a further depreciation, not of the Australian pound, but of sterling. For this would raise export prices without increasing the burden of external debt ...I suggest that the importance of consulting the interests of the Dominions in settling the value of sterling should be a major topic at the Ottawa Conference (Keynes 1982, p.98).

According to Keynes, 'every country in the world' had 'the same problem as Australia in some shape or form'. Competitive wage reductions and exchange rate devaluations, therefore, would achieve nothing (Keynes 1982, p.95). Public works and lower interest rates promised more than further reductions of wages or attempts to push exports into markets which were not likely to exist:

If, therefore, I were an Australian economist advising Mr Lyons today, I should be decidedly moderate in my ideas. I should recommend him to ride his difficult and suffering steed with as light a rein as he dare. I should not press for heroic measures (Keynes 1982, pp.95-96).

### *Assessment of Keynes's Contribution*

'Decidedly moderate' and unheroic policies were precisely what the authors of the Wallace Bruce Report were advocating and, as noted by Cain (1985, p.20), there was more than a little selective argument in Keynes's letter to accompany its patronising air. Although such a view may have been prevalent amongst Australian economists at an earlier time, the Wallace Bruce Report was patently not about reducing wage levels in order to bring costs into line with low overseas prices. Rather, to the extent they were a feature of Wallace Bruce, further wage reductions were envisaged only so far as to bring New South Wales (particularly) into line with the reductions in other States - that is, an adjustment of internal relativities of the kind Keynes allowed in his letter. That Wallace Bruce went beyond this to recommend that Arbitration Courts 'fix wages in accordance with economic conditions' was (continuing on from the Premiers' Plan) an attempt to modify the hitherto prevailing ethos of 'the living wage', but it was hardly about Australia embarking upon an attempt to out-compete everyone else on the basis of low wages (Cain 1985, p.9).

A similar mis-interpretation pervaded Keynes's reading of what the Wallace Bruce Report intended in the way of further exchange rate devaluations. Further devaluation was not, primarily, about reducing the foreign currency prices of Australian exports and thereby expanding sales in overseas markets. This was a prospect the Australian economists were all too well aware would be unlikely in glutted world markets. Devaluation, rather, was mostly about (as, in the Australian scenario, it had always been mostly about) increasing the Australian currency returns to exporters on *existing or even reduced* volumes.<sup>33</sup> Keynes recognised this principle in relation to the external debt, and the difficulties devaluation posed in increasing its Australian

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<sup>33</sup> This was because most of Australia's commodity exports were denominated in foreign currencies, particularly sterling.

currency value, but was curiously obtuse on the issue when it came to trade. In his letter Keynes was also in favour of devaluation to the extent that its protective impact was offset by a reduction in tariffs. Since, once again, this was precisely what the authors of Wallace Bruce had in mind, Keynes's reservations about what the Report advocated in terms of managing the exchange rate are inexplicable at face value.

Perhaps most striking of all, though, is the sense from Keynes's letter that he feared that the Wallace Bruce Report was about Australia attempting to strike out upon its own, an attempt to 'beggar thy neighbour' in a search for internal balance. There were movements in Australia calling for this, of course, and the initial response of the Scullin Government to the Depression in imposing a range of emergency tariff increases could only have added credence to such anxieties. But this was never true in a broader macro-policy sense, never true in the advocacy of Australian economists, and certainly not true of the Wallace Bruce Report. As the above potted stories of Copland, Shann, Melville and Giblin have indicated, Australia was all too ready to wait upon the rest of the world. The authors of the Wallace Bruce Report recognised Australia's recovery depended upon the rest of the world, and much time had been lost in the waiting.

### *What Were Keynes's Issues?*

As indicated above, Keynes's objections to Wallace Bruce, when taken at face value and in the light of his published writings, must have seemed inexplicable to the Report's authors. This was evidence, perhaps, for that already growing reputation that Keynes's was a brilliant though contrary mind.<sup>34</sup> Such a reading was understandable, but a number of factors, some discernible at the time, some only with the benefit of hindsight, make Keynes's reactions quite comprehensible when placed in an appropriate context.

The first of these factors concerned perception. It was apparent from his letter that Keynes was of the view that Australia had largely solved the dire external constraints which had existed only a short while earlier. This was a view Keynes expressed in other public forums in addition to his letter.<sup>35</sup> But it was a perception in stark contrast to that of the authors of the Wallace Bruce Report who, all too well aware of the precarious nature of Australia's trade balance, sought reflation but with an eye always to any adverse balance of payments implications. As Cain (1985, p.20) has argued, the policy proposals in the Report were entirely consistent with the theoretical framework of both the *Tract* and the *Treatise*, but were modified to suit the preoccupations of a small economy dependent upon its ability to sell a relatively narrow range of commodities into world markets.

A second factor that makes Keynes's review more comprehensible, but one that is only discernible with the benefit of hindsight, concerns theoretical development. As

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<sup>34</sup> Clarke (1988, pp.231-232) writes that the gibe 'where five economists are gathered together there will be six conflicting opinions and two of them will be held by Keynes!', was already in circulation in 1931. As Clarke goes on to add (1988, p.232), however, the gibe was misconceived and arose 'from a confusion of theory with policy, ideal solutions with second-best remedies, and rational strategies with Keynes's own preferences'.

<sup>35</sup> The most recent of which was in his Halley-Stewart Lecture of February 1932 (Keynes 1982, p.56).

previously noted, the Australian economists' reasoning was consistent with the monetary ideas of Keynes's in the *Tract* and the *Treatise*. By early 1932, however, Keynes was beginning to move away from what was essentially still a Marshallian story of an economic system which reacted primarily via price changes, to one which reacted primarily via quantities. This development, which was the beginning of his theory of effective demand, had probably been at least intuitively arrived at as early as March 1932.<sup>36</sup> Dating the intellectual progression of the ideas which would ultimately come together in *The General Theory* is a most difficult exercise and one that has spawned an enormous literature, which it is not the purpose to revisit here.<sup>37</sup> Suffice to say perhaps, that by the time the Wallace Bruce Report reached him in April 1932, Keynes was no longer convinced that monetary measures such as the exchange or interest rates were sufficient to lift economies from the unemployment-equilibrium which he now believed was not only theoretically likely, but in evidence all around him.

A third, and in the view of this author, a most important factor in explaining Keynes's reaction to the Wallace Bruce Report concerns possible anxiety that action by Australia could interfere with his own plans for international co-operation. This was a point noted by Cain (1985, p.22), who pointed to Keynes's Halley-Stewart lectures of February 1932 in which he bemoaned that almost all the remedies being advocated for recovery pitted one nation against all others, 'competitive wage reductions, competitive tariffs, competitive liquidation of foreign assets, competitive currency deflations, competitive economy campaigns, competitive contractions of new development - all are of the beggar-my-neighbour description' (Keynes 1982, p.52).<sup>38</sup> In the same lectures Keynes was confident that with Britain's abandonment of the gold standard ('a most blessed event'), scope now existed for 'a great abatement of the deflationary pressure' in the countries linked with sterling (Keynes 1982, p.55). Such a development also required that Britain use its new-found strength 'to cheapen money and increase the volume of credit, to restart home activity and to lend abroad to the utmost of our powers' (Keynes 1982, p.60).

The Halley-Stewart lectures afforded one avenue through which Keynes expressed his ideas for international economic co-operation, but they were, in fact, but the latest manifestation of a set of ideas which could be traced back to his first book, *The Economic Consequences of the Peace*. The *Treatise* too, contained plans for a supernational bank charged with stabilising the price of gold (to which currencies would be attached) against a basket of 60 or so principal commodities of international commerce, thus ensuring international deflation could not happen again.<sup>39</sup> At a less ambitious level, and one more immediately relevant to Australia, Keynes's belief that

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<sup>36</sup> Clarke (1988, p.257) claims Keynes's delivery of the Harris Lectures in Chicago in June 1931 marked the last time he was unconditionally to advance the theoretical lines of the *Treatise*. In terms of 'initial insights', Clarke also dates Keynes's realisation of the principle of effective demand to March 1932, and his Easter university lectures at Cambridge (Clarke 1988, pp.256-264).

<sup>37</sup> But for an overview of some of the different accounts, see Skidelsky (1992), pp.442-444.

<sup>38</sup> The Halley-Stewart lecture was published in 1932 in a volume entitled 'The World's Economic Crisis and the Way of Escape'. In this lecture Keynes's doubted the ability of monetary policy alone to bring recovery. In an interview with this author on 28 January 1993, Sir Leslie Melville said that this lecture had made an impression upon all the economist members of the Australian delegation to Ottawa.

<sup>39</sup> See Keynes (1930, pp.388-408) for the plan in full.

international co-operation was as yet premature led him to propose an 'Imperial Currency Conference' at which would be established 'a sterling standard, managed by the Bank of England and pivoted on London'.<sup>40</sup> This scheme, a somewhat smaller version of the global scheme imagined in the *Treatise* but representing a large portion of the world nonetheless, retained the concept of attaching sterling to a 'somewhat crude index number of the main raw commodities of international trade with its base at the 1929 figure; and then fixing a gold value for sterling...based on this norm at the outset, and modified from time to time' (Keynes 1982, p.26). The commodity index, of course, was enormously friendly to the interests of countries like Australia and the ideals pursued by the authors of the Wallace Bruce Report. That Keynes recognised that these interests were in turn crucial to British interests was also readily apparent:

It is of great importance to the trade and prosperity of the British Empire which includes a large body of producers of food and raw materials, that the prices of their output should return to a level approximating to that of 1929. It is also of great importance to Great Britain through its ownership of assets abroad, the income of which depends on the price level of food and raw materials (Keynes 1982, p.24).

### *The Government and Wallace Bruce*

As events turned out, Keynes need not have worried about Australia's actions, for the Lyons' Government, while expressing its 'enthusiasm' for the recommendations of the Wallace Bruce Report, did its best thereafter to ignore it to the extent that it could. The government, a do-little administration firmly of the view that recovery in Australia could only come after the recovery of world prices, was content merely to strive for those aspects of the original Premiers' Plan - budgetary balance, relatively modest cuts in costs, funding of the debt - which they believed contributed most to confidence and to setting Australia up for the day when commodity prices began to rise. Expansionary monetary policy and devaluation were regarded as palliatives at best, inflationary at worst. To the Conference of Commonwealth and State Ministers meeting in June-July of 1932, Lyons declared that the task of the government was to 'keep Australia steady', and he expressed his confidence that the up-coming conference in Ottawa would deliver the international co-operation necessary to restore world prices;

...despite all we may or may not do, nothing can give us effective relief until the fall in world prices is checked and the prices of our exportable products move materially upwards...Before long we may hope to see such a revival of trade and confidence as will carry Australia far along the road to security and prosperity.<sup>41</sup>

## **2.2 Ottawa**

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<sup>40</sup> Letter from Keynes to Sir Frederick Leith-Ross, then Deputy Controller of Finance at Treasury, 16 November 1931 (Keynes 1982, p.17). This letter was also sent to Montagu Norman, then governor of the Bank of England and Hubert Henderson, joint secretary of the Economic Advisory Council.

<sup>41</sup> Proceedings of the Conference of Commonwealth and State Ministers, June-July 1932, cited in Cain (1985), p.39

## *Preparation*

Sometime in early 1932, Copland, Shann, Melville and Giblin prepared a series of proposals for carrying out the London-centred monetary policy that had long been their concern. The proposals were meant for the Imperial Economic Conference in Ottawa, at which the long campaign for imperial preferences would be partially realised. Commenting on these proposals, Giblin wrote in early June 1932 that the 'stuff on monetary policy at Ottawa' was 'very aggressive' and 'will probably flutter some of the doves a little'. This was provided, of course, that 'the Govt [sic] will send them'.<sup>42</sup>

It is not clear from the surviving records precisely when the economists' proposals became a part of the government's preferred strategy for Ottawa, a strategy which was more about the issues of tariffs, quotas and preferences than about monetary policy. Certainly they could not have been approved in anything but very general terms prior to the selection of the delegation to Ottawa, which took place before Giblin's comments above. Australia's delegation to Ottawa was headed by S.M. Bruce, the former Prime Minister soon to take up residence as Australia's High Commissioner in London. On the monetary side, Bruce had only two official advisers, E.C. Riddle, the Governor of the Commonwealth Bank, and Melville. Shann was an adviser in all but name, but was travelling independently of the delegation itself.<sup>43</sup> Bruce's leadership was critical to the delegation's make-up since Sir Robert Gibson was 'suspicious and distrustful' of Melville following his agitation for devaluation, and initially refused Melville's release from the Commonwealth Bank. Eventually, under pressure from Bruce, he relented.<sup>44</sup>

What, then, were the 'series of proposals' designed by the Australian economists for the monetary side of Ottawa? Thought by historians of the period to be missing from the historical record, and revealed for the first time here, they were a familiar mix of the monetary reform agenda as adapted to the special circumstances and responsibilities of a monetary power and centre.<sup>45</sup> Written up from the discussions of the economists by Copland in May 1932, and somewhat modified by Melville and Shann en route to the Conference, the proposals nominated a 'speedy reversal of the present trend of prices' as the prime hope for prosperity, a hope which would be best realised by all nations carrying out an agreed plan of monetary action.<sup>46</sup> The 'sterling area' was picked out as a group of nations in which there was 'less divergence of immediate interests', but which was still an 'important group of nations' nonetheless.

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<sup>42</sup> Giblin to an unknown correspondent, 2 June 1932. Cited in Cain (1985), p.59.

<sup>43</sup> Shann was reporting on the Conference for the Bank of New South Wales, but was travelling with Melville.

<sup>44</sup> Gibson's suspicions of Melville are reported in a letter written by Giblin on 2 June 1932, and cited in Cain (1985), p.57.

<sup>45</sup> The proposals are contained in a memorandum entitled 'The Monetary Problem. A Memorandum for Consideration at Ottawa', and dated 30 May 1932. The memorandum is preserved in the Archives of the Reserve Bank of Australia (RBA), 'The Imperial Economic Conference - Professor Melville's Papers, 1932', C.3.7.6.71. That these proposals seemed to be lost is bemoaned in Cain (1985), p.59.

<sup>46</sup> Shann and Melville's modified version of the above memorandum, entitled 'An Initial Policy of Several and Joint Action by Britain and the Dominions to Restore Economic Balance', and dated 15 June 1932, is contained in RBA, 'League of Nations, Monetary and Economic Conference, London, Papers and Proceedings, 1933', C.3.7.6.63.

To bring about this rise in prices, the Australian economists proposed that the sterling area conduct monetary policies in such a way as to lower interest rates and stimulate investment. For the United Kingdom, and those other countries with monetary systems which would allow it, this could be achieved through a combination of:

- (i) Low bank rates.
- (ii) [The] Purchase of Government Securities by central banks.
- (iii) Encouragement of Governments and financial institutions of investment...
- (iv) Public and Municipal works...<sup>47</sup>

All of these would, in turn, require the management of both the sterling-gold exchange and the exchange rates of those countries linked with sterling. For the countries linked with sterling this would mean the adoption of a sterling-exchange standard (of the sort long adopted by Australia) in which they would hold their main reserves as sterling. Only sterling itself would be linked to gold. The rate of sterling to gold could not be too high, though, or the experiences of post-1925 would simply be revisited. In addition, and somewhat surprisingly perhaps, the Australians were also anxious that it not be too low. Their concern was the impact upon those countries outside the sterling group and still attached to gold. A sterling-gold rate that was too low would have 'disturbing effects upon industry in gold standard countries', causing a 'further fall in gold prices' and ultimately bringing little relief to sterling countries themselves. What was required, therefore, was a sterling-gold rate somewhat below that prevailing after 1925, but accompanied by the sort of monetary proposals advocated above together with 'a reduction in the barriers to trade'.<sup>48</sup> With the whole system working correctly, the Australians envisaged the following immediate effects:

- (i) Industrial activity, including exports and imports, within the sterling group would increase. As a consequence sterling prices would rise.
- (ii) Imports from outside the sterling group would increase. Exports from the sterling group would also increase, but not to the same extent until some time had elapsed.
- (iii) Sterling would depreciate in terms of gold. Imports from outside the group would decrease and exports increase. Capital movements away from low interest rates would accentuate the movement of exchange.<sup>49</sup>

Within the sterling-group, exchange rates would be determined in line with the particular circumstances of individual nations. Countries 'whose exports have fallen heavily in price should have depreciated currencies in terms of sterling', with the degree of depreciation dependent upon the size of the 'fall in export prices in relation to the reduction in costs that were practicable'.<sup>50</sup> Of particular interest to countries within the group such as Australia, they added that exchange rates could be *managed* for

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<sup>47</sup> 'The Monetary Problem. A Memorandum for Consideration at Ottawa', *op. cit.*

<sup>48</sup> *ibid.*

<sup>49</sup> *ibid.*

<sup>50</sup> *ibid.*

countries dependent on a few exports and with limited possibilities of alternative production to maintain practically the whole of their export production, leaving any contraction...to take place in countries with prospects of alternative production.<sup>51</sup>

Finally, there was a sweetener for the United Kingdom:

The net effect of this policy for debtor countries within the group would be to make them better able to pay their sterling debts.<sup>52</sup>

### *The Conference*

The Imperial Economic Conference met in Ottawa from 21 July to 20 August 1932. It was divided up into five committees, only one of which was concerned with monetary and financial questions. Though head of the delegation, Bruce was content to leave the policy details on the monetary and financial questions to Melville and Riddle.<sup>53</sup>

In the sub-committees, Melville and Riddle (and Shann unofficially) found support for Australia's monetary line from New Zealand and India, but resistance from Canada (attempting to stay at parity with the US dollar) and South Africa (the world's largest gold producer). Whatever the support of individual Dominions, however, the whole point of Australia's Ottawa advocacy was to influence the United Kingdom, whose delegation was led by Neville Chamberlain, then Chancellor of the Exchequer. Empire-wide plans for monetary expansion were not unknown in the United Kingdom in the early 1930s and, especially once gold had been abandoned, even enjoyed some official support. Both the British Treasury and the Bank of England were concerned, however, to keep such matters firmly within their own prerogative. In a memorandum prepared for the Ottawa Conference, Treasury made clear its desire that countries in the sterling area maintain exchange stability, but beyond being willing to ensure that 'the interests of the Empire would at all times be borne in mind in the framing of general policy', was not willing to countenance Dominion *participation* in monetary decisions. 'Within these limits', the memorandum concluded, 'there is room for fruitful discussion at Ottawa'.<sup>54</sup> The Bank of England nursed almost identical concerns, Governor Montagu Norman stating in April 1932 that 'Ottawa is definitely *not* the place and the Ottawa atmosphere *not* the atmosphere for discussions on this matter'.<sup>55</sup>

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<sup>51</sup> *ibid.*

<sup>52</sup> *ibid.*

<sup>53</sup> In an interview with the author on 28 January 1993, Sir Leslie Melville said that although Bruce 'was interested in what we were trying to do on the monetary side...he left all that up to me'. As shall be examined in Section II of the thesis, Bruce was responsible (as Resident Minister and then High Commissioner in London) for Australian attempts to convert the interest payable on its debt written in London to lower levels and, according to Melville, was attracted therefore to any attempt to ease credit in the United Kingdom.

<sup>54</sup> This Treasury memoranda, which was dated merely 'Spring 1932', is cited in Drummond (1981), p.16.

<sup>55</sup> Emphasis in original. Norman cited in Sayers (1976), p.448. Of course, this is contra to Keynes's assurances noted above.



Thus advised, the tactics of the British delegation on the monetary side of Ottawa was a mixture of obfuscation and attempts to assure Dominion representatives that what they most wanted in the monetary sphere was precisely what the United Kingdom was already doing. Pointing to ongoing open market operations by the Bank of England that had led to a 'reduction of bank rate to a figure equal to the lowest ever recorded and an extraordinary abundance of short term money', Chamberlain declared in his opening statement at Ottawa that he could 'fairly claim that there is now no monetary obstacle to a rise in wholesale prices'.<sup>56</sup> The government of the United Kingdom would continue to direct banking policy 'towards providing an adequate supply of credit at moderate rates, but there should be no "rash experiments" in monetary policy'.<sup>57</sup>

The Australian delegation was aware of the recent monetary moves in the United Kingdom and, indeed, used what they regarded as the beginning of a reversal of the trend in British prices as further proof of their cause. They were concerned, however, to get a much stronger commitment from the United Kingdom on the continuation of such a policy. This task was strongly taken up by Bruce, who told Chamberlain that the United Kingdom had 'made a most admirable start but the question is whether they will be prepared to stick to it in the face of what will amount to a situation that will require very great courage'.<sup>58</sup> The test, according to Bruce, would come 'if, as a result of the prevailing low rates for money in Britain, you begin to get a tremendous outward flow of the floating international money'.<sup>59</sup> In the past the obvious corrective to such an outflow had been an increase in British interest rates - a policy which 'would defeat the whole policy of cheap money'.<sup>60</sup>

In attempting to extract from Chamberlain what he referred to as a 'definite announcement...ruthlessly pursued', Bruce himself was prepared to 'ruthlessly pursue' the monetary line. This included using Australia's most powerful card - default. Writing to Senator Massey Greene after the completion of the Conference, Bruce recalled that he had

put the position very strongly that any possible step to bring about the increase in wholesale commodity prices had to be taken if default by a number of debtor countries was to be avoided. I pointed out that if Australia ran into a period of bad seasons she would be forced into such a position notwithstanding the amazing efforts we have made in the past to meet our obligations...<sup>61</sup>

Largely as a result of the prompting of Bruce, Chamberlain did make a declaration which went at least part way towards what Australia was demanding. The statement included the avowal that:

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<sup>56</sup> Chamberlain cited in Australia, Parliament (1932), p.111.

<sup>57</sup> *ibid.*

<sup>58</sup> S.M. Bruce to Senator W. Massey Greene, 14 September 1932, National Archives of Australia, (NAA) M104/1, S.M. Bruce, Folders of Annual Correspondence.

<sup>59</sup> *ibid.*

<sup>60</sup> *ibid.*

<sup>61</sup> *ibid.*

His Majesty's Government desire to see wholesale sterling prices rise ...[and]...recognizes that an ample supply of short-term money at low rates may have a valuable influence, and they are confident that the efforts which have successively brought about the present favourable monetary conditions can and will, unless unforeseen difficulties arise, be continued.<sup>62</sup>

### *Quantitative restrictions*

While the Australian delegation's efforts to secure a strong statement on monetary policy was part of the mandate they had set themselves for the Conference, it was also a product of what they saw as a most alarming development at Ottawa. This linked the issue of raising commodity prices with restriction of production. The link had been established by Chamberlain, and was itself a product of the perceived need to resist 'rash monetary experiments'. Chamberlain told the Conference that 'it cannot be contended that the world can be put right or even that prices can be restored merely by an alteration in the monetary factor'. While 'theoretical economics' held that production would fall as a result of lower prices, Chamberlain used the example of primary producers in Australia and New Zealand to demonstrate that in practice the opposite was the case, 'having to meet the pressing demands of their creditors they are apt instead of reducing production, to increase it, hoping thereby to make up in volume what they have lost in value'.<sup>63</sup>

The increase in production volumes was, in this analysis, one of the main determinants of the reduction in commodity prices. The solution? - '[I]f we are to restore stability of price and confidence in the future of the market for the great primary commodities, we must look for some means of regulating supplies in such a way that they shall not be from time to time completely out of relation to the absorbing capacity of their markets'.<sup>64</sup> For countries such as Australia this was not a mere theoretical debate, because Chamberlain proposed that for commodities in which there was little but the sterling market (a great number of Australia's exports), countries should consider 'the regulation of supply rather than of importation into Great Britain'.<sup>65</sup>

Given their claim that it had only been the great increase in the volume of Australian exports in the preceding two years that had saved Australia from default, Chamberlain's quota proposal was greeted with intense hostility from the Australian delegates. Sixty years after the event, Sir Leslie Melville still recalls 'the horror with which we listened to Chamberlain'.<sup>66</sup> Bruce was similarly incensed, referring to this section of Chamberlain's speech as 'disastrous' and writing later that he 'used every endeavour I could to prevent its publication and even went so far as to suggest that that portion of the statement should be omitted from the official record'.<sup>67</sup>

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<sup>62</sup> Chamberlain cited in Australia, Parliament (1932), p.18.

<sup>63</sup> *ibid.*, p.110.

<sup>64</sup> *ibid.*

<sup>65</sup> *ibid.*, p.111.

<sup>66</sup> Interview with the author, 28 January 1993.

<sup>67</sup> S.M. Bruce to Senator W. Massey Greene, 14 September 1932, *op. cit.*

## *The Ottawa Resolutions*

Chamberlain's quota proposal, as well as the statement on his government's 'commitment' to the maintenance of its monetary stance, duly made their way into the final published resolutions of the Ottawa Conference. These resolutions declared the desirability of a rise in the general level of prices, recorded the conviction of the delegations that international action to bring this about was 'urgently necessary' and, while acknowledging the British government's reservations as to the limits of monetary action, placed monetary policy centre stage.<sup>68</sup> The restoration of an international monetary standard, though the 'ultimate aim of monetary policy', would have to await a rise in prices. Once established, the new monetary standard should be constructed so as to avoid 'wide fluctuations in the purchasing power of the standard of value'.<sup>69</sup> In the meantime the sterling area provided a valuable haven - 'first by creating an area of stability among countries regulating their currencies in relation to sterling; and secondly, by avoiding wide day-to-day fluctuations between sterling and gold'.<sup>70</sup> The former was best achieved by first ensuring 'a rise in the general level of wholesale prices'.<sup>71</sup>

The quota issue aside, the Australian delegation to Ottawa declared themselves happy with the Conference's monetary resolutions.<sup>72</sup> They had not gained the iron-clad assurance that Britain's policy of 'cheap money' would continue, nor did they believe the British statement went quite far enough, but in every other respect the Ottawa resolutions conformed almost to the letter to the 'series of proposals' the economists had drawn up in Australia. Low prices had been unambiguously specified as a principle cause of the present difficulties and low interest rates recognised as an important tool to bring about a reversal of the trend. On the exchange side, the Conference resolved almost exactly along Australian lines. Members of the sterling group would maintain some fixed relation with sterling (adjusted for their relative price movements), but sterling itself would not return to gold until prices had risen. This commitment, made only after the British delegation's rejection of Canada's and South Africa's proposals for a quick return to gold, was deeply significant - for it recognised the monetary reform proposition that internal price stability had to have priority over exchange stability.<sup>73</sup> Writing some months after Ottawa, Melville summed up the Conference's resolutions in declaring 'they mark a step away from the fatalistic conception of depressions and towards the view that some relief can be secured by monetary policy'.<sup>74</sup>

## **2.3 Matters of Theory**

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<sup>68</sup> The resolutions are contained in Australia, Parliament (1932), pp.18-19.

<sup>69</sup> *ibid.*

<sup>70</sup> *ibid.*

<sup>71</sup> *ibid.*

<sup>72</sup> See, for example, Melville's 'Notes on the Ottawa Conference', undated memoranda, RBA, The Imperial Economic Conference, Professor L.G. Melville's Papers 1932, C.3.7.6.71. See also the Australian delegation's 'official' reaction in Australia, Parliament (1932), pp.115-116.

<sup>73</sup> For the debate between the United Kingdom, Canada and South Africa on this issue see Drummond (1974), p.228.

<sup>74</sup> L.G. Melville, 'Notes on the Ottawa Monetary Resolutions', *op. cit.*

### *Melville, Robbins and Hayek*

Following the conclusion of the Ottawa Conference, Melville and Shann travelled to the United Kingdom in order to consult with British economists on the Australian position and, in particular, the Australian pound/sterling exchange rate. Many years later, Melville revealed that this was partly an attempt to ‘shake’ Sir Robert Gibson free of his ‘obsession of wanting to get back to parity with sterling’ by demonstrating that British opinion was against such a move.<sup>75</sup> Since Melville’s ‘survey’ included such noted monetary reformers as Keynes, Hawtrey and Sir Josiah Stamp, he was not to be disappointed. Of course, it was around this time too that the ideas which were to form *The General Theory* had begun to crystallise in Keynes’s mind, but to the Australian economists he did not reveal anything beyond that which they knew from the *Treatise*.<sup>76</sup>

One British economist who was not consulted by the Australians was Lionel Robbins, Head of the London School of Economics (LSE) and, in conjunction with Frederick Hayek, the leading inter-war exponent of what would become known as the ‘Austrian theory’ of the trade cycle. In December 1932, Robbins reviewed the Ottawa monetary discussions for the *Lloyd’s Bank Monthly Review* and, *selectively* quoting from the Conference resolutions, declared himself pleased with the outcome. On the monetary side the resolutions, he wrote, committed ‘no one to anything’. Better than that, they recognised that ‘the ultimate aim of monetary policy should be the restoration of a satisfactory international standard’ and rejected the suggestion of an ‘Empire Bloc, run on “managed currency” lines’ (Robbins 1932, p.424). Such a bloc, he argued, could not but fail since it required other centres of a sterling system (apart from London) ‘to be prepared to expand or contract credit locally’ (Robbins 1932, p.424). Whilst credit *expansion* to stay in the system would likely be supported, the other side of the coin was far less likely; ‘that the inhabitants of the different centres would submit to credit *contractions* ...is most improbable’ (emphasis added, Robbins 1932, p.424). In support of this thesis, Robbins pointed to Australia’s recent history. In 1930 Australia had left the gold standard in order to avoid the credit contraction required to maintain parity with sterling. If, then, Australia had been unwilling to do this when sterling was still linked to gold, ‘how much more probable is it when sterling is tied to no such anchor?’ (Robbins 1932, p.424). Robbins added, with what can only be regarded as a certain prescience given what Australia had pursued at Ottawa, that:

Faced with the necessity of contracting credit, if parity with sterling was to be maintained, the citizens of the centre in question would always tend to argue that it was up to the monetary authorities in London to inflate to save them the trouble of deflating. (Robbins 1932, p.424)

In addition, Robbins was pleased *by what he inferred* from the Conference resolutions which others did not, namely a tacit repudiation of ‘proposals for an isolated sterling inflation’ by noting the importance *he believed* they gave to ‘stable exchanges with gold’ (Robbins 1932, p.425). For the United Kingdom, such an isolated inflation, and its necessary further depreciation of sterling, would mean ‘extensive losses in respect of all foreign debts to us which are payable in sterling’ (Robbins 1932, p.425). For the

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<sup>75</sup> Melville cited in Cornish (1993), p.443.

<sup>76</sup> Interview with the author, 28 January 1993.

rest of the world the implications of a sterling group-only inflation was even more serious, since the accompanying depreciation would impose a deflationary effect on the countries still on gold. The overall effect, according to Robbins, would be

a destruction of capital values and a shock to confidence. Traders do not know what will happen next; they endeavour at all costs to make their position liquid. At the same time, there is a great pressure on the exchange. The balance of payments tends to turn against the country of stable money: and the financial authorities impose controls on foreign business. They impose regulations on exchange dealing and capital transfer. Needless to say, this worsens, rather than improves, the situation. Financial crisis sets in: a fall of prices ensues. In some such way - and the picture is not imaginary - in the short run, the depreciation of one currency tends to produce deflation and depression elsewhere. (Robbins 1932, p.426)

As will be explained in detail below, there was some sense in Robbins's analysis of the effects of a sterling depreciation on the rest of the world, but there was much inconsistency too. Why, for example, the contagion effect of depreciation should be different from that of price deflation is not clear. But if Robbins was pleased with what *he saw* as being the very limited nature of the Ottawa resolutions, he was less pleased with the 'tendency to reflationism' in the Conference's advocacy of what he called 'world inflation'. In fact, Robbins's quoting of the Conference was again highly selective, since the Ottawa pronouncements, rather than displaying a mere 'tendency' towards reflation internationally, were, of course, utterly unequivocal in advocating this.

Robbins's hostility to the use of expansionary monetary policy to check the depression was nothing more than a statement of the Austrian theory of the business cycle, first expressed (in English) in 1931 in Hayek's *Prices and Production* (for which Robbins wrote the Foreword). In *Prices and Production*, Hayek combined price theory (prices as a communications network), capital theory (drawing on Böhm-Bawerk in emphasising the intertemporal nature of capital formation) and monetary theory (introducing the concept of 'neutral money' which, as a medium of exchange, facilitated the coordination of economic activities, while not being a source of disturbance to this coordination). So long as money was kept neutral, that is, in the absence of a credit expansion or contraction in the banking system, prices and the rate of interest (a 'natural' rate reflecting preferences between present and future goods) would ensure that production would be consistent with intertemporal preferences. According to Hayek, then, it was the banking system which was the source of economic cycles, since changes in the quantity of money (when *created* by banks) extinguished money neutrality, distorted relative prices and the signals they communicated, and led to a structure of production inconsistent with consumer preferences. In the case of a credit expansion this meant an 'artificial' reduction of the rate of interest from its 'natural' rate and an artificial stimulation of investment relative to consumption. This led to an unsustainable boom relative to the resources ultimately available. Such 'overinvestment' would be reversed, bust following boom as the system recovered by purging the least sustainable investment projects and returned aggregate investment to a level consistent with intertemporal preferences (Hayek 1931).

Hayek's system was, of course, an utterly different animal from that envisaged by the so-called monetary reformers, and throughout the 1930s Hayek engaged the leading lights of this loose group, but especially Keynes, in lively discussion. To Hayek, the central thesis of the monetary reform agenda, that prices should be maintained through the use of monetary policy in order to forestall the fluctuations in production which were *the result* of fluctuations in prices, was simply wrong. So long as money was neutral, price changes merely reflected changes in intertemporal preferences and provided the signals to producers to maintain a structure of production consistent with these. Attempts at price stabilisation through monetary policy 'to achieve certainty as to the future structure of prices', could 'least of all be achieved by seeking to prevent those price changes which are necessary for the maintenance of equilibrium in production, and such efforts thereby call forth disturbances of equilibrium which must ultimately lead to intensified price movements' (Hayek 1931, p.89). According to Hayek, the reasoning of the monetary reformers with respect to the role of prices in production was the product of an uncritical use of past correlations between falling prices and falling production, 'a beautiful example of how dangerous it is to derive theoretical propositions from the results of statistical investigations' (Hayek 1931, p.90). Hayek's *policy* prescriptions were thus equally at variance with those of the monetary reformers, whose advocacy of cheap money and an abandonment of the gold standard could only exacerbate matters. As Hayek put it,

...it is still more difficult to see what lasting good effects can come from credit expansion. The thing which is needed to secure healthy conditions is the most speedy and complete adaptation possible of the structure of production to the proportion between the demand for consumers' goods and the demand for producers' goods as determined by voluntary saving and spending. If the proportion as determined by the voluntary decisions of individuals is distorted by the creation of artificial demand, it must mean that part of the available resources is again led into a wrong direction and a definite and lasting adjustment is again postponed. And, even if the absorption of the unemployed resources were to be quickened in this way, it would only mean that the seed would already be sown for new disturbances and new crises. The only way permanently to "mobilise" all available resources is, therefore, not to use artificial stimulants ... but to leave it to time to effect a permanent cure by the slow process of adapting the structure of production to the means available for capital purposes... [W]e arrive at results which only confirm the old truth that we may perhaps prevent a crisis by checking expansion in time, but that we can do nothing to get out of it before its natural end, once it has come (Hayek 1931, pp.86-87).

Robbins's review of the Ottawa monetary resolutions was replete with Hayekian devices and closely resembled a similar review written by Hayek on Britain's departure from gold in 1931.<sup>77</sup> Thus central to Robbins's case against an active monetary policy was a scepticism that low prices were the cause of the Depression. True, price deflation had attended the depression, but 'may it not rather be the

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<sup>77</sup> See 'The fate of the gold standard' in Hayek (1984). This work was written (in German) in February 1932, but it was not published in English until it appeared in a compilation of Hayek's 'early essays' in 1984.

*consequence* of other more fundamental maladjustments?’ (Robbins 1932, p.429, emphasis in original). In support of an affirmative answer to this question, Robbins used the example of the years immediately prior to 1929. These years, he believed, had experienced ‘one of the most colossal expansions of credit that the world has ever seen’ (Robbins 1932, p.430). However, during the same period, there had been no general rise in prices across the world. According to Robbins the answer to this apparent contradiction lay in the fact that during the same period ‘productivity was increasing rapidly’. This should have meant, in the absence of inflation, that prices would fall. Somewhat adventurously, Robbins claimed this had not happened - inflation therefore *had* been taking place pre-1929, inflation which masked what would have otherwise been a healthy situation (in contrast to what the monetary reformers were advocating) in which prices *declined with productivity*. From this,

it follows that our troubles...are traceable, in the first instance not to deflation but to *inflation*. The maladjustments which the slump has revealed were due not to money rates which were too high but to money rates which were too low. The price level which refused to bend, eventually snapped. The slump is the consequence of an inflationary boom. (Robbins 1932, p.431)

But if productivity increases were behind what *should have been* price declines in the latter half of the 1920s, they could not explain the deep and persistent fall in price levels since then. But for this, too, Robbins had a ready explanation. According to Robbins money hoarding was the key. Hoarding (by which he meant holding cash or idle balances) was due to there being ‘no prospect of profitable investment’, a fact which itself was again a function of incorrect monetary policies which attempted to achieve price stability (Robbins 1932, p.431). These attempts meant that ‘costs, which by reason of the inflationary boom have become too high in relation to prices, have not been reduced’ (Robbins 1932, pp.431-432). The resulting cost rigidity, which policy had attempted to counter by raising prices, had not been addressed. The on-going price deflation was due, then,

to the failure to eliminate the maladjustments of the boom period. Were these maladjustments eliminated, it would cease... In the present depression, misled by the view that consumers’ purchasing power must at all costs be maintained, the world has delayed such readjustments. (Robbins 1932, p.432)

Ottawa’s call for international collaboration to raise prices was not only based on incorrect reasoning, it was also, in Robbins eyes, particularly ill-timed. According to Robbins, in the United States, ‘the process of liquidation, although by no means complete, has now reached a stage when, at some not altogether distant date, the very slow beginnings of a sound recovery are not inconceivable’ (Robbins 1932, p.435). Such an outcome, however, required the monetary authorities not only to desist from further monetary expansion, but ‘even to withdraw from the market some of the funds it has injected’ (Robbins 1932, p.435). In this scenario, ‘[a]nything which would commit the central banks of the world to an easy money policy which must last until we are back at the 1929 level seems to me entirely undesirable’ (Robbins 1932, p.435).

Robbins concluded his review of the Ottawa monetary resolutions by recording what he thought policy-makers should do, rather than seek higher prices through monetary expansion:

...[A]bove all, policy must be directed to restoring the freedom of the market in the widest sense of the term. By this I mean not only the lowering of tariffs and the abolition of trade restrictions but also the removal of all those causes which produce internal rigidity - rigid wages, rigid prices, rigid systems of production - which, in the period since the war, have deprived the economic mechanism...of its power of adaptation to external change. It is this inflexibility of the economic system at the present day which is at the root of most of our troubles. It was the cause of disequilibrium before the slump. Its persistence is one of the many reasons why the effects of the slump have been so peculiarly devastating. Unless it is abolished, or at least considerably weakened, no monetary system can be worked satisfactorily. Indeed, it is no exaggeration to say that unless this happens, it is highly doubtful whether, in the long run, an economic organization of the modern order of complexity can continue to exist at all (Robbins 1932, p.437).

### *Melville's reaction*

Though he did not meet Robbins during his visit to England, in late 1932 Melville put down his reactions to Robbins's article in a memorandum which, while not published, was circulated within the Commonwealth Bank and to a number of his fellow economists.<sup>78</sup> In it, he rejected not only Robbins's peculiar reading of the Ottawa resolutions, but also the Hayekian theoretical framework upon which Robbins's critique was constructed. The memorandum is a remarkable document. It implicitly revealed the theoretical position Melville had arrived at by 1932 which, as noted above, was only beginning to surface in his last published writings before Ottawa. The memorandum was thus a testament to an extraordinary journey. The Melville who was so often regarded as the standard bearer for economic orthodoxy in Australia before the publication of *The General Theory* (after which much is made of his conversion to Keynesianism), is revealed as an economist who was not only cognisant of the latest writings of Keynes and other reformers, but already disposed philosophically to a view of economics upon which the later revolution was the capstone.

Melville's first objective in the memorandum was to correct what he saw as Robbins's fundamental misreading of what the Ottawa monetary resolutions had been about. The comfort Robbins had taken in what *he* saw in the resolutions as an emphasis upon a stable exchange between gold and sterling was, according to Melville, misplaced. The resolutions contained 'no suggestion that the sterling exchange should be prevented from moving as it will, subject to the elimination of short period speculative movements'. Restoration of gold or some other standard was the *long-run* goal of the Ottawa signatories, but not until:

(1) Reflation to a higher price level has generally been achieved, so as to restore profit to industry, and;

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<sup>78</sup> 'Notes on the Ottawa Monetary Resolutions' L.G. Melville, *op. cit.*



(2) There is some security that the major countries will so manage their economies, including their currency, that the international standard can function smoothly.<sup>79</sup>

More important than the misreading of the Ottawa resolutions, though, was Robbins's theory which was based, according to Melville, 'on false reasoning'. Melville wrote that the 'economic equilibrium which Robbins and Hayek rightly seek can be found with a rising price level, a stable price level or a falling price level'.<sup>80</sup> Their contention that the quantity of money should remain constant and that prices fall in line with improvements in productivity was 'based on a fallacy, the fallacy being a failure to recognise that an increase in the quantity of money when it gives a greater command over goods is an investment just as real as a new road or a factory or a gold mine'.<sup>81</sup> Of course, Hayek had written that this could not be so, and Melville quoted at length Hayek's belief that real (and sustainable) capital could only be sourced from existing 'voluntary' saving, and the concomitant censure that 'banks must not lend more or less than has been deposited with them as savings'. To this, Melville countered that if there existed a demand for money which was but a component of a demand for real capital, '*then the increased supply [of money] is made available by the banks coincidentally with increased savings on the part of the community*' (emphasis added).<sup>82</sup>

Melville's attack on Hayek's claim that investment financed by credit creation was less sustainable than that financed from 'voluntary' saving demonstrated not only his understanding of the monetary reform agenda up to Keynes's *Treatise*, but also an awareness of more recent developments at the leading edge of theory critical of the Hayekian discourse. In March 1932, for example, Piero Sraffa's review of Hayek's *Prices and Production* for the *Economic Journal* began what would become a rather acrimonious exchange by making the point, which was theoretically consistent with Melville's critique, that the role of money in the Hayekian framework was solely as a medium of exchange.<sup>83</sup> This contention amounted to 'assuming away the very object of the inquiry' according to Sraffa, who (again, like Melville) asserted that the accumulation of capital would take place regardless of whether it arose via the 'voluntary decisions of individuals' in saving, or via the credit creation of banks (Sraffa 1932, pp.43-44).<sup>84</sup> Hayek's claim, that credit creation-derived investment was unsustainable, ignored the fact that if one did not simply assume away money as a store of value, that is, *assume* money neutrality in intertemporal choice, credit-created investment would change the consumption and saving propensities of consumers just as reliably as would be the case if the investment had come from 'the voluntary decisions of individuals' alone. Thus 'if those who had gained by the inflation chose

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<sup>79</sup> *ibid.*

<sup>80</sup> *ibid.*

<sup>81</sup> *ibid.*

<sup>82</sup> *ibid.*

<sup>83</sup> This debate between Sraffa and Hayek was later joined by others but with little goodwill on either side. It began in the March 1932 issue of *The Economic Journal* (Skidelsky 1992, pp.454-459). The controversy also included a parallel battle between Keynes and Hayek in the pages of *Economica* and in private correspondence between the two. It's something of a pity that Melville's analysis was not published, and that an Australian element in this seminal conflict was not brought into the play.

<sup>84</sup> The use of identical quotes from *Prices and Production* by both Melville and Sraffa suggests that Melville must have read Sraffa's piece.

to save the spoils, they had no reason at a later stage to revise the decision; and at any rate those on whom forced saving had been inflicted would have no say in the matter' (Sraffa 1932, p.249).<sup>85</sup>

Fallacious theory was dangerous when it bred false remedy, and as such Melville railed against a policy which sought to reduce costs to the current level of prices, a policy which would 'create more disequilibria than it removed'.<sup>86</sup> But for a country like Australia, such a policy, if carried out in the rest of the world, brought with it particular dangers. According to Melville, Australia had made adjustments to wages and other incomes to an extent that further reductions were not socially possible, but 'if wages in England and Europe were now cut by 25 per cent our work in Australia will have been in vain'. Depreciation offered one possible avenue for Australia in such a scenario, but 'Professor Robbins would not permit us that'. An illustration of what awaited a country adhering to a Hayekian solution was provided, according to Melville, by Germany, the experience of which suggested that 'a world which seeks that way out will be marching towards collectivism'.<sup>87</sup>

To Robbins's central philosophy that what the world economy really required for recovery was the removal of restrictions and rigidities, Melville declared himself to be in agreement - 'the economic machine *would* work better if there was more elasticity in its parts'. But, drawing on an analogy of constructing an aeroplane (Melville had studied engineering before economics), 'we cannot wait for the elimination of airpockets and storms before we build our machine'.<sup>88</sup> The world had 'not yet become an economist's paradise', and in this non-perfect world Melville argued that a rising price trend was preferable to a price level that was falling. For Australia this was certainly true. Dependent 'for our prosperity on a narrow range of exports', reductions in Australia's terms of trade required (for external balance) reductions in Australian wages relative to those abroad. Such an outcome was most easily achieved by rising wages in other countries, negating Australia's use of those devices (tariffs, quotas, etc) so deplored by Robbins. Such was the case for Australia, such was the case for the world. The Ottawa resolutions which called for rising price levels were, unlike the prescriptions of Hayek and Robbins, 'palpably designed for an imperfect world'.<sup>89</sup>

## **2.4 Chosen Instrument: British Monetary Policy**

Of course, theoretical excursions such as that above, while important, could to some extent be said to be unnecessary in a defence of the Australian economists' position at Ottawa. The collapse in export income and the cessation of lending had greatly reduced the London funds of the Australian banks and, as a result, *had imposed* upon Australia a severe monetary contraction. In 1932 Australia desperately needed an increase in commodity prices and a reopening of its traditional access to London finance. In this light, the Australian monetary efforts at Ottawa were surely justifiable

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<sup>85</sup> This quotation is sourced from Sraffa's 'rejoinder' to Hayek in the same issue of *The Economic Journal*.

<sup>86</sup> 'Notes on the Ottawa Monetary Resolutions', L.G. Melville, *op.cit.*

<sup>87</sup> *ibid.*

<sup>88</sup> *ibid.*

<sup>89</sup> *ibid.*

merely on the grounds that they were an attempt to do something, anything, which promised to provide for these outcomes. And, as noted, Bruce's support for the economists' monetary line was at least partly predicated on the basis that this could create conditions in which it would be easier to convert Australian debt to lower interest rates.

The issue of the appropriateness of the chosen instrument, British monetary policy, to effect a cure, is an altogether different question, therefore, to the questions of what constitutes plausible theory. The Australian economists sought an increase in commodity prices and an easing in credit conditions and sought to bring this about by an expansionary monetary policy conducted by the United Kingdom. This strategy, in turn, relied upon three possible transmission channels. Firstly, the expansionary monetary policy had to bring about an expansion in economic activity in the United Kingdom, *and* this expansion in activity had to translate into increased demand (and prices) for Australia's commodity exports. Secondly, such an expansionary monetary policy had to create the right conditions in the London money market such that Australia could both renegotiate the conditions of existing debt and, hopefully, open up channels for new credits. Finally, to the extent that the lending policies of the Australian banks were dependent upon *British* monetary conditions via their holdings of London funds, it was implicit in the Australian thesis that monetary conditions would be eased in Australia.

Contrary to the Australians' fears (but not quite to the extent of their desires), the United Kingdom monetary authorities did live up to the 'cheap money' commitments given at Ottawa. The conversion operation of British wartime debt paraded at Ottawa (which accounted for some 27 per cent of national debt) allowed for an immediate reduction in interest rates, created an environment in which improved monetary conditions were expected and eased the burden of interest payments on the budget. In June 1932 the Bank Rate was lowered to 2 per cent (from 6 per cent) and the rate on Treasury Bills to less than one per cent (Capie and Wood 1994, p.245).

'Cheap money' remained the official stance of policy for the remainder of the decade, but it did not live up to the high hopes held for it by the Australians. Low interest rates were supposed to stimulate interest-sensitive investment and, indeed, they did play a significant part in precipitating the 1930s 'housing boom' in the United Kingdom.<sup>90</sup> Non-residential investment, however, showed no similar revival and most empirical studies of the British inter-war economy conclude that, whilst accommodating, monetary policy was essentially a passive factor in the 1930s recovery (Thomas 1994, p.350).

But the impact of cheap money on interest-sensitive spending in the United Kingdom was only relevant to Australia to the extent that such spending in turn increased the demand, and prices, for Australian commodity exports. Such a hope might have been quite reasonable at a time when so much of world trade was financed through London, and when British financial institutions held so much overseas debt, giving the country and its financial system a disproportionate influence over world commodity prices. Unfortunately for the Australian efforts, however, this did not

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<sup>90</sup> Domestic dwelling construction rose by almost 50 per cent between 1932 and 1934, and remained strong for the remainder of the decade (Thomas 1994, p.350).

occur in the wake of British 'cheap money'. A dramatic increase in the price of wool (on the strength of pent up demand from *European* and *Japanese* mills) lifted Australia's terms of trade briefly in 1933/34, but it was not until 1935/36 that an improvement in Australia's export prices occurred in any sustained way. Even then, prices did not return to pre-Depression levels until the very end of the decade when *rearmament* rather than monetary policy was the driving force. After the Ottawa Conference, the *volume* of Australian exports to the United Kingdom increased, but this was neither due to a growing British economy nor to expansionary monetary policy. It was the result of the tariff, quota and other trade agreements entered into at Ottawa which had so dominated its proceedings (Dyster and Meredith 1990, p.150).

That Britain's cheap money policy, in spite of the hopes of the Australian economists, failed to have any impact on the prices Australia received for its most important exports was a function of the failure of cheap money to expand spending as hoped. But the failure of commodity prices to rise was due to other factors as well, factors which extended far beyond the powers of the British monetary authorities to influence. In this context, it must be recalled that for Australia's most important commodity exports, wool and wheat, Australian production far outstripped British consumption. The prices of these commodities, just two of many, could not diverge from that prevailing in *world* markets. Related to this was the rather obvious fact that price deflation was a global phenomenon, not one solely pertaining to commodities sold in British markets. The global deflation of commodity prices was both structural in nature (overproduction exacerbated by the dumping of commodities by debtor nations) as well as policy-induced. Britain's abandonment of the gold standard in 1931 and its cheap money policy largely removed *it* as a source of deflation for the commodities relevant to Australia, but the conclusion of the Ottawa agreements on balance accelerated the decline of multilateral trade. The demand and prices for commodities remained relatively low throughout the 1930s (Schedvin 1970, pp.21-34).

In terms of capital access, Britain's cheap money policy seems to have made conditions somewhat easier for Bruce in his attempts to renegotiate Australian government debt, but these made for little impact on capital flows overall.<sup>91</sup> After 1931, Australian governments repaid overseas considerably more than they borrowed. As such, debt renegotiation eased budgetary pressures but, since this did not lead to any equivalent increase in government spending, this only reduced the *deflationary* impact of capital outflows in conjunction with the 'tight' fiscal stance of government.

Schedvin (1970) placed much emphasis in his account of Australia's recovery from the Depression upon the development of import-replacing manufacturing, and it is perhaps in this context that Britain's cheap money policy had its most significant impact with respect to capital flows. This was because a great many of these new enterprises, established behind the walls of Australia's high tariffs, were subsidiaries of overseas (mostly British) firms with access to cheap capital. None of this occurred in any substantial way, however, until recovery was already underway. Nevertheless, net private capital inflow for such purposes 'played an important part in reinforcing recovery from 1933 onwards' (Schedvin 1970, p.295).

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<sup>91</sup> Bruce claimed that he was ultimately successful in renegotiating £200 million of the £437 million of Australian government debt held by British bond holders (Cumpston 1989, p.106).

The third possible avenue through which British cheap money could yield an expansionary influence in Australia - by enabling Australian banks to expand lending in the wake of higher levels of London funds - seems to have had little effect on domestic monetary conditions. As with capital flows, however, the failure here had more to do with domestic conditions and institutions. Considered by the Australian banks as an integral part of their reserves (and in the absence of a central bank that would engage in open market operations), the London funds were the exogenous variable of the money base and, by extension, the money supply. According to Butlin and Boyce (1988, p.197), it was the large fall in London funds (itself a function of the fall in export prices, thus highlighting the interdependence of the monetary channels under consideration here) which caused the monetary contraction in 1931. This relationship, between London funds and credit conditions in Australia, which invariably prevailed outside the crisis years, seems, however, to have broken down in the immediate recovery years after 1932. London funds did recover from 1932, though only fitfully until 1935 but, contrary to the traditional mechanism, the easing of the London position did not lead to any concomitant increase in the willingness of Australian banks to lend (Guiney 1971, pp.162-165). This was due, according to Schedvin (1971) and Guiney (1971), to the Australian banks' desire to maintain a high level of reserves at a time when they expected much internal and external instability. These high precautionary balances were 'a distinctive Australian characteristic' according to Schedvin (1971, p.178) who, with Guiney (1971, p.153), also noted that suitable investment opportunities were not readily forthcoming at this time in any case.

## **Chapter Three**

### **The World Monetary and Economic Conference**

#### **3.0 Preparation**

*The Commission of Experts and Divergent Opinion in France, the United States and the United Kingdom.*

Although the idea of a world economic conference had been ‘in the air’ since the onset of the Depression, the immediate origins of the WMEC derived from the resolutions of the 1927 Lausanne Conference, also convened by the League of Nations but concerned with World War One reparations. Lausanne effectively ended the reparations question but broader financial and economic questions - ‘the problems of monetary and credit policy, exchange difficulties, the level of prices, the movement of capital...tariff policy...producers’ agreements’ - required a new conference that would include the United States.<sup>92</sup> Accordingly, the delegates to Lausanne called upon the League to convene such a conference and to appoint from participating countries a Commission of Experts to draft an agenda. Since the resolutions coincided with exploratory moves between the United Kingdom, the United States and France to attempt to find common ground on these issues, the acquiescence of the major powers to the world conference was soon forthcoming, and the Commission of Experts was appointed in August 1932.<sup>93</sup>

From the outset of its deliberations, the Commission of Experts was divided in ways much more fundamental than those which had divided the experts at Ottawa. At Ottawa, the Australians’ principal dispute with the United Kingdom was over degree and emphasis, but there was no dispute over the underlying philosophy. If there was a certain resistance to what some British Treasury officials regarded as ‘monetary fixation’, there was no mistaking the general direction of United Kingdom policy or of the Ottawa resolutions (Drummond 1981, p.132). Not so beyond the Imperial family, where a number of countries, but notably France, maintained an inflexible commitment to gold. To France and certain other of the ‘gold bloc’ countries, monetary expansion raised not so much thoughts of an orderly rise in the prices of primary products, but the spectre of rampant inflation.<sup>94</sup> The Bank of France was not even legally empowered to conduct open market operations, would issue currency only against gold or commercial paper, and French capital markets were largely closed to capital export.

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<sup>92</sup> Resolution of Lausanne cited in Angell (1933), p.2. The United States was not, of course, a member of the League.

<sup>93</sup> For all the drama of the pre-Conference negotiations (from a British viewpoint), see Woodward and Butler (1953), pp.742-864.

<sup>94</sup> Principal members of the ‘gold bloc’ included France, Holland, Italy, Poland, Romania, Switzerland and, when it was on gold, Germany.

In contrast to the rigidity of the French position, the one uniform principle underlying United States' involvement with the Commission of Experts could only be described as manifest confusion.<sup>95</sup> Acceptance of the idea of an international conference had come from President Hoover, and coincided with a time when his administration had itself been attempting to raise internal prices by encouraging easy credit. At this time, the centrality of raising prices for the WMEC agenda was clear to the American government. Hoover's defeat at the hands of Roosevelt in the elections of 1932, however, changed matters and the United States experts, believing that they were following the wishes of the new president, pressed for exchange rate stabilisation. The principal need, according to the two United States representatives on the Expert Commission, was the 'restoration of the gold standard in the key countries, England and Germany' (Drummond 1981, p.138). But if this was not bad enough for monetary expansionists, the US delegates also proposed throughout the Commission meetings a whole series of initiatives which, to the extent that they were self contradictory, only made less certain that the Conference would achieve anything worthwhile at all. Over the course of the Expert Commission, the American representatives advocated raising commodity prices through production controls, the abolition of exchange controls, a 'customs truce' and, most striking of all for advocates of gold, opening up the issue of *bimetallism* by pressing for the inclusion of silver in a new monetary standard (Drummond 1981, pp.143-145).

In contrast to the mood prevailing in continental Europe and to the seeming confusion in the United States, the idea that there existed a monetary solution to the depression had, if anything, become more entrenched with United Kingdom policy-makers in 1933 than had been the case at Ottawa. Freed from the necessity of keeping in check what they sometimes regarded as the extreme monetary views of the Dominions, the British representatives on the Commission of Experts declared that their objective was to 'restore free and stable exchanges and raise world prices' through 'international agreements...on policy of credit expansion, better distribution of Bank reserves, abolition of exchange controls, [and the] removal or lowering of trade barriers'.<sup>96</sup> On the monetary side the British proposals were, in fact, little more than a restatement of the monetary resolutions of Ottawa. The British delegation made clear that restoration of a monetary standard would only be possible 'provided a reasonable degree of equilibrium between prices and costs can be restored'.<sup>97</sup> For this, monetary action was indispensable, but the British were convinced 'that well co-ordinated action between the leading Central Banks is likely to have more effect in improving world conditions than isolated efforts by particular countries'.<sup>98</sup>

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<sup>95</sup> A feeling for this confusion can be gleaned from Kindleberger (1986), pp.179-229.

<sup>96</sup> Sir John Simon (Foreign Office) to Sir R. Lindsay (United Kingdom Ambassador to the United States), 10 April 1933, in Woodward and Butler (1956), p.790.

<sup>97</sup> 'Instructions to His Majesty's Ambassador at Washington, February 1933', in Woodward and Butler (1956), p.763.

<sup>98</sup> *ibid*, p.765. The extent to which United Kingdom 'official' economic policy makers had moved towards accepting ideas which were not always hitherto regarded as entirely respectable, can be seen in the fact that Treasury officials presented the 'Kisch plan' to the United States for consideration. This scheme, a Treasury-modified version of the so-called 'Keynes-Henderson Plan' of 1932 (which advocated the expansion of international liquidity via the creation of new international reserves by the Bank for International Settlements to augment gold), sought to redistribute gold from creditor to debtor countries through an International Credit Corporation. In April 1933, however, the Americans rejected both the Kisch and Keynes-Henderson plans and, in the light of this, they were subsequently dropped from the United Kingdom's plans for the WMEC (Drummond 1981, p.139).

The Commission of Experts finally produced a Draft Annotated Agenda in February 1933 and, as might be expected, it was a compromise document reflecting the divergent views of its most powerful members. Declaring along French and (early) American lines that ‘the restoration of a satisfactory international monetary standard is clearly of primary importance’, the agenda noted nonetheless (along British and monetary reform lines) that ‘among the essential conditions for the restoration of a monetary standard’ was ‘the restoration of equilibrium between prices and costs and, in the future, such a reasonable degree of stability of prices as the world measure of value should properly possess’.<sup>99</sup> The experts accepted that one method for raising prices was ‘a liberal credit policy’ but, worryingly for the Australians, the restriction of production (euphemistically referred to as the ‘organisation of production and trade’) was another.<sup>100</sup>

### *Australia*

Although Australia’s relationship with the League of Nations on economic matters was to expand considerably over the decade (as outlined in Section II of this study), Australia was not represented on the Commission of Experts drawing up the agenda for the WMEC. Rather, Australia relied upon the United Kingdom to press both its own and the broader imperial interest. For Australia, this was an arrangement which worked well only up to a point - for while the United Kingdom’s monetary line was as much as Australia could hope for, the British experts were continuing to press for production controls as a complement to monetary policy in raising commodity prices. Communication of the positions being taken at the Expert Commission were also less than satisfactory from an Australian point of view. According to Drummond (1981, p.160), the British Treasury regarded the Dominions as being ‘too small to make much impact on the deflation Treasury knew to be a worldwide problem’, and to the extent that they wanted Dominion involvement at all, wanted it ‘entirely in relation to quantity controls’.

In April 1933, Bruce, now High Commissioner in London, pressed the United Kingdom for a series of meetings in which British monetary proposals could be discussed. These meetings were regarded by Sir Frederick Phillips, one of the British representatives on the Commission of Experts, as being little more than a nuisance, for ‘he did not think there was any special point in discussing with Dominion representatives at present the question of “monetary manipulation”’.<sup>101</sup> For Bruce, the meetings had some value though, enabling him to tell British ministers directly with regard to production controls that ‘Australia could only consider co-operation in any such policy if linked to definite action in political, economic, financial and monetary spheres which held out real prospect of definite improvement in wholesale commodity prices, and only then if contemplated restrictions were of a temporary character’.<sup>102</sup>

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<sup>99</sup> Annotated Agenda of the Commission of Experts, reproduced in Angell (1933), p.31.

<sup>100</sup> *ibid.*, p 46. Details of restriction schemes, pp.73-77.

<sup>101</sup> Dominion Office Minute by Sir Edward Harding, 1 May 1933, cited in Drummond (1981), p.160.

<sup>102</sup> ‘S.M. Bruce to J.A. Lyons’, 9 May 1933, J.G. Latham, World Economic Conference, NAA A981, ECO 21.



If official communication between Australia and the United Kingdom with regard to the WMEC was less than ideal, it did not preclude the Conference working its way into the consciousness of Australia's economists. This was particularly true for Melville, Copland and Shann, all of whom were nominated to attend the WMEC, and all of whom wrote of their expectations for the Conference. In the case of Copland these writings were mostly concerned with developing a theoretical case against the idea of production controls. According to Copland, it was a fallacy of composition that the restriction of the production of certain commodities could lead anywhere but to further deflation. Depending on elasticities, the income and the spending power of the producers of commodities under restriction *could* increase, 'but the income and spending power of the rest of the community is decreased proportionately'.<sup>103</sup> That the net result was deflationary was due, in Copland's analysis, to the interaction of four processes that would follow restriction:

- a) Reduced demand from producers on account of lower output, embracing reduced demand for credit.
- b) Reduced demand from consumers on account of higher prices of the product in question.
- c) Increase in saving by use of producers income to liquidate debt.  
[all of which was...]
- d) Offset by increased producers' demand for goods on account of their higher incomes.

The net effect on demand of these processes was  $d - (a+b+c)$ , 'and there is no doubt that  $d < a+b+c$ '. Point (a) was not concerned with elasticities of particular commodities, but simply with the idea that lower *volumes* would result in less demand for *ancillary* goods and services.<sup>104</sup> Copland's analysis of restriction schemes was included in the documents the economists took to the WMEC, and they were published in the *Economic Record* later that same year.<sup>105</sup>

The influence on Shann of Keynes's evidence to the Macmillan Committee has already been noted, and in his writings immediately prior to the WMEC, Shann's extraordinary journey from deflationist orthodoxy was once more apparent. In a commissioned commentary for the Bank of New South Wales *Circular* in January 1933, Shann wrote of the impact of deflation in driving a flight to liquidity - what he colourfully referred to as the 'cancer of hoarding'. This was particularly apparent in the United States, where 'an extra currency circulation of \$1,500,000,000 above normal figures, almost all of it in notes, showed how unwilling depositors had become to continue pooling their purses'. Shann remained convinced nevertheless, both of the efficacy of monetary policy and of the role of the United Kingdom in being able to induce global recovery - even if senior government figures (including the Chancellor) doubted it themselves. Such 'doubts may be ridiculed by students familiar with the time-honoured practice of regulating the money market by means of the Bank Rate and of keeping the British price-level by that means'. Citing R.G. Hawtrey's recently published *The Art of Central Banking* (1932) in support of his case, Shann also

<sup>103</sup> 'Note on the Restriction of Production', 19 June 1933, RBA: League of Nations, Monetary and Economic Conference, London - Papers and Proceedings 1933, C.3.7.6.63, File 1.

<sup>104</sup> *Ibid.*

<sup>105</sup> See Copland (1933).

bemoaned (in tones not unlike those of Keynes) the ‘inhibitions to which leaders in key positions are subject’, a situation which was ‘amongst the most important facts in the depression complex’ (Shann 1933b, pp.11-12).

Making Shann’s contribution more remarkable for what it revealed about his theoretical positions though, was his suggestion that this lead from Britain in the monetary sphere be combined with ‘concentrated measures in many lands to increase capital expenditure’. What Shann meant was public works, ‘a feature common to the relief programmes into which the growth of unemployment has pushed the French, Italian and German Governments’. If only the United States, Britain, India and the Dominions followed suit, Shann wrote, then ‘the danger, so dreaded by central bankers, of the relative depreciation of their moneys need not deter them’. Demonstrating an understanding of a multiplier concept too (if suggesting still some residual concerns of what would now be called ‘crowding out’), Shann concluded as follows:

Any nations that can build public utilities at low interest cost and continue thereby to set afoot an expansion of consumers’ outlay, to a degree which they can continue to finance themselves at a steady price-level, will have regained their economic balance. (Shann 1933b, p.12)

Melville’s position at the Commonwealth Bank constrained his public pronouncements on the WMEC but, as with his memoranda on Robbins’s critique of Ottawa, his thoughts at this time are accessible via much private correspondence. Of particular importance in this regard is a series of replies he gave to questions posed by Sir Hal Colebatch, a semi-independent Senator from Western Australia with an enthusiast’s interest in economic policy.<sup>106</sup> In these letters Melville sought to convince Colebatch not only of the efficacy of monetary policy (particularly for Australia, since ‘prices of raw materials change much more rapidly than prices of manufactured items’), but also the appropriateness of using it as a counter to deflation. Writing against what were apparently Colebatch’s concerns for inflation and the potential for abuse of monetary activism in a democracy, Melville argued that there were ‘just as serious dangers of deflation getting out of control’.<sup>107</sup> Large movements in the price level ‘either up or down... are inconsistent with the maintenance of any degree of equilibrium in our economic system’. There would be resistance to monetary action by the most extreme proponents of ‘individualism’, but ‘if the price of individualism is really to be periodical and *avoidable* breakdowns of the productive system due to rising or falling prices involving the unemployment of twenty five million wage-earners, then the socialist critics would be justified...’. Monetary action, accordingly, had to be employed ‘whatever the consequences to individualism’. And the criterion for monetary policy;

should be its success, over a number of years, in maintaining the average level of wholesale prices of important international commodities relatively stable,

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<sup>106</sup> Sir Hal Colebatch (1872-1953) was a journalist, pamphleteer and politician, who had at one time been Premier of South Australia. Colebatch’s principal ‘obsession’ was free trade, but he used the Senate as a platform to advance his ideas on economics generally throughout the Depression years (De Garis 1981, pp.64-65).

<sup>107</sup> Melville to Colebatch, 3 February 1933, RBA: Miscellaneous Correspondence, General Correspondence 1933, C.3.20.2.4.

and its success in eliminating such violent short term fluctuations as the world has recently witnessed.<sup>108</sup>

Melville told Colebatch that the Ottawa monetary resolutions were an outline of a feasible policy to raise prices by an international expansion of credit, but he was sceptical that the WMEC would bring agreement from countries still attached to the gold standard. In such circumstances, Melville, like Shann, urged the United Kingdom to go it alone in attempting to raise sterling prices. Such a task would be difficult, but it was also one to which, he believed, it was accustomed. Before the war London had managed the gold standard with little help from anywhere else; 'indeed the gold standard broke down when the co-operation from other countries became necessary'.<sup>109</sup> Most radical of Melville's advice to Colebatch though, was his suggestion as to what Australia should do in the absence of either international agreement or British leadership. This, in stark contrast to his earlier writings, included further depreciation of the currency and something he referred to as 'the direct method of cutting debts' - that is, repudiation.<sup>110</sup>

Giblin's most relevant published work in the context of the WMEC, and post-Ottawa, was a review of Keynes's *The Means of Prosperity* which appeared in the *Economic Record* in June 1933. A compilation of articles originally produced for *The Times*, *The Means to Prosperity* was written for the express purpose of influencing the WMEC (Keynes 1933). Employing what was labelled for the first time the 'multiplier theory', it was a proposal for the solution of the *global* Depression via a world reflation. This would be achieved through the latest of Keynes's proposals for reforming the global monetary system. Envisaging the creation of a modified gold standard, Keynes's proposal involved a massive increase in international liquidity through the fiduciary issue of gold certificates to each country equal to their reserves of gold in 1928. In exchange, countries would have to return to a less restrictive version of the gold standard (which would allow currencies to move within a 5 percent band of their agreed parities), eliminate exchange controls, cut tariffs and quotas and remove restrictions on foreign lending and borrowing. Keynes's purpose was to free central banks from the constraints imposed by a lack of reserves. These constraints removed, Keynes hoped his exposition of the multiplier would make an influential case for increased government spending to increase employment and demand within national economies. Whether this would happen or not, could not be determined by the WMEC:

We cannot, by international action, make the horses drink. That is their domestic affair. We can provide them with water. To revive the parched world by releasing a million rivulets of spending power is the primary task of the World Conference. (Keynes 1933, p.25)

Giblin's review of *The Means to Prosperity* was effusive. His pessimism for Australia's external position spilling over to his assessment of the world in general, Giblin declared that civilisation was 'in the balance' and could only be saved through international co-operation of the sort advocated by Keynes (Giblin 1933a, p.141).

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<sup>108</sup> Melville to Colebatch, 6 January 1933, *ibid*.

<sup>109</sup> Melville to Colebatch, 3 February 1933, *ibid*.

<sup>110</sup> Melville to Colebatch, 6 January 1933, *ibid*.

Finding that his own estimate of the size of a likely multiplier for government spending was considerably higher than that calculated by Keynes, Giblin was unambiguous in advocating public spending as the solution. Indeed, he wrote in his review that 'private enterprise had ceased to function, that government expenditure therefore was the 'only resource' and that it should be undertaken simultaneously by as many countries as possible (especially the large 'creditor' ones) (Giblin 1933a, p.142). Finally, and perhaps ambitiously, he found something of a synergy in Keynes's plan and Australian policy thus far:

It may be stated roughly that the scheme is a systematic co-ordination and generalisation for world use of the successful steps that have been taken in Australia - piecemeal, sometimes almost accidentally, without any general acceptance of economic principle - in the effort to keep afloat in the economic maelstrom'. (Giblin 1933a, p.142)

The Commonwealth Government issued no specific instructions to its delegation to the WMEC, but that it had at least broadly accepted the arguments of the economists is clear from its reply to Roosevelt's invitation to preliminary discussions on the Conference. Australia did not send a delegation to these, but conveyed its views by telegram via the British Ambassador in Washington. The telegram expressed Australia's 'almost complete agreement' with the suggestions of the Commission of Experts but, consistent with the economists, stressed policies of expansion:

On prices...it is strongly of the opinion that further cutting of costs would be attended by political dangers from extreme opinion and hence would welcome action directed rather to the restoration of price levels.

More dramatically:

It feels that much more prominence should be given to an examination of effect (sic) of a simultaneous adoption by majority of stronger countries of a vigorous public works policy as a means to an initial fostering of activity and consequent stimulation of private investment...<sup>111</sup>

### **3.1 The Conference**

The World Monetary and Economic Conference opened in London on 12 June 1933, but almost immediately its deliberations were overshadowed by the question of currency stabilisation. This was, as we have seen, the issue which had preoccupied the Commission of Experts but, in the context of a steadily depreciating US dollar, it could not but be an issue for the Conference itself as well.<sup>112</sup> Currency stabilisation was not on the agenda for the WMEC, but was the subject of conversations between treasury and central bank officials of the United Kingdom, France and the United States exclusively. France, leader of the gold bloc countries and increasingly panicked by the depreciation of first sterling and now the US dollar against the franc, urged

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<sup>111</sup> Telegram, British Ambassador, Washington to Foreign Office, 16 May 1933, Dominions Office, DO114, Confidential Print, Dominions, 1924-51, vol.47.

<sup>112</sup> The United States abandoned the gold standard in April 1933.

stabilisation. The United States, newly freed from the strictures of gold, sought characteristically and paradoxically, domestic price rises free from constraints imposed by a fixed exchange rate, and 'permanent and universal stabilisation'.<sup>113</sup> In the middle of all of this, the British delegation was resisting gold bloc pressure to peg sterling, and yet had to find a way of dealing with the United States - whose depreciating dollar was damaging Britain's own trade as well as the efficacy of the arrangements made at Ottawa.

As with the discussions surrounding the Commission of Experts, the British Government did not inform Dominion delegations of the stabilisation discussions. Nevertheless, as noted by Drummond (1981, p.173), neither the Australians nor any of the other of the Dominion delegates could have been in any doubt that such conversations would arise. The British government's secrecy therefore only raised suspicions that it would submit to the gold bloc pressure. Reflecting these fears, Bruce, as leader of the Australian delegation, arranged a meeting on 30 June between British Prime Minister, Ramsay MacDonald, and the Chancellor of the Exchequer, Neville Chamberlain, and the leaders of the other Dominion delegations. At the meeting Bruce put 'in the strongest terms our objection to any stabilising of sterling with gold currencies, and the imperative necessity of coming to some arrangement with the United States of America for a common policy to raise prices'.<sup>114</sup> Earlier Bruce had criticised the lack of British leadership on the issue, reporting to Lyons in Australia that 'the British Government has not formulated any policy and is unlikely to give definite lead'.<sup>115</sup> Bruce had also attempted to negotiate a united Empire approach on monetary policy but had been brushed off by the British. Nevertheless, he was happy with the outcome of the 30 June meeting, reporting again to Lyons that 'we obtained satisfactory undertakings from the Prime Minister and the Chancellor...'.<sup>116</sup>

### *Restriction Schemes - Again*

Bruce was less happy with Chamberlain's opening speech to the WMEC, when once again the British Chancellor advanced schemes for the restriction of production (in conjunction with cheap money) as a possible solution to falling prices. Even more

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<sup>113</sup> As with their involvement with the Commission of Experts, confusion reigned supreme within the US delegation to the WMEC. Delegation leader Cordell Hull, the US Secretary of State and from whom this quote originated, was of the view that some stability of the value of the dollar was required - a view *he thought* he shared with Roosevelt. George Harrison, O.M.W. Sprague, and James Warburg, all bankers and the 'expert' component of the US delegation, were given no policy instructions before leaving for London, apart from being told that the United States would attempt to keep the dollar as stable as possible for the duration of the Conference. It was with this in mind that they began conversations with other delegations, leading to the initial confusion that the United States placed priority on exchange stabilisation. Later their rhetoric changed in favour of raising prices first, but they were never in a position of being able unambiguously to state their government's policy. Raymond Moley, Roosevelt's personal emissary sent to London mid-way through the Conference, was able to present the President's increasingly nationalistic mood as the Conference proceeded. It was finally Roosevelt himself - via telegram - who had the final say on United States expectations of the WMEC.

<sup>114</sup> S.M. Bruce to J.A. Lyons, 1 July 1933, NAA A981, ECO21, J.G. Latham, World Economic Conference.

<sup>115</sup> S.M. Bruce to J.A. Lyons, 9 June 1933, *ibid*.

<sup>116</sup> S.M. Bruce to J.A. Lyons, 1 July 1933, *ibid*.

than had been the case at Ottawa, the Australian delegation reacted with anger at the proposal. In a speech before the Economic Commission of the Conference which stood out for its frankness, Bruce declared that it was 'unthinkable that restriction... should be regarded as the main remedy for the crisis'. It was Australia's view that the 'aim should be the restoration of confidence, the revival of purchasing power, the increase of demand'. Australia had 'obligations to the world for the development of a great continent in order to bring about the utilization of its resources for the benefit of mankind'. More prosaically, Australia had incurred debts in this process and, under schemes to restrict production, 'we should find it difficult to carry out our external obligations'. Bruce also used Copland's analysis to cast doubt on the ability of restriction schemes to raise prices anyway, declaring that 'it is doubtful if a rise in price of an individual commodity means more than the utilization of the spending power existing in the world at the present moment to a greater extent upon that particular commodity. It does nothing to raise the general level of prices which was the fundamental object we had in mind in this Conference'.<sup>117</sup> Bruce concluded his speech by declaring that by adopting such negative policies the world would be 'creating a breeding ground for Nazism and Fascism'.<sup>118</sup> On the request of the British delegation, however, anxious not to offend either the German or Italian delegations present, this portion of Bruce's speech was deleted from the official record.

### *Public Works*

A 'vigorous' programme of public works by 'stronger' countries had been a peripheral but important feature of the Australian's proposals for the WMEC as we have seen, but the idea went nowhere at the Conference itself. Supported by the ILO as well as a number of not particularly 'strong' countries, the issue of public works was fatally weakened by the British delegation's declaration that such schemes did little to help unemployment and that it could 'not participate in any international scheme or to provide funds or raise loans for such a purpose'.<sup>119</sup> The United States, which had made encouraging noises about public works to Australia before the Conference, was content to merely submit a proposal for 'lessened hours of labour and a scale of wages which should increase in proportion to the augmentation of productivity'.<sup>120</sup> The Australian economists' interest in the issue of public works had meanwhile increased since arriving in London and absorbing James Meade's (just published) *Public Works in their International Aspect*.<sup>121</sup> In the end the marginalisation of the issue at the WMEC was probably just as well since, in a change of tack whose origins remain obscure, Australia's Deputy Prime Minister, J.G. Latham, cabled the delegation in mid-Conference that 'on account of local circumstances ...international and inter-Empire financing of public works in any

<sup>117</sup> Bruce's speech to the Economic Commission is published in Australia, Parliament (1933), pp.32-33.

<sup>118</sup> Bruce cited in Cumpston (1989).

<sup>119</sup> This declaration was made by the President of the Board of Trade, Walter Runciman, and is cited in Australia, Parliament (1933), p.19.

<sup>120</sup> Australia, Parliament (1933), p.19.

<sup>121</sup> Meade's work is referred to by Melville in RBA: League of Nations, Monetary and Economic Conference, London 1933, C.3.7.6.63, File 1.

particular country has been carefully considered and is impracticable'.<sup>122</sup> By the time of the WMEC's conclusion, the question of public works had advanced little, a final recommendation being that the issue be considered by a sub-committee that the organisers of the Conference might appoint at some (unspecified) time.<sup>123</sup>

### *The Breakdown of the WMEC*

On 27 July 1933 the WMEC adjourned, ostensibly to reassemble as soon as various sub-committees of experts had considered the most intractable disagreements, but in reality never to meet again. Once more the problem concerned the stabilisation of currencies, the issue which had dogged the Commission of Experts and then the Conference itself throughout. The end, when it came, was a surprise to most of the delegates, a compromise proposal that both affirmed the gold bloc's determination to remain on gold without prejudicing the freedom of those off gold having come within days of gaining agreement. All of this was swept aside, however, by Roosevelt's famous 'bombshell' of 3 July. Fearing that he was being asked to re-fix the dollar in terms of gold, Roosevelt railed against the 'old fetishes of so-called international bankers' which argued for 'the specious fallacy of achieving a temporary and probably artificial stability in foreign exchange'. What was important to Roosevelt was not the price of one currency in terms of another, but the stability of the purchasing power in terms of 'the commodities and needs of modern civilisation'.<sup>124</sup> He spelt it out more clearly in a second declaration two days later:

The revaluation of the dollar in terms of American commodities is an end from which the Government and people of the United States cannot be diverted... What is to be the value of the dollar in terms of foreign currencies is not and cannot be our immediate concern. The exchange value of the dollar will ultimately depend on the success of other nations in raising the prices of their own commodities in terms of their national moneys and cannot be determined in advance of our knowledge of such fact.<sup>125</sup>

Roosevelt's statement was what the Australians had been arguing since 1931 and what the British Commonwealth had agreed upon at Ottawa in 1932. Nevertheless, the seeming capriciousness of the American position and the provocative nature of Roosevelt's declarations was sufficient to panic a number of the delegations, and not just those on gold. The British feared above all 'monetary disorder and confusion', and looked anxiously towards the speculative flows they felt certain would take flight to sterling if the gold bloc's position proved untenable. They wanted the gold bloc to abandon gold, but did not want this to occur in 'chaos while the Conference was actually sitting'.<sup>126</sup> The Australian government, too, was worried about the American moves and, on the 10th of July, sent a telegram to its delegation relaying that it was

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<sup>122</sup> J.G. Latham (for Prime Minister J.A. Lyons) to S.M. Bruce, 28 July 1933, NAA A981, Conf 117, Part 4, World Economic Conference. The most likely reason for the turn-around was pressure from the British Government. There is, however, no evidence of this in the files.

<sup>123</sup> This recommendation, which amounted to a mere two paragraphs, is reproduced in Australia, Parliament (1933), p.19.

<sup>124</sup> Roosevelt's statement was contained in a telegram to Secretary of State Cordell Hull, and read aloud to the WMEC on 3 July. The statement is reproduced in Australia, Parliament (1933), p.28.

<sup>125</sup> This second clarifying statement, on 5 July, is cited in Shann (1933c), pp.165-166.

<sup>126</sup> Chancellor of the Exchequer, Neville Chamberlain, cited in Drummond (1981), p.176.

‘gravely concerned with the position which has apparently developed at the Economic Conference’. They also suggested that a joint statement of Empire delegations be made ‘to avoid panic’.<sup>127</sup> The gold bloc delegations were, not surprisingly, incensed at Roosevelt’s actions and, on the same day as Roosevelt’s ‘bombshell’, they responded with a statement reaffirming their ‘intention to maintain the free functioning of the gold standard...at the existing gold parities and within the framework of existing *monetary laws*’ (emphasis added).<sup>128</sup>

The American declaration finished off any remaining hopes for serious multilateral discussions at the WMEC, but the Conference did linger on long enough for the desires of the Australian government for a British Commonwealth declaration to be realised. Heavily pushed by Bruce, this declaration reaffirmed the Ottawa line of seeking ‘the creation and maintenance within the limits of sound finance of such conditions as would assist in the revival of enterprise and trade, including low rates of interest and an abundance of short-term money’. Noting the success already of Britain’s cheap money policy in raising sterling wholesale prices, the declaration asserted that this should continue to a level ‘which restores the normal activity of industry and employment, which ensures an economic return to the producer of primary commodities, and which harmonizes the burden of debts and fixed charges with economic capacity’. The ultimate aim of monetary policy remained the ‘restoration of a satisfactory international monetary standard’, but in contrast to the gold bloc this required a rise in world prices first - an issue which should regain ‘special prominence’ should the WMEC reassemble. Exchange stability *within* the Commonwealth, however, ‘aided by the pursuit of a common policy of raising price levels’ should be pursued ‘in the interests of trade’. Public works, given the British resistance to the idea, was downplayed as ‘a matter which must be dealt with by each Government in the light of its own experiences and of its own condition’.<sup>129</sup>

### **3.2 Aftermath**

If the collapse of the WMEC is remembered for anything among historians of economic thought, it is usually for the emphatic manner in which Keynes (reporting on the Conference for the *Daily Mail*) greeted Roosevelt’s declaration. ‘President Roosevelt is magnificently Right’ proclaimed Keynes’s headline, going on to interpret the American declaration as an invitation for the rest of the world to join with them in putting ‘men to work by all means at our disposal until prices have risen to a level appropriate to the existing debts and other obligations fixed in terms of money; and thereafter we are to see to it that the purchasing power of our money shall be kept stable’ (Keynes 1982, pp.273-277). As he was to admit later, Keynes read more coherence into Roosevelt’s declarations than they warranted, understandable given that at this time he held great store in being able to influence the American President. That the Conference would collapse in the wake of the Roosevelt announcements, though, Keynes had no doubt. There was left after these, ‘no cat in the bag, no rabbits in the hat - no brains in the head’ (Keynes 1982, p.281).

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<sup>127</sup> J.A. Lyons to S.M. Bruce, 10 July 1933, NAA A981, Conf 117 Part 4, World Economic Conference.

<sup>128</sup> Press Communique Issued by the Representatives of France, Italy, Belgium, Poland, Holland and Switzerland on 3rd July, 1933, cited in Australia, Parliament (1933), p.28.

<sup>129</sup> The complete declaration is contained in Australia, Parliament (1933), pp.31-32.



Keynes's optimism with regard to Roosevelt's contribution was not shared by the Australian economists, who came away from the WMEC unhappy with the manner by which it had ended, and with what they saw as the lack of resolve from the United Kingdom - the Commonwealth Declaration notwithstanding. Reporting on the Conference for the *Economic Record* in December 1933 and an Australian Institute of Political Science 'Summer School' in 1934, Shann was critical of the manner in which the American declaration had been made, suggesting that it had generated 'more heat than light' (Shann 1933c, p.166). As a result it had unnecessarily polarised positions - prompting, for example, the gold bloc counter-declaration above. The bloc, described by Shann as nations 'largely composed of small *rentiers*', were the primary culprits for the lack of international cooperation with 'a reverence for gold little moved from idolatry' (Shann 1933c, p.166).

Shann reserved his harshest criticism though for the United Kingdom, which had missed the 'opportunity to reconcile the unnecessarily opposed claims of external and internal stability'. This was despite being urged on by both the Dominion and the Scandinavian representatives who had otherwise 'left the lead to Britain's more experienced financiers and Treasury men' (Shann 1933c, p.169). When the British delegation had been called upon to take a lead in declaring a definite position the result had been unconvincing. Too much energy had been expended into what Shann described as 'the cult of regulating supply' that 'would, taken by itself, postpone the recovery of industrial production, and perpetuate a standard of living below the world's capacity to produce' (Shann 1934, p.163). On the monetary side he was unhappy with what he saw as the lack of a binding commitment on the part of the United Kingdom to its professed aim of 'cheap money'. It was, he wrote, 'hard to suppress a doubt as to the continued activity of the Treasury and the Bank in maintaining easy credit conditions'. He was still not convinced either that the United Kingdom would still not return to gold, holding with Keynes's assessment that 'those now in authority...are not won over, in their hearts, from an ultimate return to gold as their goal and their ideal'.<sup>130</sup>

Shann's greatest disappointment was in the way the British delegation had so quickly dismissed public works - 'one recognizes here the authentic voice of national finance' (Shann 1933c, p.174). Had these been taken up they 'might have given sterling prices the strong upward movement that the Scandinavian and Dominion Governments asked as basis for a forward policy against unemployment in their own countries' (Shann 1933c, p.172). In these as in earlier writings too, the extent to which Shann embraced what would only become orthodox in the wake of *The General Theory* was extraordinary. The difference was that Shann had now lost faith in monetary policy as the solution. Writing that 'Mr J.M. Keynes is right in looking for the needed balance in equality of saving and capital construction', Shann noted that United Kingdom policy (even if cheap money was maintained) was little more than an attempt at 'coaxing' prices and recovery - as opposed to 'the policy of pushing', which was the case for public works (Shann 1934, p.170). In the end Britain had substituted action for 'an empty assertion of freedom to act', and as a result it was Shann's view that just as Britain had been driven from the gold standard, so may it be to the advantage of countries such as Australia to seek 'the same complete freedom in the management

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<sup>130</sup> Keynes cited in Shann (1934), p.174.

of their own currencies' (Shann 1933c, p.175). The conclusion to be drawn from the failure of the Conference was that countries had to sublimate all to internal conditions, only

when they have grasped the technique of finding and maintaining individual *trim* they may decide to link hands again, but to continue their sober ways alone. That is the logic of the Conference's monetary work, and, in the absence of an effective lead from Britain, it will out. (Shann 1933c, p.175)

Remarkably, the WMEC was the last venue at which a global solution to the Depression was attempted before once again a world war rendered such matters irrelevant. Australia's economists, and particularly those outlined here, remained active in the intervening period, but their activism was confined to matters which were directly concerned with Australia, even if they touched upon its relationship to the outside world. Thus, for example, Australian economists were firm opponents of the 'trade diversion' policy, actively sought reductions in the Scullin 'emergency' tariffs and were strong advocates of an Australian-Anglo-American trade agreement in the latter part of the decade. None of these were indicative of any new theoretical insights, however, and all were symptomatic of that 'preoccupation' and 'brooding pessimism' with regard to the balance of payments that Corden (1968, p.15) nominated as being a defining feature of Australian economics. This pessimistic preoccupation was particularly apparent as the decade wore on, and a recovering (and re-arming) economy once more became tightly constrained by the current account. The worsening global political situation also had a sobering effect, and by 1935 neither Giblin, Copland, Mills nor Melville were any longer willing to advance the use of devaluation as a possible strategy to maintain external balance while allowing expansionary policies at home. A new wave of young economists, many fresh with the insights at that time coming out of Cambridge, England, were beginning to move into positions of influence, but they were not yet firmly established. Cain (1983), one of the very few historians of economic thought who has attempted to tell the story of Australian economists after the worst years of the Depression, traced this developing fatalism through the works of Giblin. His assessment of Giblin's advice, which was equally true of the others, was that it

was informed throughout by a close appreciation of difficulties facing small, primary product exporting, heavily indebted and industrially immature countries seeking to pay their way in a hostile world. There were lacunae in his analytical approach but novelty and sense as well. What he lacked essentially was a theory of income determination which better fitted his intuitions. It was to such a theory, of course, that Keynes was on his way...(Cain 1983, p.218).

## Section II

### *Amateur Idealists*

## Introduction

The advocacy of the Australian economists at the Ottawa and World Economic Conferences occurred at a time when the cult of the ‘expert’ was approaching its apogee. Faith in the wisdom of expert opinion in providing answers to great national questions arrived later in Australia than elsewhere in the world, but by the 1920s it was all pervasive. This was especially so for questions of economics, for which the commissioning of economists for advice on particular issues became a regular occurrence in the decade. Prompting an extraordinary growth and ‘professionalisation’ of the discipline, by the end of the 1920s an Australian economist could proclaim that ‘the economist is (or should be) king in this as in every other country’.<sup>131</sup> Such an economist could also look back on a decade in which had been established the profession’s own association (the Economic Society of Australia and New Zealand), its own journal (*The Economic Record*) and a firm place in the halls of the academy.<sup>132</sup>

Preceding the professional economist, and from the 1920s attempting to find a voice alongside them, was that species which has been described at various times and in various places as the gifted amateur, the crank, the scribbler - contributors to economic discourse from outside the academic establishment whom Keynes collectively categorised as the ‘economic underworld’.<sup>133</sup> In a country in which the establishment of economics on a professional basis was long in gestation the contribution of this underworld to economic policy-making was a long and influential one. Indeed, such a cast ‘were major actors in the drama of the development of Australian economics’ (Groenewegen and McFarlane 1990, p.6).<sup>134</sup>

To this underground belongs the name of Frank McDougall. Rated by Hudson (1980, p.7) as ‘perhaps the most under-estimated man in twentieth-century Australian history’, McDougall was formally a lobbyist on behalf of the Australian Government and certain agricultural interests in London. Less formally, he was much more influential. The representative ‘face’ of Australia in imperial and international forums, McDougall was also the author of many of the positions Australia adopted to these same forums. In company with his great patron and collaborator, the former Prime Minister and then High Commissioner in London, S.M. Bruce, McDougall was the

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<sup>131</sup> The claimant was Copland, here cited in Macintyre (1986, p.240), from a speech he made in 1926.

<sup>132</sup> Faculties of economics had been established at the University of Sydney (1912), Hobart (1920), Melbourne (1923), Perth (1925), Brisbane (1926) and Adelaide (1929). (See Goodwin (1966), pp.555-602). For more on the professionalisation of the economics discipline in Australia, and its forebears, see Fleming (1995).

<sup>133</sup> An underworld about which Keynes wrote appreciatively, for his own purposes, in Chapter 23 of *The General Theory*. The economics profession is, of course, a relatively young one and so before the nineteenth century economic advice was given by people who we would not now regard as economists. Such individuals were scarcely interested in economic questions beyond policy. For more on the underground, and its service to government, see Coats (1989) and Stigler (1973).

<sup>134</sup> Groenewegen and McFarlane provide a review of this ‘old tradition’ in Australian economics. The great majority of the ‘actors’ they survey were concerned with purely domestic affairs, but they also highlight the contribution of one amateur, Leo St. Clare Grondona, to Australian and Imperial affairs. Grondona’s ideas on the latter were very similar to McDougall’s and he was to propagate them as a journalist and in a number of books right up until the 1970s. McDougall had essentially abandoned his imperial vision by the mid-1930s. For more, see Groenewegen and McFarlane (1990), pp.147-172.

initiator of a great deal of what was *taken to be* Australia's economic diplomacy in the interwar years.<sup>135</sup>

McDougall had two big ideas, linked through his perception of 'progressive' economic and social policy, but also separated by time, his changing perceptions of the world, the objectives of Australian governments and his understanding of economic analysis.

McDougall's first big idea was the Australian variation of the attempts to further *imperial economic integration* amongst the countries of what was then the British Empire.<sup>136</sup> A controversial yet irrepressible idea in the United Kingdom, it first emerged with the 'Fair Trade League' in the 1880s but was apparently rendered unsaleable by the defeat of Chamberlain's 'tariff reform' campaigns early in the new century. It was an idea reflecting a dissatisfaction with orthodox liberal economics and Gladstonian finance as much as it was a desire to create an imperial trading bloc. McDougall's version of the idea, which he labelled 'sheltered markets', became more broadly known under Bruce's catch phrase of 'men, money and markets'. It emerged at a time when once more 'progressive' opinion in the United Kingdom and Australia had lost faith in market outcomes, generally in favour of some form of broadly-defined 'planning'. This planning was essentially corporatist in nature and was strongly informed by the demonstrative power of the United States, whose economies of scale were used by McDougall and others in the 1920s as an example of what the countries of the Empire could likewise exploit if only they were to act as one. Notwithstanding his own lack of formal economic training, McDougall placed great faith in the ability of the 'expert' to solve economic and other problems with the appropriate application of 'science'.<sup>137</sup>

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<sup>135</sup> The extent to which McDougall influenced Bruce is the subject of some discussion in the works that have dealt with their activities, especially in the three biographies of Bruce that have appeared thus far. Gladwyn Jebb, a long-time associate of both McDougall and Bruce, wrote in his own autobiography that 'McDougall was a fascinating and brilliant man who to a great extent used Lord Bruce, ex-Prime Minister of Australia, as a vehicle for his own ideas' (Jebb 1972, p.63). Bruce's biographers, Edwards (1965), Stirling (1974) and Cumpston (1989) are in general agreement as to the strength of McDougall's influence, although Stirling (1974, p.31) took umbrage at Jebb's assessment that McDougall 'used' Bruce. Elsewhere (1974, p.31) he quoted McDougall on Bruce: 'He is one of the most intelligent men you could find, but not an intellectual. He seizes on principles but does not evolve them. He knows what will work and what will not'.

<sup>136</sup> Technically it was the 'British Commonwealth' but this expression was seldom used until much later. The use of the word 'Empire' in this section is in accordance with the context of the times, and should not be read according to more modern interpretations. Critics of the Empire abounded in this period, of course (and in whose number McDougall could be counted on occasion), but the term itself did not usually carry for its Australian users the flavour of colonial subjugation which others attached to it.

<sup>137</sup> A loose movement that originated in North America, 'progressive' thought was enormously influential in intellectual and political circles in a great many countries from the 1890s and through the 1920s. An organised and named political force only in the United States, progressivism embraced a great many causes, from economic policy, the environment, to child rearing. It was closely aligned with the cult of the expert - whose application of 'science' and 'efficiency' were the keys to the creation of a good society. What distinguished it from other liberal paradigms was its belief in the use of State power (yielded by the experts) as a beneficent force. Progressive movements typically placed great stress on moulding and improving society through education, nutrition and physical fitness. From his earliest to his last writings McDougall's ideas were archetypes of the progressive project. For more on progressivism generally, see Jones (1995). For its influence in Australia, see Roe (1984).

McDougall's second idea, like the first, was a mixture of genuine idealism with a policy prescription consistent with Australia's narrow economic interests, concerned a programme of international economic and social initiatives broadly known as the *nutrition approach*. So called by McDougall and by a later group of Australian economists seeking similar ends the next decade (Section III in this study), the nutrition approach was propagated as a means by which to restore world agricultural production on the basis of comparative advantage. It was not an exhortation of the benefits of free trade, but of the implications of the newly emerging 'science' of nutrition, that divided food groups into those whose production was best sourced locally, and the great staples whose production was best sourced according to comparative advantage-based trade. By promoting both local production and the *trade* in foodstuffs, the nutrition approach was designed to solve what McDougall identified as the most pernicious anomaly of the Great Depression - the coexistence of 'overproduction' of foodstuffs together with the malnourishment of much of the world's population. The latter was primarily due to a lack of purchasing power amongst certain groups in industrial countries. In the primarily agricultural producing countries it was, to use Keynes's term, a consequence of a more general deficiency of aggregate demand, and a result of falling exports due to agrarian protectionism. By re-opening the channels to international trade in food, the nutrition approach was presented as at least a partial solution to the problems of the agricultural producers. Its accompanying programme of greatly enlarged social welfare spending was designed to increase effective demand in the industrial countries.

Reflecting a disillusion with markets and faith in the 'expert', in scientific progress and in corporate planning structures, the nutrition approach was one of a number of non-academic and partisan campaigns that emphasised international effective demand via a crude *proto-Keynesianism* long before it was fashionable to do so. Later broadened into a general campaign for improved 'living standards' and for 'economic appeasement', the nutrition approach was adopted by a League of Nations searching for legitimacy, by 'progressive' political movements and, finally, by governments in the Second World War.

Like most members of the economic underworld, McDougall has not been well served by historians, economic or otherwise. In the context of his ideas for 'sheltered markets', references to him are contained in the small number of works dedicated to the history of imperial relations between the wars. In these he is usually portrayed as the tough Australian negotiator of interminable imperial conferences.<sup>138</sup> Missing from these accounts is McDougall the initiator and formulator of Australian economic policy, McDougall the active agent in Australian economic diplomacy, and McDougall the theorist for an *imperial* economic policy. Hancock's 1940 *Survey of British Commonwealth Affairs*, the seminal work on Commonwealth economic relations between the wars which in spirit and style of language betrays the influence of McDougall, makes no mention of him by name. Drummond (1972 and 1974) who, next to Hancock, has produced the most comprehensive examination of the period, looks no further into the role of McDougall than the endless negotiations between Australia and the United Kingdom over meat and other primary products. A more recent study of Commonwealth commercial policy by Rooth (1992) does not mention

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<sup>138</sup> Reflecting what Attard (1994, p.3) perceptively identified as the 'predominantly nationalist historiography' which has been most often applied to Anglo-Australian relations of the period.

McDougall at all. O'Brien (1987), Tsokhas (1989, 1990 and 1992), and Roe (1995) allocate to McDougall a role in the particular areas they examine, but the purpose of their works was not to explore the *economic* ideas which lay behind his actions. In 1986, Australia's Department of Foreign Affairs and Trade redressed matters somewhat by publishing (McDougall 1986) the surviving correspondence between McDougall and Bruce between 1924 and 1929, but thus far this resource has been little analysed.

The most complete account of the nutrition approach is to be found in institutional histories of the Food and Agricultural Organisation of the United Nations (FAO), the body whose establishment in 1945 was the legacy of McDougall's work. However, the account in these is very incomplete and, more broadly, the neglect of the nutrition approach in historical narratives has been much greater than the neglect of McDougall's advocacy of his imperial model. Outside of the FAO, what has been written on the nutrition approach is largely confined to the periphery of the biographies of Bruce, (Edwards (1965), Stirling (1974) and Cumpston (1989)), or to works examining some aspect of Bruce's activities (Jebb (1972), Stirling (1973), Attard (1994)).

In the following chapter, an attempt is made to remedy this neglect and, in the process, to place McDougall's work at the centre of the 'expansionary bias' which, according to this thesis, informed Australia's external economic diplomacy during the period under examination. Much better known to the wider world than the advocacy of Australian economists at Ottawa and the WMEC, McDougall's work heralded the disproportionate influence Australian economists were to enjoy when, with the arrival of another world war, that which was unfashionable and unfeasible in economics suddenly became possible and, even, *de riguer*.

## **Chapter Four**

### **F.L. McDougall**

#### **4.0 ‘Sheltered Markets’**

Like many of those whose ideas were to help shape Australian economic thought, McDougall was not born in Australia, but in London, in 1884. His background bestowed much in cultural capital (McDougall’s father had been Chairman of the London Council) but little in financial wealth. In 1907 McDougall left England for Renmark, South Australia, where he took up fruit farming. Following the First World War he became highly active in industry affairs. Elected to the Federal Council of the Australian Dried Fruit Association, McDougall became convinced that the future of the industry depended upon its ability to gain preferential access to the British market.

In 1922 McDougall was selected by the Dried Fruits Association to be part of a delegation (part financed by the Commonwealth Government) to lobby for tariff preferences in the United Kingdom. But while tariffs were common in Australia, they were anathema in nominally free-trade Britain. The issue had been a highly politicised one since the defeat of Joseph Chamberlain’s attempts to create imperial unity through tariffs and preferences in 1906, and it was to cost the Conservative Party office again at an election fought on the same issue in 1923.<sup>139</sup> Nevertheless, the idea that tariffs and preferences could construct the material conditions for imperial unity remained potent in Britain, stimulated by residual wartime sentiment.<sup>140</sup> Despite the sensitive nature of the undertaking, Bruce (then Commonwealth Treasurer) agreed with McDougall that the future viability of much of Australia’s agricultural sector depended on tariff preferences. Accordingly, he instructed McDougall prior to his departure that ‘the main duty of the delegation was to prepare the ground for further preference proposals by the Commonwealth Government’.<sup>141</sup>

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<sup>139</sup> At the beginning of his quest, Joseph Chamberlain had been Colonial Secretary in the Unionist (Conservative) Government of Arthur Balfour. His campaign split the government and precipitated its defeat at the hands of the free-trade Liberals (who successfully exploited the idea that tariffs were ‘stomach taxes’) in the election of 1906. Accounts of Chamberlain’s campaign to construct an imperial *zollverein* abound, but by far the most comprehensive is Garvin and Amery (1969). For an account of the *economics* of the movement see Gomes (1990) and, most recently, Groenewegen (1995), pp.376-398.

<sup>140</sup> In the aftermath of the First World War, a great many schemes were advanced to fashion a ‘self-sufficient’ Empire. They received some official sanction at the hands of the so-called Dominions Royal Commission in 1917 and by certain resolutions of the Imperial War Cabinet in 1918. For more on the diversity of these schemes, and the role of Australian Prime Minister, W.M. Hughes, in working this sentiment, see Hancock (1940), pp.94-110. Such schemes were components of a greater imperial mythology which had it that, notwithstanding its losses in the war and the rise of the United States, British pre-eminence remained intact. For Australia, this bred the illusion that Australia remained within the protective umbrella of the ‘brotherhood of free British nations across the seas’ (Andrews 1993, p.5). The shattering of the imperial vision would come when it was realised that the interests of Britain and its former colonies were not necessarily one and the same. The first inkling of this came at Ottawa in 1932, but it took the Second World War to break it completely. For more on these broader issues of Empire and Australia, for which there is an abundant literature, see Andrews (1993), Cain and Hopkins (1993), Madden and Morris-Jones (1980) and Drummond (1974).

<sup>141</sup> ‘F.L. McDougall to his brother Norman, 8 February 1923’, National Library of Australia (NLA), ‘F.L. McDougall Papers’, MS 6890, Box1, Folder 1. Biographical details for McDougall have been



McDougall found considerable success as an advocate and quickly established a comprehensive network of influence across the spectrum of British politics, the press (most especially *The Times*, for whom he often wrote as a 'special correspondent'), and the representative bodies of industry and organised labour. His conception of an 'imperial' economic policy, too, was evolving. In *Sheltered Markets: A Study in the Value of Empire Trade* published in 1925, he set out the economic case for 'men, money and markets' within the context of an imperial division of labour.<sup>142</sup> 'Men' simply referred to British emigration to the 'Dominions' but the other two components of the triumvirate were more complex. To secure 'markets', for example, McDougall advocated not only tariff preferences but also the wholesale reorganisation of the trade in food and raw materials via 'import and export control boards' (McDougall 1925, p.11).<sup>143</sup> These would strongly favour empire producers, to the extent indeed of creating 'semi-domestic' markets which, in turn, would provide British manufacturers with markets large enough to take advantage of the 'methods of mass production' which had so favoured the United States. 'Markets' also meant spending by the British Government on improving the living standards of indigenous peoples in what McDougall referred to as the 'non self-governing' territories. Improvements in the living standards of such peoples and increases in their purchasing power would make available 'immense reserves of prosperity... to the whole Empire' (McDougall 1925, p.115).

The provision of 'money' was similarly couched in expansionist terms in *Sheltered Markets*, with McDougall advocating that the British and Dominion governments not only provide capital themselves for projects of 'empire development', but also encourage the flow of private capital. The projects he had in mind were enormous, including, for Australia, the construction of rail lines linking all ends of the continent and large irrigation and soil improvement programmes with the aim of establishing intensive settlement.<sup>144</sup> In *Sheltered Markets* and elsewhere, McDougall constantly complained of the 'cheeseparing in the supply of money' from the British Treasury under Sir Otto Niemeyer for empire development projects.<sup>145</sup>

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gleaned from these papers and from the introduction to McDougall (1986) by W.J. Hudson and W.Way.

<sup>142</sup> 'Men, money and markets' was first articulated by (now Prime Minister) Bruce before the 1923 Imperial Economic Conference from a speech substantially written by McDougall.

<sup>143</sup> It was McDougall's contention that the purpose of the regulation of imperial production via import and export control boards was not to *raise* the prices of primary products, but to provide price stability for Dominion producers by finding an assured market (McDougall 1925, p.134). That this should be the case, when such regulation pointed so obviously in the direction of raising prices, was due to that old favourite of McDougall's, scale economies. His view was that as Australia and other Empire producers expanded their exports to meet United Kingdom requirements (other producers having been excluded), they 'could confidently concentrate on increasing output to effect a gradual reduction in cost of production per unit of output, upon improvement in quality and would be enabled to work on closer margins' (McDougall 1925, p.133). Of course, this claim was a vital one if the concept was to be sold to a British government ever wary of being landed with a 'food-tax' controversy of the Chamberlain variety.

<sup>144</sup> In this he was in sympathy with a great many 'cranks and scribblers' in Australia, who likewise typically held cornucopian visions of Australia's potential. For more on these, see Groenewegen and McFarlane (1990), pp.147-172.

<sup>145</sup> McDougall wrote that Niemeyer was 'an always available cold water douche on any schemes of Empire development'. McDougall to Bruce, 25 May 1927, in McDougall (1986), p.365.

McDougall's advocacy of his imperial model continued throughout the 1920s, and he was to align himself increasingly with sections of the British Labour Party, organised labour and with the 'left wing' of the Conservative Party under the loose leadership of Harold Macmillan.<sup>146</sup> This alignment was consistent with his inclinations, but it was also strategic. The left, he wrote, could 'preach "Empire" in their own way and in their own words without being branded as reactionary imperialists'.<sup>147</sup> By contrast, McDougall had comparatively little to do with the empire schemes of British industrialists that increasingly became a feature of British political economy in the late 1920s. The most prominent of these, the 'Empire Free Trade' campaign of Lord Beaverbrook, he judged to be 'hopeless'. McDougall did, however, contribute a number of articles on the value of empire markets to Beaverbrook's newspapers.<sup>148</sup>

McDougall had been careful throughout to cultivate Neville Chamberlain, the son of the original 'tariff reformer' and a Conservative imperial advocate whom McDougall found to be the most 'realistic' and most likely to achieve practical results.<sup>149</sup> In the end this was precisely how it turned out, and it was Chamberlain who, in February 1932 as Chancellor of the Exchequer, announced the introduction of the Import Duties Bill with its 10 percent *ad valorem* tariff (Garside 1998, p.62). Significantly for the imperial cause, Chamberlain's announcement included provision for the negotiation of imperial preferences at the coming Imperial Economic Conference in Ottawa.

#### **4.1 Disillusionment**

The imperial model was a persistent one and, on its own terms, made some sense. Attacked in the contemporary economics literature on the basis of its offences to the case for free trade, it was nevertheless consistent with alternative traditions (notably English dissenters in the manner of the German 'Historical School'), that rejected calculating 'national' economic welfare as the sum of utilities enjoyed by individuals as private consumers, in favour of an approach which assumed some 'public

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<sup>146</sup> Including, too, the Trade Union Council (TUC), the representative body of British organised labour. The TUC itself began to espouse imperial markets as the 'natural' outlet for British manufactures in the late 1920s, and in 1928 even recommended the creation of import and export control boards of the type favoured by McDougall for the trade in agriculture. Labour's traditional hostility to a 'food tax' quickly led to the abandonment of the idea, but the favourable view of Empire markets remained (Booth and Pack 1985, p.99).

<sup>147</sup> McDougall to Bruce, 3 September 1925, in McDougall (1986), pp.84-87.

<sup>148</sup> Details of McDougall's links with Beaverbrook can be found in 'Notes and Comments, F.L. McDougall, 1925-34', Archives of the Food and Agriculture Organisation of the United Nations (FAO), Frank McDougall Papers, RG 3.1. For more on Beaverbrook's extraordinary campaign see Chisolm and Davie (1992). McDougall also had only limited contact in this regard with the Federation of British Industries (FBI). The FBI had been established with the explicit aim of promoting corporatist and imperial solutions to Britain's economic problems. For most of the inter-war years the FBI was headed by Sir Alfred Mond, the founder of Imperial Chemical Industries, who regarded imperial unity as the best way to gain markets large enough to yield the economies of scale necessary if British manufactures were to compete against those of the United States. A curious mixture of autocrat and progressive, Mond saw limits to market forces and believed in an evolutionary process favouring larger economic units. He advocated high wages and the involvement of labour in corporate governance, an advocacy that led to the famous Mond-Turner (TUC) talks of 1928. These produced a joint statement of the TUC and the FBI on imperial economic policies. For more, see Booth and Pack (1985, pp.84-93) and McDonald and Gospel (1973).

<sup>149</sup> See, for example, McDougall's account of his meeting with Chamberlain, 'McDougall to Bruce', 25 July 1925, in McDougall (1986), pp.870-871.

preference' - in this case, imperial unity.<sup>150</sup> Of course, the proponents of the imperial idea tended to hold very different assumptions about the world they inhabited that, in contrast to the Ricardo-Marshall tradition, included the existence of persistent unemployment, a barely functioning gold standard, extreme differences in income distribution, barriers to trade elsewhere and the inviting prospect of scale economies. In contrast to Ricardo-Marshall, both capital *and* labour were mobile, but there was nothing in their movement in the absence of intervention which would maximise the output possibilities of the Empire.<sup>151</sup>

According to Drummond (1974, p.127), the campaign for imperial economic integration in the inter-war years was also a proto-Keynesian doctrine which recognised what it could not articulate theoretically - that 'more borrowing and more real investment would generate higher prosperity, employment and income' within the Empire. While care must be taken with this assessment, there is a modicum of truth in it. Explicit in the writings of McDougall and other Empire idealists was a belief that if the old liberal market order was inconsistent with their central objective (imperial economic unity), it was also no longer the vehicle to provide for a dynamic or prosperous economy. It was deficient purchasing power (what we would now call deficient demand) that was the cause of the persistent unemployment since the war, and an expansion in demand was the only socially acceptable way to bring about new investment and new jobs. That this expansion in demand would have to come, in the view of Empire idealists, from state expenditure on schemes of Empire development was a function of three factors.

Firstly, it was (of course) the main purpose of the McDougall and the Empire idealists to re-orientate the British economy towards the Empire, a re-orientation that would require British capital to provide the stimulus to the growth of Empire markets that, in turn, were essential for the growth of British exports. Secondly, there was in the imperial model an explicit recognition of the external constraints against national expansion. Britain's persistent weakness in its external accounts, the accumulation of war debt and the related issue of moving to (and maintaining) the gold standard at its pre-war parity were problems that, together with unemployment, were to dominate policy-making throughout the inter-war period.

Thirdly, and perhaps most importantly in this discussion of policies in a context in which the political and economic discourse had not yet been 'Keynesianised', was that McDougall and other idealists made an argument for increased government spending which ran counter to the 'canons of sound finance'. According to sound finance, such spending was either inflationary or a diversion of funds from private

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<sup>150</sup> The most significant individual in this tradition was W.A.S. Hewins, Alfred Marshall's *bête noir* during the 'tariff reform' debates and the first Director of the London School of Economics. For more on Hewin's conflict with Marshall, see Groenewegen (1995), pp.376-389.

<sup>151</sup> Regardless of ends, the imperial model continued to be attacked throughout the inter-war years, mostly along the lines of Marshall's objections to Chamberlain's version years earlier. Most tellingly in this regard was *Tariffs: The Case Examined*, a book written by a committee of economists under the chairmanship of Sir William Beveridge that was published in 1931. Among the many contributions was one by J.R. Hicks on the issue of import and export control boards. These were integral to McDougall's schemes but, as noted earlier, they had a strong following in sections of organised labour. Hicks savaged the idea, rejecting the notion of scale economies and the idea that a central organisation could pick prices any better (or fairer) than those that prevailed in free markets. For more, see Hicks (1931).

investment. These objections, moreover, were much broader than those concerned with economic theory. The historically determined perceptions as to the proper balance between state and society likewise told against such actions. The First World War had brought with it a tremendous growth of the state and this, coupled with the anxiety of political leaders in dealing with the new demands of mass politics (the bills granting universal male suffrage in the United Kingdom had been passed in 1918), highlighted the role that balanced budgets could play in defining the limits of government.<sup>152</sup> Schemes for spending on Empire development involved issues which transcended class divisions on spending, kept the state in a traditional role of advancing trade behind the flag, and were pitched to appeal to the very audience most likely to resist increased state activity for any other purposes. Investment in the Empire was not the only, nor probably the most effective, form that government spending could take in bolstering purchasing power (effective demand at home), but it was possibly the only viable option politically.

Yet, if a possible conclusion from the above is that the imperial model, and McDougall's version in particular, was not the theoretical nonsense which has sometimes been portrayed, it did not necessarily follow that it was also right. Hancock (1940, p.103), in looking back at a campaign that had barely ended, asserted that, despite its 'impressive logic', the imperial model was built upon significant assumptions with 'no sure foundation in historical reality'. The first of these, that the 'distinct self-governing communities of the Empire' had the will to return to a situation in which national economic policy was subordinate to the imperial whole, was an idea which ran counter to the trend of historical development. In retrospect, it was apparent that 'the Empire as a whole' was, in fact, a meaningless concept. There did not exist in the 1920s an economic unit that *was* the British Empire. Dominion governments and the government of the United Kingdom, could not, and did not, distinguish between 'Empire' and 'international' trade and commerce. Individual enterprises and governments cared that their production was sold, to whom was not vitally important (Hancock 1940, p.205). Further undermining the claim for the existence of an *imperial* economic unit was the fact that if the imperial centre was removed there was almost no trade between the other constituent parts. The British Empire was, in an economic sense, little more than a series of bilateral relationships between the United Kingdom and its existing and former colonies (Hancock 1940, p.207, Holland 1981, pp.23-39).

These short-comings of the imperial model became apparent to McDougall at the moment of its apparent triumph at Ottawa. At Ottawa, imperial preferences finally became policy in the United Kingdom, the shape of which owed something to the bargaining skills of McDougall and Bruce (Resident Minister in London from 1932 following his electoral defeat in 1929, and High Commissioner from 1933).<sup>153</sup> But the Ottawa agreements did not live up to the expectations of those who had seen in imperial preferences both a device allowing for an expansion of trade and a regime for channelling it along the lines of Empire development. Rather than an expansionist framework, the Ottawa agreements granted preferences only by the imposition of ever

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<sup>152</sup> For more of this idea, see Booth and Pack (1985).

<sup>153</sup> Of course, the most important factor in the final emergence of tariffs and preferences was just the sheer scale of the collapse of world markets - and the role of the United Kingdom as a market of last resort.

higher barriers against outsiders - significantly, in the United Kingdom, introducing tariffs, quotas and other barriers on most goods for the first time. In the end, Ottawa did nothing for the psychology of imperial unity either, being little more than a series of acrimonious bilateral bargaining sessions between the Dominions and an increasingly bitter United Kingdom.<sup>154</sup>

## **4.2 The 'Nutrition Approach'**

From 1933 McDougall and Bruce both came to believe that Australia's best hope for recovery lay in 'resolute and determined efforts to secure a revival of *world trade*...through an expansion in international demand' (emphasis added, Australia, Parliament 1933, p.14). This belief they took to the World Monetary and Economic Conference, the monetary aspect of which has been examined in Chapter 3. The Australian delegation to the Conference was led by Bruce. Along with Melville, Copland and Shann, who had virtual free reign on monetary matters, McDougall travelled as Bruce's principal economic adviser.

In later years Bruce was to claim that it was after the failure of the WMEC that his and McDougall's attention swung to the idea of nutrition.<sup>155</sup> According to Bruce's account, following the failure of the Conference he met with McDougall and Sir John Boyd Orr in order to arrive at a new way in which to approach questions of trade, protection and international economic policy. Recognised as a world expert on the newly emerging science of human nutrition, Orr's enthusiasm for his subject had greatly affected McDougall, who told Bruce in 1927 that he 'knew of nobody in the scientific world who has so clear a grasp of the economic objectives'.<sup>156</sup> In 1934 Orr was conducting research into the links between poverty and malnutrition. His findings, that half the British population had an income insufficient for basic nutritional requirements, were published in 1936 in his book *Food, Health and Income* and became enormously influential.<sup>157</sup>

This small group concluded that to approach the ills of the world economy via proposals to lower trade barriers or stabilise exchange rates, as the WMEC had sought to do, was to confuse the means of economic policy with its ends. Rising living standards, good nutrition and high levels of employment were the ends of economic policy and the issues which appealed to the 'average man and woman'. In the absence of clearly enunciated policy ends, proposals for freer trade or stable exchange rates were unlikely to survive assaults from special interest groups. In a memorandum written in 1934 that brought the group's ideas together (and from which all of the following is cited), McDougall argued that 'a wholly new approach was required if

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<sup>154</sup> Some idea of the degree of acrimony the Ottawa talks provoked can be glimpsed in Tsokhas (1989 and 1990), Drummond (1974), Holland (1981) and O'Brien (1987).

<sup>155</sup> See, for example, his account in Edwards (1965), pp.414-415.

<sup>156</sup> McDougall to Bruce, 16 November 1927, NAA M111 1927.

<sup>157</sup> Orr was later to become the first Director-General of the FAO and, in 1949, won the Nobel Peace Prize for his works.

governments were to find themselves with sufficient popular support to really undertake sensible economic policies'.<sup>158</sup>

Entitled *The Agricultural and the Health Problems*, McDougall's memorandum was based on an idea then emerging in the science of nutrition that food could be divided into two groups - 'energy' foods (traditionally the largest component of the diet, primarily cereal based products and normally traded in large volumes) and 'protective' foods (thought then to be especially essential in warding off disease and rich in the newly discovered 'vitamins'). The protective foods included fresh fruit and vegetables, eggs, meat and dairy products. Such foods tended not to be traded in large volume.<sup>159</sup>

Citing recent League of Nations research in the memorandum, as well as the results of Orr's surveys, McDougall argued that much of the world's population was malnourished. For countries in Europe and North America this did not necessarily imply that large numbers of people were starving, but it did mean that they maintained diets with insufficient quantities of protective foods. The cause of the imbalance according to McDougall was the high price of protective foods which, together with their relatively high elasticity of demand, meant that their consumption occupied only a small part of the diet of the poorer members of society.

McDougall contended that the most important reason for the high (retail) price of food was agricultural protectionism. Since the end of the war (and especially since the onset of depression), restrictions on agricultural imports had become increasingly severe in almost all industrial countries.<sup>160</sup> Agricultural protectionism meant that nutrition would be adversely affected, moreover, regardless of the specific foodstuff subject to restriction. A tariff on wheat would not reduce its consumption greatly since, as the principal source of calories for much of the population, its consumption was relatively price inelastic. Because it occupied such a large proportion of the average food budget, however, an increase in the price of wheat would result in a considerable reduction in consumers' real income, leaving less money available for other foodstuffs. Since protective foods tended to be both highly priced and highly price elastic, it was the consumption of these foods, important though they were for good nutrition, that would fall.

There was, of course, a paradox in all of this. Side by side with poor nutrition were ever growing surpluses of agricultural products. Restrictive trade policies in certain countries ensured that their domestic producers received higher prices than those prevailing in world markets, thus stimulating output and shielding inefficient methods

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<sup>158</sup> 'The Agricultural and the Health Problems', 1934, FAO RG 3.1, Series D1, Notes and Comments F.L. McDougall, 1925-34.

<sup>159</sup> The ability to transport such foodstuffs over long distances was problematic until the Second World War. Transporting frozen meat, for example, had been done for some time but the ability to ship chilled (fresh) meat was only financially viable in the latter part of the inter-war period (Dyster and Meredith 1990, pp.64-66).

<sup>160</sup> Installed to protect balance of payments positions after the onset of the Depression, agricultural protectionism was evident in many countries following the First World War. By no means the most damaging nor lasting legacy of that war, it was nonetheless a policy driven by the perceived necessity for countries to ensure security of supply in food and other raw materials in case of another war. There is an enormous literature on the collapse of the liberal-internationalist order in the wake of the First World War but one of the best, and most enduring accounts, is Arndt (1944).

of production. Effectively subsidised by the consumer, a number of normally food-importing countries in Europe had become almost self-sufficient. While ‘almost every country...is familiar with the situation of supplies in excess of available demand’, it was not, according to McDougall, an excess supply judged by the nutritional needs of the world, but merely by a lack of purchasing power.

But the harm done by agricultural protection was not limited to the consumer in the industrial countries. The restriction of trade in agricultural products reduced the income of the food-exporting countries both through the reduction in the quantity of their exports and because of the depressive impact of protectionism on wholesale commodity prices in glutted *world* markets. This lowered not only their living standards but also their ability to purchase the manufactures of industrial Europe.

Reducing the *retail* price of food was the most important single measure by which better nutrition could be secured. It was also, according to McDougall, the means to a solution of the crisis in world agriculture. Cheapening the price of food required a reorientation of agricultural production on the basis of comparative advantage. European agriculture, based on small holdings, high value land, high labour costs and short growing seasons, was ‘better suited to mixed farming embracing mainly animal husbandry and small crops’ than to the large scale cereal cultivation that it was presently attempting to emulate. Such farming, in other words, was best suited to the production of the protective foods.

The production of protective foods in the industrial countries would, under a ‘nutrition approach’ to agriculture, *displace* the production of energy foods and re-open the channels of trade in such commodities. The mostly food-exporting countries, as the cheapest and most efficient producers of energy foods, stood not only to regain this trade but also additional trade, flowing from the *increased* consumption of these foods, both from the world’s poorer countries in which people *did* go hungry, and from the increased demand for animal fodder in the industrial world.<sup>161</sup> No less real were the benefits accruing to the industrial countries from a reorientation of agriculture, where increased demand for food imports would likely be more than offset by ‘the beneficial effects upon their industrial exports’. It was a move to freer trade, but it was dressed in very different robes.

Giving McDougall’s memorandum a radical flavour were two other measures designed to improve the ability of the ‘poorer classes’ to obtain the foods necessary for good health. The first of these was simply a demand for a redistribution of wealth and income. In the original memorandum, McDougall did not elaborate on what this might mean, other than it would include higher taxation and a vague reference to ‘measures to increase the proportion of the profits of industry paid to employees’. McDougall thought that with the election of Roosevelt and his championing of ‘the cause of social justice’, government actions to secure a more equitable distribution of wealth were likely to meet less resistance than previously. In any case, he warned that ‘the well-to-do classes must increasingly realise that, at least for some time to come, the alternative to such endeavours as Mr. Roosevelt is making is not a swing back to the right but wild schemes of confiscation from the extreme left’.

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<sup>161</sup> A consequence of the increased consumption of meat in the industrial countries.

The second measure designed to improve access to basic foodstuffs was a favourite of McDougall's - indeed, it was one which was a standby for 'progressive' opinion generally in the interwar years - the exhortation for 'efficiency' in distribution.<sup>162</sup> McDougall pointed to the 'large profits' made by the 'great distributing and processing firms' during even the worst years of the Depression as evidence of exploitation, and suggested that perhaps the time had come for such activities to be made the preserve of public utilities. He also proposed the creation of 'cash and carry' food markets in industrial areas as a counter to the rent-yielding 'credit and delivery systems' of retailers.<sup>163</sup>

### *Propagating the 'Nutrition Approach'*

After unsuccessfully attempting to enlist the support of the British Government in promoting what they now called the 'nutrition approach', McDougall and Bruce took up the propagation of the idea themselves. Their first success came in June 1935 when they persuaded Australia's delegate to the annual conference of the ILO, Sir Frederick Stewart, to move that the ILO investigate the question of workers' nutrition and whether measures designed to improve it could also 'raise standards of life and reduce the depression in agriculture'. Stewart's resolution was adopted unanimously and in 1936 the ILO published the results of its enquiries in *Workers Nutrition and Social Policy*.<sup>164</sup>

It was, however, the League of Nations that was the focus of McDougall's and Bruce's efforts. By 1935 both had become increasingly involved in the work of the League and increasingly convinced of its worth as a vehicle for advancing economic and social goals. Australia's chief delegate to the Assembly since 1932, Bruce was appointed to a seat on the League Council in 1933, became its rapporteur on financial and economic questions in 1934 and became President of the Assembly in 1936. McDougall had been Australia's delegate to the League's Economic Section since 1927 as well as Australia's substitute delegate to the Assembly. McDougall was impressed with the work of the Economic Section, writing to Bruce in 1928 that it could be of 'very considerable use to the world, to the British Empire and to Australia'.<sup>165</sup> Concerned that it could be captured though by the 'economic doctrinaire', McDougall also found himself regarded 'as the spokesman of those who are opposed to the League tying itself up with free trade dogma'.<sup>166</sup>

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<sup>162</sup> The idea that foodstuffs (especially) were made expensive by distributors (who exploited *both* the farm producer as well as the consumer) was pervasive amongst 'conservative' and 'liberal' dissenters in the inter-war years as much as it was a feature of 'socialist' tracts. See, for example, Macmillan (1938), pp.66-89.

<sup>163</sup> It must be remembered, of course, that McDougall was writing before the advent of the modern supermarket. In a later memorandum he wrote of the success of retail enterprises such as 'Woolworths, Sears and Roebuck, Boots, or Marks and Spencer' in supplying mass consumer goods but noted that, '[i]n most countries this modern trend has not been applied to food'. Memorandum by F.L. McDougall, 'Economic Appeasement', 21 December 1936, Public Record Office (United Kingdom - Kew) (PRO): Foreign Office Files, FO 371/21215, W373/5/50.

<sup>164</sup> For details of Stewart's speech to the ILO and the resolutions adopted see Australia, Parliament (1936).

<sup>165</sup> 'McDougall to Bruce', 24 May 1928, in McDougall (1986), pp.578-583.

<sup>166</sup> 'McDougall to Bruce', 9 May 1928, in *ibid.*, p.568.



Bruce and McDougall remained reluctant, however, to be seen as the initiators of the nutrition approach lest Australia 'be accused of putting forward a rather cunning device to get rid of our wretched surplus product'.<sup>167</sup> It was also, according to Bruce, 'absurd that little Australia should be the father of this great conception'.<sup>168</sup> The idea of linking nutrition, health, agriculture and economics 'was the sort of idea that ought to be produced by a great power'. With this in mind, Bruce again approached the United Kingdom and, after having his own entreaties rejected once more, convinced Australian Prime Minister Joseph Lyons to approach the British Government. This also having failed, Bruce 'hawked it to every government I could think of'. He tried France and then Italy, 'but none of them could see it and none would touch it'. They thought 'our heads were in the clouds... So, very regretfully, we decided that I had to take the plunge'.<sup>169</sup>

Bruce launched the nutrition approach at the League's annual Assembly at a time of increasing tensions in international affairs.<sup>170</sup> Notwithstanding this, the launch was extremely successful. Discussion on the idea continued for three days, and in the end the Assembly produced a set of resolutions identical to the draft presented by Bruce. The Assembly also appointed a 'Mixed Committee' of agricultural, economic and health experts to take the issue further. McDougall represented Australia on the Committee and became its driving force. The Mixed Committee's final report was presented to the Assembly in 1938 and published the same year. Largely written by McDougall and a faithful representation of his ideas, the *Final Report of the Mixed Committee of the League of Nations on the Relation of Nutrition, Agriculture and Economic Policy* became the League's largest selling publication ever. The Report was also critically well reviewed, the *New York Times* calling it 'by all odds the most important book published in the year'.<sup>171</sup> Alexander Loveday, the Director of the Economic and Financial Section of the League thought, somewhat rhetorically, that its implications were indeed profound:

The nutrition campaign seems to me to be of paramount importance not only on account of its immediate object...but on account of the influence it is likely to have on our whole economic outlook. Ever since the time of Adam Smith economic thought has centered around the art of production or the conditions of citizens as producers. The nutrition movement reflects the first serious endeavour, certainly on an international scale, to consider the economics not of production but of consumption.<sup>172</sup>

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<sup>167</sup> Bruce cited in Edwards (1965), p.415.

<sup>168</sup> *ibid.*

<sup>169</sup> *ibid.*, p.416.

<sup>170</sup> The dispute between Italy and Abyssinia was the principal item on the agenda of the 1935 Assembly of the League (League of Nations 1935).

<sup>171</sup> Cited in McDougall (1938), p.14.

<sup>172</sup> Loveday cited in Lamartine Yates (1955), p.41. The nutrition approach also appeared in the political manifestos of a whole range of groups in the 1930s, but none more prominent than that group of 'left-wing Conservatives' under the loose leadership of Harold Macmillan. The most prominent of the non-socialist 'radicals' in the United Kingdom in the inter-war years, Macmillan and his acolytes shared with McDougall a faith in corporatist structures to replace the 'anarchy' of the market and to re-invigorate the British economy. In successive publications, from *Industry and State* (1924) through to *The Middle Way* (1938), Macmillan and his loosely aligned group demonstrated their faith in the 'expert' who, armed with the 'facts', would determine economic policy (Booth and Pack 1985, pp.59-61). The nutrition approach featured prominently in *The Middle Way*, where statistics provided by Orr

The Mixed Committee Report recommended the establishment of *national* nutrition committees, through which most of the practical steps in improving nutrition could be undertaken and which would be co-ordinated by the League. By 1938 over 30 of these had been established including Australia, following Bruce and McDougall's lobbying of Lyons. These were effective, though perhaps not in ways their original promoters might have envisaged. They were used, for example, as the administrative machinery for rationing in a number of countries during the Second World War. In the United Kingdom, the successor to its nutrition committee presided over a regime in which nutritional standards were 'maintained, and perhaps even improved' during the course of the conflict (Hammond 1951, p.220). To the adherents of the nutrition approach this was not a surprise since, of all the devices available, rationing represented the most complete means of directing consumption (and pegging prices) according to nutritional needs rather than according to income (Hammond 1951, pp.218-230).<sup>173</sup>

#### **4.3 'Economic Appeasement'**<sup>174</sup>

Following success at the League, McDougall sought to expand the nutrition approach after 1936 into a much broader campaign for improving living standards through social provision and policies designed to stimulate aggregate demand. Regarded as intrinsically worthwhile in their own right, these measures were also considered as essential to addressing the economic ills which McDougall was certain lay beneath the increasing political tensions between nations. The campaign, which McDougall most often referred to as 'economic appeasement', followed his by now usual pattern of personal advocacy and the placement of memoranda with prominent individuals and organisations. He eventually produced countless of these memoranda, their tempo and sense of urgency increasing as the decade wore on.<sup>175</sup>

Of course, the idea that economic considerations were a force in determining peace and war was hardly a radical one, especially not in the United Kingdom, whose foreign policy had been in the sway of Cobdenite orthodoxy for the better part of a

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and the 'Mixed Committee' Report were heavily cited. Macmillan used the 'protective' and 'energy' food division, too, and found (like McDougall) that high costs of the latter meant that poorer sections of society had to do without the former. Macmillan proposed that the best way to reduce the costs of all foodstuffs was to reduce the costs of distribution which, using a plethora of tables and graphs, he claimed was a function of too many small units - the downside to the 'nation of shopkeepers' (Macmillan 1938, p.341). In idea and presentation strikingly like McDougall's, essentially he advocated the replacement of the market mechanism for food distribution by 'public utilities' which would impose 'control and rational organisation [upon] the supply of essential commodities so that their price can be reduced to the lowest possible level' (Macmillan 1938, p.358). Macmillan even recommended the regulation of overseas trade by the creation of 'purchasing boards' of the type advocated by McDougall the previous decade (Macmillan 1938, p.348).

<sup>173</sup> As the United Kingdom's official historian of food policy in the Second World War noted, certain nutrition experts welcomed the opportunity the war gave them as a way of testing the practicality of a nutrition-based food distribution policy (Hammond 1951, p.101).

<sup>174</sup> Linked indelibly to Chamberlain and Munich, the word 'appeasement' in its modern manifestation has become a perjorative term suggesting weakness and unprincipled concession. This was *not* its meaning in 1936, when it simply meant to bring peace, to assuage, to settle *just* grievances and fears. See Little *et al* (1933).

<sup>175</sup> 'Economic Appeasement', *op.cit.* The memorandum was also later published by the League of Nations (League of Nations 1937a).

century.<sup>176</sup> McDougall's conception of economic appeasement, however, was not Cobdenite, and he maintained throughout his writings that familiar scepticism to free trade as the panacea for the world's economic ills and political tensions. The repeated failure of such efforts in the past 'had been too complete to allow of the interpretation that the crusades for Free Trade have failed owing to the influence of vested interests or the short-sightedness of politicians'.<sup>177</sup> They failed, rather, because their proponents saw only a part of the truth. The average citizen, as well as the policy-maker, desired, for reasons not necessarily connected with economics, a 'balanced economy'. This desire was manifested in the determination of the industrial countries to protect their agriculture and, equally, the determination of the mostly-agricultural countries to industrialise.

A revival of world trade was essential for international peace in McDougall's schemes, but this would not come from a direct attack upon the barriers which most countries had erected against it. What was required were programmes of economic action which would 'appeal to both the idealism and self-interest of the average man'. Low incomes, poor nutrition, unemployment and low living standards had created an environment ready-made for the 'peddlers of exaggerated nationalism and the dreams of national aggrandisement'.<sup>178</sup>

The nutrition approach was the core of economic appeasement, but McDougall incorporated into it complementary notions enjoying contemporary currency. The following includes the most important of these, drawn from a number of his memoranda concerned with economic appeasement. They are labelled according to the categories McDougall himself employed:

### 1. 'Poor' Countries

In its original manifestation, the nutrition approach had included a reference to countries which were deficient in both protective and energy foods, but its focus was on the richer countries of the world. In his later memoranda McDougall redressed this emphasis markedly, often noting the comment by China's representative to the League of Nations that 'most Chinese are in a state of malnutrition all the time' (League of Nations 1937c, p.28). The world's 'poorer' countries could expect to benefit from the application of a nutrition approach through the increased trade in foodstuffs, but McDougall also advanced a number of other proposals directly addressed to the issue of their access to world markets. These were concerned mostly

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<sup>176</sup> There was also amongst *economists* of the period something of a consensus that economic distress bred political extremism and conflict. Such an idea was *de rigueur* in the writings of classical economists too, of course, and Smith, Ricardo and Mill all took the view that there existed an inverse relationship between affluence, the openness of an economy to trade, and war. It was also central to twentieth century writers such as J.A. Hobson, Norman Angell and J.B. Clark. Less centrally, the links between economics and war were apparent in the writings of a great many economists, including a famous digression by Keynes in the concluding pages to the *General Theory*. Interestingly, the view that economic hardship was a cause of war was in opposition to the view generally held before the nineteenth century that wealth, and the wherewithal to wage conflict, was the cause of war. For more on this view, see Blainey (1988). Gilbert (1966) proposed that the interwar attitudes of economists were strongly influenced by Keynes's *Economic Consequences of the Peace*, a view with some validity given the frequency with which it was cited in contemporary works. For a modern overview of economics, economists, and war, see Goodwin (1991).

<sup>177</sup> 'Economic Appeasement', *op.cit.*

<sup>178</sup> *ibid.*

with colonial trade, and were also an attempt to answer the ‘totalitarian states’ long-standing grievance that their lack of colonies denied them access to raw materials.<sup>179</sup> McDougall did not accept this claim, but he regarded regions hitherto locked away under colonial relationships as ripe for ‘immense development’ and an ‘especially elastic margin to world trade’.<sup>180</sup> In this context, the example he most liked to highlight was India, the application of the nutrition approach to which would ‘simultaneously affect the purchasing power of hundreds of millions of agriculturists...and would have a marked effect on world economic affairs’.<sup>181</sup>

To effect this access, McDougall proposed that the existing colonial powers adopt an ‘open door’ with regard to the trade and development of ‘their’ colonies. This would require the colonial powers to abandon any preferential access they enjoyed in the markets of the colonies and leave all decisions of trade and access to local authorities. The open door would not only include trade in goods, but also in the granting of government contracts and the provision of financial services. Overseeing all of this and adjudicating on the ‘openness’ of the door, McDougall proposed the establishment of an ‘International Commission’. The International Commission would comprise representatives of the existing colonial powers, the inhabitants of the ‘non-self governing’ regions and other interested parties. This would not necessarily satisfy ‘the Nazi or Fascists but it would go far to demonstrate to the peoples of Germany and Italy our complete goodwill’.<sup>182</sup>

## 2. ‘The ILO Method for Improving Living Standards’

It was poor living standards which, in McDougall’s analysis, was the principal political and economic problem facing the world. Improved standards required, however, increased purchasing power for ‘the great mass of people’ internationally. A number of measures to bring about such an end were outlined, one of which was to secure ‘international agreement for the improvement of the remuneration and conditions of labour’.<sup>183</sup> This McDougall labelled the ‘ILO method’, after the International Labour Organisation’s efforts in drawing up conventions on minimum rates of pay, reductions in working hours and a host of other measures. In the past it had been difficult to get countries to ratify ILO conventions, but in the wake of

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<sup>179</sup> German demands for the return of the colonies confiscated under Versailles grew increasingly strident from 1933 and the arrival of the Nazi regime. Never central to their ideology, the colonies issue was used by the regime nonetheless to project the idea of Germany as a ‘have not’ power with special grievances. Significantly, it was also an issue used to pressure the United Kingdom and other colonial powers into allowing Germany a free hand in central and eastern Europe. Hjalmer Schacht, President of the Reichsbank in the early years of the regime, seems to have genuinely hoped for colonial access as a means through which to conserve Germany’s foreign exchange reserves. He made a number of approaches to the United Kingdom and France on the issue in the 1930s. In these Schacht hinted that concessions were required lest Hitler fall under the sway of ‘insane elements in the party’. These approaches were seized upon by advocates of appeasement as an avenue through which ‘moderate’ opinion in Germany could be strengthened. As a non-party member Schacht was often seen as the centre of these moderate elements. Schacht’s comments are recorded in a letter, from Leith-Ross (Chief Economic Adviser to the British Government) to Chamberlain, 4 February 1937, PRO: FO371/20725, C958/78/18. A League of Nations inquiry into the issue of access to raw materials rejected Germany’s claims that it was excluded from colonial markets. For more on the colonies issue in relation to the appeasement story, see MacDonald (1972) and Parker (1993).

<sup>180</sup> ‘Economic Appeasement’, *op.cit.*

<sup>181</sup> *ibid.*

<sup>182</sup> *ibid.*

<sup>183</sup> *ibid.*

Roosevelt's re-election in the United States, the election of certain 'progressive' governments in Europe, as well as what he saw as the increased presence and power of trade unions around the world, McDougall was confident such resistance could be more easily overcome.<sup>184</sup>

By the 'ILO method' McDougall was also referring to the quite specific writings of the ILO economist, P.W. Martin who, through the pages of the *International Labour Review* in the 1920s and 1930s, presented a view which countered the hitherto long-standing position of ILO economists that economic instability was *monetary* in origin.<sup>185</sup> Martin instead presented an 'underconsumptionist' view of the global Depression which had at its core the belief that employment was a function of purchasing power which had to be constantly 'adjusted so as to make effective demand in the hands of the community always sufficient and no more than sufficient to provide a market for all that industry can produce'.<sup>186</sup> Since labour income was by far the largest source of effective demand for 'the great mass of people', it followed in Martin's work, as well as McDougall's, that this was also a key area for ameliorative government policy.

Of course, one country acting unilaterally would quickly find itself in a less competitive position relative to countries not adhering to ILO conventions. In a proposal with echoes in the present day, McDougall suggested that 'it is even possible to contemplate a new interpretation of the Most Favoured Nation clause in commercial treaties whereby the granting of equality of tariff treatment might be conditional upon effective adherence to International Labour Conventions'.<sup>187</sup>

### 3. Social Provision and Income Redistribution

A more liberal provision of social services, not only in the form of more comprehensive and generous social security payments, but also increased spending by the State on 'housing, medical treatment, transport, public utility services, educational and recreation facilities', was also part of McDougall's schema.<sup>188</sup> The provision of such items as a social service would increase the purchasing power of the poorer sections of society and also (to the extent they were financed by taxation) provide for a modicum of income redistribution.

Redistributing income had become an expanding component of McDougall's schemes as the 1930s wore on. Important for its own sake in improving the nutrition standards of poorer people, it was also the vehicle through which, McDougall believed, aggregate demand could be increased. In this he was consistent with standard 'underconsumptionist' thought (on which more below), but McDougall's was inspired by the work of a number of economists on the subject, especially Keynes. In the *General Theory*, Keynes had noted the rather simple point that wealthy individuals were likely to have a lower marginal propensity to consume than those in poorer classes, a point McDougall expressed as 'the greater the degree of income inequality in a society, the wider will tend to be the gap between its actual and potential

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<sup>184</sup> *ibid.*

<sup>185</sup> The view, of course, was also taken by the Australian economists at Ottawa and at the WMEC.

<sup>186</sup> Martin (1938), cited in Endres and Fleming (1996), p.217.

<sup>187</sup> 'Economic Appeasement', *op.cit.*

<sup>188</sup> *ibid.*

production'.<sup>189</sup> McDougall also quoted Keynes on the implications for investment of low consumption, and the problems parsimony would bring;

a poor community will be prone to consume by far the greater part of its output, so that a very modest measure of investment will be sufficient to provide full employment; whereas a wealthy community will have to discover much ampler opportunities for investment if the saving propensities of its wealthier members are to be compatible with the employment of its poorer members. If in a potentially wealthy community the inducement to invest is weak, then, in spite of its potential wealth, the working of the principle of effective demand will compel it to reduce its actual output, until, in spite of its potential wealth, it has become so poor that its surplus over its consumption is sufficiently diminished to correspond to the weakness of the inducement to invest.<sup>190</sup>

#### 4. *Consumers' Credits*

Keynes was only one of a number of economists McDougall quoted in support of the view that increased consumption was the key to economic recovery. Another of these was James Meade. Known to McDougall personally during his tenure as an economist with the League of Nations Intelligence Service, the future Nobel Laureate was part of an extraordinary team of young economists befriended by McDougall (which included another future Nobel Laureate, Jan Tinbergen, as well as Gottfried Harberler, Tjalling Koopmans, Ragnar Nurske, J.M. Fleming and Folke Hilgerdt) who were assembled by the Service's Director, Alexander Loveday, during the latter half of the 1930s.<sup>191</sup> The idea which caught McDougall's attention, though, was Meade's 'consumers' credits' scheme which was first set out in Meade's 1936 book, *Economic Analysis and Policy*, and elaborated in his *Consumers' Credits and Unemployment* in 1938.

Meade's consumers' credits proposal was motivated by his belief that monetary action and the application of public spending on capital works would not be sufficient solutions to unemployment. The first because of the likely interest-insensitivity of investment and the latter because of substantial lags before such spending could be brought to bear (Meade 1936, pp.49-50). Consumption spending, by contrast, could be expanded or contracted instantaneously through consumer credits. Paid to the unemployed by an Unemployment Assistance Board, the credits would be financed according to a levy imposed upon the employed and employers. The aggregate size of these contributions could not, however, exceed that which would be sufficient to finance the credits paid to what Meade called a 'standard volume' of unemployed (Meade 1936, p.52).<sup>192</sup> When unemployment drifted above this standard level, the extra credits paid would be financed by the issue of new notes from the Bank of England, giving the proposal its expansionary bias. In this way, the increased

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<sup>189</sup> 'The Road to Economic Appeasement', 31 January 1938, FAO, RG3.1, Series D3, Notes and Comments F.L. McDougall 1938-39.

<sup>190</sup> Keynes (1936, p.31) cited in 'The Road to Economic Appeasement', *op.cit.*

<sup>191</sup> James Meade told this author of his friendship with McDougall in written correspondence in December 1993.

<sup>192</sup> According to Meade, 'unemployment is of the "standard" size when it has been just sufficiently reduced for money wage rates to start rising at the same rate as the marginal product of labour' (Meade 1936, p.77).

purchasing power of one group came at no expense to any other, something which was not the case if unemployment benefits were a claim on the budget (and financed by taxation or debt). Nor, according to Meade, was the scheme inflationary. During periods in which unemployment fell below the standard volume, the Board would be required to use its excess funds to either pay off its debts to the Bank of England or, if none existed, accumulate reserves for later use (Meade 1936, pp.52-55).

McDougall incorporated Meade's proposals into a number of memoranda he circulated in the late 1930s, including one sent to Jan Tinbergen for comment. Tinbergen was in favour of Meade's scheme and wrote that, with respect to McDougall's own ideas also, he was 'generally in full sympathy with the objects and the ways chosen'.<sup>193</sup>

### *5. The Importance of Consumer Good Industries*

McDougall's cultivation of economists and his reading of their works had become more pronounced with his growing conviction that it was the recurrence of 'trade depressions' and the existence of a 'trade cycle' which posed the greatest threats to world peace and prosperity.<sup>194</sup> Generalising on his more or less constant theme that policies designed to improve living standards could be a substitute for the production of armaments, McDougall also propagated the idea that consumer good industries were a more stable sector of the economy than capital goods industries. McDougall saw capital goods industries as the source of macroeconomic instability because of the 'leads and lags' inherent to them, and in this way reasoned that policies designed to increase consumption 'may have a not unimportant part to play in the future in diminishing the intensity of trade depressions'.<sup>195</sup>

As with his advocacy of income redistribution, this was, at one level, fairly standard underconsumptionist stuff of the type long advanced by J.A. Hobson. The cause of the downturn was insufficient consumption, mostly because of a maldistribution of income and 'over-saving' by those groups with most of the income. This oversaving was then translated into investment (their divergence not being the issue in these simple analyses) which, in turn, brought forth an increased production of consumer goods. The problem, and the downturn, occurred because this increased production came into an environment in which demand was already insufficient. The solution was to increase consumption in some way relative to investment. In the work of Hobson, as in McDougall, the policy was to redistribute income from groups with high marginal propensities to save to those whose income was mostly used for consumption (Schneider 1996).

On the question of sectoral stability, though, McDougall was also heavily influenced by Denis Robertson.<sup>196</sup> A writer long concerned with the nature and causes of

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<sup>193</sup> 'Tinbergen to McDougall', 24 June 1938, Frank McDougall Papers, NLA MS 6890, Folder 6.

<sup>194</sup> 'Note on Consumption Policies in Relation to the Trade Cycle', 25 August 1938, FAO, Notes and Comments, F.L. McDougall 1938-39, RG 3.1, Series D.3.

<sup>195</sup> *ibid.*

<sup>196</sup> McDougall was particularly enamoured of a memorandum, *Note on Measures to Promote Recovery from Depression*, penned by Robertson during his tenure at the League of Nations. This author has been unable to locate the memorandum in Robertson's published work, including the compilations of Presley (1979) and Dennison and Presley (1992). As such, it is set out here according to McDougall's rendition of it in 'Economic Depressions and the Standard of Life', 24 June 1938, Frank McDougall

fluctuations in economic activity, Robertson's view of economic cycles at this point in time was that they were primarily caused by 'over-investment' - by which he meant that the demand for capital goods fell short of their production (Presley 1979, pp.59-63). That this might occur was a function of over-expansionary or contractionary monetary policies as well as the 'leads and lags' referred to by McDougall, all of which increased uncertainty and fluctuations in the marginal utility of investment. Over the corpus of his writings, fluctuations in economic activity were regarded by Robertson as an unavoidable part of the capitalist dynamic - the unfortunate flip-side to the vitality of the system. In the late 1930s, however, Robertson was much less sanguine. Appointed by Alexander Loveday as Special Adviser to the League of Nations on business cycle research, Robertson came into contact with McDougall and other like-minded individuals and, according to McDougall's account of it, began a campaign which advocated that governments promote consumer good industries at the *expense* of those concerned with capital goods.<sup>197</sup>

McDougall's rendition of Robertson's argument was that:

- (1) the leading Western countries had so specialised in the production of capital goods that their economies, like these industries, could not be anything but highly unstable;
- (2) with population growth stagnating and the level of real wealth that was now technically feasible, Western countries could afford to attach increasing importance to 'stability' rather than 'progress';
- (3) as a consequence of (1) and (2), the world's long term problem lay in converting production not just from guns to butter, but from guns *and machine tools* to butter. What was required was international consultation for a huge transfer of public resources - a 'rebutment campaign, in preference even to a public works campaign, to take the place of the gap which it is to be hoped will be left, some time during the next hundred years, by the completion of re-armament'.<sup>198</sup>

#### 6. *Reducing trade barriers.*

Notwithstanding his oft-repeated statements of opposition to Cobdenite orthodoxy, in his later memoranda McDougall wrote that the lowering of trade barriers was the 'natural corollary' of policies designed to increase consumption and living standards. High trade barriers would reduce purchasing power so long as production was not acquired from its cheapest and most efficient source. In advocating a lowering of trade barriers, McDougall even approvingly referred to the efforts of United States Secretary of State, Cordell Hull, to secure freer trade via bilateral trade agreements in company with a rigid application of the 'most favoured nation' principle.<sup>199</sup>

For the United Kingdom and the Commonwealth to participate in such a scheme, the Ottawa framework had to be modified considerably. This did not present any

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Papers, NLA MS 6890, Folder 6. This caution noted, the memorandum is not very different from other works included in Dennison and Presley (1992).

<sup>197</sup> 'Economic Depressions and the Standard of Life', 24 June 1938, Frank McDougall Papers, NLA MS 6890, Folder 6.

<sup>198</sup> *ibid.*

<sup>199</sup> Hull was presenting his campaign for tariff reduction through bilateral trade treaties as 'the most powerful single force for easing political tension and averting the danger of war'. Hull cited in Fisher (1938), p.56.



difficulties for McDougall, who by now saw Ottawa as a serious impediment not only to a revival of world trade but also in the negotiations of Commonwealth countries to secure markets outside the bloc. For the United Kingdom itself McDougall was not averse to suggestions that it unilaterally move to reduce its trade barriers. Whatever the outcome, nations such as the United Kingdom and the United States had to recognise 'that an "adverse" balance of visible trade is the proper and natural concomitant of their creditor status'.<sup>200</sup>

### 7. Germany

McDougall reserved special attention in his writings for Germany, whose exchange position in the late 1930s was under severe strain, the root cause of which was its racial policies. Germany had excluded itself from international commerce, a situation which McDougall feared would lead to foreign adventure and war. If, however;

large scale moves for economic appeasement for the restoration of world trade and for the improvement in the standards of living could be initiated by the United Kingdom, the United States of America and by France...and if it was clear that the great democracies were anxious and willing to secure German participation, then the result should be to give Germany a peaceful way out of her difficulties.<sup>201</sup>

## **4.4 Propagating Economic Appeasement**

As with the nutrition approach, the League featured strongly in McDougall's attempts to 'sell' economic appeasement, and in 1937 he was instrumental in it establishing an ad-hoc committee (along the lines of that created to examine nutrition) to investigate measures to improve living standards and to investigate the trade cycle.<sup>202</sup> McDougall's memoranda and other pieces were also published by *The Times* whose editor, Robert Barrington-Ward, was a strong advocate of an economic solution to the tensions between Britain and Germany.

McDougall was also concerned to influence policy processes more directly. The methods chosen were familiar - Bruce, the front man, circulating memoranda written by McDougall following an introduction (personally or in a letter) making clear Bruce's disinterested support for the ideas as well as his position as Australian High Commissioner, Chief Delegate to the League and former Prime Minister. As with the nutrition approach, it was a broad campaign which maintained its focus upon the United Kingdom, but extended beyond it. The circulation list for McDougall's original *Economic Appeasement* memorandum, for example, included United Kingdom Foreign Secretary Anthony Eden, Ambassador to Germany Sir Neville Henderson, Chief Economic Adviser to the Government Sir Frederick Leith-Ross, head of the civil service and Chamberlain adviser, Sir Horace Wilson, Bank of England Governor Sir Montagu Norman, the Secretary-General of the League of Nations, J.L.A Avenol, the Prime Ministers of Belgium and the Netherlands, and

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<sup>200</sup> 'Economic Appeasement', *op.cit.*

<sup>201</sup> *ibid.*

<sup>202</sup> Whose work and findings were subsequently published as League of Nations (1943) and (1945). McDougall was a member of this committee, which also included the economists Bertil Ohlin and Gottfried Harberler.

Cordell Hull.<sup>203</sup> Interestingly, no copy of *Economic Appeasement* was sent to the Australian Government at this stage, which was almost certainly in ignorance of the proposals being advanced (at least partly) in their name.<sup>204</sup>

A copy also made its way to the British Foreign Office, whereupon it provoked an internal debate that lasted several months. The Department's Economic Section was enthusiastic about the ideas which, under the leadership of Frank Ashton-Gwatkin, largely mirrored its own.<sup>205</sup> Coming as they did from such an 'eminent Dominion statesman' (in Bruce), McDougall's memoranda were also regarded as highly marketable to the political leaders the Section was trying to influence.<sup>206</sup> Gladwyn Jebb, a member of the Section who was to write later that the first time he saw the word appeasement was in a memorandum written by McDougall, thought his memorandum contained 'a number of fruitful ideas'.<sup>207</sup> He also thought such ideas could be used in direct but unofficial discussions with the German Government. If nothing else, economic appeasement could gain time, which was now 'the whole object of our policy'.<sup>208</sup>

Ideas remarkably similar to those of McDougall were used in a number of unofficial approaches to certain German emissaries, and large sections of his original memorandum were included in a briefing document on British trade policies prepared by the Foreign Office in April 1937, a document used a month later to brief the

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<sup>203</sup> The letters are contained in NAA, M104, 5(2).

<sup>204</sup> Eventually it was told, and at the Imperial Conference in 1937 McDougall succeeded in having Prime Minister Lyons read a speech he had prepared advocating economic appeasement. For more on Australia's role in the appeasement story more generally, see Andrews (1970).

<sup>205</sup> Ashton-Gwatkin had been greatly influenced by Halford Mackinder's *Democratic Ideals and Reality*, a largely forgotten work now, but one which had a similar impact at the time as Keynes's *Economic Consequences of the Peace*, also published in 1919. Mackinder's principal vision was of an economically unified Europe in which political conflict had been rendered obsolete. Ashton-Gwatkin had some influence in British economic diplomacy between the wars and was responsible for a number of initiatives designed to relieve Germany's economic position. For an example of his version of economic appeasement, see his 'Note on Germany's Economic Position', 21 November 1935, in Woodward and Butler (1956), pp.724-726.

<sup>206</sup> 'Note by Gladwyn Jebb', 9 January 1937, PRO: FO 371/21215, W373/5/50. This is not to say, however, that there was not opposition to economic appeasement generally, and to McDougall's ideas in particular, within the Foreign Office. William Strang of the Office's American Section, for example, thought that McDougall's emphasis upon living standards would have little appeal in totalitarian states whose objective was in 'creating a spare and vigorous people with thoughts above bread'. 'Note by William Strang', 13 January 1937, PRO: FO 371/21215, W373/5/50.

<sup>207</sup> 'Note by Gladwyn Jebb', 9 January 1937, *op.cit.* Jebb's account of his first encounter with the word 'appeasement' is recalled in Jebb (1972). Later an acting Secretary-General of the United Nations, Jebb was close to McDougall personally throughout the inter-war and wartime years. He was even a member of a small group McDougall got together to discuss ways and means by which the objectives of economic appeasement could be achieved. This group included a number of politicians, academics and government officials. It also included Barrington-Ward of *The Times*, and sometimes the paper's owner, Lord Astor. After the outbreak of the Second World War, the contemporary press made much of a similar group that met at *Cliveden*, the home of Lord Astor, which discussed appeasement generally. Notwithstanding that McDougall's group had members in common in Astor and Barrington-Ward, it has escaped the opprobrium levelled at the 'guilty men' of the 'Cliveden Set'. For more on Astor's group, see 'Cato' (1941). Jebb's accounts of McDougall's group is contained in 'Note by Gladwyn Jebb', 9 January 1937, *op. cit.* His later recollections of McDougall and this period are contained in Jebb (1972).

<sup>208</sup> 'Note by Gladwyn Jebb', 9 January 1937, *op. cit.*

incoming Prime Minister, Neville Chamberlain.<sup>209</sup> Curiously, Neville Chamberlain, with whom the word appeasement is inextricably linked, did not himself favour *economic* appeasement, declaring in 1938 that he disagreed ‘with those who think you can solve political difficulties by removing economic thorns from the flesh. Politics in international affairs govern actions at the expense of economics, and often of reason’.<sup>210</sup>

McDougall and Bruce continued their advocacy of economic appeasement right up until the outbreak of war - though the increasing opprobrium attached to its political aspect meant that they dropped the *word* ‘appeasement’ in favour of the expression ‘economic development’ in their final memoranda. They also began to write in the expectation of war, and the need for a ‘just peace’ at its conclusion - for its own sake and, consistent with their philosophy, to ensure that war did not happen again.<sup>211</sup>

## **4.5 Influence, Achievements and ‘Underconsumption’**

### *Influence*

In his monumental report of what went wrong in the inter-war period, *The Economic Lessons of the Nineteen-Thirties*, Heinz Arndt (1944, p.244) noted that following the failure of the WMEC, attempts to repair the workings of the world economy fell into three categories. Firstly, there were the efforts of the United States to secure liberal economic internationalism via the pursuit of bilateral trade treaties. Secondly, there were the attempts by the League of Nations to secure ‘a new approach to economic problems in the subordination of economic policy to social objectives’. Finally, there were the attempts, ‘initiated by the British Government’, to secure peace through economic appeasement.

It has been the purpose of this chapter to examine the role played by the representatives of Australia in the last two of these, and to highlight the part they played in the ultimately fruitless search for peace and prosperity in the inter-war years. And herein lay the most important aspect of this narrative - that Australia, a country hitherto hardly noted for its contributions to the great questions of the international economy, played a portentous role in these efforts not only by participating in them but, indeed, in leading them. Australia, as represented by McDougall and Bruce, was the driving force behind the League’s ‘new approach’ to economics via nutrition and, with a number of others, was at the forefront of efforts to extend this campaign to a broader one embracing a belief that rising living standards were the key to international peace.

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<sup>209</sup> These included an approach by Britain’s Ambassador to Germany, Sir Neville Henderson, to Hitler in March 1938 over the colonies issue (also a device now seen by the British Government as a possible vehicle for appeasement). In July 1939 Helmuth Wohltat, an official of the German Ministry of Economics, visited London. He was presented with a range of economic initiatives, a number of them similar to those advocated by McDougall. Like Henderson’s earlier approach, it came to nothing. For more on these, and the many other informal meetings between British and German officials in the lead-up to war, see MacDonald (1972).

<sup>210</sup> Chamberlain cited in Gilbert (1966), pp.1156-1157.

<sup>211</sup> See, for example, ‘A Co-Operative Peace’, 24 November 1939, ‘Notes and Comments F.L. McDougall 1938-39’, FAO RG 3.1, Series D3.

As we have seen, however, the efforts of McDougall and Bruce were not at the behest of an activist Australian Government, but rather as a function of a unique set of circumstances which placed McDougall and Bruce in a position to influence the *discourse* of international political economy in the inter-war years. Why they were so successful in this role of propagation (if not the influence of policy) is a most difficult question. One answer would give priority to personal factors - to wit, the remarkable proselytising skills of McDougall. Such a proposition would be most difficult to sustain in any rigorous way. It is the nature of such channels of influence that they are often necessarily informal and, importantly for later historians, unwritten. Notwithstanding this, it would also be less historically accurate *not* to note the array of accounts attesting to the remarkable *personal* influence McDougall had upon a great many significant figures of the inter-war years.<sup>212</sup> In addition to these, of course, are the surviving written records themselves - McDougall's books (*Sheltered Markets* and *Food and Welfare*, the latter of 1938 and being the most polished and comprehensive statement of his ideas), the countless memoranda, and the numerous letters to people at the highest levels of government, government agencies and international organisations.

More conventionally explicable, but perhaps no more certain as an explanation, was the way in which the pair exploited Bruce's *official* position. The idea that Bruce was a much more influential figure in the counsels of the British Empire in the inter-war years is one of comparative recent origin, and owes much to Edwards (1979 and 1983). Edwards saw Bruce as occupying three distinct yet simultaneous roles as High Commissioner in London. Firstly, Bruce was the official representative of the Australian Government in London and in this role was the instrument for the presentation of Australia's views on international and Commonwealth affairs. This role was much more important at the time than it might appear to a modern reader. Until 1935 Australia did not even have a separate department for external affairs and had no distinct diplomatic representation outside of Britain until 1940. This meant that through much of the period under examination, Australia's foreign policy was enacted *through* the United Kingdom. As Australia's representative with the British Government, Bruce's role as High Commissioner gave him enormous scope for the presentation of policy of ideas (nominally of the Australian Government) and, importantly, access to officials and the highest political offices in the country.

In his role as the representative of Australia, Bruce was also, *ex officio*, Australia's chief delegate to the League of Nations. This, as has been examined, was heavily used by both McDougall and Bruce and, together with certain sections of the British press, was the primary vehicle through which their ideas were granted their widest audience. The failure of the League to prevent the Second World War has tended to obscure the

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<sup>212</sup> The extent of this influence is remarked upon in almost all accounts in which McDougall is mentioned. Some of the most pertinent in this context are Jebb (1972), Stirling (1973, 1974 and 1975), Coombs (1981), Cumpston (1989), Edwards (1965), Orr (1953 and 1966), Marchisio and Di Blase (1991), Lamartine Yates (1955), Fisher (1938) and in the introduction to McDougall (1986) by W.J.Hudson and W. Way. In a private memoir written on McDougall's death in 1958, Wallace Aykroyd, then Director of FAO's Nutrition Division, made the interesting point (of importance in Section III of this work) that McDougall had the advantage of influencing 'when they were young, many people who later became important officials of their governments and who regarded him with great respect and affection' (Wallace Aykroyd, 'Frank McDougall', F.L. McDougall Papers, NLA MS 6890).

popular support it enjoyed in the 1930s, even after political events had rendered it moribund in its primary objective of keeping the peace. In 1935, for example, the year McDougall and Bruce launched the nutrition approach, the so-called 'peace ballot' in the United Kingdom attracted over 11 million votes of support for the League and its role - a figure which rivalled voter turn-out for most general elections (Parker 1993, p.46). Whatever their private thoughts, political leaders in the United Kingdom and elsewhere in the 1930s were always careful to couch foreign policy in terms of its consistency with the League's covenant. In 1935 Stanley Baldwin (then British Prime Minister) could still say that supporting the League was to 'hitch your wagon to a star' (Parker 1993, pp.46-47).

Bruce's second role in London called upon the way in which his official position gave him a voice in the British political system independent of his specific role as the representative of Australia. This was something shared generally by the Dominion High Commissioners in London in the inter-war years, to be exploited more or less at will to gain access to political leaders in Westminster or the bureaucracy in Whitehall. For the High Commissioners the advantages of such a system were obvious, but so were there advantages to the British Government, which had a channel of 'consultation' with the Dominions which short-circuited the complexities of full scale inter-Commonwealth negotiations. For Bruce this was an opportunity that he made much use of, both in the nature of the causes he championed (most no more connected to Australia than any other country) and the way he went about advancing them. This independent role was enhanced in Bruce's case too in that he enjoyed the cachet of being a former Prime Minister and serving Privy Councillor.<sup>213</sup>

Bruce's third role in Edward's schema concerned that of being an *initiator* of what was *seen to be* Australian foreign policy.<sup>214</sup> Though Edward's broad claim in this regard could be open to some doubt, with regard to nutrition and economic appeasement it almost certainly captured the truth.<sup>215</sup> As has been demonstrated throughout this chapter, neither of these initiatives were the result of instructions from Canberra. Indeed, at critical moments Canberra knew nothing of them. Edwards (1979, pp.46-47) also made much of the team Bruce assembled around him in London which, with McDougall as its economic component, constituted 'a sort of miniature foreign office'. This was made all the stronger by the lack of the same in Australia.

An important point in assessing the influence of Bruce according to these three roles is that he (and McDougall in his name) appeared to make little attempt to distinguish between them. Was Bruce, the propagator of memoranda on nutrition and economic appeasement, acting as the representative of his Government, or was he acting as S.M. Bruce, the distinguished former Dominion leader and Privy Councillor with some rather radical views on economics and foreign policy? To the recipients of his

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<sup>213</sup> Bruce observed in October 1938 that because he 'was a Privy Councillor it enabled me to be told of and consulted with regard to matters which if I had not been could not have been disclosed to me even as the Representative of Australia'. Bruce cited in Edwards (1979), p.52.

<sup>214</sup> This view is generally supported in O'Brien (1987).

<sup>215</sup> Attard (1994, p.27) notes the limits of Bruce's influence on the Government with respect to commercial policy and cites his complaints of his lack of 'close contacts with members of the [Australian] Government'. This did not matter with regard to the nutrition approach or economic appeasement which, as this chapter has noted, had little to do with the Australian Government.

advocacy there could not have been an easy answer, even if they had thought to ponder the question.

The point, however, is not a trivial one - particularly in regard to economic appeasement. Since the 1960s a good deal has been written on the degree to which the United Kingdom predicated its foreign policy decisions in the 1930s on the desire to maintain Commonwealth unity. Although Australia was not generally bothersome in this regard (Canada and South Africa being the principal recalcitrants), the fact that its spokesman was, in the Foreign Office's own estimation, the world's leading exponent of economic appeasement could not have failed to have an effect. Appeasement was the one policy that was certain not to clash with the increasingly diverse interests of the United Kingdom and the Commonwealth.

### *Achievements?*

Successfully establishing a *voice* for advocacy, and having such advocacy implemented as policy were two very different things - and in the policy context of the 1930s, the efforts of McDougall and Bruce can only be said to have failed. The nutrition approach, particularly, promoted an extraordinary amount of interest and led to the establishment of national nutrition boards and other institutions concerned with food and health policies in a great many countries throughout the world. For it to have succeeded along the lines predicted by McDougall, however, it required *fundamental* changes in economic policy, in the role of the state and in the very structure of economic activity in individual countries as they adjusted their agricultural and industrial production according to what was, in essence, comparative advantage. None of this came to pass. There were, indeed, only two instances (outside of the war) - a decision by the government of Estonia to reduce the duties on dried fruit, and that of the government of India to reduce duties on dried skim-milk - in which commercial policies were *specifically* adjusted according to nutrition. Overall, Arndt (1944, p.248) concluded that the League's 'consumer economics' (the umbrella term under which he placed the efforts of McDougall and Bruce ) was as 'barren' in results as had been its efforts in attempting to directly reduce trade barriers. Consequently, it 'could not by itself solve the economic problems or overcome the political obstacles which prevented their realisation' (Arndt 1944, p.248).

Notwithstanding their lack of immediate success, most contemporary assessments of the nutrition approach were encouraging with regard to its longer term prospects and the spirit in which it had been propagated. Arndt (1944, p.248), for example (and notwithstanding the above), declared that it 'provided a valuable corrective to the confusion of thought which tended to turn shibboleths of "finance", "economic laws", and "free trade", balanced budgets or gold standards, into ultimate criteria of economic policy, and pointed to a saner approach to economic problems'. A.G.B. Fisher, who in his annual economic surveys for the Royal Institute of International Affairs was wont to put a greater stress on the reduction of trade barriers than many other contemporary accounts, noted too that it was a 'damning commentary' that the nutrition approach sought to emphasis living standards. Such an emphasis *should* have been a truism:

Unfortunately, it was not possible always to assume that this principle could be taken for granted as an obvious platitude, and on that account the argument...was not likely to be rejected (Fisher 1938, pp.64-65).

The nutrition approach was also defended on the grounds that, if it was not successful in delivering the fundamental changes in economic policy it required, it was no less successful than any other approach. This was particularly the case if it was compared to more 'direct' methods of reducing trade barriers. Fisher (1938, pp.100-101) even criticised the apparent success of the bilateral negotiations of Cordell Hull, noting that until the discussions with Britain in 1938, none had been attempted with another major trading nation, many agreements were less than 'liberal' when one looked beyond their preambles and they very often involved more in the way trade diversion than trade creation. Noting the reduction of trade barriers would benefit the world economy as a whole was hardly in dispute, Fisher (1938, p.86) nevertheless argued, along lines which would have gladdened McDougall's heart, that '[t]he immediate practical task was to discover means whereby...small, but not necessarily unimportant, advances might be made on a number of limited fronts'. It was, of course, precisely on such fronts that McDougall and Bruce were engaged throughout the latter half of the 1930s.

At a theoretical level though, the prescriptions of McDougall and Bruce were almost certainly 'more right' than those who saw such efforts as peripheral to the 'main game' of reducing trade barriers. The nutrition approach, and McDougall's earlier Empire advocacy were, in essence, little more than crude forms of demand management. And it was this or, more specifically, the maintenance of demand at a level consistent with full employment, which was a *requirement* if the promised benefits of reducing trade barriers were to be realised. In this context it must be remembered, though the issue will be taken up in detail in Section III of this study, that the laws of comparative advantage depended upon the *assumption* of domestic full employment. Keynes made the point clearly enough in the *General Theory* (p.349), using the autonomous rate of interest as a proxy for a level of demand sufficient for full employment:

It is the policy of an autonomous rate of interest, unimpeded by international preoccupations, and of a national investment programme directed to an optimum level of domestic employment which is twice blessed in the sense that it helps ourselves and our neighbours at the same time. And it is the simultaneous pursuit of these policies by all countries together which is capable of restoring economic health and strength internationally, whether we measure it by the domestic level of employment or by the volume of international trade.

For a 'national investment programme', McDougall would have substituted 'nutrition' or 'consumption'. To this issue, which clearly categorised his thought as part of the corpus of writing broadly identified as 'underconsumptionist', we shall return shortly.

Perhaps the most problematic components of the advocacy of McDougall and Bruce were those which dealt specifically with the question of the economic appeasement of

the totalitarian states. With regard to these regimes, it is apparent with hindsight that economic appeasement could not possibly have succeeded in its immediate objective of lessening the political tensions of the inter-war period. As noted, their call for higher living standards to be placed at the forefront of economic policy-making was not merely a platitude, but it could have little appeal within systems which deliberately sought the subordination of such ends. On the few occasions that policies of economic appeasement were actually put before the leadership of the totalitarian states (most, admittedly, in relation to the issue of colonies), they were either rejected immediately or acceded to for a time after which higher stakes were demanded from the democracies. The failure of McDougall's and Bruce's efforts in this regard was a failure to understand that Nazism and its kind were an assault upon the very morality and reason out of which the philosophy underlying economic appeasement was derived. In the end, economic appeasement had to fail because its proponents failed to grasp the essential dynamics of totalitarianism, which lay not in the domain of economics, but in the politics of power.

### *Underconsumption Theory*

It has been the purpose of this study to document and analyse the policy advocacy of McDougall and Bruce and to present it in the context of a broader Australian advocacy for expansionary economic policies internationally. It is a further purpose of this study, however, to contextualise this advocacy in terms of economic theory. Earlier in the chapter, a case was made that McDougall's early ideas concerned with imperial markets constituted a vulgar form of proto-Keynesianism. Such a broad label can be similarly specified for his ideas in the 1930s but now they can be more narrowly categorised since, as noted above, there was in McDougall's ideas much that can be identified within the broad spectrum of opinion of 'underconsumptionist' thought.

Underconsumptionism, which at its core was simply the idea that consumption expenditure was insufficient to absorb the total output of an economy at prices consistent with normal profits, was very much a part of public discourse throughout the 1930s (Schneider 1987, p.741). An idea (or, more accurately, a set of ideas) which had been around for centuries, it had re-emerged with particular vigour amidst what Lee (1989, p.133) described as the 'new wave of business-cycle studies' which had come about with the onset of the global Depression. Most were not very sophisticated, and were simply based on what Lee (1989, p.132) similarly described as 'no great leap of intuition' in the conception that slumps could be countered by the injection of purchasing power. Underconsumptionist ideas had 'come of age' with Hobson and A.F. Mummery's *The Physiology of Industry*, first published in 1889 but reprinted many times throughout the inter-war years, and Hobson himself revisited the idea in a number of other publications in the same period.<sup>216</sup> Underconsumptionist ideas also formed a part of the extraordinary ideas of Major Douglas and a host of other 'cranks' and 'scribblers' with a nostrum to push in these desperate times. They were particularly common in the United States, and reached a reasonable degree of

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<sup>216</sup> For more on Hobson's activities during this period, and his relationship to Keynes and *the General Theory*, see Schneider (1996), pp.12-14 and pp.71-77.



sophistication and even academic respectability in the writings of Foster and Catchings.<sup>217</sup>

McDougall's writings were redolent with the *lingua franca* of underconsumptionist thought. That he *self-consciously* identified his own ideas as being consistent with this tradition was apparent in a memorandum he penned in August 1938. This memorandum, *Note on Consumption Policies in Relation to the Trade Cycle*, drew heavily upon Chapters 22 and 23 of the *General Theory*, the chapters in which Keynes paid tribute to those precursors whose ideas he construed came closest to his own, and his attempt to construct an alternative intellectual genealogy of thought outside the 'classical' mainstream.<sup>218</sup> A number of people were celebrated in these pages, from the Mercantilists to Major Douglas, but it was the underconsumptionists (as classified, that is, by Keynes), and especially Mandeville, Malthus and Hobson, that receive most of the attention. The chapters have been criticised by various of Keynes's supporters and detractors alike. Harrod thought that Keynes 'allowed himself to be carried too far by the exhilaration due to emancipation from old fetters' and that Chapter 23 especially was 'a tendentious attempt to glorify imbeciles' (Harrod 1951, p.560). Skidelsky (1992, p.569) thought their inclusion a mistake; 'the discussion confirmed critics in their view that Keynes's theory, by rehabilitating old fallacies, marked regression, not progress, in economic science'.

Whatever the political wisdom of the chapters, they contained a clear exposition of the logic of the underconsumptionist position and how it fitted with the reasoning of the *General Theory*, and it was upon this aspect that McDougall drew. He was particularly taken with Keynes's explanation (1936, p.325) of how his ideas differed from the underconsumptionists, but left open a theoretical door which McDougall used in the memorandum:

Theoretically...they [ the underconsumptionists] are open to the criticism of neglecting the fact that there are two ways to expand output. Even if we were to decide that it would be better to increase capital more slowly and to concentrate effort on increasing consumption, we must decide this with open eyes after well considering the alternative. I am myself impressed by the great social advantages of increasing the stock of capital until it ceases to be scarce. *But this is a practical judgement, not a theoretical imperative.*

Moreover, I should readily concede that the wisest course is to advance on both fronts at once. Whilst aiming at a socially controlled rate of investment with a view to a progressive decline in the marginal efficiency of capital, I

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<sup>217</sup> For more on these 'proto-Keynesian' nostrums, and their influence in the United States, see Lee (1989) and Salant (1989). Of course, underconsumptionist thought was also widespread in Australia, where it had taken root in the labour movement and at the fringes of the economics discipline during the depression of the 1890s. For more on underconsumptionist thought in Australia, see Goodwin (1966), pp.251-259. In Kindleberger's (1989) classification of seminal ideas, underconsumptionist thought could come under the label of the 'simple idea, largely ignored or rejected by the profession, which refuses to disappear and keeps making its way' (Kindleberger 1989, pp.51-52).

<sup>218</sup> 'Note on Consumption Policies in Relation to the Trade Cycle', 25 August 1938, FAO RG 3.1, Series D3, Notes and Comments F.L. McDougall, 1938-39. Chapter 23 of the *General Theory* was also in part a platform from which Keynes could make some personal amends. In this context the prominence paid to the work of Hobson had much to do with his desire to make good a hostile review he had written in 1913 on Hobson's *Gold, Prices and Wages* (Skidelsky 1992, p.535).

should support at the same time all sorts of policies for increasing the marginal propensity to consume. For it is unlikely that full employment can be maintained, whatever we may do about investment, with the existing propensity to consume. There is room, therefore, for both policies to operate together....not merely to the level which with the existing propensity to consume would correspond to the increased investment, but to a higher level still [emphasis in McDougall's citation].<sup>219</sup>

In this same memorandum, McDougall defended deficit-financed government spending, particularly in the context of social security payments and in the provision of social services that traditionally had been discounted on the basis that they were 'unproductive'. Liberally employing a multiplier concept, McDougall rejected these traditional 'displacement' arguments and attacked also the arguments that 'radical social policies...may give a fresh shock to business confidence and so prolong the depression'. As the answer to this latter problem, he suggested that social security payments, unemployment relief and policies designed to ensure good nutrition should be *permanently* in operation, and not just salves for times of economic downturn. This way their cyclical growth 'would give no such shock to the "nerves" of business when a depression occurred'.<sup>220</sup>

Consistent with the great mass of underconsumptionist and proto-Keynesian literature which emerged during the inter-war years, McDougall's ideas were not based upon any rigorous theoretical base. A grab bag of many approaches, they nonetheless had a certain consistency in recognising that the operation of market forces did not necessarily generate an outcome in which all that a society was capable of producing would find consumers with a sufficient income to purchase it. And government in McDougall's schemes, as it was in 'progressive' accounts more generally, was a beneficent institution with the wherewithal to correct the failures of the market.

The lack of theoretical rigour in McDougall's work should not obscure the contribution it, and others like it, made to preparing the ground for the transitions in the role of government and economic policy which would follow in the wake of Keynes's *General Theory*. This is especially the case with regard to the creation of international economic institutions - foreshadowed by McDougall via his work with the League, but brought to fruition after the Second World War (McDougall's role in which shall be examined in Section III). McDougall's advocacy was, in terms of theoretical rigour, little different from most attempts at policy advocacy during the period, including that of most professional economists. Keynes's own advocacy of government spending and public works had begun well before he had established any strong theoretical justification for it. His most famous advocacy of expansionary fiscal policy prior to the *General Theory*, the 1929 pamphlet with Hubert Henderson, *Can Lloyd George Do It?*, came at a time when he was completing what he thought would be his great theoretical work, *A Treatise on Money*. The *Treatise*, however, devoted less than a single page to the issue of public works. Keynes came to see that his policy advocacy required a theoretical revolution to accompany it, but for much of the interwar period he was content to agitate without a *developed* theoretical basis for what his intuition told him to be correct.

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<sup>219</sup> 'Note on Consumption Policies in Relation to the Trade Cycle', *op.cit.*

<sup>220</sup> *ibid.*

Of course, even after the publication of the *General Theory*, Keynes and his disciples presented to politicians a story far removed from the theoretical intricacies which inspired *them*. Simple solutions to complex problems was what politicians wanted. The Keynesian revolution *required* a theoretical breakthrough, but this was just one part of it. As noted at the beginning of this Section, political leaders after the First World War were anxious to maintain distinct limits on the call on the state in these relatively early days of mass-participation democracy. In this context, the idea that rigid adherence to ‘balanced’ budgets’ and related issues of sound finance had something to with these anxieties, as much as they did to any acceptance of particular economic theories, is one which has increasingly caught the attention of historians of economic thought.<sup>221</sup> Eventually these anxieties would be swept away after another world war that simultaneously demonstrated the validity of the theoretical revolution which had occurred in the meantime. The advocacy of McDougall and his like were part of an ongoing long term process in turning around perceptions of the role of the state. Revolutions in ideas could (and in the 1930s, did) occur at the speed of cognition, revolutions in policy took rather longer.

In their history of Australian economic thought, Groenewegen and McFarlane (1990, p.147) note the contribution that amateurs from outside the ‘inner-core establishment academic world’ were able to make in mobilising public opinion against ‘respectable’ economic policy in Australia. Groenewegen and McFarlane did not include McDougall in their survey, but his contribution was, as one voice among many, part of a similar process taking place in the discourse of international political economy in the inter-war years. Theoretically uninformed and institutionally constrained, ideas such as McDougall’s were, in practical terms, marginal prior to the Second World War. With the arrival of war, much changed. Just as destructive of institutions as it was of people and material things, the Second World War suddenly allowed a great deal that was hitherto unthinkable. New protagonists, theoretically newly-armed but maintaining a Marshallian sense of mission appeared on the scene. Once more Australian economists were prominent. It is to this new era, and a new set of campaigns, that we now turn.

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<sup>221</sup> The most comprehensive selection of writings highlighting this idea are those contained in Hall (1989). Of course, Drummond (1974) has already been cited in this context.

## **Section III**

### ***Keynesian Crusaders***

## **Introduction**

At this meeting the Australians began to take up what was their characteristic attitude. They were anxious not to commit themselves to multilateral arrangements on the side of money or commerce, unless there was some international guarantee that world-wide effective demand and full employment would be sustained (Harrod 1951, p.542).

Roy Harrod's recollection of a meeting between the United Kingdom and the Dominions in October 1942, which appeared as an episode in his biography of Keynes, accurately captured what was to become the mainstay of Australia's economic diplomacy during, and immediately after, the Second World War. This was the 'employment approach', the 1940s manifestation of the 'expansionary bias' in the advocacy of Australian economists on international economic matters throughout the interwar and postwar periods. The unilateral product of the leading economists called up for service in the Australian government during the war, the employment approach was born out of theoretical conviction and in response to pressures from the United States to impose a 'multilateral' solution to global postwar reconstruction - an unusually stark and immediate presentation of Australia's traditional dilemma of internal *or* external balance.

This expansionary bias was manifested in previous episodes via the 'monetary reform' advocacy of Australian economists at Ottawa and the WMEC, and by the campaigns of McDougall. The employment approach was also distinct from these earlier efforts, and was undertaken under very different circumstances from those prevailing before the war. The first and most obvious of these differences pertained to the economist-protagonists themselves. The founding generation of Australian economists in the 1930s advocacy were conspicuous in the employment approach, as was McDougall, but they were increasingly overtaken in its propagation by a younger generation of economists assuming important positions in the bureaucracies which were made more permeable by the demands and shortages of war.

There were also theoretical differences between the generations.<sup>222</sup> As has been maintained throughout this thesis, the advocacy of expansionary monetary policies in the 1930s (and McDougall's schemes in other ways) was informed by a type of proto-Keynesianism which was partly a product of the first generation's largely 'practical' appreciation of the Australian economy. The new generation, by contrast, were all formally trained in economics, tended to be much more 'theoretical' in outlook, and were almost universally exposed in their formative years to the revolution in macroeconomics which followed Keynes's *General Theory*. As will be documented in Section IV of this thesis, a burgeoning line of research has opened up in recent years which has attempted to explain the existence or otherwise of a 'Keynesian revolution' in Australia. Suffice to say on this issue at this point, that the employment approach was explicitly Keynesian in its theoretical underpinnings - to an extent which was sometimes 'more royal than the King' with respect to Keynes himself.

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<sup>222</sup> A generational shift within academia was also underway, and would accelerate following the conclusion of the war. For more on this aspect of the generational change, see Smyth (1994), p.57.

A further obvious point of difference between the employment approach and earlier campaigns was the external environment. In the 1930s, international trade and the international monetary and financial mechanisms were barely functioning, but in wartime they broke down completely. Even 'Lend-Lease', one of the great unifying and positive policies of the Allied war effort, acted to destroy what international trade and financial mechanisms still existed by establishing alternative arrangements which could not function beyond the war. Of course, all of this was particularly important in the context of the United Kingdom, the greatest importer before the war and the linchpin of the international financial system. During the war the United Kingdom accumulated liabilities far beyond its prewar holdings of foreign assets, and it had become apparent relatively early in the war that it could thereafter play but a limited role in the postwar reconstruction of the world economy.

The great physical destruction of the Second World War and its disorganisation of administrative, social and economic structures in a great many of the belligerent countries was in stark contrast to the impact it had on the United States. Its productive capacity enormously enlarged by the war, the United States ended it far the world's greatest creditor nation, the largest exporter, the largest producer of manufactured goods and the largest economy (Bennett Woods 1990, p.22). The disparity between one enormous creditor nation and a legion of debtor nations whose obligations far outweighed their capacity to meet them was itself one of the greatest difficulties of the postwar period, and one very apparent before war's end. In this context, the United States' subsequent attempts to create a multilateral liberal trading order by exerting pressure upon countries directly and by creating international institutions consistent with these ends were difficult to resist. Amongst other motivations, the employment approach was, in part, a particularly creative way of attempting to precisely do just that.

The fatalism and adherence to 'sound finance' of the Lyons Governments had formed the domestic backdrop to the advocacy of McDougall and the Australian economists in the 1930s and provided, therefore, another area of contextual contrast to the employment approach. The employment approach not only had the support of the Labor Governments of John Curtin and Ben Chifley, but to a large extent was formulated and propagated through a combination of the economists acting in their official capacities and of the Government which increasingly appropriated the campaign as it developed. Care must be taken before specifying any government or political institution as adhering to any particular economic theory or discourse, for clearly the political process is motivated by factors extending far beyond the boundaries of economics, but equally it can be said that the approach of the Labor Governments of the 1940s was in sympathy with a broadly Keynesian approach. The popularity of underconsumptionist and 'money' theories of the Depression within the rank and file membership of the Labor Party made it particularly amenable to Keynes's prescriptions, as did its general predisposition towards intervention in the economy, its desire to reduce inequalities through redistributive taxation and, not least, the example of wartime in removing unemployment through macroeconomic management. The economic policy of the Labor Governments was about direct controls and other 'non-Keynesian' devices too, but at its core was a fundamental break with the past and a new vision that saw the economy as an aggregative and interdependent whole determined by aggregate demand. Management of aggregate

demand, and through it the level of economic activity and employment, was explicitly recognised as the responsibility of the Federal Government in the famous 'Full Employment White Paper' of 1945, but it was recognised by the Government well before then. As but one example amongst many, H.V. Evatt, then Commonwealth Attorney-General and Minister for External Affairs, declared as follows in a speech delivered in 1942 (the year the employment approach was launched):

With the lesson that it took the war to teach us, we can no longer assert that the problem of unemployment is insoluble, that men are out of work only because they are unfit or unwilling to work, that financial policy prevents their employment, that the task of maintaining full employment is not a responsibility of the national Government. (Evatt 1942, p.57)<sup>223</sup>

The employment approach was the means by which the economists, as well as the Labor Governments, hoped to reconcile the above domestic objectives with perennial anxieties for Australia's external position. It was an attempt to deliver economic security for Australia by modifying the United States' campaign for multilateralism, and in this context it pitched the principles of Australia's foreign economic policy (the primacy of domestic policy to achieve full employment) against those of the United States (non-discriminatory trade, the reduction of trade barriers, convertible currencies at fixed exchange rates, and the loosening of exchange controls).<sup>224</sup> It was also an approach consistent with the foreign policy of the Labor Governments more broadly. This policy, which was driven through the years under consideration here by Curtin, Chifley and, especially, Evatt, sought for Australia a distinct international identity as a representative 'middle power', especially in the forums of the various new international economic institutions and the United Nations.

The settlement of wars had, since the Napoleonic era in the European tradition at least, usually been decided by international conferences and in this the Second World War was no exception. Indeed, in the case of the Second World War, the conferences began well before the completion of hostilities. Concerned both with the peace itself and postwar reconstruction, it was the format of the international conference through which questions of the international economy were decided, thus giving them a significance unusual before or since. In Australia's efforts to propagate the employment approach therefore, the international conference was to feature strongly. This, combined with the distances involved for Australian participants and the difficulties of international transport and communication, meant that conference delegates were granted enormous opportunities to shape the positions of the countries they represented - causing, in turn, tensions to develop between Government ministers and their chosen delegates. As a consequence, the following narrative will devote much space to the succession of conferences through which the countries that were to form the 'United Nations' planned the postwar world. Each conference

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<sup>223</sup> Of course, if the motives of the Government were consistent with a Keynesian discourse, then so were the means at their disposal. During the war years, the economic power of the Federal Government increased immeasurably, partly because of wartime controls (many of which carried over into the peace for a time), but largely as a consequence of the moving of income-taxing powers from the states to the Commonwealth. The issue of the powers and the growth of the Commonwealth will be examined later, but for more on this, see Lee (1996), p.82.

<sup>224</sup> The idea that the foreign policy of the Curtin and Chifley Government's was especially motivated by this idea of achieving economic, as opposed to military, security is advanced strongly in Lee (1995).

marked, in this sense, a stage in the progression of the employment approach, not only in terms of its propagation, but in its nature, as it was shaped to fit changing circumstances and shifting alliances.



## **Chapter Five**

### **The Beginnings of the ‘Employment Approach’**

#### **5.0 Article VII**

In February 1942, representatives of the United States and the United Kingdom signed the Anglo-American Mutual Aid Agreement. As *quid pro quo* for the provision of ‘Lend-Lease’ aid to Britain and its allies (including Australia) in the Second World War, the Mutual Aid Agreement set out the preferred payment option of the United States. This was not in money or in goods, but in the form of an undertaking by the Governments concerned to collaborate in a post-war trade policy directed towards the objectives desired by the United States.

These ‘desired objectives’ were manifested in the draft Article VII of the Agreement, the contents of which had been argued over by American and British officials since July 1941. The core around which much of the controversies of international post-war reconstruction would revolve, the first draft of Article VII sought;

to promote mutually advantageous economic relations between [the United States and the United Kingdom]...and the betterment of world-wide economic relations; they shall provide against discrimination in either the United States of America or the United Kingdom against the importation of any produce originating in the other; and they shall provide for the formulation of measures for the achievement of these ends.<sup>225</sup>

It was the issue of ‘discrimination’ which was to prove the sticking point, both then and later. Article VII was the product of the State Department, and Cordell Hull, the Secretary of State, who (as noted in Section II) had been a keen advocate of non-discriminatory free trade throughout his long term in office. Sharing a Cobdenite conviction that barriers to trade and the denial of access to raw materials were the prime causes of war, Hull had used the United States bargaining strength in the late 1930s to bring about a reduction in trade barriers in a number of countries via bilateral agreements. Faced now with the opportunity to deploy even greater bargaining strength against the United Kingdom and, more specifically, against the imperial preference arrangements that had long been a particular irritation, Hull was determined to ensure that the elimination of trade restrictions become part of the war aims of the United States. Hull’s version of multilateralism was in many ways simply a throwback to the particular American version of progressive thought which sought to combine ‘humanitarian ideals with free enterprise and the profit motive’ (Bennett Woods 1990, p.15). A twentieth century manifestation of Jeffersonian internationalism, multilateralism was an article of faith within key elements of the

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<sup>225</sup> This first draft of Article VII was the product of the US State Department and was handed to Keynes on 28 July 1941. It is cited here from Moggridge (1992), p.661.

Roosevelt administration and outside of it, an answer within elite American opinion to 'the human dilemma of security versus freedom' (Bennett Woods 1990, p.20).

British reaction to this first draft of Article VII was unfavourable. Keynes, in the United States during 1941 on behalf of the British Treasury, handled much of the early negotiations over Article VII with the State Department. Keynes was less concerned than some others within the British government over imperial preference, but he greatly feared a return to the old 'gold' order. Writing to Assistant Secretary of State Dean Acheson the day after receiving the draft, Keynes explained his views:

My strong reaction against the word 'discrimination' is the result of my feeling so passionately that our hands must be free to make something new and better of the post-war world; not that I want to discriminate in the old sense of that word - on the contrary, quite the opposite.

But the word calls up, and must call up...all the old lumber, most-favoured nation clause and the rest which was such a notorious failure and made such a hash of the old world. We know also that it won't work. It is the clutch of the dead, or at least the moribund, hand. If it was accepted it would be cover behind which all the unconstructive and purely reactionary people of both our countries would shelter.<sup>226</sup>

Keynes's reaction to Article VII was based upon fears of its implications for his own plans for the post-war world and his assessment of the source of failure between the wars. His reaction was also informed, however, by a knowledge of the likely precarious financial position of the United Kingdom at war's end. Keynes told the Americans that because of shipping losses, the loss of export and other income, the sale of overseas assets to finance war purchases and the subsequent demands for reconstruction itself, Britain would need to increase exports by over 50 percent above pre-war levels to maintain external balance. Keynes also told the American officials that should world income be insufficient to deliver such an increase, Britain could be forced to go it alone via hefty increases in trade barriers. Keynes's own plans for the restoration of the international economy will be examined in detail below. Suffice to note at this stage that they envisaged the extension of *General Theory* reasoning into the international sphere. As he told Hubert Henderson in April 1942: 'If effective demand throughout the world is adequate, the demand for exports will always be equal to the supply of them, and gluts will not occur'.<sup>227</sup> Unfortunately this was not often recognised by officials in the State Department who, indeed, often assumed that the projection of the *General Theory* into an international context spelled economic nationalism (Bennett Woods 1990, p.49).

In December 1941, in a bid to at least partly meet British objections, the State Department produced a revised draft of Article VII. The commitment to the elimination of trade barriers and discrimination remained, but there was also reference

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<sup>226</sup> It was Acheson who handed the Draft to Keynes the day before, and who was therefore present for Keynes's verbal explosion at its contents. The note the next day was in explanation of this outburst. Keynes's letter to Acheson is contained in Keynes (1979a), pp.177-178.

<sup>227</sup> 'Keynes to Henderson', 5 April 1942, Keynes Papers, Treasury Records, PRO T247/67. This letter is also cited by Bennett Woods (1990), p.49.

to the expansion of employment and consumption. To these ends, the relevant passages of the redraft included the;

provision for agreed action by the United States of America and the United Kingdom open to participation by all other countries of like mind, directed to the *expansion by appropriate international and domestic measures of production, employment and exchange and consumption* which are the material foundation of liberty and welfare of all peoples; to the elimination of all forms of discriminatory treatment in international commerce and to the reduction of tariffs and other trade barriers...[emphasis added]<sup>228</sup>

British reservations with regard to the unqualified elimination of trade barriers nevertheless remained, and led to attempts to delay signature of the Agreement. Pressure from the United States continued though, and it was made known to British officials that great importance had been attached to the Agreement by Roosevelt personally and that continued negotiation would not be entertained. In the light of these pressures, representatives of the British and United States governments finally signed the Mutual Aid Agreement on 23 February 1942 (Gardner 1956, pp.60-62).

### *Australia*

The Australian Government had been kept informed of all these developments via the Dominions Office, its High Commissioner in London (still Bruce), and its Minister in Washington, Richard Casey. Australia's traditional relationship with the United Kingdom, and the perception in the United States that Britain spoke for all of what it still regarded as the British Empire, meant that London was by far the most important source of information for the Australian Government for Article VII. Nevertheless, the information gleaned in Washington was useful in balancing the 'insiders' view Australia enjoyed from London, and in obtaining a perspective from the other side. Casey was able to report, for example, that the State Department regarded Keynes as being 'too preoccupied with internal conditions' and only able to see 'national controls' as the solution.<sup>229</sup> He reported too, the Department's confidence that the United States could, in the absence of agreement, make its own way. This would not be the preferred option, but in the end the 'U.S. would win a trade war because she is relatively less dependent on foreign trade'.<sup>230</sup>

Despite keeping the Australian government more or less informed of developments, neither the British nor the Americans sought the view of Australia during these early stages of the Article VII negotiations. The matter had not passed without interest in Australia though, and in late 1941 the Commonwealth Government formed an Inter-Departmental Committee on External Relations (ICER), representing the Departments of Treasury, External Affairs, Trade and Customs, Commerce and Agriculture and Labour and National Service. Importantly, the membership of the ICER also included the economists of the Financial and Economic Advisory Committee (F&E; more of

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<sup>228</sup> The re-draft is reproduced in Gardner (1956), pp.58-59.

<sup>229</sup> Casey, reporting a conversation with Hawkins of the U.S. State Department in October 1941, is cited in an undated memorandum written by Gerald Firth, 'Notes taken from material privately in October 1941, with an important bearing on the early history of Article VII', NAA, A9816/3, 1943/444 Part 1, Article VII - Economic Policies (I.C.E.R. and F&E Reports and Material).

<sup>230</sup> *ibid.*

which below) whose members included at this time Giblin, Copland, Melville, James Brigden, H.C. Coombs, and Roland Wilson.<sup>231</sup> From the beginning, the consideration of the *economic* implications of Article VII was the preserve of the economists of the F&E.

With very little time remaining before the United Kingdom and the United States would sign the Mutual Aid Agreement, the ICER prepared a preliminary report in February 1942 which recommended to the War Cabinet that Australia support Article VII, subject to future negotiations over the details.<sup>232</sup> Basing its recommendations on a most pessimistic reading of the postwar situation, this preliminary advice cautioned against the rejection of international co-operation in a world which was very likely to disintegrate at war's end into one divided by restrictive trade and other barriers, and in which countries 'would exploit economic, political and military advantages to secure favourable trade terms'.<sup>233</sup> Such a world offered 'little future for Australia' and should be avoided, even if 'a sympathetic understanding of the American viewpoint' meant the abandonment of imperial preferences.<sup>234</sup> The ICER recommended, however, that Australia highlight the 'positive' aims of Article VII, 'the expansion of production, employment and the exchange and consumption of goods', to smooth the process.<sup>235</sup>

The ICER's recommendations were accepted by the War Cabinet and formed the basis of a telegram despatched to the Dominions Office, officially notifying the British Government of Australia's preliminary reactions.<sup>236</sup> The telegram was also made known informally to United States officials by Casey.<sup>237</sup>

The ICER's preliminary report was consistent with what would become the employment approach, but it is important to note that at this stage its acceptance by the Government scarcely a month after the beginning of the Pacific war had little to do with economics. Recalling the issue later, Chifley wrote:

At that time Australia was in a most desperate position, and it had no alternative but to join in the undertaking given to the United States by the United Kingdom. At that time the United Kingdom could not help us because physically it was incapable of doing so, and it was only because of the volume

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<sup>231</sup> At this time, Giblin, the Committee's Chairman, had just retired as Ritchie Professor at the University of Melbourne, James Brigden was Secretary of the Department of Supply and Development and Dr H.C. Coombs was Economist at the Treasury. Copland had been appointed Economic Consultant to the Prime Minister by the previous United Australia Party Government's of Menzies and Fadden, and was retained in this post by the new Curtin Labor Government. Melville was Economic Adviser to the Commonwealth Bank and Roland Wilson was Commonwealth Statistician and Economic Adviser to Treasury. Other members were co-opted when needed. Soon after this initial consideration of Article VII, R.C. Mills, Professor of Economics at the University of Sydney and E.R. Walker, Professor of Economics at the University of Tasmania, joined the F&E. For details of the composition of the F&E, see Maddock and Penny (1983).

<sup>232</sup> The ICER report became War Cabinet Agendum No.88, 1942. The Agendum can be found in NAA A989/1, 43/735/50/1.

<sup>233</sup> *ibid*, p.4.

<sup>234</sup> *ibid*, p.5.

<sup>235</sup> *ibid*, p.5.

<sup>236</sup> Cablegram, Prime Minister's Department to Secretary of State for Dominion Affairs, 12 February 1942, NAA A989/1, 43/735/50/1.

<sup>237</sup> Australia was not asked to sign the Mutual Aid Agreement until September 1942.

of aid supplied by the United States in the form of personnel, aircraft, equipment and services that Australia was not invaded...<sup>238</sup>

### *Giblin*

The War Cabinet's acceptance of the ICER's preliminary recommendations had also included the proviso that the F&E consider further the 'positive aims' by which British and United States collaboration should operate but, with more pressing issues at hand, the matter was not considered in detail until May 1942.<sup>239</sup> Then the issue once more became urgent and, once more, the stimulus was external - in this case the information that conversations would soon begin between officials of the United States and the United Kingdom over Article VII. The list of likely topics to be covered by the talks, which included not only considerations of the relaxation of trade barriers, but also the first hints of what would emerge as Keynes's Clearing Union proposal, excited the interest of the members of the F&E and, in particular that of Giblin, its Chairman.

Giblin was the most senior economic adviser to all three Commonwealth governments during the Second World War and in the early war years, the most influential. Certainly he was the driving force behind the F&E. As the Committee's only full-time member since his retirement from the University of Melbourne in 1940, Giblin seems to have served as the 'one-man synthesiser' of its many papers and reports and the conduit through which they were ultimately presented to the politicians (Maddock and Penny 1983, p.31). Appointed chair of the F&E at the time of its creation by Prime Minister Lyons in 1938, Giblin maintained the trust and confidence of the Curtin Government when it took power in October 1941.<sup>240</sup>

Giblin has often been regarded as one of the principals behind the propagation of Keynesian economics in Australia, in which context his pioneering work on the multiplier is most often cited. Giblin's move to a more expansionist stance from his 'relative cost adjustment' advocacy in the earliest years of the depression, clearly evident (Section I) with regard to Ottawa and the WMEC, took on a more pronounced form as the decade proceeded. This was particularly the case with regard to public works financed by Treasury Bills. Writing to the Secretary of the Treasurer in November 1934, Giblin expressed his fear that recovery was under threat and that labour, 'miraculously steady and sane' throughout the depression, could not wait upon international recovery.<sup>241</sup> In this context, Giblin believed that the only means 'of preventing greater unemployment and an increase of State deficits is public expenditure from loans on Treasury Bills'.<sup>242</sup> The Commonwealth Bank had resisted such financing before, but should it continue to do so, 'Government and Parliament

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<sup>238</sup> Speech by the Prime Minister, J.B. Chifley, in the House of Representatives on 26 February 1948, cited in Crawford (1968), p.15.

<sup>239</sup> War Cabinet Agendum No.88, 1942, *op. cit.*, p.6.

<sup>240</sup> For more on Giblin's relationship with the new Government, see Crisp (1961).

<sup>241</sup> This memorandum, which is contained in the 'Treasury Secretary's Papers 1932-5', NAA A1968/391, item 46, is cited from Cain (1988a), p.7.

<sup>242</sup> This same memorandum, cited from Cain (1983), p.215.

must use their powers...If this Government will not take a firm stand with the Bank Board, we shall soon see a Government that will...'.<sup>243</sup>

For several months over 1937-38, Giblin took up residence as a fellow at King's College, Cambridge, where he had been a student in the 1890s and where he was able to renew his personal contact with Keynes. The then Provost of King's recalled many years later that Giblin and Keynes shared during this tenure 'many fruitful talks', and that Giblin had even boasted of having 'converted Keynes on some points to his own view'.<sup>244</sup> Frustratingly, though, for those seeking to establish a theoretical rapport between the two at this time, there is nothing in Giblin's own writings to suggest a convergence of theoretical conviction. Indeed, according to Giblin's student, R. I. Downing, Giblin did not read the *General Theory* until January 1938, and only then aboard ship on his way to Cambridge. He quoted Giblin as writing that this reading imparted not much more definite result 'than the need to read it again', and that in 'so many places' he could not get 'the convincing picture of things happening just so - there are so many alternatives and qualifications to be thought out'.<sup>245</sup>

Giblin's return to Australia in 1938 and his Chairmanship of the F&E thrust him into planning for war and it was here that a clear conception of the economy akin to that contained in *The General Theory* can be glimpsed in his work. From 1939 to late 1941, the overriding concern of the F&E was the direction of as many resources as possible into the war effort. This concern was, in fact, a twofold one. Firstly, output had to be maximised by ensuring the full employment of the factors of production. Secondly, once this had been achieved, as much of this output as possible had to be applied to the war.<sup>246</sup>

With the external constraint no longer an issue under wartime controls, Giblin and his colleagues at the F&E had no difficulty in proposing a solution to the first of these concerns - public works (of a defence nature) financed by borrowing from the central bank to quickly absorb the unemployed and leaving the private sector (in this initial phase) unaffected. Plans along these lines were advanced by the F&E in 1939 and largely accepted by the Government, despite the opposition of the Secretary of the Treasury. They became a central component of the budget of November 1939.<sup>247</sup> The second concern, the diversion of resources in a fully employed economy, was more difficult but crucial if the inflation which had occurred during the First World War was to be avoided. In this context, the F&E advanced a further series of proposals

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<sup>243</sup> *ibid.* Giblin maintained throughout the later half of the 1930s, however, great fears for Australia's external position. These fears, expressed in his evidence before the 1936 Money and Banking Royal Commission, were such that on numerous occasions through the same period he was to return to the extreme pessimism of works such as his 'Australia in the Shadows' article of 1933. For more on the fits and starts of Giblin's advocacy during this period, see Cain (1988a).

<sup>244</sup> The Provost was John Sheppard, who quotes Giblin in Earp (1960), p.20.

<sup>245</sup> Giblin letter, January 1938, quoted in Downing (1960), pp.45-46.

<sup>246</sup> For more on this issue, see Maddock and Penny (1983), from which these paragraphs draw heavily, as well as Butlin and Schedvin (1977).

<sup>247</sup> These plans were contained in a number of memoranda over 1939/40, many of which are cited in Maddock and Penny (1983), pp.31-35. The F&E was formally a committee of Treasury, and as such reported to it and the Treasurer. The Committee seems to have had some success in convincing the then Acting-Treasurer, Percy Spender, of its views, but was less successful in convincing long-time Treasury Secretary, S.M. McFarlane, who remained suspicious of such financing. For more on this, and the political influence of the F&E during this time, see Maddock and Penny (1983), pp.35-37.

designed to limit private consumption and production - reducing non-war government spending, increasing taxes, raising loans, imposing controls on capital raisings by private companies, and so on. Direct controls only later became part of the F&E's armoury. Whether a function of the F&E's influence, or simply a function of practical imperative learnt through experience, all of these artifices found their way into Government policy at some point by war's end. The process was a slow one, though, and the political weakness of the Menzies Government meant that most of the increases in taxes did not occur until the coming of the Labor Government in October 1941 (Maddock and Penny 1983, pp.33-40).

The advice of the F&E on financing the war was informed by the knowledge and experiences of its members, but there is also no doubt that it was heavily influenced by Keynes's similar advocacy in the United Kingdom - with whom Giblin corresponded with regard to the Australian situation on a number of occasions over 1940-41.<sup>248</sup> Keynes's advocacy, which took the form of a series of articles in *The Times* in November 1939, but which were expanded in his *How to Pay for the War: A Radical Plan for the Chancellor of the Exchequer* in 1940, outlined a scheme by which the diversion of resources would be achieved by way of taxation and via the payment of a progressive proportion of incomes as compulsory savings. These would be released after the war - timed to coincide with the post-war slump many were expecting. The amount of resources which would need to be withdrawn from the private sector in order to forestall inflation - the 'inflationary gap' - could be calculated by estimating national income and deducting from this war spending, remaining non-war government spending and private sector outlays.<sup>249</sup> Because Keynes's plan also required estimates of income distribution (since different sectors of society would face different tax and compulsory saving levies), it required a much more sophisticated and systematic national accounting framework than was then available in the United Kingdom. For his own plans Keynes initially relied on estimates based on Colin Clark's work on devising a system of national accounts, but the take-up by the British Government of several aspects of *How to Pay for the War* quickly led to the appointment of James Meade and others to oversee the construction of a full national accounting framework.<sup>250</sup>

National accounting in Australia was more advanced than it had been in inter-war Britain, in part because of Colin Clark's work in his home country and in part because of what amounted to something of a national tradition in the area.<sup>251</sup> Nevertheless, it was the 'gap methodology' of Keynes which was used by Giblin and others in the F&E in submitting their war finance proposals. The importance of this in the context of the 'Keynesianising' of economic discourse in both countries is not something which should be overlooked. *How to Pay for the War* has, with some justification, come to be regarded as the first policy application of the model of the economy implicit in *The General Theory*.<sup>252</sup> Commenting upon the British Government's adoption of this methodology in its budget of 1941, Moggridge (1992, p.647) wrote

<sup>248</sup> This correspondence is contained in a number of files in the National Australian Archives, but is here cited from Maddock and Penny (1983), p.33.

<sup>249</sup> This is but a brief summary of the formulae in Keynes (1940), Chapter IX.

<sup>250</sup> In *How to Pay for the War*, Keynes referred to the 'brilliant... efforts of Mr. Colin Clark'. Keynes (1940), p.13. For more on the appointment of Meade, see Moggridge (1992), p.645.

<sup>251</sup> A tradition celebrated in Groenewegen and McFarlane (1990), Chapter 5.

<sup>252</sup> See, for example, Skidelsky (1996), p.91.

that it represented a 'revolution' in that it changed the whole question to be addressed in budgetary policy - from the issue of balance in the government's accounts, to the issue of balance in the economy itself. A similar 'revolution' had occurred in Australia a little earlier too, such that Crisp's observation of Casey's budget of 1938-39 that '[o]ne gathered that the general level of economic activity had an effect on budget totals but hardly the reverse', was untenable even by 1940.<sup>253</sup> In both cases, to use Moggridge's description (1992, p.647), 'it was all rather crude...but it was a beginning'.

### *Giblin's 19 questions - and the beginning of the 'employment approach'*

Giblin's response to the coming talks between American and British officials over Article VII was to circulate a list of questions (19 in total) to the members of the F&E.<sup>254</sup> Calling for a quick response, Giblin was acting on the ICER's desire to use the results to report to the Government and to instruct Bruce in London. Giblin's questions ranged from the political shape of the post-war world, trade and investment policy, to methods of propaganda which might prove necessary to counter the 'widespread prejudices and misunderstandings' with regard to economic policy amongst the general public.

By far the most important of Giblin's questions for the development of the future employment approach were two questions which specifically related to internal and external balance. Denominated as questions two and three, they recalled Giblin's own pre-occupation with internal *and* external balance but, surprisingly given his long experience of past failures, pointed to international co-operation as a necessary and obvious solution:

Question Two. What will be the world employment problem after the war, and how far can it be solved without international co-operation?...

Question Three. What will be the possibilities of maintaining employment in Australia after the war by an expansionary policy? What are the difficulties in the absence of international collaboration? To what extent can these difficulties be overcome and at what cost?...<sup>255</sup>

Questions two and three on Giblin's list were allocated to the Department of Labour and National Service where, in turn, each were referred respectively to two 'young' economists newly attached to the Department - Arthur Tange and Gerald Firth.

### *Tange*

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<sup>253</sup> Crisp's observation is cited from Whitwell (1986), p.54.

<sup>254</sup> The list of questions, under the heading 'Mutual Aid - Article VII', with Giblin's annotations directing each to an appropriate department for an answer, is contained in NAA, CP 184/1, Bundle 4. A list identifying the authors of various F&E documents, including answers to Giblin's 19 questions, is contained in a letter written by F.H. Wheeler (who generally acted as the Secretary to the F&E) to the Secretary of the Treasury, 25 June 1942. This letter is contained in NAA, CP13/1/1, 53.

<sup>255</sup> *ibid.*



A former student of Edward Shann, Arthur Tange was seconded from the Bank of New South Wales in 1942 to work for various Commonwealth Government Departments. Greatly influenced by Keynes's work, Tange's studies in economics at the University of Western Australia had been disrupted by the appearance of the *General Theory* in 1936, an event which he recalled caused a great deal of excitement amongst students and lecturers alike.<sup>256</sup> Tange was one of a number of young graduates recruited in the late 1930s to work in the Economics Department of the Bank of New South Wales, that creation of Davidson and Shann which, as discussed above, had done much via its *Circular* to propagate expansionist policies. Together with a number of other economists at the Department, as well as some of the leading younger economists at the Commonwealth Bank including Coombs, J.G. Phillips and E.B. Richardson, Tange was a member of the famous 'tea group' which assembled most mornings in Sydney in the late 1930s and early 1940s to discuss economics and other matters.<sup>257</sup> Keynesian economics informed much of their debate, as did their own Depression experiences and their 'reading of what was wrong with world economic relations'.<sup>258</sup>

Keynesian methodology was certainly apparent in Tange's 'answer' to Giblin's Question Three.<sup>259</sup> This was, undoubtedly as Giblin had expected, a most pessimistic view as to the chances of full employment being achieved in Australia without international co-operation. What must have surprised even Giblin though, was the degree of scepticism throughout Tange's paper as to the ability of the private sector to generate anything like full-employment in any case, notwithstanding the existence of any external constraint.

The underlying assumption of Tange's memorandum was that a new consensual social philosophy would emerge in the post-war world 'which will demand the eradication of unemployment more forcibly than before the War'. This would, in turn, demand a whole new relationship between government and business, since it would be the government that would become responsible for ensuring that the goals of this social philosophy were achieved. The enormity of this task could (using Keynesian

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<sup>256</sup> Interview with the author, 2 October 1992. Since the conduct of this interview, Sir Arthur Tange has published a small personal memoir of his role in Australia's attempts to secure an international full employment agreement. See Tange (1996).

<sup>257</sup> Phillip's became Governor of Reserve Bank of Australia after the retirement of Coombs in 1968, while Richardson was a Deputy Governor of the central bank and (after the Reserve Bank was hived off as a separate entity in 1959) Managing Director of the Commonwealth Bank. Other members of the group from the Economics Department of the Bank of New South Wales included Leslie Bury (later Commonwealth Treasurer under Menzies after turning to politics) and James Plimsoll (later Governor of Tasmania). The tea group was mentioned by a number of the economists interviewed in the preparation of this work, but details are available in Coombs (1981), pp.5-6. There was also a more 'senior' group which met at the same time which consisted, in the late 1930s at least, of Leslie Melville, Tor Hytten and W.C. Wentworth. The tea groups were started by Melville and Shann when the latter was at the Bank of New South Wales (interview with Sir Leslie Melville, 28 January 1993 and with Mr W.C. Wentworth, 8 September 1992).

<sup>258</sup> This quote is taken from an interview with Sir Arthur Tange by Professor J.D.B. Miller in February and April 1989, and preserved in the National Library of Australia (NLA), Oral History Collection, TRC-2447. In the interview with *this* author on 2 October 1992, Tange noted that the influence of Keynes was not so much on the surface, but in the methodology; as he put it, 'it got into their blood, was at the back of their mind'.

<sup>259</sup> Tange's memorandum was circulated amongst the members of the F&E from 18 June 1942. The memorandum can be found in NAA, CP13/1/1, 53.

‘gap-methodology’) be roughly calculated by first estimating the level of national income required for full employment, and then attempting to account for the primary determinants of short term changes in national income in Australia - changes in export income, private investment and changes in import replacement. Tange suggested that a starting point could be made by considering national income in 1940-41 (when the level of involuntary unemployment was close to zero) as a level acceptable to the new demands of the postwar era.<sup>260</sup>

Ensuring that national income would be at a level consistent with full employment was not something in Tange’s analysis which could be left to the private sector. According to Tange, ‘over the long-term Australian business will not have sufficient vitality to maintain an “acceptable” level of employment’. Significantly, given the position taken by Australian economists in the 1930s, Tange did not see this as a situation which could be rectified by monetary policy. There was, indeed, ‘little in the post-depression history of Australia to suggest that private enterprise will provide sufficient jobs, even if we make the monetary authorities bear some responsibility for unemployment’. In phraseology redolent of *General Theory* reasoning, Tange declared that the ‘conclusion is that monetary expansion will not achieve full employment if the technical means used are directed *merely to providing opportunities for private initiative*’ (emphasis added).<sup>261</sup>

What was required for full employment, therefore, was public investment. The efficacy of fiscal policy had been demonstrated, in Tange’s view, by the experience of wartime expenditure in reducing unemployment. This spending, moreover, had been largely financed by the issue of Treasury Bills by the Commonwealth Bank - another of the taboos of the Depression years. Demonstrating yet more of the confidence of what might be called ‘first order Keynesianism’, Tange was optimistic that the taboos of the past might be negated, and that ‘[w]ith the experience of wartime organisation of money and materials behind them, Australian business may put up with considerable controls and a heavy government debt-spending programme’. Tange even speculated that ‘new bogeys’ could be erected in place of the old; in particular, the ‘fear that Government expansion may slacken and throw their expectations out of joint’, which would ‘deter enterprise as effectively as the pre-war suspicion of “unsound finance” and “national bankruptcy”’. In such a changed philosophical setting, the idea that government spending was the ‘dependent variable’ fluctuating in inverse proportion to private investment would itself begin to change, creating the circumstances in which ‘business confidence and expectations may not allow Government activity to remain dependent and it may be forced to encroach more and more into a diminishing private sector, with ever-growing responsibilities for organising production and employment’. Finally, totally rejecting ‘crowding out’ arguments, Tange also noted that whatever the method of financing, government spending in Australia was always more likely ‘to borrow or tax savings of the community which would have been used to less effect or not at all’.<sup>262</sup>

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<sup>260</sup> *ibid.* Unemployment in 1940 has been estimated by Barnard, Butlin and Pincus (1977) to be around 5.3 percent.

<sup>261</sup> *ibid.*

<sup>262</sup> *ibid.*

Of course, the wartime experiences were precisely that - wartime experiences - the special circumstances of which were not likely to continue beyond the war. In this context, what was important was the way the circumstances of war protected Australia's balance of payments while the government-induced expansion of national income took place. But these circumstances - the assurance of a stable and high export income (mainly via Britain's purchase of the entire wool clip) and especially the boost given to import replacement - would not continue after the war, and led to Tange's conclusion that in the absence of international cooperation, 'it does not seem likely that Australia could maintain stable employment over the long period without restriction of imports' and without, therefore, a substantial cost to standards of living.<sup>263</sup>

In the absence of international cooperation, Tange painted a bleak world resembling an ever repeating 1939 with progressively higher tariffs and more stringent exchange controls. In such a world there might be some flows of capital, especially from a rich and dominant United States, but this 'would probably take the form that United States trade followed the dollar fairly directly and that the value to Australian exports was limited'. Under such a scenario Australia's prospects were grim. A short boom in the demand for primary commodities immediately after the war would soon be replaced by a world in which 'the markets for Australian primary industries would...tend to fall rather than rise'. With limited London funds and a public debt to service on account of war spending, Australia's net export income 'would not support imports on a pre-war scale, much less a higher level of imports by an increased working population'. Australia could use its trade bargaining power to some extent, and 'at a pinch get some financial support from Britain', but with certainty policy makers would have to keep one eye on the balance of payments. It was, in short, the 1930s revisited, when the attempt to get the 'best of both worlds...was accompanied by persistent unemployment'.<sup>264</sup>

### *Firth*

Another rising young economist who responded to Giblin's questions was Gerald Firth. Like Tange, Firth was attached to the Department of Labour and National Service, but prior to the war (1938-40) he was Ritchie Research Fellow at the University of Melbourne under Giblin.

The substantive component of Firth's 'answer' to Giblin's Question Two was contained in a memorandum he circulated to members of the F&E from 24 June 1942.<sup>265</sup> The memorandum was unequivocal in stating the theoretical positions upon which it was based, declaring that

the "classical" theory of international trade is accepted throughout as being substantially correct, *and the same attitude has been adopted towards the Keynesian theory of employment* (emphasis added)<sup>266</sup>

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<sup>263</sup> *ibid.*

<sup>264</sup> *ibid.*

<sup>265</sup> This memorandum is contained in NAA CP13/1/1, 53.

<sup>266</sup> *ibid.*

The main insight of the ‘Keynesian theory of employment’ was, according to Firth, that ‘the “natural” tendency of employment in a “closed” economy is to fluctuate about an average position corresponding to “less than full employment”’. Firth wrote that up until the 1930s Depression, the ‘majority of economists would probably have agreed that general fluctuations in employment were mainly due to “unnatural” behaviour of institutions such as bank and stock exchanges’. Unemployment, therefore, was the result of unwise policies such as the lowering of the rate of interest below its ‘natural’ rate in what would otherwise be a situation in which ‘Say’s law’ underwrote the ‘tendency of the “free” economy...towards competitive equilibrium with full employment’. This view was, he wrote, ‘naive’, but it remained important ‘chiefly in its probable influence over the decisions of the more conservative Treasury officials, central bankers and influential business men in the majority of capitalist countries’.<sup>267</sup>

Confronting the naivety of the old orthodoxy was Keynes’s *General Theory* as well as more dynamic analyses, of which Firth approvingly referred to the work of Roy Harrod and Joan Robinson.<sup>268</sup> There was, according to Firth, no doubt the remedies from these theories would deliver higher levels of employment and there was no *a priori* reason why they would necessarily distort the economic system of an otherwise private enterprise economy. But the political obstacles to such policies, ‘on account of the long-standing tradition of “producer-dominated” politics which exists in all capitalist countries’, remained strong.<sup>269</sup>

A much greater complication to the maintenance of full employment via expansionary policies, however, came from the need to maintain external balance. According to Firth, this ‘balance of payments problem’ was ‘likely to impede national efforts to maintain an internal rate of investment corresponding to a high level of employment’.<sup>270</sup> In the face of this constraint, the obvious temptation was for governments to attempt to insulate themselves as much as possible from international trade. For most countries complete insulation was neither possible nor desirable in terms of the costs to living standards which would come from being divorced from international specialisation. Of course, to the extent that some countries could attempt such a national solution, the employment problem of all other countries would be greatly magnified. Firth concluded this point with the observation (of which Giblin would have approved) that;

the total reduction in the standard of living is likely to be greater if attempts are made to solve the world employment problem on national lines, than it is if similar policies are pursued under conditions of genuine international collaboration.<sup>271</sup>

If the above story was true for most countries, it was certainly true, Firth argued, for Australia. Poorly endowed in relation to its standard of living (in terms of a market large enough to support scale economies), Australia was more dependent than most

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<sup>267</sup> *ibid.*

<sup>268</sup> And in particular to the latter’s *Introduction to the Theory of Employment* (1937).

<sup>269</sup> Firth memorandum, NAA, CP13/1/1, 53.

<sup>270</sup> Emphasis added.

<sup>271</sup> *ibid.*

on the regime of international specialisation which had grown up in the nineteenth century. Australia could not maintain full employment on its own and as far as post-war planning went, little could be done until it had 'more precise indications of the lines of policy likely to be followed by the other "capitalist" countries'.<sup>272</sup>

Firth concluded his memorandum with what he called the obvious 'moral' of the story - that Australia 'should energetically participate in the formulation of a *world* employment policy'. The American proposals were, he argued, little more than the reiteration of the 'naive' orthodoxy of pre-Depression economics, whose obvious solution could simply 'be reduced to the level of devising ways and means of removing barriers to international trade'. Firth insisted that the issues were broader than this, and if the 'employment problem' was to be effectively tackled by measures based on international co-operation, it was important that early agreement should be reached on overcoming the 'political, institutional and technical difficulties of instituting countervailing measures which are sufficiently flexible to keep employment fluctuations within moderate limits'. In a final rejoinder reminiscent of Keynes, Firth noted that 'the "entire (capitalist) world" could itself be regarded for all practical purposes as a Closed Economy'.<sup>273</sup>

## **5.1 The ICER Report**

On 26 June 1942, a meeting of the F&E was convened in order that the answers to Giblin's questions could be 'defended or oppugned', and to draft a final report of the economists for the ICER on Australia's position in relation to Article VII. Before the meeting, which was attended by Giblin, Melville, Copland, Wilson and Frederick Wheeler as secretary, Giblin circulated his own summary of the responses.<sup>274</sup> This summary differed in no substantial way from the employment scenarios painted by Tange and Firth. The members in the F&E in turn, made what were only cosmetic changes to Giblin's synthesis in what then became the economists' final report.<sup>275</sup>

The report, which was printed by the Department of External Affairs as an ICER paper in August 1942 and circulated to government ministers, took up Tange's and Firth's line that the unemployment levels that prevailed in the inter-war years would not be tolerated by the general populace (in particular by returning soldiers) after the war.<sup>276</sup> It also highlighted the constraints imposed by the external accounts, noting that if employment was maintained at anything like its wartime level, consumption would be substantially higher than it had been in the inter-war years. What was required, therefore, was 'a prospect of export income and of London funds appreciably higher than in the pre-war years'. The ICER report shared the pessimism of Tange and Firth, however, noting that, in the *absence* of international

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<sup>272</sup> *ibid.*

<sup>273</sup> *ibid.* A similar argument is implicit, for example, in Keynes's treatment of 'Mercantilism' in Chapter 23 of *The General Theory*.

<sup>274</sup> Giblin's summary, which was titled 'Theses Quaedom Oeconomicae', is contained in NAA CP184/1, Bundle 4.

<sup>275</sup> This can be seen from the minutes of this meeting written up by Wheeler. The minutes are contained in *ibid.*

<sup>276</sup> The report, which was titled 'Australia's Position in Relation to Article VII of the Anglo-American Mutual Aid Agreement' and dated 20 August 1942, is contained in NAA CP43/1/1, Bundle 5/1943/444/Pt.1.

collaboration, London funds were likely to be low, exports were likely to boom in the initial reconstruction phase but 'the long-term prospects' for exports were 'not very good'. Capital movements were likely to be negative or small.<sup>277</sup>

Nevertheless, the ICER report presumed that it would 'be socially undesirable and politically impossible to meet these difficulties by abandoning the policy of maintaining employment *at all costs*'.<sup>278</sup> Accordingly, 'possible defences' of Australia's external position considered by the ICER report included exchange depreciation, negotiation of Australia's debts, exchange controls and restrictions on imports. Exchange depreciation had been one device deployed by Australia in the Depression (and advocated by these same economists), and was something which could be used in the future - 'boldly and objectively as possible' as required. Debt re-negotiation was a desperate measure only, while exchange controls should be continued after the war but with a generally 'nominal' degree of control.<sup>279</sup>

Restriction of imports via tariffs and other trade barriers was perhaps the most obvious measure, and the most likely to work, in maintaining the external accounts while pursuing full employment. But, as noted by Tange, Firth and Australian economists *ad nauseam* before them, such a policy would not come without great cost to average real incomes. The imports excluded were likely, the report contended, 'to be replaced by very uneconomic industries, which...will persist and be a lasting drag on the country when active measures are no longer needed to maintain employment'. Import restrictions were also likely to cause resentment in other countries and with it, retaliation.<sup>280</sup>

The obvious answer to Australia's difficulties, then, was precisely that framed by Giblin from the outset - international co-operation. The report put it thus:

If the principal countries of the world, and particularly [the] United States of America, adopted consistently and effectively the same policy to maintain employment, the danger in the export market might be much reduced.<sup>281</sup>

It was against this ideal then, that Article VII had to be considered. According to the report, what was required of Article VII was that its 'positive features' - the expansion of production and employment, should precede its 'negative' features - the removal of barriers to trade. But in this all depended upon the attitude of the United States. This would not be known until the exact nature of any proposals for international collaboration were known. In the meantime, the economists' report concluded with a strong appeal to the political decision-makers for whom it was written that, while Australia was amongst the countries likely to suffer most in a world depression;

international collaboration offers a fair prospect of escaping these difficulties...and [of] taking part in a systematic upward movement of world

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<sup>277</sup> *ibid.*

<sup>278</sup> Emphasis added, *ibid.*

<sup>279</sup> *ibid.*

<sup>280</sup> *ibid.*

<sup>281</sup> *ibid.*

prosperity which will benefit no country more than Australia ...It should be the policy of Australia to do everything possible to bring these aims and aspirations to a successful issue.<sup>282</sup>

## **5.2 The ‘Clearing Union’**

The ICER Report was distilled into a telegram for communication to the British Government, but the issuing in late August 1942 of an invitation to the Australian and other Dominion Governments to ‘intimate consultations’ with the United Kingdom meant that the message was never sent.<sup>283</sup> As it turned out, the scheduled talks between British and American officials over Article VII were postponed to a later date.

The British invitation to talks, to take place in London in October, made scant reference to Article VII but placed much emphasis upon the plans for an ‘International Clearing Union’, as well as a proposed ‘buffer stocks’ scheme designed to promote stability in commodity prices. Of these two schemes, the Clearing Union proposal was by far the most advanced, and, by the time the London talks had begun, the scheme was part of a formal Treasury document which had been passed on to the Americans. Although the ICER Report had been written for the proposed Article VII talks, it proved adaptable to these new proposals as well. The employment approach was on its way to becoming a ‘policy for all seasons’ (Butlin and Schedvin 1977, p.654).

### *Keynes’s Plan*

The latest in the long line of proposals advanced by Keynes for the reform of the international monetary system, the Clearing Union plan had evolved through a series of drafts, the first of which had been written in August 1941. The scheme had become less radical with each successive redrafting as it met the resistance of colleagues and officialdom, but its *raison d’être* remained the replacement of regimes that Keynes maintained had not solved the problem of maintaining balance of payments equilibrium between countries since ‘methods of barter gave way to the use of money’ (Keynes 1980a, p.21). The inter-war years had been a useful laboratory for demonstrating the failures of ‘alternative false approaches to the solution’, as a quasi-gold standard gave way to floating rates which in turn had collapsed into competitive deflation, devaluation and the erection of devices to ‘restore the balance of international commerce by restriction and discrimination’ (Keynes 1980a, pp.22-23). With the arrival of war, the international monetary system had disappeared completely but this, at least, according to Keynes, was no bad thing. It made things ‘possible to-day which would have been impossible if they involved the prior disestablishment of a settled system’ (Keynes 1980a, p.22).

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<sup>282</sup> *ibid.* Even at this comparatively early stage, Treasury was generally sceptical of what would become the ‘employment approach’, and in some notes written for the Secretary, Frederick Wheeler (secretary to the F&E but still in the employ of the Treasury) criticised the F&E’s ‘abstract’ rather than ‘realistic’ approach to Australia’s post-war position. As shall be taken up below, such hostility was only to grow with time.

<sup>283</sup> Details of the Dominion Office Cables are contained in a memorandum of Treasury titled ‘Mutual Aid - Article VII’, undated (but sometime in late May 1942), and contained in NAA, CP 184/1, Bundle 4.

In Keynes's view, the principal problem of what he collectively categorised as 'international currency *laissez-faire*' was its in-built deflationary bias. Under *laissez-faire*, the adjustment for balance of payments imbalances fell disproportionately upon the debtor country. A debtor country could not allow its reserves to fall below zero, but there was no upper limit to the amount of reserves that a creditor country could acquire. For the debtor country, then, adjustment was compulsory, this involving, price and wage deflation, currency depreciation and the like. By contrast, the creditor country was under no compulsion to adjust at all. The old system had 'worked' only by forcing adjustment in the most socially disruptive way upon countries least able to cope with it. The object of the new scheme, accordingly;

must be to require the chief initiative from the creditor countries, whilst maintaining enough discipline in the debtor countries to prevent them from exploiting the new ease allowed them in living profligately beyond their means. (Keynes 1980a, p.30)

Such were the broad presumptions which underlay the Clearing Union. The Draft which was to be the subject of the talks between Britain and the Dominions in 1942 was the fifth one, modified after correspondence with Dennis Robertson, James Meade, Richard Kahn, R.G. Hawtrey, Roy Harrod and other Treasury officials.

#### Proposal for an International Clearing Union: Fifth Draft

The central idea underlying the Clearing Union was the extension of the principle of banking into the international monetary system. More specifically, the Clearing Union was to act as a kind of 'central bank for central banks', within which member states could settle their exchange balances between each other by debiting and crediting their accounts with the Union. The principle was the same as that traditionally employed by commercial banks, under which the myriad of transactions between their customers were distilled down into a limited number of offsetting transactions between each other. As with any closed system, debits and credits were necessarily equal, so the system could never be short of liquidity, nor could there be any doubts as to the credit risk of the Clearing Union itself. The ability to avail of an overdraft facility meant that the accumulation of credit balances by one country did not necessarily lead to unemployment in another. According to Keynes, the 'substitution of a credit mechanism in place of hoarding would have repeated in the international field the same miracle, already performed in the domestic field, of turning a stone into bread' (Keynes 1980a, p.171).

Balance of payments deficits would be represented as an overdraft on a member's account, and surpluses as a credit balance. These accounts were to be denominated in the form of a new international currency, called in the fifth draft 'Bancor'. Bancor was fixed in terms of gold, but its value against gold could be changed by the Governing Board of the Clearing Union. Gold could be exchanged for Bancor, but the reverse could not occur so that in this aspect alone the Clearing Union would contribute to international liquidity. In seeing off gold, the purpose of the Clearing Union was not so much as to dispense with the metal as *one form* of liquidity, but its purpose certainly was 'to supplant gold as a governing factor' (Keynes 1980a, p.183).



A member's debit position with the Clearing Union would be limited by its 'quota'. The quota was non-contributory, and was calculated as a percentage (75 percent in the fifth draft) of the average of the sum of a member's exports and imports over the previous three years. In any one year, a member could overdraw its account by up to a quarter of the quota. Should a member's balance of payments deficit be in excess of this, a charge of 1 percent per annum interest would be levied, but it would also be entitled to devalue its exchange rate by up to 5 percent. Should a member's balance of payments deficit reach over half of its quota, a further 1 percent charge would be levied and the member could be *required* by the Governing Board to devalue, impose exchange controls or undertake other measures the Board thought necessary.

A truly novel feature of the Clearing Union, and one which again highlighted its expansionary bias, was that *credit* balances attracted many of the same penalties imposed upon debtors. Credit balances in excess of a quarter of a quota would have a 1 percent charge levied upon them and the member concerned would be permitted to revalue its exchange rate by 5 percent. Should a credit balance exceed one half of a member's quota a further 1 percent charge would be levied (Keynes 1980a, pp.173-174). In earlier drafts such a situation *required* a member state to revalue, but this was dropped in the draft seen by the Australians in favour of a recommendation from the Governing Board to engage in one or more of the following:

- (a) Measures for the expansion of domestic credit and domestic demand;
- (b) The appreciation of its local currency in terms of bancor, or, alternatively, an increase in money wages;
- (c) The reduction of tariffs and other discouragements against imports;
- (d) International loans for the development of backward countries. (Keynes 1980a, p.175)

In early versions also, any surplus in excess of 100 percent of a quota could be confiscated, this being again deleted in the version examined by the Australian economists. However, in a further measure to improve liquidity, Keynes proposed that countries could avoid these charges by lending and borrowing Bancor between each other.

Member states entering the Clearing Union would agree amongst themselves the initial exchange values of their currencies in terms of bancor, and these would remain unaltered, except with the approval of the Governing Board or for the reasons outlined above. A transition period of about five years would be allowed during which special consideration would be granted 'on the ground of unforeseen circumstances' (Keynes 1980a, p.172). Keynes recognised that the transitional period after the war presented his scheme with possible difficulties if, as some believed, world effective demand exceeded the supply of goods. In these circumstances, Keynes proposed that the overdraft quotas be delayed or be allowed at a reduced level. Keynes himself did not think this likely, and he remonstrated that in the early post-war years that '[w]e must not be over-cautious. A rapid economic restoration may lighten the tasks of the diplomatists and the politicians in the resettlement of the world and the restoration of social order' (Keynes 1980a, p.194).

Membership of the Clearing Union would be open to all nations, but only the 'founder' members, the United States, the United Kingdom and later the Soviet Union, could individually appoint representatives to the Governing Board. Other states could appoint representatives to the Board only in geographical groups (Keynes 1980a, p.175).

Finally, while the Clearing Union aimed at 'the substitution of an expansionist, in place of a contractionist, pressure on world trade', it was not itself *sufficient* for long term equilibrium (Keynes 1980a, p.176). For this, there was needed a new way of thinking. In a passage which must have delighted his Australian readers, Keynes referred to this new way of thinking thus:

It used to be supposed, without sufficient reason, that effective demand is always properly adjusted throughout the world; we tend to assume, equally without sufficient reason that it never can be. On the contrary, there is a great force in the contention that, if active employment and ample purchasing power can be sustained in the main centres of world trade, the problem of surpluses and unwanted exports will largely disappear...(Keynes 1980a, p.180).

### *Australian Delegation*

The 1942 London talks were conducted at the 'official' level only. The meetings were for the most part formally 'chaired' by Sir Richard Hopkins, Head of the British Treasury, but in practice 'the actual conduct and initiative of the meetings was largely in the hands of Keynes'.<sup>284</sup> Other economists, in what could only be regarded as an extremely 'heavy-weight' British team, included D.H Robertson, Lionel Robbins and James Meade. Australia's delegation to the talks was led by Roland Wilson, at that time head of the Department of Labour and National Service. Wilson's economic education had begun at the University of Tasmania but he had completed doctorates at both the Universities of Oxford and Chicago, the latter under Jacob Viner. Wilson had joined the Treasury in 1932 and had been Commonwealth Statistician from 1936.<sup>285</sup> Like many of his generation of Treasury officials, Wilson regarded himself as a pragmatist with regard to economic theory. Less a disciple of the economics of Keynes than some of his colleagues in Australia, Wilson nevertheless was keen to adopt many of its prescriptions, particularly in the context of international policy.<sup>286</sup>

According to Wilson's report of the talks, the intention of the British officials with regard to the Clearing Union was to invite Dominion debate upon a draft which could then form the basis for formal discussions with the United States. This caused some confusion with Dominion delegates at first, with Wilson reporting that 'it appeared that we were being invited to assist in the revision and even the editing of the papers under discussion, while at other times a suggestion appeared to be in the air that the British representatives retained full freedom to make such modifications in the

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<sup>284</sup> 'Notes on R.W's Account of his Travels', Minutes of F&E meeting of 22 January 1943 by F.H Wheeler and G.G. Firth, NAA A9816/3, 1943/444 Part 1. See also Roland Wilson's report to the Prime Minister, John Curtin, on 'Post-War Economic Talks, London, October-November, 1942', 16 January 1943, NAA A601/1, 40/1/8.

<sup>285</sup> This, and subsequent, biographical details are gleaned from Groenewegen and McFarlane (1990), pp.216-219.

<sup>286</sup> For more on Wilson's economic philosophy, see Whitwell (1986).

proposals as they might subsequently deem fit'.<sup>287</sup> Nevertheless, in the end, Dominion representatives got much of what they wanted.<sup>288</sup>

The revisions sought by Wilson primarily related to the obligations of creditor countries in the Clearing Union and the exercise of the powers of its Governing Board. His submissions on both of these came after consultation with members of the F&E in Australia (with Melville playing the leading role), to whom Wilson had sent a copy of the Clearing Union draft as soon as he had arrived in London.

The F&E regarded the provisions of the Clearing Union as they related to debtor countries as 'effective', but they saw the restraints on creditor nations as 'very insufficient'.<sup>289</sup> In particular, they were concerned that while the Clearing Union encouraged members to keep credit balances within limits, it did not specify at all the method by which this might be arrived at. Credit balances could be used, for example, to 'buy up the capital assets of other countries', rather than being extinguished by the creditor nation increasing its level of imports.<sup>290</sup> As such, the F&E proposed that, as a condition of membership of the Clearing Union, member countries be compelled to 'accept definite obligations' should it find itself in a creditor position. These obligations, the F&E acknowledged, might be difficult to define, but they could include a 'pledge...to maintain a policy of full employment'.<sup>291</sup> The F&E also favoured, as Keynes had in earlier drafts, the confiscation of credit balances should they persist beyond a certain level.

With regard to the exercise of powers within the Union, the F&E was anxious to ensure that countries 'which are not great powers', such as Australia, should be able to have an effective voice.<sup>292</sup> They recognised the 'necessity of a comparatively small executive' as that envisaged in the Governing Board, but proposed that 'there should be a General Council of the Union, with over-riding powers on general policy, meeting at least once a year, on which each Member Country would be separately represented'.<sup>293</sup>

Wilson advanced both of these concerns in the London meetings and, on the position of creditor obligations, was successful in having a new paragraph inserted in the Clearing Union draft which made clear that it was against the 'spirit and expectation of the Plan for large credits to exist'.<sup>294</sup> Wilson was also partially successful in having the concept of a General Council accepted, the new draft requiring the Governing Board 'to make annual report and shall convene an annual assembly at which every member State shall be entitled to be represented individually and to move proposals' (Keynes 1980a, p.456).<sup>295</sup>

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<sup>287</sup> Wilson to Curtin, 16 January 1943, *op. cit.*

<sup>288</sup> *ibid.*

<sup>289</sup> The F&E's views on the Clearing Union draft, and its instructions to Wilson, are contained in 'Cablegram to Bruce', undated (but clearly January 1943), NAA CP 184/1, Bundle 4.

<sup>290</sup> *ibid.*

<sup>291</sup> *ibid.*

<sup>292</sup> *ibid.*

<sup>293</sup> *ibid.*

<sup>294</sup> Cablegram, 'Wilson to Prime Minister, Canberra, 6 November 1942', NAA A601/1, 40/1/8.

<sup>295</sup> The changes to the draft following the Dominion discussions are detailed in Appendix 2 to Keynes (1980a), pp.453-458.

## The Stabilisation Fund

It was somewhat of a surprise to Wilson that much time was spent at the London talks considering, not Keynes's Clearing Union, but an alternative plan emanating from the United States. This plan, the definitive version of which emerged in April 1942, was the creation of Harry Dexter White, then Assistant Secretary of the United States Treasury. In 1942 White had formal responsibility for all Treasury matters that had implications for foreign relations, but his thinking and writing upon international monetary affairs dated back to at least 1938 (Horsefield 1969, p.3). Like Wilson, White had enjoyed the tutelage of Jacob Viner, and had joined the Treasury in 1934 when Viner was its chief economic adviser. The first drafts of White's Plan had been written sometime in late 1941, but his proposals did not reach the United Kingdom until July 1942 (Horsefield 1969, p.16).

White's plan proposed the formation of two institutions - a Stabilisation Fund and an International Bank for Reconstruction and Development. Of the two, it was the Fund that was in direct competition to the Clearing Union and was, therefore, the most controversial and the most critically analysed at the London talks.

The Stabilisation Fund was a vastly more orthodox mechanism than the Clearing Union, a fact readily apparent from White's preamble outlining its purposes.<sup>296</sup> No reference here to the extension of the principle of banking, or the reversal of the deflationary bias of previous international monetary systems. Rather, the purposes of the Fund, in the order that White wrote them, were to; stabilise exchange rates, *encourage* capital flows, free blocked balances, correct the maldistribution of gold, shorten the periods of international disequilibrium and aid the stabilisation of price levels, *reduce* the need and use of exchange controls, abolish bilateral clearing arrangements, promote *sound* note issue and monetary policies amongst member nations, and reduce the barriers to trade (emphases added).<sup>297</sup>

The divergent purposes of the Clearing Union and the Fund were reflected in the mechanisms by which they sought to bring about their respective ends. Unlike the Clearing Union, the Fund was contributory. A member nation was required to provide subscriptions to the Fund in a complicated formula based on its holdings and output of gold, national income, foreign trade and investments, population and foreign debt. In the draft available at the London talks this formula would provide total subscriptions of around 5 billion US Dollars (Horsefield 1969, p.73). Largely because of its extraordinary gold holdings, the United States would be by far the largest contributor followed by the British Commonwealth grouped together, with a large gap then to other countries. On joining the Fund, members would be required to pay 12 ½ percent of their subscription in gold, 12½ percent in their own currency and 25 percent in interest-bearing government securities, the interest and principal for which were payable in gold 'or its equivalent'. The remaining 50 percent of the subscription

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<sup>296</sup> This first definitive version of the Fund is contained in White's April 1942 memorandum, 'Preliminary Draft Proposal for a United Nations Stabilization Fund and a Bank for Reconstruction and Development of the United and Associated Nations'. The memorandum is reproduced in Horsefield (1969), pp.37-82.

<sup>297</sup> This list of the purposes of the Fund is cited from Horsefield (1969), pp.46-48.

would only be paid up when called upon by the Fund's Board of Directors (Horsefield 1969, p.74).

The size of a country's subscription dictated the amount by which it could operate a balance of payments deficit within the Fund and, in this way, it played a similar role to that of the quota in the Clearing Union (though, as noted, it did not add any where near as much to international liquidity and held no negative implications for a country whose balance of payments *surplus* exceeded its subscription). Thus a member could purchase foreign currencies from the Fund to meet a balance of payments deficit, but only so long as these purchases did not exceed the value of its subscription. A member could purchase additional foreign currencies only by securing the votes of 80 percent of the Fund's members and provided that the situation was rectified within a reasonable time. In such situations, the Fund could also stipulate that a member undertake any measures the fund thought necessary to correct its balance of payments deficit (Horsefield 1969, pp.49-52).

The values of member countries' exchange rates would be fixed by the Fund and would only be allowed to change 'when essential to correction of a fundamental disequilibrium' in the balance of payments. Even then, a change to the exchange rate would require the consent of 80 percent of members votes. Given the size of the subscriptions noted above, this gave an effective veto over exchange rate changes to the United States or the British Commonwealth as a group (Horsefield 1969, pp.24, 60).

A device which would add to global liquidity was created in provisions which would allow the sale of 'blocked' foreign balances held by any country to the Fund.<sup>298</sup> Similarly, a further provision that was potentially liquidity creating was one which allowed the Fund itself to borrow from its members. This would provide, for example, additional amounts of a currency in strong demand.<sup>299</sup>

Membership of the Fund was open to all members of the 'United and Associated Nations', provided that upon the completion of hostilities, or within one year of joining, they agreed to: abolish all restrictions on foreign exchange transactions with other members; maintain a fixed exchange rate set by the Fund (allowing for a narrow band also set by the Fund); not allow investment from another member without the approval of that member while, simultaneously, allowing the nationals of another member access to their investments; not enter into any preferential or bilateral clearing arrangements; not adopt any monetary or general price measure or policy which, in the view of a majority of members would cause a serious disequilibrium in the balance of payments; gradually reduce barriers to trade; not default on the foreign obligations of the government or its agencies; and not subsidise exports in any way (Horsefield 1969b, pp.63-72).

The Bank, on the other hand, was a much less orthodox institution. Its main objects were; the provision of capital for reconstruction; the elimination of international

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<sup>298</sup> This was a particularly important device for those countries with large sterling claims (India and the countries of the Commonwealth particularly) who, in order to protect the value of sterling, were blocked during and sometime after the war from converting these balances into other currencies.

<sup>299</sup> Details of the provisions for 'blocked' balances are reproduced in Horsefield 1969, pp.54-59.

financial crises and the mitigation of depressions; the stabilisation of primary product prices by financing ‘buffer stocks’ schemes; the raising of living standards and the facilitation, as far as this was possible via economic measures, of international peace.<sup>300</sup> To do all this, it would have a capital base of up to \$US10 billion, to be contributed by its members. The Bank could also borrow in private capital markets and would lend directly to members as well as guarantee loans to members by private investors. Members would have access to loans of up to 100 percent of their contributions issued in the form of the Bank’s own gold-convertible notes. These notes effectively provided for a new international currency - nameless in this version of the Bank and not spelt out in any detail (Moggridge 1992, pp.686-687).

### *Reaction to White’s Plans*

The British and American proposals for the reconstruction of the international monetary system were very different animals which reflected their very different purposes. The British Clearing Union, the product of Keynes and the British interwar experience of an overvalued currency maintained at the expense of output and employment, placed great stress on the ability of countries to be able to pursue full employment free, as much as possible, from balance of payments constraints. Of course, the United Kingdom was also likely to end the war a debtor nation. Thus the Clearing Union provided a generous source of credit and a censure for *creditors* as well as debtors. The United States proposals similarly reflected its experiences and position. The problems with the exchange rate in the United States in the inter-war period only really began after the collapse of the gold standard and it would end the war the world’s greatest creditor. Accordingly, the Stabilisation Fund was concerned with exchange stability and was much more modest in its provision of liquidity.

Keynes’s initial reaction to White’s proposals was to label them as ‘not much more than a version of the gold standard’ (Keynes 1983, p.160).<sup>301</sup> The Fund would provide for a multiplication of the gold base under such a standard but, as with the old system, it was ‘only helpful to those countries which have a gold reserve already’. For countries without large holdings of gold, the Fund was scarcely of any use at all. The volume of international currency was not to be ‘adjusted to need, but remains as before mainly dependent on the volume of gold mining and the policy of those countries which already have large gold reserves’ (Keynes 1983, p.160). The details of the Fund as set out by White were ‘very complicated, discursive and diffuse’ and, according to Keynes, it seemed ‘quite unworkable’ (Keynes 1983, p.161). Nevertheless, certain subsidiary aspects of White’s plans - among them the solution to ‘blocked’ balances, the restrictions implied on capital flows, the funding for ‘buffer stocks’ schemes provided by the Bank - were favourably greeted by Keynes and where relevant, were incorporated into later drafts of the Clearing Union (Keynes 1983, p.160).

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<sup>300</sup> An extract of the Bank’s purposes, part III of White’s memorandum, is reproduced in *ibid.*, pp.78-82.

<sup>301</sup> Keynes’s initial reaction to White’s proposals are contained in notes attached to a letter sent to Sir Frederick Phillips, the Treasury representative in the United States, dated 3 August 1942 and included in Keynes (1983), pp.159-167.

Although it was still very much a secret, Wilson was able to see a copy of White's plans and to talk to White himself when travelling through Washington to and from London.<sup>302</sup> Wilson too was critical of the Stabilisation Fund proposal. Though he regarded it as a 'generous' scheme in terms of what the United States itself would contribute to its operation, he described it (in the final report of his trip to Prime Minister Curtin) as 'proceeding along very orthodox lines'.<sup>303</sup> This being the case, he was dismayed, like Keynes, that the resources of the Fund would be provided by subscription and that a proportion of these would have to be in gold. This not only meant that voting strength in the Fund would lie with gold-holding countries, but also that international liquidity would be distributed on the same basis and not, as in the Clearing Union, on the basis of need as determined by trade. Wilson's strongest criticism, though, was the degree of loss of sovereignty implied by membership of the Fund. This was, he told Curtin, 'an even greater sacrifice' than under the British proposals, particularly in relation to the exchange rate, but also in that 'the American plan involves rather wide restrictions on a country's freedom in regard to "monetary or general price measures or policies"'.<sup>304</sup>

As noted above, Wilson and the Australian economists back home were concerned that the Clearing Union imposed too little restriction upon creditors, but this imposition hardly existed in the Fund. On this, Wilson wrote that the absence of any censure on persistent creditors robbed the Fund of even the 'psychological advantages' of its British alternative 'in assisting towards an understanding of the fact that persistent credit balances on current international accounts are equally if not *more reprehensible* economically than persistent debit balances' (emphasis added).<sup>305</sup> On a related matter, Wilson also speculated on what would happen should the Fund run out of creditor-country currencies. Apart from renegotiating the whole agreement, the Fund seemed to offer no provisions against this (likely) occurrence.<sup>306</sup>

Like Keynes and other critics of the Fund, Wilson was quite favourably disposed towards the proposed international Bank. It was, he thought, 'conceived on fairly sound and generous lines' and, since it was the United States which would be the principal source of long term lending after the war, there was 'a lot to be said for encouraging the Americans to prepare the document to serve as a basis for international discussions on this subject'.<sup>307</sup> Indeed, the Bank proposal offered countries such as Australia a 'most useful' approach to the whole question of international monetary reconstruction. According to Wilson, Australia would do best by supporting the Clearing Union as far as possible alongside the American proposal for the Bank - a ready welcome for which 'might help to cure the United States Treasury of any infatuation with its own scheme for an Exchange Stabilisation Fund,

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<sup>302</sup> Which makes the comment by Butlin and Schedvin (1977, p.644) that the Fund was not known to the Australians at this time nor discussed at the London talks hard to fathom. Details of Wilson's travel arrangements, and of his discussions with White, are contained in his report to the Prime Minister, 'Post-War Economic Talks, London, October -November 1942', 16 January 1943, *op. cit.* and in 'Notes on R.W's Account of his Travels', Minutes of F&E Meeting of 22 January 1943 by F.H. Wheeler and G.G. Firth, *op. cit.*

<sup>303</sup> 'Post-War Economic Talks, London, October-November 1942', 16 January 1943, *op. cit.*

<sup>304</sup> *ibid.*

<sup>305</sup> *ibid.*

<sup>306</sup> *ibid.*

<sup>307</sup> *ibid.*

and would have the added advantage of allowing the Americans to take the initiative in designing a long-term lending institution to which they would necessarily be the largest contributors of capital'.<sup>308</sup>

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<sup>308</sup> *ibid.*



## **Chapter Six**

### **Coombs and Consolidation**

Wilson's return from London produced within the F&E a certain introspection as to what should be the next step in Australia's approach to the evolving post-war plans. Wilson himself was convinced that the ICER Report had been rendered obsolete by the speed at which various plans in the United States and the United Kingdom had appeared on the scene. These meant, he told a meeting of the F&E in January 1943, that Australia was 'still presenting a frame of mind', whereas what was required now were 'concrete plans and proposals'.<sup>309</sup> Reflecting his own 'pragmatic' approach and the doubts of the Treasury, Wilson also questioned at this time the whole basis of this rather early version of the 'employment approach'. According to Wilson, the extent of assurances which could be gained by an agreement pledging countries to the maintenance of employment had already been secured under the auspices of the Atlantic Charter and Article VII itself, and the idea that anything more binding than these could be achieved was illusory. It was 'impossible to bind succeeding Governments on matters of this nature' and any written agreement which could be got 'would not be worth the paper it was written on'.<sup>310</sup>

Wilson's scepticism as to the value of an employment agreement did not, however, reflect the majority of opinion on the F&E. Melville, for example, told the same F&E meeting in January 1943 that unless Australia obtained guarantees with regard to employment policies in the larger countries, then all other considerations under Article VII should be jettisoned too. In such circumstances we 'must put ourselves in the position of leaving our hands entirely free to take any action regarding tariffs, exchange rates, exchange control, etc'.<sup>311</sup> There were, moreover, possible benefits of *Realpolitik* to be considered with regard to the pursuit of an employment agreement, since 'if the only result were a refusal it would place Australia in a better tactical position against the levelling of any charges of not living up to the undertakings given in Article VII'. Giblin, too, remained convinced as to the general line of the ICER report, and noted that even without binding commitment, an employment approach 'would have some value in building up international opinion on the matter'.<sup>312</sup> The most enthusiastic support for an employment agreement, however, came from H.C. Coombs, the Director-General of the (new) Department of Post-War Reconstruction. Coombs told the January meeting of the F&E that while the prospect of international collaboration after the war on employment policies was 'remote', it was not time to 'throw up our hands'. Just as it was 'now accepted in Australia that the maintenance of employment and incomes is the primary social purpose... so there is the same chance of having these things recognised internationally'.<sup>313</sup>

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<sup>309</sup> 'Post-War Economic Talks, London, October-November 1942', 16 January 1943, *op. cit*

<sup>310</sup> *ibid.*

<sup>311</sup> *ibid.*

<sup>312</sup> *ibid.*

<sup>313</sup> *ibid.*

## **6.0 Coombs**

The employment approach was established by Giblin and given sanction by the F&E, but its impetus from 1943 onwards was primarily the result of the strong and well-placed advocacy of Coombs - with whom, indeed, the approach has since become most identified. Educated at the University of Western Australia and the London School of Economics (LSE) from which he took a doctorate in economics in 1933, Coombs was an early admirer of Keynes via the *Treatise*. He had been surprised at the low esteem to which Keynes was held at the LSE and his tenure there coincided with the high watermark of its dominance by Lionel Robbins and Frederick Hayek.<sup>314</sup> Upon completing his doctorate, Coombs returned to Australia to take up the position of Economist at the Commonwealth Bank.

Neither Robbins nor Hayek left much of an impression on Coombs, who opened his 1981 autobiography with the observation that the 'publication in 1936 of John Maynard Keynes's *General Theory of Employment, Interest and Money*, was for me and many of my generation the most seminal intellectual event of our time' (Coombs 1981, p.3). This excitement was shared by a number of his colleagues at the Commonwealth Bank and elsewhere, and Coombs recalled (consistent with Tange above) the Sydney 'tea group' meetings to discuss the *General Theory*. Included in these groups was Melville and a group of academic economists at the University of Sydney led by R.C. Mills together with E.R. Walker, Robert Madgewick, John La Nauze, Hermann Black and Trevor Swan (Coombs 1981, pp.4-5). This Sydney connection was particularly important, allowing Coombs to be a regular guest at the University's Economics Department's staff seminar programme at which, he recalled, his grasp of Keynes's work was developed more fully. This understanding was reflected in a highly regarded paper on Swedish economic theory that Coombs produced in 1939 which, he suggested, had pre-empted many of the policy implications of the *General Theory*.<sup>315</sup>

Upon the outbreak of war in 1939, Coombs was seconded from the Commonwealth Bank to the Treasury, where he was meant to work in collaboration with Wilson and with Giblin as Chairman of the F&E. Coombs was to act as the personal link between Treasury and the F&E and, as a result, became involved in the latter's work on war financing (Coombs 1981, p.7). Coombs later recalled that his job at Treasury left him plenty of time to consider and to write upon post-war policy, including the implications of Article VII. In 1941 Coombs replaced Giblin on the Commonwealth Bank Board - where he was involved in 'modifying the traditional conservatism of the Bank's financial policies to meet the needs of the war' - and in May 1942 he was appointed Director of Rationing by Curtin at the behest of the new Treasurer, Ben Chifley (Coombs 1981, p.27). This rather rapid rise to prominence continued when, in January 1943, he was appointed Director General of the new Ministry of Post-War Reconstruction.<sup>316</sup>

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<sup>314</sup> Interview with author, 3 February 1993. A not altogether flattering portrait of Robbins is contained in Coombs (1981, pp.42-43), which is also the best source for Coombs's early life and career. See also, though, Groenewegen and McFarlane (1990, pp.214-216), Markwell (1985, p.38) and Whitwell (1986, p.70).

<sup>315</sup> See Coombs (1939).

<sup>316</sup> This latest appointment was less of a surprise than the preceding ones. While Director of Rationing Coombs had been approached by Curtin to draw up a memorandum detailing the organisational

The Ministry of Post-War Reconstruction has assumed mythic proportions in Australia's political and economic history.<sup>317</sup> Conceived at the Annual Conference of the Australian Labor Party in November 1942, it was a vehicle through which the Party could reconcile its inherent opposition to war (a consequence both of the convulsions of the First World War and the common assertion that wars themselves were the self-serving devices of capital-owning classes) with the needs of a wartime government calling for sacrifices but with the promises of a new order to come. From the outset, the Department was seen as an engine of social change whose task, according to Coombs, 'was to ensure an economic and social context in which positive opportunities were present rather than merely an absence of constraints' (Coombs 1981, p.26). These opportunities consisted primarily of employment and, as such, 'the Ministry was...identified from its inception with the idea of full employment' (Coombs 1981, p.26). Chifley was the minister in charge of the new department, while remaining Treasurer.

### *The 'Positive Approach'*

Within the Department of Post-War Reconstruction there was, according to Coombs, a faith in an 'intellectual model of the economic system [Keynesianism] and our capacity to manage it' (Coombs 1981, p.27). That this faith was matched by influence - 'we had the ear and the confidence of a Prime Minister and a Treasurer' - meant that the Department was increasingly the primary source of economic advice to the Curtin government (Coombs 1981, p.27). This advice was often counter to that emanating from older departments (especially Treasury), continuing a struggle of demarcation which had been foreshadowed with the advice of the F&E, and which was to last the remainder of the war and beyond.<sup>318</sup>

One aspect of post-war planning which came the way of Coombs's new department was preparation for international conferences, and it was in this context that his involvement with Article VII deepened from its merely peripheral nature as a member of the F&E. Given the ethos of the department, this involvement was sensitive to the likely reservations of the Curtin government that had 'inherited convictions and prejudices which made it difficult for it to join wholeheartedly in these international moves, especially insofar as they were predicated on the traditional "free trade" convictions of liberal economists' (Coombs 1981, p.33). Such a sensitivity did not have to be feigned by Coombs, though, who similarly found that the liberal free trade approach 'provided no possible basis for a generally acceptable set of policies for Australia to pursue in any international negotiations' (Coombs 1981, p.34). Just what was an 'acceptable' approach for Australia to take to such negotiations was set out by Coombs in a memorandum circulated to the F&E and government ministers in January 1943. Obviously drawing upon the ICER Report, it was also a much bolder statement of the employment approach, and one which set a benchmark for all the negotiations to follow.

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structure required for a body to deal with post-war reconstruction. In October 1942 Coombs presented this to Chifley, and together they produced a charter for the new department, 'which Curtin duly promulgated' (Crisp 1961, p.187).

<sup>317</sup> See, for just one example of this, Crisp (1961) pp.183-197.

<sup>318</sup> Sir Frederick Wheeler, interview with the author, 15 January 1993.

The purpose of Coombs's memorandum was 'to establish beyond all doubt that the Commonwealth Government regards Article VII primarily as an undertaking to collaborate in the achievement of a clearly defined political objective' which, he specified, was 'the raising of living standards'.<sup>319</sup> A sound political objective, Coombs also believed it made economic sense. Spelling out the theoretical rationale for an employment approach within the context of orthodox trade theory, Coombs drew attention to its assumption of 'full employment in all the international trading states', in the absence of which the theory became 'largely irrelevant'.<sup>320</sup> It was Coombs further belief that the level of national income, and hence the level of employment, was a far more important factor in the demand for traded goods than the level of trade or exchange barriers. It followed, therefore, 'that policy designed to expand the volume of world trade is far more likely to be effective if it is directed towards the maintenance of income than if it is directed to towards altering the level of the tariff'.<sup>321</sup>

Maintaining national income implied a willingness to implement what Coombs called a 'certain type of policy' domestically as well as internationally. Domestically this meant full employment - 'maintained if necessary by governmental expenditure on public works and by public control of investment'.<sup>322</sup> But it also entailed a whole new level of government social responsibilities. According to Coombs, this included responsibility for the provision of 'food, clothing and housing at socially acceptable levels' along with a system of social security 'against unemployment, sickness, old age, etc'.<sup>323</sup> This could involve the continuation of wartime production controls beyond the end of the war, and it would likely involve government subsidisation of consumption. In his memorandum Coombs also referred to McDougall's 'nutrition approach' as an example of how Australia had conducted similar (successful) advocacy in the past. Together with 'full-employment', these 'social' aspects of Coombs's plan led it to being labelled the 'positive' approach within Post-War Reconstruction (Coombs 1981, p.35).

What was required *internationally* was an acceptance by countries of a responsibility to 'avoid large positive balances of payments'.<sup>324</sup> The desire to attain positive balances in the inter-war years had been, according to Coombs, a major cause of the restriction of international trade. Should large positive balances arise, the first policy response of government should be to ensure that the economy was fully employed. If this was already the case, then a surplus country could undertake a number of measures including encouraging investment overseas, making direct government purchases overseas, and the extension of 'gifts' to poorer countries.<sup>325</sup>

According to Coombs, the realisation of the 'positive' aspects of Article VII rendered its 'negative' aspects - the reduction of barriers to trade, exchange controls - both much less significant in their impact upon world trade, and at the same time much

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<sup>319</sup> Coombs's memorandum, which was simply titled 'Article VII', is located in NAA A 606/1, 40/1/8.

<sup>320</sup> *ibid.*

<sup>321</sup> *ibid.*

<sup>322</sup> *ibid.*

<sup>323</sup> *ibid.*

<sup>324</sup> *ibid.*

<sup>325</sup> *ibid.*

more achievable as countries had less need for defensive measures to protect their balance of payments. For Australia, this meant that Coombs was much less concerned about reducing tariffs. In great contrast to the prevailing wisdom within institutions such as the Tariff Board, Coombs saw few industries for which economies of scale required anything beyond the Australian domestic market. Accordingly, Australian industrial development could be limited only to the extent that ‘technical factors’ intervened, rather than notions of scale efficiencies.<sup>326</sup> In a similar vein, Coombs also declared in his memorandum that Australia should ‘refuse to accept the judgement of established industrial countries as to the potentialities of our own resources’.<sup>327</sup> Prophetically, he also added that Australia’s industrial development depended upon finding ‘appropriate allies’, and these could ‘be found without difficulty in under-developed countries particularly in the Pacific area’.<sup>328</sup> Like his economist colleagues, Coombs did not see any advantages in maintaining imperial preference.

### *Giblin - Again*

Having initiated the employment approach via his ‘19 questions’ the previous year, Giblin returned to the idea in January 1943 in a memorandum which he wrote in response to some of the criticisms of the approach within the F&E (especially Wilson and the Treasury above).<sup>329</sup> This memorandum was as strongly worded as Coombs’s, but was more practical in that it set out to try and define precisely the aims of the Australian approach and even the form of an agreement through which these could be realised.

Like Coombs, Giblin sought to establish within the Commonwealth Government the thought that Article VII was *primarily* about the raising of living standards. In contrast to Wilson he did not believe that this central objective was incapable of being precisely expressed in the form of an international agreement. Agreeing to precise obligations with respect to living standards would be difficult but, according to Giblin, it would be no more difficult than obtaining agreements on a new international monetary order or agreements on trade policy. An agreement on living standards was, moreover, required *before* any others. All the plans for new machinery for the operation of the international economy would be rendered useless without an agreement on living standards by the ‘more important nations’.<sup>330</sup> As in Coombs’s memorandum, Giblin pointed out that the orthodox doctrines of free trade required the assumption of full employment before they could be considered meaningful. In this light, it was essential to link the ‘secondary’ objectives of Article VII with the prime objective of raising living standards ‘*whenever there is an opportunity to do so*’.<sup>331</sup>

To other protests voiced within the F&E that an agreement on living standards could not possibly be binding upon governments and therefore, would ‘not be worth the paper it was written on’, Giblin was equally dismissive.<sup>332</sup> Repudiation of such an

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<sup>326</sup> *ibid.*

<sup>327</sup> *ibid.*

<sup>328</sup> *ibid.*

<sup>329</sup> This memorandum, entitled again simply (and confusingly!) as ‘Article VII’, is dated 25 January 1943. The memorandum can be found in NAA CP43/1/1, Bundle 5/1943/444/Pt.1.

<sup>330</sup> *ibid.*

<sup>331</sup> Emphasis added, *ibid.*

<sup>332</sup> This was, of course, the assessment of Wilson above.

agreement would 'throw publicly on the repudiating country the full onus of repudiation as a matter of confessedly international concern'.<sup>333</sup> This, Giblin argued, would 'not prevent repudiation', but it would make it much more difficult. This was especially so for policies which had the broad support of the mass of people since the 'effect will be always to mobilise public opinion in support of the policy, whenever it is in danger'.<sup>334</sup>

The level of employment was the key indicator as to whether a particular country was living up to its international obligations. In order to give this an objective meaning, Giblin proposed that any agreement include provisions which required countries:

- a. To keep a record of unemployment on some plan approved by an international body such as the I.L.O;
- b. Not to allow the percentage of unemployed to population to exceed an arbitrary figure, e.g. 5 per cent, for more than a short stated period, unless a higher figure is approved by some international authority.<sup>335</sup>

Penalties for countries not complying with these requirements could be imposed, under Giblin's schema, by a body such as the Clearing Union exacting a fine on excess credit balances.

### *Stabilisation Fund - 1943*

An opportunity to test this enhanced commitment to the employment approach came unexpectedly in early 1943, via an invitation from the United States for bi-lateral discussions (in Washington) on the Stabilisation Fund. Ironically, this invitation coincided with the approval of Curtin, Chifley and Evatt (but not yet Cabinet) of the principle of the Clearing Union, subject to the same reservations expressed by the F&E. It also coincided with the beginning of what Coombs referred to as the active 'encouragement' by these same ministers for the employment approach itself (Coombs 1981, p.35). Because he was due to go to the United States anyway to argue for an increased American commitment to the Pacific War, Australia's delegation to Washington was led by its mercurial Minister for External Affairs, Dr H.V. Evatt. Ensuring that the employment approach would get its most articulate airing though, Evatt was accompanied by a team of experts led by Coombs and including Brigden, McDougall (from London) and the fast-rising John Burton from the Department of External Affairs (Butlin and Schedvin 1977, p.647).<sup>336</sup>

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<sup>333</sup> 'Article VII', 25 January 1943, *op. cit.*

<sup>334</sup> *ibid.*

<sup>335</sup> 'Article VII', 25 January 1943, *op. cit.*

<sup>336</sup> Dr. John Burton was an officer of the Department of External Affairs who, at this time, was seconded to Evatt's personal staff. According to Hasluck (1980), p.15, Evatt operated a 'substitute for the department [of External Affairs] from his own ministerial office with Burton doing more of the fixing and arranging than any departmental officer did and having much more influence on shaping the minister's opinions than anyone in the department'. Interestingly, for the purposes of this study, McDougall had been an adjunct supervisor to Burton's doctoral studies in London in the 1930s and, as shall be revealed below, the pair kept in touch throughout the 1940s. Dr. John Burton, interview with the author, 23 August 1993.

At the talks in Washington, the Australian delegation pushed the employment approach strongly - both at the ministerial level, via meetings between Evatt and the Secretary of the Treasury, Henry Morgenthau, as well as at the 'expert' level in the meetings between Coombs, Brigden, and Harry White.<sup>337</sup> Nevertheless, whatever the level of discussion, the line did not get very far. Morgenthau told Evatt that his department could not be concerned with something they regarded as not fitting within their field of responsibility. White took a similar view, but added that he saw that 'Australia was one of the countries to benefit most from a successful [Stabilisation Fund] scheme and the U.S.A. one of the least'.<sup>338</sup>

With non-monetary issues therefore rejected from the discussions, the 1943 Washington talks got down to a debate between the experts over the Stabilisation Fund itself. In these, Coombs and Brigden made clear to White their preference for the Clearing Union, but highlighted how *both* schemes fell short in certain critical areas, although the sins of omission of the Fund were the greater. Chief amongst these omissions were that *neither* plan took the level of employment sufficiently into account as the prime determinant of world trade, neither plan imposed adequate censure against countries with excess credit balances, and both plans were set up in a way which would ensure their dominance by large creditor countries with very little voice for 'dependent' countries such as Australia.<sup>339</sup> Particular problems with the Fund itself which were put to White included the principal complaint that it was contributory in nature rather than potentially credit-creating, that the fixing of exchange rates was much too rigid, that the quotas were much too small and that it was generally much more restrictive than the Clearing Union.<sup>340</sup>

In reply to these criticisms, White told the Australian delegates that anything more expansionary than his own plan did not have any hope of being approved by Congress. This was particularly true for the Clearing Union proposal which, he said, would be seen by Congress as a vehicle through which other countries could extract funds from the United States. White also outlined four points which he regarded as inviolable for any monetary plan to be acceptable by the Congress, most of which were incompatible with the objectives sought by Australia:

- (a) The scheme must be contributory in character;
- (b) The share of the countries in control of the organisation must be related to the size of their contributions;
- (c) The exchange rates between major currencies must be fixed before the Fund is established and variations in these rates made possible only with a substantial agreement from countries other than that desiring to alter its own exchange rate;

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<sup>337</sup> Details of these discussions can be found in a memorandum prepared by Brigden, 'Discussions with U.S. Treasury on S.F. - April 23rd, 1943' in NAA A989/1, 43/735/56/2.

<sup>338</sup> *ibid.*

<sup>339</sup> 'Report by the Director General of the Ministry of Post-War Reconstruction on Stabilisation Fund and Clearing Union, Report of Discussion in Washington and London', 27 September 1943, NAA A989, 43/735/56/3.

<sup>340</sup> *ibid.*

(d) There should be a definite limit to the financial obligations of the United States to the Organisation.<sup>341</sup>

Coombs's attempts to have a full employment obligation inserted into the articles of the Fund also met with rejection. Once more White pointed to a recalcitrant Congress, which would regard such an insertion as 'politically suspect' and, as such, 'unacceptable'.<sup>342</sup>

Before returning to Australia, Evatt and his party continued on to the United Kingdom for preliminary discussions on trade policy. At these discussions the British Government proposed a plan for multilateral reductions in tariffs and other barriers. As has been noted, Australian economists were not particularly perturbed about the abandonment of imperial preference, but they were reluctant to enter into any commitments to reduce trade barriers in the absence of a broader employment agreement. Certainly Evatt would not countenance such a suggestion, and as a result of Australian obfuscation the discussions did not achieve anything substantial.<sup>343</sup>

The London discussions provided Coombs with an opportunity, however, to meet Keynes and discuss with him the post-war monetary plans. Though he did not go into any detail of what Australia had in mind with the employment approach, Coombs discussed with Keynes the general possibilities of international collaboration on employment and living standards. Unbeknownst to the Australians, by this time Keynes had just about given up on the Clearing Union being made the basis of the post-war money discussions and was turning his mind to grafting upon the Stabilisation Fund as many features of the Clearing Union as possible. Because of this, Coombs learnt that the British too were urging the Americans to modify the Fund. These modifications included the use of a new international currency (White's 'Unitas' which, under his own plans, was merely a unit of account in the proposed International Bank). A country's initial holdings of this currency would still depend on its gold and currency contributions, but Coombs believed the British proposal here was 'based upon the hope that at some future date it will be possible for the Stabilisation Fund itself to become a credit-creating agency and so operate more expansively'.<sup>344</sup> Britain was also seeking to expand the bands around which exchange rates were allowed to vary, the inclusion of at least *some* provision for penalties on persistent creditors and a rewriting of the Fund's articles to include a directive that it act to check economic downturns and the spread of depressions.<sup>345</sup>

These improvements sought by the British would, Coombs thought, dramatically increase the acceptability of the Fund, but they would still leave the institution far short of Australia's aspirations. In concluding his report on the Stabilisation Fund talks in Washington and London, Coombs noted that while 'it might not be politically wise' for Australia to consider remaining outside the Fund should it be established, a number of severe problems still remained:

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<sup>341</sup> White reported by Coombs in *ibid.*

<sup>342</sup> *ibid.*

<sup>343</sup> See Evatt's cablegram to Curtin, 8 July 1943, NAA A989, 43/735/57/1.

<sup>344</sup> 'Report by the Director General of the Ministry of Post-War Reconstruction on Stabilisation Fund and Clearing Union, Report of Discussion in Washington and London', 27 September 1943, *op. cit.*

<sup>345</sup> *ibid.*



- (a) The additional foreign exchange reserves which it will make available to Australia are unlikely to be adequate for her possible needs;
- (b) It may require Australia to accept as a condition of using overdraft facilities, advice and pressure concerning her domestic policy from an international body on which her representation is negligible;
- (c) It calls for a serious sacrifice of economic freedom to vary her own exchange rate, and to impose exchange controls;
- (d) It offers no assurance that the major economic countries of the world will maintain a high level of employment and incomes and avoid the accumulation of persistent credit balances. Only confidence in these conditions would justify Australia continuing to accept these limitations to her freedom of action.<sup>346</sup>

## **6.1: Old Themes at Hot Springs**

### *McDougall Again*

The inclusion of an economic team in Evatt's 1943 mission was primarily because of the monetary discussions, but in early March 1943 a further *raison d'être* for its inclusion emerged with a sudden announcement from the United States. This was an invitation to all members of the United Nations to attend a conference in the United States to discuss post-war plans and prospects for the production and trade in foodstuffs - particularly 'in the light of possibilities of progressively improving in each country the levels of consumption within the framework of an expansion of its general economic activity'.<sup>347</sup> The conference would also consider the question of 'equitable' agricultural prices from the point of view of both consumers and producers, and '[t]he possibilities of international co-ordination and stimulation of national policies for the improvement of nutrition'.<sup>348</sup>

The American invitation to what would officially become the United Nations Conference on Food and Agriculture took most governments by surprise. An attempt to initiate United Nations collaboration on post-war policy in a relatively uncontroversial way, the invitation nevertheless created some anxiety. Within the British Government these concerns primarily centred around the scope of topics to be discussed. Anxious that the Conference avoid 'controversial topics on which the ground has not been prepared', the British Foreign Office sought assurances that the Conference not concern itself with 'wider questions of economic and financial policy'.<sup>349</sup> The Foreign Office also questioned the usefulness of more talks on

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<sup>346</sup> *ibid.*

<sup>347</sup> 'Sumner Welles, Acting Secretary of State, to the Chargé in the United Kingdom', 8 March 1943, telegram contained in United States of America, Department of State (1963), p.821.

<sup>348</sup> *ibid.*

<sup>349</sup> 'The British Ambassador (Lord Halifax) to the Secretary of State', 27 March 1943, telegram contained in United States of America, Department of State 1963, p.827.

nutrition, regarding the issue as having been largely dealt with before the war by the League of Nations (Hammond 1951, pp.357-359).

Part of the reservations held in official circles in the United Kingdom, however, concerned what they believed to be the origins of the American invitation - and it is through this issue that the Food and Agriculture Conference moves to the centre of this study. For, despite the fact that the invitation came from the United States Government, it was, at least partially, the result of the on-going agitation of McDougall and Bruce. As noted in Section II above, the degree to which these two were regarded as ring leaders of a 'ginger group' on nutrition and other issues had earned them the ongoing hostility of a section of the British civil service, but especially the Foreign Office.

Tracing the involvement of McDougall and Bruce in the initiation of the Food and Agriculture Conference returns the narrative to 1940, and the pair's agitation of the British Government to produce a statement of 'war aims' to counter Nazi 'new order' propaganda. This again was a program of action which created a degree of hostility in some circles, not least because their agenda continued to be that of a modified version of economic appeasement. In a most extraordinary memorandum authored by McDougall and sent to the Secretary of State for Dominion Affairs, Anthony Eden, in February 1940, for example, they argued that the only chance of victory was to hold out 'hope' to a 'reformed Germany'.<sup>350</sup> To this end, the memorandum declared that (learning the lessons of Versailles) there should be no dictated peace terms by the victors, an international settlement of the colonial question and access to raw materials, and a programme of economic reconstruction along the lines of the nutrition approach - all to be overseen by a new 'World Organisation for Economic and Social Affairs'.<sup>351</sup> This latest advocacy received some cautious support from Chamberlain and the British Foreign Secretary, Lord Halifax, polite rejection from Eden and outright hostility from Churchill (at this time back in government as First Lord of the Admiralty).<sup>352</sup> It also received most wholehearted support from the new Australian Prime Minister, R.G. Menzies, to whom Bruce had also sent the memorandum. Menzies told Bruce that its central ideas accorded with his own but that his ministers had been unresponsive, most sharing what he labelled 'the so-called realistic approach, and an almost pathetic belief that the dismemberment of Germany would alter the German spirit and outlook'.<sup>353</sup> Revealing that his well-known animosity to Churchill pre-dated the dramas of his visit to the United Kingdom in 1941, Menzies attacked Churchill's bellicosity, labelling him a 'menace', a 'publicity seeker', someone 'lacking in judgement' and a stirrer of 'hatreds in a world already seething with them'.<sup>354</sup>

McDougall's and Bruce's most important support, however, came from the United States and its Ambassador to the United Kingdom, John G. Winant. A one-time Governor of New Hampshire, Winant had been a strong supporter of the 'New Deal'

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<sup>350</sup> The memorandum, 'The Peace Settlement: Methods for Securing a Co-operative Peace', is dated 'January 1940' and can be found in NAA M103, 1940 (January - June).

<sup>351</sup> *ibid.*

<sup>352</sup> As reported by Bruce in a letter to the Australian Prime Minister, R.G. Menzies, 6 February 1940, NAA M103, 1940 (January - June).

<sup>353</sup> 'Menzies to Bruce', 22 February 1940, NAA M103, 1940 (January - June).

<sup>354</sup> *ibid.*

and, with Roosevelt's support, had been elected Director of the ILO in 1939 and Ambassador to the United Kingdom in 1941. Bruce had first approached Winant in March 1941 and found to his surprise that Winant was an enthusiastic supporter of the ideas of the 'nutrition approach' and their usefulness in any statement of war aims. Winant sent a memorandum on nutrition written by McDougall to Roosevelt, Vice-President Henry Wallace, and Roosevelt's principal aide and adviser, Harry Hopkins. He also reported to Bruce that he had had lengthy conversations on the issue with Wallace, who in turn was urging the Australians to approach him directly.<sup>355</sup>

The interest taken in McDougall's ideas by Wallace was not surprising. From a prominent farming and political family (his father had been Secretary of Agriculture under President Harding), Wallace had studied economics and agriculture and had come to some prominence within agricultural circles by experimenting with crops of high-yield corn. Editor of the family-owned newspaper, *Wallace's Farmer*, through the 1920s, he was a propagator of what he called a 'scientific' approach to agriculture and a philosophy (in sympathy with McDougall's) that scientists and managers would 'fashion an abundant life for the common man' (Blum 1973, p.16).<sup>356</sup>

A devotee of 'radical New Deal' policies, Wallace was appointed as the United States Secretary of Agriculture by Roosevelt in 1933. In charge of the Agricultural Adjustment Administration (AAA), Wallace reluctantly oversaw the 'ploughing-in' of crops as a device to restore prices, but regarded this as an emergency measure only. Like his colleague in the Roosevelt cabinet, Cordell Hull, Wallace was a firm opponent of tariffs and other trade barriers which, apart from their economic cost, he regarded as the harbingers of war. Wallace's great passion during his tenure as agriculture secretary, however, was his plan for the 'ever-normal granary' - a kind of buffer-stock scheme in which government purchases, sales and storage of foodstuffs would eliminate gluts and shortages. By 1941, and in the light of small scale experiments with similar devices in the United States and elsewhere (particularly in wartime Britain), Wallace's ambitions for his proposal had become global. Wallace became Roosevelt's running mate, and subsequently Vice-President, in the 1940 Presidential elections (Blum 1973, pp.15-31).

In July 1941 the International Wheat Conference (to which McDougall had been appointed as Australia's delegate) brought McDougall and Wallace together.<sup>357</sup> Although very actively involved in this Conference's proceedings, its location in Washington meant that McDougall was not only able to pitch his ideas to Wallace directly, but also use the authority of the Vice-President to approach other officials in the administration. McDougall subsequently reported very favourable reactions to his ideas from the Department of State (particularly two of the Department's fast-rising Undersecretaries, Dean Acheson and Sumner Welles), the Secretary of the Treasury, Henry Morgenthau, the Agriculture Secretary, Claude Wickard, as well as a number

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<sup>355</sup> Bruce's account of Winant's interest and his subsequent actions is contained in a memorandum on a meeting with him, 24 June 1941, NAA M100XM1, June 1941.

<sup>356</sup> Blum was the editor of *The Price of Vision, The Diary of Henry A. Wallace*. His 'Introduction' to this work is the best source of biographical information on Wallace.

<sup>357</sup> The Wheat Conference was itself an important event for the shape of agricultural trade in the postwar world. For details, see Hammond (1951), pp.347-356.

of officials and economists at the Department of Agriculture - within which Wallace had insisted McDougall's memoranda be circulated.<sup>358</sup>

McDougall returned to London at the end of 1941, but in July 1942 he was back in the United States once more, selected by Curtin as Australia's representative on the International Wheat Council. As before, he took up the nutrition message but found that, with the United States now at war, much thought was already being given to post-war reconstruction and America's role in it. Nevertheless, to Wallace and Sumner Welles he reported that comparatively little was being done on the problems of food and agriculture. Notwithstanding his status as the representative of Australia, McDougall's reports of slow progress led to him being asked by both Wallace and Welles to head up an informal group which would collaborate with both the Departments of State and Agriculture to prepare proposals with regard to food and agriculture. The group included officials from both the Departments mentioned as well as experts from other bodies. Two interesting inclusions were the United States Surgeon-General, Dr Parran and the Harvard economist, Alvin Hansen.

### *Freedom from Want*

The subsequent report of this group, 'A Memorandum on a United Nations Programme for Freedom from Want of Food', was written primarily by McDougall and Parran and was pitched to appeal as a practical measure which would give substance to the 'four freedoms' of the Atlantic Charter.<sup>359</sup> The 'freedom from want', the memorandum implied, meant a war against poverty through an 'expansive economy' supplying 'full employment, better labour conditions and social security'. Following the familiar McDougall line, the memorandum argued that improving nutrition was not only an end in itself, but that such an emphasis would provide a solution to the economic nationalism which had destroyed world trade before the war. The approach was updated though to include Article VII which, McDougall claimed, promised 'a reversal of the pre-war movement toward agricultural self-sufficiency'. As such, it would 'greatly assist in the provision of diets adequate for health at a cost within the reach of all by encouraging the production of protective foods, as well as of staple [energy] products, in countries and regions where production is most efficient'. For all of this to be realised, the memorandum recommended the creation of an International Agricultural Authority which in turn would report to an economic council of any proposed 'World Authority'. Finally, the memorandum provided the

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<sup>358</sup> Sumner Welles (1892-1961) was perhaps the strongest 'progressive' influence on Roosevelt at this time, and was the author of the 'four freedoms' which he popularised out of the Atlantic Charter. He was a strong backer of McDougall and his ideas, and the two corresponded regularly. His sudden resignation in 1943 removed from McDougall a most significant point of influence within the Roosevelt Administration. Dean Acheson (1893-1971) later became Secretary of State under Truman and was similarly a supporter of McDougall's ideas, if not to the extent of either Welles or Wallace (Johnson 1966, p.6).

<sup>359</sup> This memorandum, 'Draft Memorandum on a United Nations Program for Freedom from Want of Food' can be found in the 'F.L. McDougall Papers', NLA MS6890. As noted, the 'four freedoms' were popularised out of the Atlantic Charter resolutions by Sumner Welles, who attended the secret meeting between Roosevelt and Churchill in Placentia Bay, Nova Scotia, in August 1941 as Roosevelt's chief adviser. The four freedoms - the freedom of speech, of religion, the freedoms *from* fear and want, are set out in Welles (1943), as is the full text of the Atlantic Charter itself.

United Nations with ‘ammunition of psychological warfare’ whose use could ‘shorten the war’.<sup>360</sup>

### *Meeting with Roosevelt*

McDougall’s memorandum was subsequently presented to the State Department where, he reported at the time, it had a good chance of becoming ‘the basis for Administration views on the subject’.<sup>361</sup> But around this time another channel opened up that had a profound effect on what followed. At the urging of Wallace in August 1942, McDougall approached Eleanor Roosevelt - the wife of the President and (unusually in that position) a campaigner for social and economic issues in her own right. Impressed by McDougall and his ideas, she invited him to the White House and subsequently arranged for him to present them to the President. This occurred at a dinner at which McDougall was ostensibly the special guest. According to McDougall’s own account of the proceedings, Roosevelt’s proud boast that he was the architect of the Atlantic Charter and the United Nations was countered by a rejoinder from McDougall that both concepts were fine as long as they had ‘something to do’. Pressed to explain what he meant, McDougall then told to an ‘astonished’ President that the problems of food and agriculture, being both ‘a really important but not very controversial subject’ offered a wonderful opportunity for the first conference for the United Nations in considering the post-war world. In this, McDougall recorded, Roosevelt ‘expressed considerable interest’.<sup>362</sup>

McDougall’s meetings with the Roosevelts have entered the folklore of what would become the FAO, but it is very difficult to establish what importance they had in the decision by Roosevelt to call the Hot Springs Conference. He was, of course, most unlikely to have been a decisive influence in convincing Roosevelt that food and agricultural policies were going to be important in the scheme of post-war reconstruction but, equally, it was more than possible that his advocacy was influential in the timing of the conference. As any history of decision-making within the Roosevelt Administration will attest, policy decisions were very often the outcome of a delicate balancing of different forces within it. In the case of postwar economic policy, these ‘forces’ were finely (and jealously) balanced between a number of competing factions. These included the Treasury under Morgenthau, Vice President Henry Wallace and his advisers (which tended to be a much more ‘radical’ faction than the others), the Departments of Agriculture and Commerce and the traditional centre of foreign policy advice, the State Department. The last Department was, however, itself divided - between the Secretary of State, Cordell Hull, and a group of a more reform-minded and ambitious set of younger officials led by Sumner Welles and Dean Acheson. And, of course, on top of this was the contrary nature of Roosevelt himself. In this rich brew, it was just possible that an external adviser with connections with all of these competing centres, offering an uncontroversial issue to

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<sup>360</sup> ‘Draft Memorandum on a United Nations Program for Freedom from Want of Food’, *op.cit.*

<sup>361</sup> ‘McDougall to Bruce’, 25 June 1942, S.M. Bruce, Monthly War Files, 1939-1945, NAA M100 XM1.

<sup>362</sup> McDougall’s account of these events can be found in a memorandum titled simply ‘Roosevelt’, in FAO, Meetings with Mr. F.L. McDougall, RG 3.1, Series I1.

begin the process of international postwar reconstruction, might have been able to make the difference.<sup>363</sup>

### *The Food and Agriculture Conference*

The Australian Government accepted the American invitation to the Food and Agriculture Conference with enthusiasm - not least because Bruce had written to Curtin beforehand telling him both of the benefits Australia could derive from the Conference and the key role played by McDougall in instigating it.<sup>364</sup> In announcing the Government's acceptance, Curtin took the opportunity to take a swipe at the British attempts (above) to ensure that the Conference did not stray from very narrowly defined limits. In a telegram to Attlee, Curtin declared that Australia's 'opinion on whether the scope of the Conference should be limited or expanded would be governed largely by the hope of attaining concrete results'.<sup>365</sup> He also added, with a statement which would have pleased the economists of the F&E, that it was Australia's view that 'the time has come to progress beyond general declarations and to proceed towards working at the measures by which the declared principles of the United Nations will be applied'.<sup>366</sup>

The United Nations Food and Agriculture Conference was held in Hot Springs, Virginia, in May-June 1943. Given the proximity of Evatt's delegation in Washington, a section led by Coombs and including Brigden, Burton and McDougall made up the Australian representation. Coombs was given permission to push the full employment line as strongly as he could at the Conference, but his position on this was fortified by a press release issued by Evatt in Washington which declared that Australia's objectives for the Conference included:

- (a) The recognition by all governments of an international responsibility to improve nutritional standards and increase productive efficiency within their own territories.
- (b) The acceptance by each country of an obligation to report periodically to other nations on action being taken to achieve these purposes and on the progress which has been made.

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<sup>363</sup> For more on the divisions within the Administration and the idea that an 'outsider' could exert an influence on decision making, see Bennett Woods (1990, *passim*). Hasluck (1980, p.91) expresses some doubt that McDougall could have had much to do with the calling of the Hot Springs Conference, but bases his doubts on the lack of links between McDougall's work at the League of Nations in advancing the nutrition approach and the events above. Hot Springs, he wrote, was the result of 'various inter-governmental communications and various studies throughout 1942 before the conference was called' (Hasluck 1980, p.91). It is doubtful that Hasluck knew anything of McDougall's activities in 1941 and 1942. For more, see also Turnell (2000).

<sup>364</sup> Bruce to Curtin, 26 February 1943, S.M. Bruce, Monthly War Files, 1939-1945, NAA M100 XM1, February 1943.

<sup>365</sup> Curtin to Attlee, 18 March 1943, S.M. Bruce, Monthly War Files, 1939-1945, NAA M100 XM1, March 1943.

<sup>366</sup> *ibid.*

(c) The acceptance by each country of an obligation to assist as far as possible, those in need by preventing want and by improving living standards everywhere throughout the world.<sup>367</sup>

The above and, indeed, all of the instructions from the Australian Government relating to food and agriculture, were based on McDougall's memoranda updated by the F&E. Reflecting the new and broader employment approach, Evatt's press release also included the following statement:

A similar approach can be made to the crucial problem of full employment. A basic requirement of an expanding world economy in the post-war period is the building up and maintaining of the highest level of employment in industrial countries. For this reason we believe that this Conference should recommend to Governments the recognition of an international responsibility for maintaining a high level of employment. It is necessary to remember that a reasonable "food" standard is only one part of a general "living" standard which is impossible of achievement without stable employment or occupation at a reasonable wage or income level.<sup>368</sup>

Coombs regarded the Food and Agriculture Conference to have been 'a very real success'.<sup>369</sup> Certainly he was successful in bringing the employment aspect to the forefront, and using it to add a qualification to the American insistence that the Conference resolutions contain a statement recommending a multilateral reduction in trade barriers. The Australians' general point, that it was useless to produce more and better food if large sections of the population could not afford it due to unemployment and poverty, was also recognised in the Conference resolutions. Highlighting perhaps why the British were right to be worried about where the Conference might head if given free rein, Coombs and the Australians also succeeded in inserting resolution number XXIV. This asserted

the close interdependence between the level of employment in all countries, the character and extent of industrial development, the management of currencies, the direction of national and international investment, and the policy adopted by the nations toward foreign trade.<sup>370</sup>

While acknowledging that the Conference had not been invited to examine policies to be adopted by governments to expand economic activity, it went on to declare that 'freedom from want of food could not be fully achieved without such an expansion' and it urgently recommended governments 'take action individually, and in concert, in order to secure this objective'.<sup>371</sup>

But if the Conference had been a successful one for Australia's approach generally, it was an unmitigated personal triumph for McDougall. The Hot Springs Conference

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<sup>367</sup> The press release was issued from Washington on 26 May 1943 and is contained in NAA CP 43/1/1, Bundle 5/1943/444/Pt.2.

<sup>368</sup> *ibid.*

<sup>369</sup> Coombs to Chifley, 7 June 1943, NAA A571, 43/1354.

<sup>370</sup> This, and the other resolutions of the Food and Agriculture Conference can be found in AA A989/1, 43/735/39.

<sup>371</sup> *ibid.*

had resolved in favour of almost every issue which McDougall and Bruce had campaigned upon the previous decade, including the establishment of a permanent organisation through which countries would be required to report to each other on progress they had made. Upon completion of the Conference, McDougall wrote to Bruce that 'our initiative of 1935 looks like getting fully launched'.<sup>372</sup>

That the final resolutions mirrored so closely McDougall's long desired goals was no accident. Not for the first time at an international conference, the will of the United States delegation had generally prevailed at Hot Springs and upon this, McDougall had had some influence. Immediately before the Conference opened, McDougall was approached by Dean Acheson to prepare a memorandum outlining 'some ideas about the *outcome* of the Conference'.<sup>373</sup> This memorandum was circulated amongst the American delegation, various Administration officials and the President himself. The subsequent approach employed by the American delegation at the Conference was consistent with what McDougall had outlined. As well, various League of Nations documents were heavily cited at the Conference, particularly by the British delegation. Most of these were either authored by McDougall, or were the result of the investigations set in motion by him and the nutrition campaigners in 1935.

McDougall's role in instigating the Food and Agriculture Conference and in guiding it towards a successful outcome was recognised by the Roosevelt Administration which requested the Australian Government in June 1943 to appoint him to the Interim Commission charged with establishing what would become the United Nations Food and Agriculture Organisation (F.A.O.).<sup>374</sup> Despite some reluctance at first, this was agreed to.<sup>375</sup> McDougall became a very forceful figure on the Interim Commission, but he never lost touch with Australian policy and Australian policy makers.<sup>376</sup> Soon after the Food and Agriculture Conference, he circulated a memorandum among his contacts within the Roosevelt administration a memorandum written by Coombs on full employment and the international economy.<sup>377</sup> He was also

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<sup>372</sup> McDougall to Bruce, 3 June 1943, NAA M104/1, 11(4).

<sup>373</sup> Emphasis added, McDougall to Bruce, 13 May 1943, NAA M104/1, 11(4).

<sup>374</sup> This request came from Wallace via the United States Ambassador to the United Kingdom, J.G. Winant ('Memorandum on telephone conversation with J.G. Winant', 19 June 1943, S.M. Bruce Monthly War Files, 1939-1945, NAA M100 XM1, June 1943).

<sup>375</sup> In a letter to Bruce, McDougall suggested that this reluctance came from Evatt - who, McDougall reported, had 'expressed annoyance because some highly placed Americans have spoken to him of my having had much to do with the success of the Conference'. McDougall's experience of Evatt's jealousy on this matter was to be an experience similarly visited upon many of Australia's representatives in the coming years ('McDougall to Bruce', 8 June 1943, NAA M104/1, 11(4)). For more on the sometimes bizarre behaviour of Evatt on his overseas trips, see Crockett (1993).

<sup>376</sup> McDougall's dominance of the Interim Commission caused its own problems in that it once more excited hostility against him from the British Foreign Office. Regarded by them, as we have seen, as a 'ginger man' and an 'extremist', it wrote to the British delegates on the Interim Commission that while it would support a Dominion representative as chairman of that organisation, 'we should not be agreeable to McDougall being appointed chairman should there be any question of this' (Foreign Office to United Kingdom Delegation to the Interim Commission of the United Nations Food and Agriculture Organisation, 25 June 1943. PRO FO 371/35377, U2719/320 70). Up until his formal appointment to the F.A.O., McDougall continued to represent Australia intermittently at various international conferences. He was one of the delegates, for example, at the London talks in 1944 which are discussed below.

<sup>377</sup> Once more, primarily Vice President Wallace, ('McDougall to Bruce', 17 July 1943, NAA M104/1, 11(4)).



instrumental in getting Coombs to write to Keynes outlining Australia's approach (of which more below). At the United Nations Conference in San Francisco in 1945, McDougall actively propagated the full employment approach amongst the delegates. By this time, however, he was not representing Australia, but the FAO.

## **6.2: Keynes, London and a Diversion in Philadelphia**

### *More Royal than the King?*

In July 1943 Coombs wrote to Keynes, seeking his opinion on the next steps Australia could take in its full employment advocacy.<sup>378</sup> Coombs had spoken with Keynes in London only a few weeks earlier (see above) about the general principles of international collaboration on employment, but was anxious now to get Keynes's opinion on his proposal that Australia take the initiative in calling for a conference which would discuss, and seek agreement on, a commitment on employment as a necessary prerequisite for any of the other post-war plans. As the first step towards establishing an international organisation which would disseminate information and coordinate employment policies, Coombs also proposed in his letter that thereafter regular meetings be convened between officials on employment conditions in member countries.

Coombs's letter caused some concern in the British Treasury, whose opinion Keynes sought before making his reply. Sir Wilfred Eady, Second Secretary in Treasury, wrote to Keynes that the letter was not 'quite so harmless as it looks'.<sup>379</sup> Referring to Coombs's efforts to have the maintenance of employment listed as one of the directives for the Board of the Clearing Union at the talks in London, Eady wrote that Australia would likely seek such a clause listed in all agreements - a development that in the context of the broader Article VII negotiations would not likely 'produce anything very safe'.<sup>380</sup>

After casting around for further views, and in the process telling his correspondents that Australia meant this advocacy 'very seriously indeed', Keynes replied to Coombs in three letters over August - September 1943. In them he wrote that there was no disagreement in London about the principle, but that the order of issues did present difficulties. According to Keynes, unemployment was not likely to be a pressing issue immediately after the war:

First, because the normal problems of unemployment are not very likely to arise immediately after the war and belong to the more normal conditions about which we can legislate at greater leisure. But also - and perhaps this is more important - because one may be forced to deal too much in generalities on this subject unless one has more knowledge than one has at present of the

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<sup>378</sup> Coombs's letter, dated 17 July 1943, was written at the urging of McDougall while the pair were in New York and was sent to Keynes in London. The letter can be found in 'Lord Keynes's Papers', PRO T247/84, 15587.

<sup>379</sup> Eady to Keynes, 6 August 1943, 'Lord Keynes' Papers', PRO T247/84, 15587.

<sup>380</sup> *ibid.*

international institutions and instrumentalities through which one will be working.<sup>381</sup>

Notwithstanding his view that a conference on employment at this point would be premature, Keynes sought to assure Coombs that maintaining full employment was a goal which would be placed 'to the forefront' of Article VII negotiations with the United States.<sup>382</sup> He also did not discount the possibility that at some later stage an international employment conference 'might be of help both in educating public opinion in the various countries and in facilitating the international acceptance of whatever plans may ultimately be agreed upon in the monetary, commodity, commercial and investment fields'.<sup>383</sup>

Keynes's correspondence with Coombs was understandably diplomatic, but in an earlier private exchange with Sir Frederick Phillips of the Treasury he voiced his concerns that the Australian approach on employment could interfere with the plans on monetary and other issues. Writing in May 1943, he told Phillips that at the talks with the United States Treasury the previous year he had been

rather impressed by the very small amount of progress the Australians really made in clearing matters up. They seem to have wasted a good deal of time discussing full employment and came away not knowing very much more about it all than they knew when they went in.<sup>384</sup>

### *Cabinet Submission*

Keynes's less than encouraging replies to Coombs coincided with events in Australia that were to firmly entrench the employment approach as Australia's chosen instrument in international negotiations and, for the first time, made it the formal

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<sup>381</sup> Keynes to Coombs, 12 August 1943, *ibid.*

<sup>382</sup> Keynes to Coombs, 3 September 1943, *ibid.*

<sup>383</sup> *ibid.*

<sup>384</sup> Keynes to Sir Frederick Phillips, 8 June 1943, 'Lord Keynes's Papers', PRO T247/84, 15587.

Keynes reactions to specific Australian proposals will be detailed throughout this study but, breaking the chronological sequence of events momentarily, his overall attitude to the employment approach was perhaps best illustrated in a letter to T.S. Eliot in April 1945 in which he wrote:

Not so long ago I was at a Conference where the Australians urged that all the Powers in the world should sign an international compact in which each undertook to maintain full employment in their own country. I objected on the ground that this was promising to be 'not only good but clever'...

...the main task is producing first the intellectual conviction and then intellectually to devise the means. Insufficiency of cleverness, not of goodness, is the main trouble...

That is the first, ought-to-be obvious, not-very-fundamental point. Next the full employment policy by means of investment is only one particular application of an intellectual theorem. You can produce the result just as well by consuming more or working less. Personally I regard the investment policy as first aid. In U.S. it almost certainly will not do the trick. Less work is the ultimate solution (a 35 hour week in U.S. would do the trick now). How you mix up the three ingredients of a cure is a matter of taste and experience, i.e. of morals and knowledge (Keynes 1980c, pp.383-384).

policy of the Australian government. In the process though, the employment approach also became less directed by the economists (though they remained throughout the architects of the proposals presented) and more controlled by political and diplomatic processes.

The key to this change was Evatt. Having taken up the employment approach on his 1943 mission, Evatt used it as the centrepiece of a submission to Cabinet in January 1944 in which he sought its authority for an agreed stance to take to the host of international conferences scheduled that year.<sup>385</sup> The first of these, and the one which determined the timing of the submission, was for the latest in the series of discussions between London, the Dominions and India. This Conference was to begin in February but since it was closely followed by an ILO Conference soon after, and the much awaited monetary conference later in the year, Evatt canvassed and sought approval upon the full range of Article VII issues.

Evatt's submission typically exaggerated the role of the Department of External Affairs in the progress of the Australian approach thus far, but it was not inaccurate about the large role they expected to take in the future. The approach itself was justified in the document on the basis that international machinery concerned with monetary and commercial policies could only operate successfully if all countries, but especially the larger ones, maintained high and stable levels of employment. Demonstrating the influence of Coombs and Giblin, what this required in turn was machinery all its own - a formal agreement in which countries would pledge their commitment to maintaining a high level of employment. Should this not prove to be practical, the submission suggested countries undertake to report through 'an appropriate international secretariat' the state of its domestic employment situation, any methods being adopted to combat unemployment, and to 'consult with others if domestic unemployment reaches serious proportions, for the purposes of examining possible national and international measures to restore the level of employment'.<sup>386</sup>

Evatt's submission noted the inadequacies of the Stabilisation Fund for Australia's plans. Nevertheless, he told Cabinet that he saw 'no reason why we should not attempt to reach agreement on some plan for stabilising rates of exchange'. Further, he noted that 'there may be certain advantages in having an international monetary fund which would guarantee to us a satisfactory quantity of overseas exchange, and would increase the purchasing power of others'.<sup>387</sup> Whether the Fund would deliver such advantages would depend upon how much the United States was willing to modify its proposal. Evatt noted that British officials were attempting to influence the United States in this direction, and he was encouraged that in the latest negotiations some of the modifications suggested by Australia and Britain were likely to be introduced. Nevertheless, much remained to be done to make the monetary plans acceptable to Australia and Evatt concluded that he viewed 'the discussions with much scepticism and with no enthusiasm'.<sup>388</sup>

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<sup>385</sup> Full Cabinet Agendum 594, Cabinet Meeting 24 January 1944. The submission, titled 'United Nations Economic Proposals' can be found in NAA CP184/1, Bundle 4.

<sup>386</sup> *ibid.*

<sup>387</sup> *ibid.*

<sup>388</sup> *ibid.*

## *Australia-New Zealand (ANZ) Agreement*

Evatt's submission was approved by the Cabinet and, although ultimately only one of a triumvirate (with Curtin and Chifley) in overseeing Australian foreign policy, he was from this moment the Minister most identifiably in charge of Australia's external economic relations. This was to have profound consequences for the employment approach and the forums to which it played. Evatt had very little idea of economics, but the employment approach was handily consistent with other objectives for postwar reconstruction that he loudly pursued in the international arena. These, which included the creation of structures to more rigorously apply legal principles to international affairs in the pursuit of social justice, national self determination, universal human rights and other objectives that Lowe (1996, p.177) collectively categorised as 'international liberalism', were in turn primarily motivated by the objective to give 'voice' to Australia as a 'middle power' with regional ambitions.<sup>389</sup> Paul Hasluck, one of Evatt's sternest critics and then an official in the External Affairs Department, was also later (Hasluck 1980, p.62) to attribute Evatt's adoption of the employment approach to an attempt to give the Government greater *domestic* legislative authority through international agreements interpreted through the Commonwealth's external affairs powers. This motivation, though perhaps not totally implausible given the defeat of a referendum designed to deliver increased powers in 1944, was explicitly denied by those most intimately involved in formulating and propagating the employment approach.<sup>390</sup>

At the same time as he made his submission to Cabinet, Evatt was also pursuing a broad agreement with New Zealand in an attempt to realise these middle power ambitions. The resultant treaty, formally the 'Pacific Charter', proclaimed a united front of both countries in demanding to be parties to any armistice talks, in calling for an international conference before any settlement on Pacific matters was reached, and in nominating much of the South and South-West Pacific as a regional defence zone overseen by Australia and New Zealand (Crockett 1993, pp.204-205). Importantly for the employment approach, a memorandum of agreement was attached to the Charter on a combined approach to the coming London talks. This agreement, made directly with the New Zealand Prime Minister, included a five-point understanding on economic matters. The first of these promised a joint campaign on the employment approach:

- (1) Because a high level of employment is a fundamental condition of better standards of living throughout the world, it is agreed to press strongly for an international agreement by which (a) subscribing countries will bind themselves to pursue domestic policies aimed at full employment and (b) existing organisations (such as the I.L.O.) will be used, or a new international

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<sup>389</sup> There has, of course, been much written about Evatt and of his ambitions for Australia during his time as Minister for External Affairs. For the most critical and hagiographic respectively, see Hasluck (1980) and Tennant (1970), but for more objective accounts see Edwards (1983), Crockett (1993), Lee (1995) and Lowe (1996).

<sup>390</sup> When asked specifically about this during a series of interviews over 1992-1994, Coombs, Melville, Tange, Wheeler and, perhaps most importantly, Evatt's former Private Secretary, John Burton, all denied that this was a motivation for Evatt or anyone else in pursuing the employment approach. It would not have worked in any case, as any casual present-day observation of Commonwealth Government adherence to ILO conventions would attest.

organisation established, to facilitate the exchange of information and consultation with each other on employment policy, and generally to give effect to the international agreement...<sup>391</sup>

Leslie Melville was chosen to lead the Australian delegation to London in 1944. He was provided with a copy of Evatt's Cabinet submission but his specific instructions for the discussions were an almost exact reproduction of the Australia-New Zealand Agreement. Not that he was in any doubt from where his instructions would come, Evatt's letter of appointment making clear that he was 'responsible to Cabinet for all matters relating to Foreign Affairs, including international discussions, international agreements and international conferences'.<sup>392</sup> Evatt told Melville to ensure all his communications were directed through the Department of External Affairs and to 'work in close concert with the New Zealand representatives, and act with them in all matters'.<sup>393</sup>

### *London Discussions, 1944*

The 1944 talks between the United Kingdom, the Dominions and India began on 23 February 1944 and were divided into five sections - monetary policy, commercial policy, commodity policy, cartel policy and employment policy. Given their brief, and their own inclinations, the last of these was of most interest to the Australian delegation and was the one for which they had come most prepared. Unfortunately for the Australians, the talks on employment did not commence until after the talks on monetary and commercial policy had been completed. Nevertheless, the Australians made the most of what time they had, with much of it devoted to discussing a memorandum written by Melville outlining the need for an international employment agreement - together with a draft of the agreement itself.<sup>394</sup>

In this memorandum, Melville outlined the by now familiar line that while the monetary and other plans were all likely to facilitate improved living standards, 'the lack of effective demand [was] the most serious enduring world economic problem', and hence the stimulus of demand was the critical issue.<sup>395</sup> Elsewhere in the memorandum, Melville hoped that 'the way should be left open for adherence by ex-enemies as soon as possible' to the employment agreement.<sup>396</sup> What Melville called 'underdeveloped-countries' should be excluded - the high employment solution might not be relevant and their acceptance of an employment agreement could bring with it reservations which could 'weaken its commitments'.<sup>397</sup>

The memorandum was accompanied by a 'Draft International Employment Agreement'. This required that 'each signatory government recognises and hereby

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<sup>391</sup> The five points are outlined in a letter from Evatt to Chifley, 24 January 1944, NAA CP184/1, Bundle 4.

<sup>392</sup> Evatt to Melville, 27 January 1944, NAA CP43/1/1, Bundle 6/1943/484/Part 1.

<sup>393</sup> *ibid.*

<sup>394</sup> The memorandum, 'An International Employment Agreement' dated 4 April 1944, together with a draft of such an agreement, can be found in NAA A989/1, 43/735/27/1, Pt.3.

<sup>395</sup> *ibid.*

<sup>396</sup> *ibid.*

<sup>397</sup> *ibid.*

undertakes a national obligation to its own people and an *international obligation to the other signatory governments* henceforth to take all measures necessary to provide such opportunities for its people that all who are able and willing to work may do so' [emphasis added].<sup>398</sup> To bring this about, signatory governments would also have to undertake;

(a) to consult with other governments and with appropriate international authorities on methods of collecting on an agreed plan detailed statistics of national employment and unemployment which will, inter alia, enable the performance of each signatory government's obligation...to be measured;

(b) to take such necessary internal measures as may be necessary and within its powers to collect the statistics relating to its own country required by the agreed plan;

(c) to submit, at intervals not exceeding three months, such statistics to other governments and to such international monetary or other authorities as may be agreed upon through an appropriate organisation;

(d) to report to other governments and representatives of international monetary and other authorities at an annual conference on the state of employment of its people and to provide information to the other governments and authorities about economic policies which have been used or are contemplated to combat unemployment;

(e) to meet with other governments and authorities at a special conference called by an appropriate organisation, if, in the opinion of that organisation, the level of unemployment in any signatory country represents a serious failure on the part of that country to observe the responsibilities herein declared to its own people and to other signatory countries, for the purpose of examining and reporting upon possible national and international measures to restore the level of employment and to prevent the spread of unemployment to other countries;

(f) to send as its representatives to such conferences high officials who are intimately concerned with advising the government on economic and social policy.<sup>399</sup>

Melville labelled the level of unemployment in any one country which would 'trigger' censure as its 'quota'. The quota would be determined according to local peculiarities, as well as a country's exposure to the international economy and to seasonal and other influences. Should a country exceed its quota, it would be required 'to consider' measures such as;

- (a) stimulation of private investment;
- (b) increase in public investment;
- (c) increased consumption expenditure;

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<sup>398</sup> *ibid.*

<sup>399</sup> *ibid.*

(d) expansion (under appropriate circumstances) of overseas investment.<sup>400</sup>

Melville's memorandum envisaged that the 'appropriate organisation' overseeing all of this would consist of little more than a 'small secretariat' which would rely on other organisations, particularly the ILO, for research and the collection of data. Since the ILO was essentially a tripartite body encompassing the representatives of labour, employers as well as government, the ILO was not itself seen as 'the' appropriate organisation. The paucity of reliable national employment statistics was noted by Melville as a cause of concern, but the 'improvements during the war in the collection of statistics have indicated that the way towards the provision of adequate statistics may not be so difficult'.<sup>401</sup>

### *Reaction*

The reaction of British officials to Melville's proposals was initially much the same as that outlined by Keynes in his correspondence with Coombs the previous year. Keynes, himself a member of the British team at the employment discussions, reiterated his concerns that nothing could be done until more was known about the proposed bodies concerned with monetary and commercial policy. He also stated that the United States would never agree to anything that hinted at international interference in domestic policy. Keynes went on to outline what he thought were the changes in policy required in the United States if it was to maintain high levels of employment. In remarks that gave an extraordinary insight into his longer-term vision of the post-war world, Keynes viewed the end of its large military expenditure as forcing the United States to engage in 'less orthodox expedients'.<sup>402</sup> These included large reductions in working hours, 'drastic' changes in policies towards saving, a redistribution of income and wealth and, 'even the endowment of some members of the community with an income, whether they worked or not'.<sup>403</sup> None of these changes could be dictated by an external body. Far better it was, in Keynes's view, to proceed with plans for bodies with more limited objectives than full employment, such plans insulating the rest of the world 'while the enormous social experiments in prospect in the United States were proceeding'.<sup>404</sup> James Meade and Lionel Robbins, also members of the British team, similarly declared that they thought the monetary and commercial proposals were sufficient to ensure that countries at least could not *export* unemployment.<sup>405</sup>

The other Dominion delegations were 'sceptical and sarcastic' about the Australian proposals.<sup>406</sup> Even New Zealand, supposedly Australia's steadfast ally in propagating an employment agreement, prefaced its submission supporting Melville's memoranda with the observation that countries had to learn 'the lesson that high tariffs were not a

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<sup>400</sup> *ibid.*

<sup>401</sup> *ibid.*

<sup>402</sup> Keynes's reply to Melville on behalf of the United Kingdom can be found in 'Mutual Aid Agreement, Article 7: Discussions with Dominions; Employment; Minutes, February - March 1944', 'Lord Keynes's Papers', Treasury, PRO T247/25.

<sup>403</sup> *ibid.*

<sup>404</sup> *ibid.*

<sup>405</sup> Statements of Mr. J.E. Meade and Prof. L. Robbins, *ibid.*

<sup>406</sup> N.G. Butlin, Personal Report for Dr. Coombs, London Discussions on Article VII Feb-March 1944, NAA CP43/1/1, Bundle 6/1943/484/Pt2.

remedy for unemployment'.<sup>407</sup> This lack of total support from New Zealand and the reaction of the British prompted a series of telegrams from Evatt, urging Melville to continue to pursue an employment agreement regardless, and declaring that he was 'most disturbed' that Keynes had taken up cudgels for the United States.<sup>408</sup>

In the end, however, the lack of support from the other Dominions did not matter because, for reasons which remain obscure, the British delegates suddenly announced towards the end of the talks that they would support Australia's proposal for a draft employment agreement. The form of this agreement was somewhat modified from Melville's original memorandum, with the subsequent compromise 'Draft International Employment Agreement' differing from its precursor in that the idea of an unemployment 'quota' was abandoned, the agreement was expressed in terms of a 'high level' rather than 'full' employment, and the removal of the provisions which allowed an 'international body' (as opposed to other signatory governments) to censure a country because of its failure to maintain employment.<sup>409</sup> The final Draft was somewhat less assured in its policy advocacy, too, the confident tones of Melville's call that governments 'take all measures necessary' to provide employment being replaced with the more passive commitment that they 'take such measures as may be necessary and *practicable* to fulfil this purpose'.<sup>410</sup> Many similar changes of linguistic style (with nonetheless important policy implications) also separated the compromise Draft from its more strident original. The other Dominion governments fell into line behind the United Kingdom, which also promised to take the new Draft into talks with the United States.<sup>411</sup> Butlin and Schedvin (1977, p.658) allege that United Kingdom acquiescence on the employment agreement 'was to create a diplomatic carousel which Australia could enjoy harmlessly'. If this was true, it was a mistaken belief that the Australians could be so easily shaken off. Contrary to the expectations of many British officials at the talks, and contrary to Butlin and Schedvin's later assertions, the employment approach was not about providing a blanket escape clause from commercial negotiations, but was a coherent and consistent policy based upon (as shall be discussed below) sound theoretical footings. Australia did not step back from the employment approach but, with draft agreement now in hand, expected a united Commonwealth front to work for its ordination

Melville told Curtin in his final report on the London discussions that the United Kingdom's acceptance of the (albeit amended) employment agreement marked a 'big

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<sup>407</sup> Statement of Professor A.G.B. Fisher on behalf of New Zealand, Article VII Discussions with Representatives of the Dominions and India, Committee on Employment Policy, Minutes of Second Meeting, 6 March 1944, NAA CP43/1/1, Bundle 6/1943/484/Pt.2.

<sup>408</sup> Two such telegrams dated 9 March 1944 can be found in NAA A989/1, 43/735/55/3/4. Melville himself also fell into Evatt's disfavour, prompting him to send to Evatt upon the completion of the London talks a long telegram defending his actions. 'Melville to Curtin', 27 March 1944, NAA A989/735/55/3/2.

<sup>409</sup> A document prepared by the Department of External Affairs which compares Melville's original with the London compromise, authored by F.C. Pryor and dated 21 March 1944, can be found in NAA CP184/1, Bundle 4. A copy of the London compromise is contained in 'Article VII Discussions with Representatives of the Dominions and India, Committee on Employment Policy, Minutes of Second Meeting, 6 March 1944', *op.cit.*

<sup>410</sup> 'Article VII Discussions with Representatives of the Dominions and India, Committee on Employment Policy, Minutes of Second Meeting, 6 March 1944, *op.cit.*

<sup>411</sup> *ibid.*



step forward' for Australia's approach.<sup>412</sup> The modifications sought by the United Kingdom were, in themselves, 'quite satisfactory' and should the agreement be taken up by the United States it would 'do much to ensure that Governments will take the steps necessary to maintain a high level of employment and will help greatly to mobilise public opinion in all countries in favour of the necessary domestic policies'.<sup>413</sup> Melville's doubts, however, remained. Telling Curtin that agreements were one thing, but that actually maintaining high levels of employment was something else again, he doubted whether even in the United Kingdom (where he approvingly reported that much thought had already been devoted to employment policies), plans were 'sufficiently comprehensive' to do the trick. In particular, Melville believed that the United Kingdom's approach, 'under Lord Keynes's guidance', was being 'prepared on too narrow a front'.<sup>414</sup> It was, he thought, over-reliant on monetary policy while the proposed public works and taxation measures were too limited to 'mobilise sufficient force at the right time to overcome a developing depression'.<sup>415</sup> When there was added to this the likely 'hesitation of the Government in giving legislative force to plans worked out by Commissions and officials', Melville did 'not regard the maintenance of employment in the United Kingdom as at all assured'.<sup>416</sup>

But if the maintenance of high employment was not assured in the United Kingdom it was, in Melville's view, even less assured in the United States. Concluding his report with remarkable pessimism, he agreed with Keynes that the maintenance of high levels of employment in the United States would likely require 'unconventional measures' - for which American public opinion was not as yet ready.<sup>417</sup> Accordingly, it remained Australia's task, notwithstanding the results of all the conferences, negotiations and agreements thus far, to examine in all agreements still to be made the ways in which they could be written to ensure 'that they will enable us to protect ourselves in the event of falling world employment'.<sup>418</sup> Melville's tactical advice to Curtin to this end was two-pronged. Firstly, Australia could attempt to establish a general preamble in all agreements which accepted 'the principle that all the proposals are interdependent and if one agreement fails all are to be suspended'. Secondly, as Melville rightly suspected that this would be strongly resisted, 'we should try to ensure, by suitable provisions *in each of the various plans*, that we would be damaged as little as possible' (emphasis added).<sup>419</sup>

### *Diversion in Philadelphia*

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<sup>412</sup> 'Report on London Discussions on Article VII, February-March 1944', L.G. Melville, 21 April 1944, NAA A5934/1, 658/2. This is not to say, however, that Melville thought that the United Kingdom itself was convinced on the matter. In an interview with the author on 28 January 1993, Melville recalled that amongst British officials there was 'scepticism but not hostility to an employment agreement. They didn't really believe that we would get anywhere with it, and they themselves didn't seem prepared to do much except just give a few words of encouragement...'

<sup>413</sup> *ibid.*

<sup>414</sup> *ibid.*

<sup>415</sup> *ibid.*

<sup>416</sup> *ibid.*

<sup>417</sup> *ibid.*

<sup>418</sup> *ibid.*

<sup>419</sup> *ibid.*

The increasing influence of Evatt upon events was in evidence at the twenty-sixth conference of the ILO held in Philadelphia from 20 April 1944. This marked the next stage in the propagation of the employment approach. The conference, which had been convened in order to chart the ILO's future, was not regarded by Melville (who, with the rest of the London delegation, was making his way through to Washington) nor indeed any of the economists back in Australia as the appropriate venue in which to push the Australian proposals.<sup>420</sup> The economists, however, had no say in the matter. The delegation chosen by Evatt to represent Australia at Philadelphia was headed by his fellow cabinet minister, John Beasley, and, apart from the economics-trained John Burton, included no economists. This exclusion of the economists reached a high point immediately before the opening of the ILO conference when, fearing that 'Melville's delegation' would brief American officials before his own efforts commenced, Beasley sought Evatt's approval that their arrival in Washington be delayed.<sup>421</sup>

Discounting for what Tange (1996, p.264) recalled as the 'braggadocio' in Beasley's cabled reports of events back to Evatt in Australia, the Australian delegation made an impression with the other delegates at Philadelphia, particularly those who had never been exposed to the employment approach before. It was an impression that was quickly tainted, however, by the very public conflict which emerged between the Australian and American delegations after the latter's unexpected presentation of its *own* resolution on employment. This resolution, introduced by Frances Perkins, the United States Secretary of Labour and leader of its delegation at Philadelphia, restated the Atlantic Charter, made reference to minimum standards of welfare, argued that the '*opportunity* of useful and regular employment' should be available to all and declared that there should be a 'liberation from unreasonable restriction of trade [and the] movement of capital...'<sup>422</sup> It was, of course, a total anathema to the Australians

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<sup>420</sup> As apparent in interviews between the author and Tange in 1992, and Melville and Coombs in 1993, it was a view they still shared. Sir Arthur Tange in particular, remained extremely critical of the use of the ILO in 1944. He maintained that the venture 'was a sideshow that reflected the anxiety of the Australian ministers to get hold of what was going on and this was the first occasion in which responsible cabinet ministers were able to attend these matters, to express their view, and not rely on Coombs, Melville and the rest of us' (Sir Arthur Tange, interview with author, 2 October 1992).

<sup>421</sup> This appeal to Evatt was a curious affair:

In the light of the difficulty you had in establishing responsibility for Foreign Economic Policy and in view of the fact that the Melville Delegation made it apparent to you that they did not always interpret their instructions as you would wish, and in fact *seemed to miss the employment approach on occasions*, I think I should inform you that Melville and Wheeler are in Ottawa now and proceeding to Washington on Monday...

Naturally officials in Washington will wish to discuss with them my statement that I will have made here and our proposals as it will be *the first time* they have heard of them as a formal proposal. I would prefer this not to happen before I have met the Secretary of State and others and have been able to stress the political implications of our proposals and their broader significance. Even the so called technical discussions must lead to discussions of general principles and unless you see some useful purpose in informal official discussions at this stage, I think they should be avoided ( 'Beasley to Evatt', 19 April 1944, NAA A3195, 1944, 1/14910, emphasis added).

<sup>422</sup> The American resolution is cited in Australia, Parliament (1944), pp.11-12. Frances Perkins (1882-1965), had been Roosevelt's Secretary of Labor since 1933. She was the first female Cabinet member

and Beasley wasted little time in diplomatic niceties in condemning it. He told the Conference that the lack of binding obligations in the American proposal meant ‘that it merely paid lip service’ to the principle that the Secretary of Labour had herself admitted when introducing it - ‘that domestic policies were of international concern’. Beasley also attacked the individualistic tone of the American document, and stated that he believed its provisions had the effect ‘not merely of weakening our proposals, but also of denying to workers the right of collective bargaining’.<sup>423</sup>

With this issue threatening to undermine the Conference itself, the Australian and American delegations agreed to try and find a compromise between them. As noted by Butlin and Schedvin (1977, p.660), what followed was ‘a tangled story of misunderstanding, backroom manoeuvring, charge and countercharge’, but which nevertheless came up with a compromise draft not materially different from the Draft Employment Agreement which emerged from the London talks the previous month.<sup>424</sup> All of this was dramatically reversed, however, by the last minute intervention by the State Department. Apparently alarmed at what Perkins was about to agree to, the State Department not only vetoed the revised draft but even withdrew the original American proposal. A much-watered down version of the latter was substituted that said little more than that governments had *some* responsibility to fight unemployment. It was this version that was subsequently included in the final resolutions of the Philadelphia Conference.<sup>425</sup>

Beasley was justifiably angered at the United States turnaround, though his statements before the Conference and his reports back to Australia were characteristically histrionic. He told the Conference that the events which had occurred were ‘more than a difference of view between two governments’, but were revealing of ‘a fundamental weakness which is likely to threaten the whole future of United Nations economic collaboration’.<sup>426</sup> More immediately, with the proposed monetary discussions fast approaching, he declared for Australia that ‘if the United States Government is unwilling to undertake some employment obligations, we must hesitate before entering into discussions on other aspects of international economic collaboration, and we could not feel ourselves obliged to undertake any commitments which limited our freedom of action to protect our economy against depressed conditions overseas’.<sup>427</sup> The Australians could savour one success at Philadelphia, though. A resolution advanced at the beginning of the Conference for a further conference dedicated exclusively to considering ‘an international agreement on domestic policies of employment and unemployment’ was passed unanimously at the final session.<sup>428</sup>

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in the United States, and was greeted with typical distrust by conservative business interests (Johnson 1966, p.628).

<sup>423</sup> Commonwealth of Australia (1944), p.13.

<sup>424</sup> This compromise draft is include in *ibid.*, pp.13-14.

<sup>425</sup> *ibid.*, p.4.

<sup>426</sup> *ibid.*, p.14.

<sup>427</sup> *ibid.*

<sup>428</sup> This resolution can be found in *ibid.*, p.11. Despite the outcome of the Philadelphia Conference, Beasley remained convinced that his had been the correct approach. In another remarkable telegram to Evatt on 3 May he justified his actions thus:

The formal procedure for us to follow would have been to wait until the United Kingdom had approached the United States on an employment agreement, but I am convinced that we have done the right thing. With the freedom you gave me, I had no hesitation in pressing the matter

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into the open. Negotiations on an official level would have got us nowhere. *You and I understand better than the officials* how necessary it is to take matters of this kind into the open and I am convinced that we have done right in bowling it up to the Americans at this time and publicly. We cannot afford to wait for formal procedure and must be prepared to fight. I see clearly now that our whole future is at stake in negotiations such as these and realise the valuable line *you* have put us on to. It will be a great thing when party and people fully understand what *you* have done (emphasis added). 'Beasley to Evatt', 3 May 1944, NAA A989, 44/1320/13/3.

## **Chapter Seven**

### **Bretton Woods**

#### **7.0 The Joint Statement**

In May 1944, an invitation was issued by Roosevelt to all members of the United Nations to attend a conference ‘for the purpose of formulating definite proposal[s] for an international monetary fund and possibly a bank for reconstruction and development’.<sup>429</sup> The Conference was to be held at Bretton Woods, New Hampshire from 1 July 1944 and would include the representatives of forty-four governments. Prior to the conference, a smaller group of countries would meet in Atlantic City, New Jersey, to act as a drafting committee. Invited countries were informed that delegates need not hold ‘plenipotentiary powers’ since ‘the proposals at the conference would be referred to the respective Governments and authorities for their acceptance or rejection’.<sup>430</sup> The basis of discussions at both meetings would be the ‘Joint Statement of Experts’, a compromise between the Stabilization Fund and the Clearing Union, both of which had been published separately the year before. Australia was included in the select group of countries invited to Bretton Woods and the meeting of the drafting committee in Atlantic City.

As noted earlier, from mid-1943 Keynes had privately conceded that whatever the intrinsic merits of his Clearing Union proposal, the likely postwar economic dominance of the United States dictated that it would be *its* wishes which would prevail. Accordingly, his purpose from around this time was to attempt to graft as many features of the Clearing Union as possible onto the Fund. This process formally got under way in September 1943, with the first of a series of meetings between British and American officials, and with Keynes and White playing the leading roles. The discussions produced a succession of drafts of what would become the Joint Statement, the final form of which was published in April 1944. In its final manifestation, the Joint Statement had reconciled all but one of the outstanding differences between the British and American negotiators. Of course, this ‘reconciliation’ was a one-sided affair, with the proposals, assumptions and even the name of the American approach (‘International Monetary Fund’) being used as the basis for the drafting document (Horsefield 1969, pp.54-57).

Of most importance to Australia, and the already voiced concerns of its representatives with regard to the Stabilisation Fund, the Joint Statement settled the following issues:

- 1) The size of quotas.

The Joint Statement’s aggregate of quotas totalled \$US 8.5 billion - up from the \$US 5 billion allocated in the Stabilisation Fund but short of the \$US 12 billion in total

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<sup>429</sup> The Australian invitation is contained in a letter from the United States Ambassador to Australia to Evatt and dated 26 May 1944. The letter is contained in NAA A989, 44/735/56/8.

<sup>430</sup> *Ibid.*

available funds sought by Keynes. For Australia, the Joint Statement allocated a quota of \$US 149 million (Horsefield 1969, p.58).

## 2) The ability to change exchange rates.

One of the most important alterations to the Fund's rules sought by Keynes was a significant relaxation of the restrictions upon countries to vary their exchange rate. He wanted amendments that would allow a country to unilaterally vary its exchange rate by up to 10 percent every ten years, on the understanding that such variations only take place to deal with 'fundamental disequilibrium'. He also proposed that if a country wanted to vary its exchange rate by a further 10 percent, it should *consult* the Fund, but that it should not need the Fund's approval before doing so. In the end, the Americans agreed to the first of these amendments and even allowed that requests for exchange rate movements beyond 10 percent be considered by the Fund 'within 48 hours'. What remained, however, was that permission from the Fund would be required for changes in the exchange rate beyond 10 percent and that this authorisation was still to be based on the Fund's interpretation of 'fundamental disequilibrium' (Horsefield 1969, pp.61-62).

## 3) Withdrawal.

Since a member country unhappy with the restrictions on its ability to alter its exchange rate could simply withdraw from the Fund, a clause in White's original proposal had included a range of penalties and advance notice requirements before a member country could leave. These restrictions were opposed by the British negotiators, and subsequently removed from the Joint Statement (Horsefield 1969, p.59).

## 4) New international currency.

A fundamentally expansionary feature of the Clearing Union, and one which was immensely attractive to the Australian economists, was its provision of the new international currency, 'Bancor'. White's Stabilisation Fund had no such provisions and Keynes's attempts to convert 'Unitas' (in White's plan, a unit of account *only* and to be used solely by the International Bank) into a true international currency for inter-Fund settlements were constantly resisted. Eventually, Keynes had to accept the inevitable on the issue of a new international currency, and it was a non-Unitas version of the Fund which was published in the Joint Statement (Horsefield 1969, pp64-67).

## 5) Scarce currency clause.

A great fault of the Stabilisation Fund in the eyes of the Australians had been its lack of any censure on persistent creditors. During the negotiations between the Americans and the British, however, a new device with implications for creditors emerged in the *scarce currency clause*. The idea, which was championed by Keynes, was that for a country whose credit position was such its currency had become *scarce*, a declaration of the Fund to this fact would release other countries of any of the obligations to that currency. This would mean, for example, that exchange controls and other

protectionist devices could be applied against that currency or against the exports of the country concerned. After much wrangling, this proposal was included in the Joint Statement (Horsefield 1969, pp58-59).

#### 6) Drawings from the Fund.

A final issue which was, in fact, left unresolved in the Joint Statement concerned the ability of member countries to draw on their quotas. The American negotiators had come up with a formula which would allow a member to draw-down up to 25 percent of their quota within a given year. The ability to draw down was, however, subject to the provision that 'the Fund has not previously given notice that a member country is making use of the Fund's resources at an unwarranted rate or in a manner that clearly has the effect of preventing... the establishment of a sound balance in its international accounts'.<sup>431</sup> Keynes had vigorously opposed these restrictions and the degree of power of the Fund over member countries implicit in the American proposals. It would be, he wrote to Jacob Viner in October 1943, 'very unwise to try and make an untried institution too grandmotherly'.<sup>432</sup> On the specific issue of quotas, this meant that member countries should be given sufficient confidence that 'they must be able to rely in all normal circumstances on drawing a substantial part of their quota without policing or facing unforeseen obstacles'.<sup>433</sup> In practice, Keynes did not believe that the Fund should have any powers over the ability of a member to draw down until that member had drawn at least two-thirds of its quota. In the end, the issue was left open in the Joint Statement (Horsefield 1969, pp.67-75)<sup>434</sup>.

#### *Australian Reaction to the Joint Statement*

Melville was able to examine the penultimate version of the Joint Statement during the talks in London in February-March 1944 where it was used as the basis of his discussions with British officials. Successfully convincing the British that the preamble of the Joint Statement should be reworded to make it clear 'that the pressure put on a country to correct a maladjustment in its balance of payments will not prevent it from following a policy of expansion intended to maintain a high level of employment', he was also successful in enlisting their support for an increase in Australia's quota in the Fund.<sup>435</sup> There were, however, two other issues, at the heart of the controversies surrounding the Joint Statement, without whose resolution Melville did not think the Fund could be of any use to Australia.

The first of these issues related to the great unresolved question in the Joint Statement - the limitation on the total annual draw-downs on the quotas of member countries. The United States proposal, that annual drawings on the Fund be limited to 25 percent of the quota, was totally unacceptable to Melville. In his final report on the talks to Australia, Melville wrote that even if the increase in Australia's quota was accepted,

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<sup>431</sup> White cited in Horsefield (1969), p.71.

<sup>432</sup> Keynes's letter to Viner was written on 18 October 1943, and is cited in Horsefield (1969), p.72.

<sup>433</sup> *ibid.*

<sup>434</sup> As Horsefield (1969, p.77) notes, underlying the United States opposition to the ability of countries to draw down their quotas automatically was a probable conviction that the United States would never have to draw from the Fund.

<sup>435</sup> 'Report on London Discussions on Article VII, February-March 1944', L.G. Melville, 21 April 1944, *op.cit.*

only £19 million sterling would be available in any year - a situation which was 'likely to be very embarrassing in view of the large fluctuations to which our overseas funds are subjected by the unstable nature of the prices and volume of our exports'.<sup>436</sup> Under the American proposals, Australia could access more funds but these would be subject to the Fund's supervision. This was something that would not be desirable, economically or politically, and Melville argued that Australia should 'press for an increase in the annual drawing to 33% of the quota'.<sup>437</sup>

The second issue of concern to Melville - the limitations on countries in varying their exchange rates unilaterally - was even more important. Indeed, seemingly to question the whole project, Melville wrote in his final report that 'in the course of the discussions in London, my conviction has grown that it would be imprudent for Australia to surrender this liberty to an international body'.<sup>438</sup> The three safeguards provided by the Fund in this regard - that the Fund would have to respond to a request for an exchange rate change beyond 10 percent within 48 hours, that the Fund *must* permit a variation in the exchange rate to correct fundamental disequilibrium, and that a member country could freely withdraw from the Fund - were not, in Melville's eyes, sufficient. The presumptions of the Fund would always favour exchange stability and, Melville concluded, '[t]he discussions in London...seem to me to suggest that the Fund would have no difficulty in deciding, in the circumstances in which Australia might ask for a depreciation, that that was not an appropriate remedy for her difficulties'.<sup>439</sup>

### *Correspondence with Keynes*

As an addition to these 'safeguards', Melville proposed at the London talks that the restrictions upon exchange rate changes be relaxed 'for countries whose export price levels had fallen more than their import price levels'.<sup>440</sup> This was a suggestion, however, which brought Melville into conflict with Keynes. As noted above, Keynes himself had fought against the American exchange restrictions but, not for the first or last time in his dealings with Australia, he seems to have been more than willing to play devil's advocate. Keynes missed the discussions in which Melville's objections were initially raised, but he replied to some of them in a series of letters in which he rejected the assumptions upon which he believed they were based. On the issue of the Fund allowing exchange rate changes beyond an initial 10 percent, Keynes hoped that, contrary to Melville's fears, 'one can assume that, if there is a good and reasonable case, approval will be easily given'.<sup>441</sup> Keynes also told Melville (not entirely truthfully) that the discussion with the United States had been about whether exchange rate changes could be made unilaterally or not, and not whether they should be made at all. It was, 'important not to confuse the amount of unilateral discretion with the question of changes generally'.<sup>442</sup>

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<sup>436</sup> *ibid.*

<sup>437</sup> *ibid.*

<sup>438</sup> *ibid.*

<sup>439</sup> *ibid.*

<sup>440</sup> *ibid.*

<sup>441</sup> 'Keynes to Melville', 14 March 1944, NAA M2271/1, 11.

<sup>442</sup> *ibid.*



Keynes was even more concerned to take up with Melville the issue of the efficacy of varying exchange rates in response to changes in the terms of trade. Using the example Melville had employed in discussion with other officials, Keynes wrote that he found it ‘extraordinarily difficult to see how an alteration in the exchanges could possibly be the right remedy for a catastrophic fall in some staple export commodity, such as wool’.<sup>443</sup> The maintenance of the incomes of wool producers by such means would also greatly increase the income of other exporters as well, but all at the expense of the spending power of the rest of the public and the country in general. Such a policy was akin to ‘burning down the house for roast pork’.<sup>444</sup> A much better solution to the problem of fluctuating prices for important export staples was in buffer stocks and related schemes - and on this Keynes expressed his disappointment ‘by the lack of enthusiasm which the primary producers seem to feel for plans to keep their prices more stable’.<sup>445</sup>

Melville replied to Keynes’s criticism in a letter that also more fully set out his reluctance to accept that the ‘safeguards’ of the Fund meant very much. He questioned Keynes’s assurances that there would exist a presumption in the Fund in favour of approving requests for exchange rate changes. He told Keynes that the methodology employed by the Fund in these decisions would likely be flawed since the Fund ‘however expert and impartial’, would be ‘made up largely of people familiar with the very different needs of highly industrialised countries’.<sup>446</sup> The needs of countries dependent upon a narrow range of export commodities was poorly understood and he envisaged a scenario in which in a time of falling prices, ‘this “impartial” body might start talking about hard cases making bad law...and refuse the second ten percent’.<sup>447</sup> In support of this thesis, Melville cited Keynes himself - ‘[t]hey also might feel as you do, that a depreciation of the exchange rate was not the appropriate remedy’.<sup>448</sup>

On the appropriateness of varying the exchange rate in response to a collapse in export prices, Melville was unequivocal. He referred Keynes to Australia’s experiences in 1931, when cutting wages and government spending had been seen as a solution, but this was ‘a way out which I believe is no longer open’.<sup>449</sup> To such policies after the war, ‘workers would not remain docile and to the economic dislocations would be added grave social disorders which would greatly intensify the loss of income’.<sup>450</sup> Specifically referring once more to wool, Melville wrote that Australia depended on the economic rent this industry generated, the loss of which, if wool prices fell, would need to be spread across all sectors of the economy. There was, he thought, ‘no way of doing this other than by a depreciation of the currency or a cut in wages’.<sup>451</sup> On the buffer stocks schemes Melville declared himself to have ‘enthusiasm for the idea’, but Australia could not entirely trust buffer stocks ‘until we

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<sup>443</sup> *ibid.*

<sup>444</sup> *ibid.*

<sup>445</sup> *ibid.* For more on Keynes’s buffer stocks schemes, and reactions to them, see Dimand and Dimand (1990) and Turnell (1998).

<sup>446</sup> ‘Melville to Keynes’, 24 March 1944, NAA M2271, 11.

<sup>447</sup> *ibid.*

<sup>448</sup> *ibid.*

<sup>449</sup> *ibid.*

<sup>450</sup> *ibid.*

<sup>451</sup> *ibid.*

have found by experience that they provide us with firm ground'.<sup>452</sup> Finally, suggestive of the extent to which he was out of sympathy with the Fund as outlined in the Joint Statement, Melville observed that:

...I have long felt that stable exchange rates may not provide the most satisfactory monetary system for countries producing a narrow range of staple commodities and if a country, greatly daring, took advantage of the provision to link exchange rates and export price levels it may be that it would provide an experiment that would eventually lead us to higher and more stable levels of international trade.<sup>453</sup>

In his correspondence with Keynes, Melville did not mention the scarce currency clause, but on this, too, he thought 'Lord Keynes exaggerates its usefulness in preventing the spread of depression'.<sup>454</sup> According to Melville, the clause might allow other countries to discriminate against American exports and impose exchange controls upon the movements of dollars (if this was the currency so designated), but it still remained that in order to avoid depression in response to say, an American downturn, 'internal demand...would need to be increased to offset the fall in the United States demand for their products'.<sup>455</sup> But with the limitations imposed by the Fund as well as those likely under Article VII more broadly, 'this would not be easy'. The final option for a country at odds with the Fund - namely, withdrawal - was similarly not much of an option. Even if there were no specific penalties, withdrawal from the Fund was likely to require withdrawal from other international bodies, potentially imposing 'intolerable burdens on us'.<sup>456</sup>

The Joint Statement suggested a transitional period of up to three years before member countries would have to meet the criteria set down by the Fund. Melville did not regard this as enough. Perceptively, he believed that there was 'no prospect of Great Britain overcoming her post-war difficulties so soon'.<sup>457</sup>

### *Discussions with White*

Melville had the opportunity to take up some of these issues with the principal author of the Fund when he called upon White in Washington following the talks in London. This meeting, however, was an inauspicious one with regard to Australia's relationship with the Fund. In the aftermath of London, Melville had (reluctantly) recommended that subject to the granting of easier restrictions on countries facing a downturn in their terms of trade and an increase in permissible annual drawings to 33 percent of the quota, Australia should accept membership of the Fund. In Washington, however, he found White strongly opposed to any suggestions that the maximum drawings on quotas be raised and for 'making provision in the Fund for any greater flexibility of exchange rates'.<sup>458</sup> Melville also found that White was reluctant to alter

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<sup>452</sup> *ibid.*

<sup>453</sup> *ibid.*

<sup>454</sup> 'Report on London Discussions on Article VII, February-March 1944', L.G. Melville, 21 April 1944, *op.cit.*

<sup>455</sup> *ibid.*

<sup>456</sup> *ibid.*

<sup>457</sup> *ibid.*

<sup>458</sup> 'Melville to Evatt and Chifley', 27 April 1944, NAA A989, 44/735/56/6.

the wording to the preamble of the Fund to suit Australia's suggestions on employment. Finally, if Australia was to receive an increase in its quota, then this would have to come at the expense of another country willing to reduce its own.

Following his discussions with White, Melville sent a telegram to Evatt and Chifley in late April 1944 in which he told them that a conference on the Fund would likely be held within the next few months. He also told them that, in his view, the Fund as now drafted was 'quite unsatisfactory for Australia'.<sup>459</sup>

### *Cabinet Considers Bretton Woods*

Melville's verdict on the Fund from Washington coincided with the issuing of the invitations to the Bretton Woods conference. There was sufficient time, however, for Melville and Wheeler to return to Australia in order to brief ministers more fully before they would need to return to the United States as part of the Australian delegation. In the meantime, though, Cabinet decided to accept the invitation to the Conference. Overcoming what was already resistance within sections of the Labor ministry to the Fund, Chifley painted a scenario in his Cabinet submission concerning what could happen in the *absence* of such an institution;

...there is one important consideration which should not be overlooked - viz. the post-war position if there is no International Monetary Fund or co-operation. There are many people who view such a position with grave foreboding and prophesy competitive exchange depreciation and restriction by countries in order to reap some temporary benefit. Such action would cut right across the aims of expanded trade and employment and might lead quickly to an era of economic nationalism rather than international co-operation.

...Both the U.K. and the U.S.A. place great importance on an International Monetary Fund and regard it as an essential part of post-war plans. Australia would need to have very strong grounds in principle if she decided to stand out or adopt an unfriendly attitude.<sup>460</sup>

Chifley's Cabinet submission was supported by Evatt and together they served on the Cabinet Sub-Committee charged with deciding upon the stance to be taken at Bretton Woods. By the time the Sub-Committee met, Melville and Wheeler had also arrived back in Australia, and their views on the Fund, together with the comments of other economists, were gathered together in a memorandum, 'Australia and the International Monetary Fund', which formed the basis of the Sub-Committee's report to the Cabinet.<sup>461</sup> This report found that the Fund would both strengthen Australia's ability to meet fluctuations in its balance of payments as well as deliver 'indirect

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<sup>459</sup> *ibid.*

<sup>460</sup> 'Supplement by the Treasurer to Full Cabinet Agendum No.669. International Conference on Post-War Monetary Organisation', 30 May 1944, NAA A2700/XM1, Volume 11.

<sup>461</sup> 'Australia and the Monetary Fund', 10 June 1944, NAA A2700/XM1, Volume 11. At this time Curtin was in London and, although Francis Forde was acting Prime Minister, real Cabinet authority rested with Chifley and, to a lesser extent, Evatt. During his talks in London, Curtin himself pushed the employment approach, telling Winston Churchill that 'full employment and rehabilitation was the pedestal on which we must work out a good monetary policy' ('Curtin to Forde', 19 May 1944, NAA A989, 44/735/56/6).

benefits through its potentially expansive effects on international trade'.<sup>462</sup> It also found, however, that commitment to the Fund would also require sacrifices, the most important of which were grouped along the lines of Melville's objections:

- (a) Purposes and policies of the Fund.
- (b) The Australian quota and annual drawing rights.
- (c) Control of movements in exchange rates.
- (d) Right of withdrawal.
- (e) The form of management and the discretionary powers in its hands.<sup>463</sup>

The economists' memorandum had also concluded that the 'successful working of the Fund will depend largely on a high level of employment being maintained in all major trading countries'. Accordingly, Australia should press for an employment agreement to be concluded 'before final decision is sought on whether countries will become members of the Fund'.<sup>464</sup> Leaving diplomatic room, the memorandum added that should such an agreement not be reached at Bretton Woods or otherwise in time, it might still be to Australia's interests to join the Fund. Nevertheless, merely by making clear its views on the importance of 'the employment aspect', Australia 'would have greatly strengthened its bargaining power for special assistance and increased the practicability of withdrawal from the Fund if that body failed to meet our requirements'.<sup>465</sup>

The Cabinet accepted the arguments of the Sub-Committee's report and the employment emphasis of the economists' memorandum. Accordingly, it issued instructions to the delegates to Bretton Woods to seek amendments to the Fund along the following lines:

- A. To press strongly for substantially increased accommodation both in respect of the "quota" and the annual drawing rights.
- B. To seek:
  - (a) the inclusion...of a provision that the Fund shall not reject a requested change in the exchange rate which is designed to meet a serious and persistent deficit in the balance of payments on current account accompanied by a substantially adverse change in the terms of trade.
  - (b) the alteration of the "purposes and policies" of the Fund to give more emphasis to employment and less emphasis to exchange stability and to strengthen the safeguards against the Fund interfering with the domestic policies of a country.

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<sup>462</sup> 'International Conference, Proposed International Monetary Fund', Cabinet Agenda No.669, J.B. Chifley, Treasurer and Minister for Post-War Reconstruction and H.V. Evatt, Minister for External Affairs, 10 June 1944, NAA A2700/XM1, Volume 11.

<sup>463</sup> *ibid.*

<sup>464</sup> 'Australia and the Monetary Fund'. 10 June 1944, *op.cit.*

<sup>465</sup> *ibid.*

C. To ask that it should be made clear that the right of withdrawal from the Fund should not be prejudiced by making membership of the Fund a condition of membership of any other international body.

D. To urge that an employment agreement should be concluded before a final decision is sought on whether countries will become members of the Fund.

E. To report any proposals made concerning the time of commencement of benefits and obligations before a decision regarding the Australian attitude is made.<sup>466</sup>

The Australian delegation to Bretton Woods was led (once more) by Melville and included Wheeler, Tange (now of the Department of External Affairs) and Brigden, the latter joining the delegation from his position at the Australian Legation in Washington.

One item for which the Cabinet could issue no real instructions was the proposal for the creation of the mooted International Bank. As a supplement to a Cabinet Agendum of Chifley and Evatt rightly noted, there had been some discussion between American and British officials on the subject, but ‘no concrete proposal for discussion at the Conference had been put forward’.<sup>467</sup> Such an institution was of interest to Australia because, as the Cabinet Agendum noted, it could encourage ‘overseas investment by creditor countries, assist other countries to bring about equilibrium in their balance of payments, and thus facilitate the successful operation’ of the Fund and ‘any other post-war economic proposals’.<sup>468</sup> Given the amount of information they had, however, Cabinet could do little but to instruct the delegation ‘to inform the Conference that the Commonwealth Government is interested in further action being taken’.<sup>469</sup>

## **7.1 The Conference**

Before Bretton Woods itself, the Australian delegation joined that select group of delegates in Atlantic City charged with drafting a formal agenda for the broader conference. These meetings achieved their objectives, but were of little importance for Australia’s purposes. Though Melville advanced most of the modifications to the Fund that the Australians were seeking, these met both with resistance from the United States delegation and with the diverting reply that they were, in any case, items for the full conference.<sup>470</sup>

The United Nations Monetary and Financial Conference began on 1 July and concluded on 22 July 1944. It was divided into three ‘commissions’. Commission I

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<sup>466</sup> ‘Summary of Instructions to the Australian Representative, International Conference, Proposed International Monetary Fund’, Cabinet Agendum No. 669, 13 June 1944, NAA A2700/XM1, Volume 11.

<sup>467</sup> ‘Supplement to Agendum on International Monetary Conference. Proposal for a United Nations Bank for Reconstruction and Development’, Cabinet Agendum No.669, J.B. Chifley and H.V. Evatt, 10 June 1944, NAA A2700/XM1, Volume 11.

<sup>468</sup> *ibid.*

<sup>469</sup> *ibid.*

<sup>470</sup> See, for example, Melville’s telegrams to Chifley and Evatt, 29 June 1944, NAA M2271/1, 1.

was concerned with the Fund, Commission II with the proposed International Bank and Commission III with 'the task of considering other means of international financial co-operation'. It was to Commission III that Australia's employment resolutions were confined. As well as the three Commissions, the Conference also consisted of a great many formal and informal committees, sub-committees and informal negotiations, causing the small Australian delegation considerable difficulty in representing Australia on everything they felt they should. Melville was later critical of the decision to send so few people, declaring that 'no country can expect to play an effective part at a conference of this kind unless it has a large and strong delegation'.<sup>471</sup> The need for the Australians to ration their efforts meant that they were particularly hamstrung in keeping up with the number of informal negotiations in play. These were 'not part of the formal organisation of the Conference but [were] where some of the most important decisions [were] made'.<sup>472</sup>

Commission I was formally chaired by White and Commission II by Keynes. Given that the latter Commission did not meet until half way through the Conference, this gave Keynes time to represent the United Kingdom on the negotiations over the Fund. Keynes was particularly concerned to fight Britain's case with respect to two issues - the length of the transition period before the rules of the Fund would apply, and the convertibility of sterling.<sup>473</sup> On these he had mixed success, but on all other major issues the British were unable to shift the United States much beyond the Joint Statement. As events were to reveal, this was not so surprising - Roosevelt having instructed the head of the United States delegation, Secretary of the Treasury, Henry Morgenthau, in the following terms:

In formulating a definite proposal for an international monetary fund both you and the other delegates will be expected to adhere to the joint statement of principles of an international monetary fund announced on April 21st, 1944.<sup>474</sup>

Given the above, the Australians also had mixed success in their attempts to have the Fund modified in the ways they sought. On the question of the quota and drawing rights there was some success, with Australia's overall quota being increased from the £A47 million under the Joint Statement to £A62.5 million. The 25 percent limit on annual quota drawings remained 'but a waiver provision has been inserted to meet the needs of countries subject like Australia to conditions of a periodic and exceptional nature'.<sup>475</sup> A kind of victory could also be claimed on the question of the ability of countries to unilaterally vary their exchange rates beyond 10 percent. Under the Fund as drafted at Bretton Woods, countries could vary their exchange rate unilaterally for any amount, but having done so their drawing rights from the Fund would then cease.

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<sup>471</sup> 'Melville to Curtin', 26 August 1944, NAA A 989, 44/735/56/10/i.

<sup>472</sup> *ibid.*

<sup>473</sup> Of particular concern to the British in this regard was the large sterling balances being built up by nations supplying Britain's war effort. Not surprisingly, Keynes and other officials were concerned at the implications for Britain's post-war solvency if sterling was made convertible with such large balances outstanding.

<sup>474</sup> Roosevelt's instructions are cited in 'Supplementary Notes on the Monetary Conference', A.H. Tange, 1 August 1944, NAA CP10/1, Bundle 1, (13).

<sup>475</sup> 'Report on Discussions at United Nations Monetary and Financial Conference held at Bretton Woods, U.S.A. from 1st July to 22nd July, 1944', L.G. Melville, 26 August 1944, NAA A989, 44/735/56/10/i.

The Fund would also continue to have the right to expel a member who took such action when such a move was in clear conflict with its recommendations.

On the question of the ‘purposes and policies’ of the Fund, the Australian delegation had some success in modifying the exhortations of the value of fixed exchange rates but, notwithstanding these changes, Melville concluded in his final report on Bretton Woods that ‘the purposes of the Fund still place too much emphasis on exchange stability and too little on the maintenance of high levels of employment to be altogether satisfactory to Australia’.<sup>476</sup> The attempts to secure an assurance that countries could withdraw from the Fund without prejudice was similarly unsuccessful. Melville reported that, in the wake of Bretton Woods, it now seemed ‘clear that the right of withdrawal from the Fund may be prejudiced by membership of the Fund being made a condition of membership of other international bodies’.<sup>477</sup>

The Australian delegation’s attempt to have an employment agreement concluded concurrently with the international monetary agreements was perhaps the biggest single failure of its advocacy at Bretton Woods. Australia’s proposal, which was almost identical to that put forward at Philadelphia was relegated to Commission III.<sup>478</sup> Here it found strong support from the United Kingdom and New Zealand but, together with ‘a mob of stray hobby horses’ from other nations, it ran into strong opposition from the United States and, to a lesser extent Canada.<sup>479</sup> Both of these regarded the issue as being outside the terms of reference of the Conference, with the United States formally opposing the Australian resolution on the grounds that the idea that domestic policy could become the subject of international concern and assent required ‘more careful study than can be given in a few days available at this Conference’. As such, it was much better considered ‘as part of any subsequent Article VII conversations’.<sup>480</sup>

Melville reported, as did Tange in his own supplement to Melville’s final report, that a number of United States officials had confided that their opposition reflected their belief that such an agreement was not politically possible domestically. Melville was not entirely despondent over the result at Bretton Woods though. An agreement had not been reached, but he believed ‘that after the educational work the Australian representatives have done at the Hot Springs Conference, in the London discussions, at Philadelphia and at Bretton Woods, there are now good prospects of securing widespread support for an employment agreement as part of a programme of international economic co-operation’.<sup>481</sup> The United States would continue to oppose it, but even here an ‘agreement would obtain influential support from sections of the administration and from an important part of the United States public’.<sup>482</sup>

The modifications made to the Fund at Bretton Woods led Melville to conclude that ‘it would, on balance, be to Australia’s advantage to participate in the Fund as now

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<sup>476</sup> *ibid.*

<sup>477</sup> *ibid.*

<sup>478</sup> *ibid.*

<sup>479</sup> ‘Supplementary Notes on the Monetary Conference’, A.H. Tange, 1 August 1944, *op.cit.*

<sup>480</sup> Cited in ‘Report on Discussions at United Nations Monetary and Financial Conference held at Bretton Woods, U.S.A. from 1st July 22nd July, 1944, L.G. Melville’, 26 August 1944, *op.cit.*

<sup>481</sup> *ibid.*

<sup>482</sup> *ibid.*

drafted'.<sup>483</sup> The remaining defects of the Fund, which for Australia's purposes continued to centre on the inadequacy of the quota and drawing rights, as well as the capacity to vary the exchange rate, were all significant, but they had to be judged according to what effect they would have on the ability to maintain full employment. And on this, Melville was reasonably confident. The collapse of employment overseas and the maintenance of employment in Australia via public spending could result in a situation in which the balance of payments came under strain, but the Fund at least allowed for *some* room to manoeuvre. The ability to draw on the Fund, though inadequate, was nonetheless a supplement to other international reserves that, before the war, were the only cover for balance of payments shortfalls. Membership of the Fund did not itself prevent the use of import restrictions and even the exchange rate was not a precluded option. Variations in the exchange rate beyond 10 percent required the Fund's approval on the basis of 'fundamental disequilibrium', but even if the Fund refused this, depreciation could occur provided a country was then willing to forego the use of the Fund's resources. Expulsion from the Fund under such a scenario was considered by Melville to be 'unlikely'. Summing up the case for acceptance, Melville concluded that '[p]rovided we built up international reserves outside the Fund, for use in the event of the Fund denying us the use of our drawing rights, our freedom to follow a policy of maintaining a high level of employment in Australia should...not be *hampered* by membership of the Fund (emphasis added).'<sup>484</sup>

### *The Bank*

Melville also recommended that Australia accept membership of what was now officially the International Bank for Reconstruction and Development. He did not believe that Australia would either be a borrower from, or large lender to, the Bank, but could stand to benefit from the indirect effects of the Bank's activities on world trade. What Melville had in mind in this context was not only the Bank's role in the restoration of old export markets through reconstruction, but also the possibility of new markets through the 'development of backward countries'.<sup>485</sup> For Australia, the latter was important in that it helped to provide the 'necessary conditions for a lasting peace in the Pacific'. More prosaically, it could mean 'the prospect of exports of capital equipment to the Far East and the Netherlands East Indies'.<sup>486</sup>

### *Signature*

The Bretton Woods Conference concluded in some drama for Australia's delegation. This arose because of a controversy over signing the Final Act, something the delegation had been ordered not to do by Cabinet if it had meant any commitment on Australia's part to anything resolved at the Conference. The original United States invitation, of course, had specifically excluded the need for delegations to have 'plenipotentiary powers' but, in any case, what was being asked for in signing the Final Act was not that the delegates recommend the Conference resolutions to their governments, but merely that they certify 'the accuracy of the record'.<sup>487</sup> This

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<sup>483</sup> *ibid.*

<sup>484</sup> *ibid.*

<sup>485</sup> *ibid.*

<sup>486</sup> *ibid.*

<sup>487</sup> *ibid.*



interpretation was conveyed back to Australia by Melville, who also recommended 'on purely technical grounds' that he sign as requested.<sup>488</sup> This, however, met with another fusillade of telegrams from Evatt ordering him not to sign.<sup>489</sup> The resultant confusion led to much hostility from other delegates and a flurry of diplomatic entreaties from Britain and the United States. Eventually Melville received instructions that he could sign the Final Act, so long as he appended his signature with the words 'for purposes of certification'. Melville recorded that this lifted the 'unfavourable atmosphere' slightly, but 'other delegations remained unsympathetic and critical of the Australian attitude'.<sup>490</sup>

This lack of sympathy for Australia's position on the Final Act was partially a function, Melville believed, of widespread misunderstandings generally about what was perceived as Australia's unwillingness to co-operate with other countries on economic matters. Too often, he wrote in his final report on Bretton Woods, other countries perceived the employment approach as being nothing other than a ploy to get around the commitments required to achieve international economic co-operation. He concluded his report on the Bretton Woods Conference with his belief that it was

urgently necessary that Australia should state her general attitude towards international arrangements as soon as possible, on the highest possible plane. And it appears to me that Australia has a suitable opportunity not only to explain her attitude but also to become a spokesman for a positive and constructive policy of international co-operation, which would make the various international proposals now under discussion subsidiary to the general requirement that all nations should commit themselves to maintain high and stable levels of employment...What has been interpreted as a negative approach by Australia to international questions would then appear in its positive aspect, as a constructive attempt to direct international activities towards objectives which the people of all countries wish to attain.<sup>491</sup>

Keynes's final assessment of Australia's role at Bretton Woods was more welcoming, and characteristically patronising. Reporting to London after it was all over, he wrote;

...we have had our final banquet and celebration. The love feast was completed by the two black sheep, the Australians and the Russians [also initially refusing to sign], receiving their telegrams in time. Melville was able to sign the Final Act and the Russians raised their subscription...amidst loud and continued applause, and embraces all round, the erring sheep were received into the fold.<sup>492</sup>

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<sup>488</sup> *ibid.*

<sup>489</sup> See, for example, 'Evatt to Melville', 17 July 1944 and 'Evatt to Dixon', 18 July 1944, NAA A 989, 44/735/56/10/i.

<sup>490</sup> 'Report on Discussions at United Nations Monetary and Financial Conference held at Bretton Woods, U.S.A. from 1st July 22nd July, 1944, L.G. Melville', 26 August 1944, *op.cit.*

Notwithstanding this hostility, history was to prove that Australia's anxiety on the matter of signing was well placed. The draft agreements from Bretton Woods *were* presented to governments on a take-it-or-leave-it basis for signing soon after the Conference, contradicting assurances before it that the absence of ministers made its draft articles non-binding.

<sup>491</sup> *ibid.*

<sup>492</sup> Keynes (1980c), p.112. As it turned out, continuing hostility within sections of the Australian Labor Party to the very concept of the IMF meant that Australia did not join until 1947, and then only after

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the determined advocacy of Chifley in overcoming divisions on the issue which came close to splitting the Party. For more, see Crisp (1965).

## **Chapter Eight**

### **An International Employment Agreement**

Melville's proposal that the employment approach be reconsidered - so that it was not a point to be negotiated in each and every agreement, but a 'general requirement' to which all others would be subsidiary - corresponded to a similar conclusion drawn in Australia. Initially at the volition of the economists, these deliberations over the merits of a 'stand-alone' employment agreement increasingly involved and, like the other efforts, came to be directed by, Evatt and his Department.

The economists' deliberations had begun in June 1944 in the wake of the United Kingdom's acceptance of the compromise draft employment agreement at the talks in London. They took the form of a number of meetings over several months and included Coombs, Copland, John Crawford, R.I. Downing, Giblin, Walker, and Wilson. Melville and Wheeler also participated following their return from Bretton Woods in September.<sup>493</sup> Though dominated by those intimately connected with the Article VII negotiations, the meetings also gave an opportunity for hitherto less prominent voices on the issue to be heard. Upon the importance of an employment agreement, however, there was near unanimity. Copland, for example, asserted the 'first priority' of an employment agreement over 'secondary' issues such as those concerned with monetary and exchange matters.<sup>494</sup> Giblin, the originator of the employment approach though never an active participant in the international negotiations, similarly reasserted that 'any significant achievement in commercial policy will depend very largely on an employment agreement'.<sup>495</sup>

By the conclusion of these meetings, the consensus of the economists was that a stand-alone employment agreement and conference was required. This would be Evatt's directive in any case, but they arrived at this conclusion independently from Evatt's later instructions in September that the economists come up with the framework for a conference to continue the work of Philadelphia.<sup>496</sup> The strength of feeling on this was particularly apparent following Melville's return from Bretton Woods, and his painting of an extremely pessimistic picture of the impact of United States policy. Melville had been impressed by the lack of disruption the war had placed on American industry and, as a result, its enormous productive potential in the post-war period. This potential would mean that its competitive position and ability to export would be much greater than Australian and British economists had imagined. Such a scenario would place upon institutions such as the Fund immense strain unless there existed some constraints against persistent and large creditors. Should the United States adopt policies of full employment, the situation would be greatly

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<sup>493</sup> A full list of the economists included in these discussions, which took place over a series of meetings and in (limited) written correspondence, can be found in 'Hodgson (Secretary, Department of External Affairs) to Copland', 11 August 1944, NAA A989/1, 44/735/58/3, Pt.1

<sup>494</sup> 'Copland to Hodgson', 14 June 1944, NAA A989/1, 44/735/58/3, Pt.1.

<sup>495</sup> 'Giblin to Hodgson', 16 June 1944, NAA A989/1, 44/735/58/3, Pt.1.

<sup>496</sup> Evatt's directions in this regard were conveyed to the economists in a meeting convened by John Burton on 4 September 1944. 'Notes on Economists' Discussion on Employment Policy', R.I. Downing, 5 September 1944, NAA A1066/1, ER 45/2/3/1/1.

relieved, but Melville was likewise pessimistic that such policies would be adopted. He reported that the 'New Deal' was 'unpopular in America and its institutions are being fairly quickly thrown out'.<sup>497</sup> He believed that whatever the colour of the administration in the United States, public works and other expenditure *would* be brought forward to counter a depression, 'but it is doubtful whether that expenditure would be properly planned or sufficiently large to be effective'.<sup>498</sup>

The arbitrary nature of United States policy could be relieved by its adherence to an employment agreement. But, anxious to avoid the way in which such an agreement had been evaded by the simple ploy of declaring its consideration outside the terms of reference of the conferences thus far, Melville pressed 'strongly that the problem should be put formally to an international conference...specially convened for its discussion'.<sup>499</sup> Melville's account of his dealings with the United States also included the warning that he believed the State Department was opposed politically and theoretically to an employment agreement. Nevertheless, the United States' acceptance of the Philadelphia resolutions meant that they were not in a position to refuse an international conference and, like Melville, Coombs thought Australia should 'insist' that such a conference take place.<sup>500</sup> It was agreed in one of the final meetings of the economists that the best way to win the United States over to this approach was to target the United Kingdom, gaining first their support but stating that 'we consider that the matter should be raised immediately', that 'we are preparing a case' and that if there was no alternative, Australia would take the matter up directly.<sup>501</sup>

Tactics aside, the economists' meetings were also concerned with the substance of any employment agreement. From June 1944, Coombs had begun preparing a more substantial set of proposals than those which had been taken to the conferences already held.<sup>502</sup> This set of proposals, which had been earmarked by Evatt for international publication along the lines of the published variants of the Clearing Union and the Stabilisation Fund, went through a number of drafts, the final version of which was completed in January 1945.

The 'Proposal for an International Agreement Concerning Employment Policies' carried through the same basic arguments as pursued by Australia since 1942 but, heeding the lessons of Bretton Woods and other forums, was 'presented in a more sophisticated and internationally acceptable form' (Butlin and Schedvin 1977, p.667). Better integrated with the monetary and other proposals, it differed little in substance from the compromise draft drawn up in London the previous March. Thus while there was to be a binding agreement and an employment organisation to oversee it, the only sanction against a country which failed to maintain 'high' (not full) employment was

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<sup>497</sup> Melville cited in 'Notes on Economists' Discussion on Employment Policy', R.I. Downing, 5 September 1944, *op.cit.*

<sup>498</sup> *ibid.*

<sup>499</sup> *ibid.*

<sup>500</sup> Coombs cited in *ibid.*

<sup>501</sup> 'Meeting of Economists, 4 September 1944', J.W. Burton, 5 September 1944, NAA A989/1, 44/735/58/3, Pt.1.

<sup>502</sup> Coombs was assisted in the drafting of these proposals by Tange.

‘attendance at a conference to discuss means of overcoming their problems’.<sup>503</sup> As in London too, the organisation proposed would consist of a small secretariat, with most statistical and research activities being undertaken by other bodies, particularly the ILO. Nevertheless, the possibility that such an organisation might have some real power was not discounted. There was, for example,

much in the contention that an organisation should be built which...is able to exercise a strong influence on the policies of other international organisations and of member countries. Nations might consider giving the organisation...the duty of issuing reports upon the employment policies being pursued by members and of making recommendations.<sup>504</sup>

The Proposal was much more sympathetic in tone to the push for lower trade barriers than previous Australian overtures had been, declaring for example that the ‘history of the failure of extreme tariffs to provide a cure for unemployment is recent and well known’.<sup>505</sup> In an attempt to answer the charge that all Australia was seeking was an ‘escape clause’ from other obligations, the Proposal suggested that with the cooperation of other bodies such as the Fund, the use of trade barriers and ‘competitive’ currency depreciations ‘should be restricted and controlled, not only by the existence of the currency agreements and commercial policy agreements...but also by the emphasis of the employment agreement itself...and by the continuous influence of the employment organisation’.<sup>506</sup>

But at the same time as it attempted to make conciliatory noises on trade barriers, the Proposal made no concessions to the dominant idea within the United States administration that the reduction of trade barriers, and multilateralism, was in *itself* the solution to world-wide unemployment. It emphasised that ‘international commercial and monetary arrangements cannot *by themselves* solve the domestic problems of unemployment’.<sup>507</sup> There was even the danger that the emphasis on commercial and currency agreements could divert attention from the importance of domestic measures to maintain high employment, without which ‘international agreements would sooner or later cease to function’.<sup>508</sup>

Extending the relevance of the employment approach, and with it the likely acceptance of Australia’s line should it ever come to a vote, the Proposal expanded upon the likely benefits to ‘less advanced countries’. In these countries, employment was less of the central issue than the provision of capital resources. The ‘developed nations’ not only had obligations as the source of this capital but also as the trading partners of recipient countries whose borrowings had to be serviced and eventually repaid. For this to work, ‘a high level of employment and consumption is required in developed countries to provide a demand for the exportable surpluses of the expanding regions’.<sup>509</sup>

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<sup>503</sup> ‘Proposal for an International Agreement Concerning Employment Policies’, 15 January 1945 (final version), NAA A1066/1, ER45/2/3/1/1.

<sup>504</sup> *ibid.*

<sup>505</sup> *ibid.*

<sup>506</sup> *ibid.*

<sup>507</sup> *ibid.*

<sup>508</sup> *ibid.*

<sup>509</sup> *ibid.*

The economists' Proposals and their later meetings were co-ordinated by John Burton, the traditional link between the economists and Evatt. Burton's own enthusiasm for the employment approach and his role at Philadelphia has been noted, but his enthusiasm had been given a new impetus by his reading of William Beveridge's *Full Employment in a Free Society* which had just been published in London. Together with Britain's own 'White Paper on Full Employment', Beveridge's book was to be enormously influential in promoting a version of a Keynesian policy programme in the United Kingdom in the postwar period. Burton's interest in the book was particularly concerned with a section devoted to the international implications of employment policy - a section which was almost identical with the approach taken by the Australians since 1942. Burton wrote a review of the book and sent it to McDougall in Washington.<sup>510</sup>

Following Cabinet's approval, the economists' Proposals duly made their way into a cablegram drafted by Evatt and Burton to be sent to the United Kingdom. This telegram invited the United Kingdom's participation in a joint approach (with New Zealand and Australia) to the United States Government to ask it whether it 'would join in calling an employment conference or at least attend such a conference if called'.<sup>511</sup> As part of the attempt to sell the idea to the United Kingdom, Evatt cited in the telegram the extracts from the British White Paper and, at Burton's suggestion, extracts from Beveridge's book.<sup>512</sup> Evatt proposed that the conference take place in February 1945 and, remarkably, hoped 'that consideration would be given to Canberra for location'.<sup>513</sup>

Evatt's initial telegram met with what Tange described as a 'not over-subtle brush-off'.<sup>514</sup> In fact, the British Government's initial reaction (this time in the form of a Dominions' Office telegram) was consistent with their earlier responses since 1942, and Keynes's correspondence with Coombs in 1943 - that is, the appeal to stay within the parameters of the Article VII talks, whenever these might occur. Within this framework, according to the British reply, progress was more likely to be made than by holding a separate conference. This, coupled with their reminder that a coming Presidential election in the United States made Australia's timing inopportune, led to the counsel 'that it would be wise to defer approach to the Americans for the time being but that special point should be made of raising the matter with them as soon as opportunity arises for discussions under Article VII'.<sup>515</sup>

The British telegram sparked off a minor diplomatic incident, and once more a flurry of correspondence made its way between the Dominions Office and Evatt. One vocal supporter of an Australian hard line was Bruce, who cabled Evatt mid-way through the dispute that however unsatisfactory the Dominions Office reply had been, it was

<sup>510</sup> 'Burton to McDougall', 9 December 1944, NAA A989/1, 44/735/58/7.

<sup>511</sup> 'Evatt to Secretary of State for Dominion Affairs (Lord Cranborne)', 15 September 1944, NAA A989/1, 44/735/58/7.

<sup>512</sup> 'Evatt to Secretary of State for Dominion Affairs (Lord Cranborne)', 5 December 1944, NAA A571/61, 44/643 Pt.2.

<sup>513</sup> *ibid.*

<sup>514</sup> Memorandum by Tange, 25 October 1944, NAA A989/1, 44/735/58/7.

<sup>515</sup> Cablegram, 'Secretary of State for Dominion Affairs (Lord Cranborne) to Evatt', 23 October 1944, NAA A989/1, 44/735/58/7.

considerably more supportive than an earlier unsent draft had been. He advised that while the British Government was in sympathy with the Australian approach, sections of the Dominions Office paid little more than 'lip service' to it and, as such, Australia should 'insist on necessity of the matter being raised with the Americans' as soon as their election was over.<sup>516</sup> In the end Australia prevailed and, just as in the case of the draft employment agreement at the London talks the previous March, the British Government acceded to the Australian Government's wishes. On 22 December 1944 a telegram was despatched from the Dominions Office advising agreement with Australia's suggestion that the Australian, New Zealand and United Kingdom Governments mount a joint approach.<sup>517</sup>

## **8.0: Approach to the United States**

The approach to the United States took place on 29 January 1945 in the form of a delegation from the Australian, New Zealand and British embassies in Washington to the State Department. Australia was represented by Brigden, the United Kingdom similarly by its Economic Adviser at the Embassy, Redvers Opie, while New Zealand was represented by J.S.Reid. All three carried letters from their ambassadors declaring their governments' support for an employment conference and agreement. With both Roosevelt and the new Secretary of State, Edward Stettinus, away at the 'Big Three' talks at Malta and Yalta, the delegation met with William L. Clayton, the newly appointed Assistant Secretary of State for Economic Affairs.<sup>518</sup>

The meeting was not a success. Clayton, hand-picked by Roosevelt and given immense powers over foreign economic policy, personified that view in the Administration that saw in multilateral tariff reductions the panacea for all economic ills. Clayton 'was committed to multilateralism as a general theory', and his appointment in December 1944 heralded the victory for this view over others within the United States bureaucracy (Bennett-Woods 1990, p.207). Clayton did not accept the idea that full employment was a *requirement* for multilateralism and, as such, he rejected the entire basis of the employment approach. At the meeting, he told the delegation that he could not see what a dedicated employment conference could decide upon which was not already being covered by talks on financial and commercial policy. Indeed, such a conference would be less than useful since 'it would be difficult to keep out of an Employment Conference such financial and commercial policies as were to be discussed further'.<sup>519</sup> On this basis it was important that 'the conference on commercial policy should be held first'.<sup>520</sup> An employment conference was both 'unnecessary and might create special difficulties' and he told the delegation that his personal reaction to their proposal was 'not favourable'. This view was backed up by Charles Taft, 'Special Assistant' to Clayton and handpicked

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<sup>516</sup> Cablegram, 'Bruce to Curtin (Department of External Affairs)', 25 October 1944, NAA A989/1, 44/735/58/7.

<sup>517</sup> Cablegram, 'Secretary of State for Dominion Affairs (Lord Cranborne)', 22 December 1944, NAA A1066/1, ER45/2/3/2.

<sup>518</sup> 'Legation in Washington to Department of External Affairs', 30 January 1945, NAA A1066/1, ER45/2/3/2. Brigden's personal report is contained in a separate letter, 'Brigden to Department of External Affairs', 31 January 1945, NAA A1066/1, ER45/2/3/2.

<sup>519</sup> Cablegram, 'Legation in Washington to Department of External Affairs', 30 January 1945, *op.cit.*

<sup>520</sup> *ibid.*

by Roosevelt. Taft was the only other American at the meeting and, like Clayton, saw multilateralism as the 'hope of the world' (Bennett-Woods 1990, p.122).

The disappointment over what seemed like the failure of the approach to Clayton spilled over once more into another minor diplomatic incident as Evatt, suspicious that the United Kingdom remained less than fully committed to the approach, accused the British Government of contriving with its embassy in Washington to ensure that it was made at a low level by 'relatively subordinate officials'.<sup>521</sup> What was required, he told both the Dominions Office and the Australian Legation in Washington (which did not escape blame), was a 'diplomatic approach' to the Secretary of State and the President via the ambassadors.<sup>522</sup> That Australia had not been informed of the latter pair's absence at the time of approach was regarded by Evatt as 'unfortunate'. As a practical measure to correct the situation, Evatt instructed the Australian legation in Washington to advise the State Department that the Australian Government 'did not expect a departmental approach or decision ...but a decision after a *diplomatic* approach to the Secretary of State and the President'.<sup>523</sup> This second approach would be made by the ambassadors themselves, at an opportune moment judged by Canberra.

Both the Dominions Office as well as the Australian Legation in Washington defended themselves against Evatt's charges, implicitly accusing Evatt in turn of being out of touch with both the system of government in the United States and with political events currently in play there.<sup>524</sup> The Legation expressed (reasonable) surprise, for example, that Canberra seemed not to know that Roosevelt and Stettinus would not be in Washington, the Malta and Yalta Conferences having attracted considerable coverage in the press. Brigden, too, reminded Canberra that the division of powers in the United States between the President and Congress meant that negotiating with it was a difficult process in that there was no 'government policy' as Australia understood it.<sup>525</sup> Brigden speculated that Clayton's opposition to an employment conference was partly informed by his own ideology, but also partly because he would have 'in mind present relations between Congress and the Administration'.<sup>526</sup>

A particular problem emerging in the United States with grave implications for an employment conference was the controversies which were rapidly surrounding the 'retiring' Vice-President (and collaborator with McDougall), Henry Wallace. Dropped as Roosevelt's Vice-Presidential candidate in the 1944 elections, Wallace was seeking endorsement as Secretary of Commerce. He had the support of Roosevelt for this post, but not yet of Congress. The problem for Australia, as reported by Brigden, the Australian Ambassador and even McDougall (in Washington for the Interim Commission of the FAO) was that Wallace had 'made employment an important domestic issue' and had come to be identified with a full employment

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<sup>521</sup> Cablegram, 'Commonwealth Government (Evatt) to Secretary of State for Dominion Affairs (Lord Cranborne)', 2 February 1945, NAA A1066, ER45/2/3/2.

<sup>522</sup> *ibid.*

<sup>523</sup> *ibid.*

<sup>524</sup> See, for example, the cablegrams 'Legation in Washington to Evatt', 6 February 1945 and the letter, 'Watt to Hood', 20 February 1945. Both documents are contained in NAA A1066/1, ER45/2/3/2.

<sup>525</sup> 'Brigden to Department of External Affairs', 31 January 1945, *op.cit.*

<sup>526</sup> *ibid.*



policy.<sup>527</sup> The Australian First-Secretary in the Washington Legation, Alan Watt, reported to Canberra that in this context, it would be ‘difficult for the Administration to give an affirmative answer to our representations, at least until the Senate has confirmed Wallace’s appointment’.<sup>528</sup> An announcement by the Administration that they had agreed to an international conference on employment on the other hand, ‘might be used by Administration opponents as an additional reason for not confirming the Wallace nomination and for attacking the Administration’.<sup>529</sup> McDougall confirmed the Wallace troubles in a number of letters to Burton over this period, who seems to have used McDougall as an independent observer of events in Washington. In this context McDougall was important in diffusing the tension between Australia and the United Kingdom over the approach to Clayton. He told Burton that *he* was wrong in claiming (in a previous private letter) that Britain’s role in the matter ‘was something bordering on sabotage’, and stated his own belief that ‘the U.K. has very substantial interests in seeing the United States committed to policies of full employment’.<sup>530</sup>

A second attempt to approach the United States over an employment conference was made in mid-February 1945, this time by the ambassadors - Frederick Eggleston for Australia, Lord Halifax for the United Kingdom and C.A. Berendsen for New Zealand. With Roosevelt and Stettinus still away at Yalta, the ambassadors saw Joseph Grew, the Acting-Secretary of State. Grew was not expert on economic and trade matters but, primed by Clayton, he repeated the line that ‘it might be unwise to deal with employment policy before tying up trade policies’.<sup>531</sup> Grew also pointedly asked Halifax whether his Government was fully supportive of the proposal, to which Halifax replied that they were. Importantly, in what appeared to be some shifting of ground on the issue, Grew told the delegation that ‘a conference on both trade *and* employment might be appropriate’ (emphasis added).<sup>532</sup> Grew told them the United States views on the matter had not ‘crystallised but would be reconsidered in the light of the present discussion and of ...[the delegation’s] oral representations’.<sup>533</sup> Eggleston telegraphed Evatt after the meeting that he thought Grew’s comments marked ‘some advance’ and that the way was ‘left open’.<sup>534</sup>

Watt’s advice to Australia that the United States would take some time to respond to their approach because of the Wallace imbroglio turned out to be correct, and it was not until mid-March that any more was heard from the Administration. In mid-March, however, a letter signed by Stettinus was sent to the Australian, New Zealand and British Governments which declared:

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<sup>527</sup> ‘Watt to Hood’, 20 February 1945, *op.cit.*

<sup>528</sup> *ibid.*

<sup>529</sup> *ibid.*

<sup>530</sup> ‘McDougall to Burton’, 24 February 1945, NAA A1066/1, ER45/2/3/2. McDougall nonetheless told Burton that Australia was right to pursue the employment approach, and included for Burton’s comments a new memorandum of his own on the role of ‘underdeveloped countries’ in the process.

<sup>531</sup> Cablegram, ‘Legation in Washington (Eggleston) to Evatt’, 17 February 1945, NAA A1066/1, ER45/2/3/2.

<sup>532</sup> *ibid.*

<sup>533</sup> *ibid.*

<sup>534</sup> *ibid.*

The Government of the United States fully recognises the urgency of the development by all nations of effective domestic programmes for the attainment of high and stable levels of productive employment if the objective of freedom from want is to be realised. My Government further recognises the desirability of international collaboration for the attainment of full employment and *in agreement with the view of the Australian Government that the employment policy should be considered at an international conference* (emphasis added).<sup>535</sup>

However, there was a hint that this change of heart might be less than complete:

My Government feels however, that the employment problem is inextricably linked with the problems of exchange and trade which have been under consideration by several Governments for some time.

While the maintenance of a sound and stable commercial and financial system may not be possible if serious unemployment exists in any major country, *there can be no sound basis for stability of productive employment at a high level in the various nations if there is not a general agreement to remove excessive barriers and prevent discriminatory practices in the past...*(emphasis added).<sup>536</sup>

Consequently,

...my Government would be pleased to participate at the earliest practicable date in an international conference on trade and employment. The conference would consider the entire problem of post war international trade relations ...[and also] full consideration to the international aspects of the maintaining high and stable levels of productive employment in all countries, and would explore the essential areas of international co-operation with a view to achieving agreement on the methods of the objectives and the procedures of co-ordinated action in this field.<sup>537</sup>

Evatt's reaction to this turn was extremely positive:

I regard the United States answer on the employment conference a great triumph for Australia-New Zealand policy, especially having in mind the strong disinclination of the United States Government to recognise the importance of full employment.<sup>538</sup>

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<sup>535</sup> The letter from Stettinus, which was dated 13 March 1945, was cabled to Australia a few days later. The content of the letter is therefore contained in 'Legation in Washington (Eggleston) to Department of External Affairs', 16 March 1945, NAA A1066/1, ER45/2/3/2.

<sup>536</sup> *ibid.*

<sup>537</sup> *ibid.*

<sup>538</sup> Cablegram, 'Evatt to Hood', 21 March 1945, NAA A3195, 1/9713. Evatt was in Washington at the time, and on his way to the United Nations Conference in San Francisco. A handwritten version of this message can be found in NAA A1066/1, ER45/2/3/2.

Events would proceed such that Australia's 'triumph' was not quite what it seemed but, for the moment, the advocates of the employment approach savoured an unexpected achievement.

### **8.1: The United Nations**

The 'earliest practicable date' for the conference on trade and employment proved to be some time off, but in the meantime there was the United Nations Conference in San Francisco of April - June 1945. This Conference was primarily about the creation of a new global security organisation to replace the League of Nations and, as such, was not originally meant to be a forum in which economic matters would feature. The Draft Charter on the United Nations drawn up at the Dunbarton Oaks talks made scant reference to any economic function of the organisation, referring merely and vaguely in its 'Purposes' that it should aim to 'achieve international cooperation in the solution of international economic, social and other humanitarian problems'.<sup>539</sup>

The pivotal role of Evatt at the San Francisco Conference, particularly in advancing the cause of 'middle powers' such as Australia, is well known.<sup>540</sup> Rather less well known was that the Conference was also quickly identified by Evatt as the forum into which once more Australia's 'foreign economic policy' could be advanced. On his way to the Conference, Evatt drew up a proposal which in essence sought the insertion into the Charter of the employment approach *in toto*. Drawn up as a formal submission by the two economists in the delegation, Wilson and Brigden, the Australians once more sought an agreement on employment policy. In fact, the 'pledge' contained in the submission to the San Francisco Conference was little different from that advanced in London in March 1944 and in subsequent conferences. One minor difference was the nomination of the proposed Economic and Social Council of the United Nations as the body which would undertake much of the data collection, and to which employment levels would be reported (Crisp 1965, pp.5-9).

As had been the experience in the other conferences, the employment approach ran into determined resistance from the United States delegation. Evatt, Burton, Wilson and Brigden were all approached formally and informally by members of the American team and asked to drop the proposal, being assured in any case that a Charter which contained a full employment pledge would not be ratified by the United States Senate.<sup>541</sup> In the negotiations and compromises which followed, one interesting concession agreed to by Australia was the insertion in the full employment pledge of the words 'who seek it' after 'work for all'. As noted by Crisp (1965, p.11), 'a purely verbal and tactical concession to the alleged belief of hardheaded Americans that there were millions of natural-born incorrigible loafers who cleave to the dole of their own free choice'.

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<sup>539</sup> Cited in Crisp (1965), p.6. The campaign to have a full employment agreement inserted into the Articles of the United Nations at San Francisco is described in great detail by Crisp, who had attended the Conference himself as part of the Australian delegation.

<sup>540</sup> See especially Renouf (1983), Dalziel (1967) and Edwards (1983).

<sup>541</sup> This was, of course, a tactic familiar to Australian delegations.

Eventually a compromise was reached, and though significantly watered down from the pledge sought by Australia, the Charter of the United Nations contained the following articles:

Article 55. With a view to the creation of conditions of stability and well-being which are necessary for peaceful and friendly relations among nations based on respect for the principles of equal rights and self-determination of peoples, the Organisation shall promote:

(a) higher standards of living, full employment, and conditions of economic and social progress and development;

(b) solutions of international economic, social, health, and other related problems, international cultural and educational cooperation...

Article 56. All members pledge themselves to take joint and separate action in cooperation with the Organisation for the achievement of the purposes set forth in Article 55.<sup>542</sup>

As pointed out by Butlin and Schedvin (1977, p.670), however, the essential irrelevance for practical policy making of even these modest Articles was contained in another:

Article 2...Nothing contained in the present Charter shall authorise the United nations to intervene in matters which are essentially within the domestic jurisdictions of any state or shall require the Members to submit such matters to settlement under the present Charter...<sup>543</sup>

Australia was successful in San Francisco in elevating to some extent the powers of the Economic and Social Council, including its ability to initiate international conferences on economic and social matters, and prepare reports and submissions to the General Assembly. Later, in 1946, Australia also successfully lobbied to have established an 'Economic and Employment Commission' under the Economic and Social Council. This body was specifically charged with monitoring the employment performance of member countries but, as Tange (1996, p.266) recalled, despite the efforts of the Australian representative on the Commission (Wilson again), the United Nation's activities on employment had 'withered away' by the early 1950s and the Commission itself 'went out of existence'. Even before this had happened, the other international economic institutions, notably the International Monetary Fund and the World Bank, had effectively distanced themselves from the Economic and Social Council and any form of control from the United Nations. Tange accordingly saw the propagation of the employment approach at San Francisco and in later United Nations forums as a grave mistake, and the culmination of the derailment initiated by Evatt at Philadelphia of the concept from an 'instrument of economic management' into a vague 'campaign for social justice' (Tange 1996, p.265). In retrospect, it would be hard to mount a case contrary to Tange's, but Australia's involvement with the United Nations on employment was not totally without result. In 1948, largely because of

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<sup>542</sup> Articles cited in Crisp (1965), p.18.

<sup>543</sup> Article cited in Butlin and Schedvin (1977), p.670.

Australia's representations, the 'Universal Declaration of Human Rights' proclaimed by the General Assembly adopted Article 23 as follows:

Everyone has the right to work, to free choice of employment, to just and favourable conditions of work and to protection against unemployment.<sup>544</sup>

## **8.2: The Beginning and End of the I.T.O**

The United States' plans for a conference on trade and employment finally re-emerged in November 1945 with the international publication of a pamphlet which argued for the creation of an International Trade Organisation (ITO) to operate alongside the other international bodies. The pamphlet, 'Proposals for Consideration by an International Conference on Trade and Employment', was the product of 'a group of experts drawn from all the interested departments and agencies' of the United States Government, but brought together under Clayton and the State Department.<sup>545</sup> The 'Proposals' were 'not regarded as final and perfect', but as the basis for discussion which would lead, it was hoped, to the proposed Conference.<sup>546</sup> The Conference would provide for the final resolution of the 'considerations' of Article VII and, rather optimistically, was slated to meet by the middle of 1946.

The American pamphlet largely separated the issues of trade and employment, with the former occupying by far the largest portion of the document.<sup>547</sup> The trade proposals, though spelled out in greater detail than had hitherto been the case, were familiar enough. The most important principle was that of non-discrimination and the rigid application of 'most-favoured-nation' to all parties. Members of the proposed ITO would enter into arrangements 'for the substantial reduction of tariffs' but, unlike previous United States proposals, an 'across the board' cut in tariffs was no longer the ideal.<sup>548</sup> Rather, reflecting the realities of protectionist sentiment within Congress, the proposal now was for a return to the bilateral bargaining approach traditionally employed by the United States, but with the provision for talks to run parallel with the Conference in which 'many pairs of bilateral negotiations could be carried on simultaneously' (Gardner 1956, p.151). There would be a general elimination of quantitative restrictions on trade, but with qualified exceptions for 'restoration of equilibrium in the balance of payments' - another important departure from principle recognising the realities of United States domestic politics.<sup>549</sup>

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<sup>544</sup> United Nations (1948). The Economic and Employment Commission also produced a report in 1949 on 'National and International Measures for Full Employment', a most thorough and theoretically sophisticated account of the issues. E. R. Walker from Australia was the Chairman of the group of economists who produced the report, which also included J.M. Clark, Arthur Smithies and Nicholas Kaldor (United Nations 1949).

<sup>545</sup> The pamphlet, which was considered by the Department of Post-War reconstruction over December-January 1945, can be found in NAA A1067, ER46/1/2.

<sup>546</sup> Covering letter by Clayton to 'Proposals for Consideration by an International Conference on Trade and Employment', 1 December 1945, *op.cit.*

<sup>547</sup> Proposals concerning employment occupied one page of the 22 page document.

<sup>548</sup> 'Proposals for Consideration by an International Conference on Trade and Employment', 1 November 1945, *op.cit.*

<sup>549</sup> *ibid.*

The United States proposals sought (as always) to confine and ultimately eliminate the imperial preference arrangements between the United Kingdom and the Commonwealth. It recognised in turn, however, the political reality that existing preferences would only come down in conjunction with the reduction in trade barriers more generally. Margins, however, could not be increased and no new preferential arrangements would be allowed. An important exception to non-discrimination was allowed for countries applying restrictions 'in pursuance of action they may take under...the International Monetary Fund Agreement, relating to scarce currencies'.<sup>550</sup>

On the employment side, the American pamphlet recognised that the attainment and then the maintenance 'of approximately full employment by the major industrial and trading nations' was 'essential to the expansion of international trade on which the full prosperity of these and other nations depends'.<sup>551</sup> As such, it was proposed that each signatory country to the ITO should undertake to 'take action designed to achieve and maintain full employment within its own jurisdiction, through measures appropriate to its political and economic institutions'.<sup>552</sup> Countries would also make arrangements for the 'collection, analysis, and exchange of information on employment problems, trends and policies'.<sup>553</sup> The American proposal did not envisage any role here for the ITO (which was to be purely concerned with trade) but the process could be carried out by the Economic and Social Council of the UN. This Council would also be the body which would 'hold special conferences in case of threat of widespread unemployment'.<sup>554</sup>

All of this sounded very similar to what Australia had been advocating since 1942 but, as with the letter from Stettinus which first opened the possibility of American involvement in a trade and employment conference, any change to American policy was more apparent than real. Signatory nations to the ITO, for example, would not be permitted to maintain their own employment levels through measures which could increase unemployment in other countries 'or which are incompatible with international undertakings designed to promote an expanding volume of international trade and investment in accordance with comparative efficiencies of production'.<sup>555</sup> Even more important in exposing the theoretical underpinnings of the American proposal, though, was its statement that acceptance of the ITO would imply a recognition that measures to reduce restrictions on trade would '*contribute substantially to the maintenance of productive employment*' (emphasis added).<sup>556</sup> It was, in short, simply a restatement of the 'multilateral' position: trade liberalisation was the key to global employment, and not the other way round.

The State Department's pamphlet was reviewed in Australia by the Department of Post War Reconstruction (principally by Coombs), and passed to a Cabinet Sub-Committee comprising the Ministers for Post War Reconstruction (now J.J. Dedman), Trade and Customs (R.V. Keane) and Commerce and Agriculture (W.J. Scully). This Sub-Committee, which had been appointed in December 1945 to instruct ministers on

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<sup>550</sup> *ibid.*

<sup>551</sup> *ibid.*

<sup>552</sup> *ibid.*

<sup>553</sup> *ibid.*

<sup>554</sup> *ibid.*

<sup>555</sup> *ibid.*

<sup>556</sup> *ibid.*

how to respond to the Conference proposal, submitted its findings to the Full Cabinet in January 1946.<sup>557</sup>

These were broadly sympathetic to the American proposals. In something of a movement from the consideration of *principles* which had occupied the consideration of previous plans, the Submission was notable for its sensitivity to the likely political and economic realities of the postwar world. Australian trade was identified as being 'multilateral' in the sense that Australian trade with most countries was not in balance, even if it approximated this in aggregate. As such, Australia stood to gain from the 'limitation of constraints on multilateral trade', especially for commodities, such as wool and wheat, for which there was a clear comparative advantage.<sup>558</sup>

Of course, all of this was dependent upon that proviso for which Australia had sought assurances all along - that the level of international demand remained satisfactory. The problems with the American proposals emerged when this was not the case, and in these circumstances, the Submission informed Cabinet that Australia *could* be prevented from using measures to defend domestic employment.

The employment side of the American proposal needed 'strengthening' if it was to meet Australia's position, but the Submission noted with satisfaction that the proposals nonetheless showed 'a considerable advance towards the Australian view that the volume of world trade is largely dependent on the domestic economic conditions in the participating countries'.<sup>559</sup> Nevertheless, modifications would need to be made at the foreshadowed Conference, since the American proposal contained a number of significant 'defects'. Chief amongst these was the assertion that the removal of trade barriers would, in itself, create employment. This was central to the United States' position as noted but, as the Submission recognised, 'a disproportionate expansion of exports by a country such as [the] U.S.A. might conceivably bring about a net reduction of employment in the world as a whole' (emphasis in original).<sup>560</sup> Some other 'defects' noted by the submission included the separation of employment from trade within the proposed structure of the ITO, and the lack of certainty surrounding the use of protectionist devices to maintain domestic employment in the face of world depression (these seemed outlawed, but the possible use of quotas for balance of payments purposes seemed to allow them). The provision for the 'general sponsorship' of efforts to coordinate employment policies by the Economic and Social Council also could not, the Submission concluded, 'be regarded as satisfactory'.<sup>561</sup>

The conclusions and recommendations of the submission were approved by the Full Cabinet, with minor revisions, on 18 January 1946. These recommended that Australia 'take an active part' in the forthcoming trade and employment conference and attempt to derive an outcome from it acceptable to Australia. In order to bring this about, however, the Australian delegation to the Conference should push for amendments which would ensure;

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<sup>557</sup> 'United States Trade and Employment Proposals, Full Cabinet Submission by Cabinet Sub-Committee on Trade and Employment', 11 January 1946, NAA A1976/34/1, Box 1.

<sup>558</sup> *ibid.*

<sup>559</sup> *ibid.*

<sup>560</sup> *ibid.*

<sup>561</sup> *ibid.*

- (a) that international collaboration is directed to maintaining satisfactory economic conditions throughout the world, particularly to promote full employment in the major industrial countries in the world;
- (b) that the operation of the system actively promotes the development of new forms of production and higher levels of productivity in relatively under-developed countries;
- (c) that the agreement permits the use of defensive measures in economic emergencies.<sup>562</sup>

Though full Cabinet approval would be required before any agreements were entered into, Cabinet recommended that provided an 'agreement satisfactory to Cabinet is reached in negotiations, Australia is prepared to join the International Trade Organisation'.<sup>563</sup>

### *Preparatory Committee, London.*

In October 1946, a Preparatory Committee of nineteen countries gathered in London to prepare a Charter for the ITO. Australia was included in this number, represented by a delegation led by Coombs. Preceded by a meeting between Commonwealth countries at which Australia received strong support for the line approved by Cabinet, the Preparatory Committee discussions used as their starting point a Draft Charter, which in style and substance was almost identical to the pamphlet issued by the State Department in November 1945.<sup>564</sup> This draft was much amended in London, not least through the efforts of the Australian delegation. In a report back to Dedman they recounted that 'the Australian Delegation left with the impression that it counted for something and that should I.T.O. be established we should be able to influence its proceedings markedly'.<sup>565</sup>

The confidence of the Australian delegation was a function of the success that had been achieved in London in strengthening the links between employment and trade in the Draft Charter. In this it must be noted, however, that the Australians were greatly aided by the strong advocacy on this matter from the United Kingdom.<sup>566</sup> The United Kingdom was represented in much of the employment discussions by James Meade, who (unbeknownst to the Australians) had pushed the links between trade and employment during preliminary commercial policy negotiations in the United States in 1943, but his advocacy here was little short of Australia's position. The United Kingdom delegation even tabled a memorandum on 'International Employment

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<sup>562</sup> *ibid.*

<sup>563</sup> Cabinet's approval of the Sub-Committee's submission is cited in editorial comments by Hudson and Way in Department of Foreign Affairs and Trade (1991a), p.44.

<sup>564</sup> This 'Suggested Draft of a Charter for an International Trade Organisation of the United Nations' can be found in NAA A1976/34/1, Box 1.

<sup>565</sup> 'Memorandum for the Minister, Trade and Employment Conference, Meeting of Preparatory Committee of Economic and Social Council, London, 1946', 14 January 1946, NAA A1976/34/1, Box 1.

<sup>566</sup> The extent to which the United Kingdom was championing causes accepted only after Australia's representations must be borne in mind. It was also the case that for almost all the positions taken by the United Kingdom, Australia's position went even further. This issue is raised by Gardner (1956), pp.273-277.



Policy’ which contained a rebuttal to the philosophy underlying the American approach that was virtually identical to that of Australia’s:

The fundamental advantage of more liberal international trading conditions is not so much that it will give a greater volume of employment all round, but that it will raise output per head all round by allowing each country to concentrate more on the production of those goods and services which it is relatively most fitted to produce...We must not get into the position in which it is assumed that, if trading conditions can be liberalised, employment will thereby automatically be maintained. The maintenance of employment, on which all our hopes for a permanent liberalisation of trading conditions must ultimately rest, requires separate and positive action.<sup>567</sup>

In the end, most of the amendments sought in the Charter by Australia and the United Kingdom on employment were achieved. Article 3 of the London Draft committed members of the ITO to the recognition that ‘rising effective demand...is a *condition* for the expansion of international trade and...for the realization of the purposes of the organization’ (emphasis added).<sup>568</sup> Article 7 went even further, declaring the responsibility of persistent creditor nations in prolonging the balance of payments difficulties of other countries and their duty therefore to ‘make their full contribution to action designed to correct the maladjustment’.<sup>569</sup> Article 26 of the Charter clarified the role of quantitative restrictions for balance of payments purposes. These were allowed, especially when used for carrying out ‘domestic employment reconstruction development or social policies’, but members had to refer such actions to the ITO for approval prior to *or after* their application.<sup>570</sup> Even here, the ITO could not refuse the use of quantitative restrictions which were used for the protection of employment, development, reconstruction or social policies.<sup>571</sup>

Finally, Australia and the United Kingdom together successfully argued for a greater emphasis on possible international action to maintain employment. Though it would all still be coordinated by the Economic and Social Council, Article 9 of the London Charter now extended international cooperation beyond the collection of statistics and the exchange of information, to possible ‘concerted action on the part of governments and inter-governmental organisations in the field of employment policies’.<sup>572</sup>

### *Broadening Australia’s Approach*

In February 1947, Coombs wrote a long memorandum to Prime Minister Chifley in which he put down his impressions, in the light of the London discussions, of the international situation faced by Australia and the likely ‘basic economic issues’ which he believed should ‘vitally affect’ the Government’s judgement on policy.<sup>573</sup> The

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<sup>567</sup> ‘Memorandum by the United Kingdom Delegation on International Employment Policy’, cited from Gardner (1956), p.274.

<sup>568</sup> The London draft ‘Charter of the International Trade Organisation of the United Nations’ is cited from Australia, Parliament (1947).

<sup>569</sup> *ibid.*

<sup>570</sup> *ibid.*

<sup>571</sup> *ibid.*

<sup>572</sup> *ibid.*

<sup>573</sup> Coombs to Chifley, ‘International Economic Policy’, 11 February 1947, NAA A1976/34/1, Box 1.

memorandum was extraordinarily broad in its scope and cognisant, like only a few memoranda before it had been, of the political economy of the postwar world. The employment approach remained central, but it was now joined by considerations which it would not have been possible to appreciate when Australia first adopted this stance in response to Article VII.

Just as Melville had done following Bretton Woods, Coombs came away from London profoundly impressed by the dominance of the United States in the world economy. As a proportion of its internal economy the United States' purchases from the rest of the world were relatively small, but in absolute terms they were both extremely large and, more importantly, fluctuated widely.<sup>574</sup> This assessment was not new, but Coombs's interpretation of what this should mean for Australia was. Up until now the dominance of the United States had justified the employment approach itself, since in the end it was about attempting to ensure that the United States would not be a deflationary influence on the world economy. Coombs's concern was still to advance the employment approach, for he believed its reasoning remained valid, but it was also to ensure that the United States continued to participate in the kinds of international economic collaboration he had just witnessed. In this context, '[o]ne of the main reasons' for Australia to participate in such collaboration was to help 'keep the United States in the international field', enabling countries such as Australia to concentrate the attention of the United States 'on her international responsibilities'.<sup>575</sup>

A similar reason for Australia's on-going collaboration existed with regard to the United Kingdom. The United Kingdom faced 'a desperate economic situation' which would quickly become 'impossible' in the absence of a 'a very great expansion of world trade'.<sup>576</sup> For Australia this held critical implications. The United Kingdom remained Australia's most important market, a situation that had intensified during the war. Australia's own hopes for its export industries could not afford to rely on this market in the absence of a substantial recovery of its purchasing power. From this, Coombs believed that two conclusions for Australia followed:

- (i) We should do all in our power to maintain the prosperity in the international purchasing power of the United Kingdom. United Kingdom experts believe that their best prospects lie in an international system based upon the maintenance of full employment in major countries combined with a general reduction in trade barriers, in particular the American tariff, together with support of international financial organisations designed to provide short-term assistance in balance of payments difficulties and to promote long-term development in under-developed countries. In brief, *participation in the general programme of international economic collaboration sponsored by the United Nations and including the I.T.O. and Bretton Woods proposals.* (emphasis in original)<sup>577</sup>

Such was the importance of the United Kingdom market to Australia that Coombs believed that there was even 'a strong case for supporting a programme of

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<sup>574</sup> *ibid.*

<sup>575</sup> *ibid.*

<sup>576</sup> *ibid.*

<sup>577</sup> *ibid.*

international economic collaboration *if only because the United Kingdom itself believes that in it lies the United Kingdom's best chance of maintaining her prosperity*' (emphasis added).<sup>578</sup> On the other hand, his second conclusion was that:

(ii) We should plan consciously to reduce our dependence on the United Kingdom market...<sup>579</sup>

For the moment, the market of the United States offered the best alternative, but, in the longer term, Australia's participation in aiding the development of currently 'under-developed' countries, particularly in Asia, offered the best prospects. Coombs told Chifley that 'the tide of nationalism is running strongly in India, China and other Asiatic countries, in Syria, Lebanon and other Arab countries, the Middle East, in Malaya, Indonesia and in Brazil, Chile and other South American countries'.<sup>580</sup> These 'nationalisms' were political, but they were also economic, and although many could be of *traditional* concern to Australia politically, Coombs believed that it would be

unwise for us to allow these potential differences to lead us to oppose in any way the legitimate economic aspirations of these peoples. On the contrary, for political as well as economic reasons it would be wise for Australia to promote rather than to restrain them. Indeed, I believe that Australia should make a conscious attempt to identify herself with these developments.<sup>581</sup>

### *Geneva and Havana*

The Preparatory Committee of the ITO met in Second Session in Geneva in April 1947. In order, however, to 'take early concrete measures' to promote the objectives of the ITO, the Committee sponsored negotiations on tariffs and preferences to run concurrently with the on-going discussions over the Draft Charter.<sup>582</sup> These tariff negotiations were the realisation of the simultaneous bilateral bargaining process favoured by the United States which, because of the principle of 'most-favoured-nation', meant that they led to a *multilateral* reduction in trade barriers. The tariff negotiations, which were to be embodied in the form of the General Agreement on Tariffs and Trade (GATT), overshadowed much else at Geneva and were not completed until October 1947.

Australia's delegation to Geneva was not led by Coombs, but by John Dedman, the Minister for Post War Reconstruction.<sup>583</sup> The increasing role of the politicians in the

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<sup>578</sup> *ibid.*

<sup>579</sup> *ibid.*

<sup>580</sup> *ibid.*

<sup>581</sup> *ibid.*

<sup>582</sup> 'Statement by the Prime Minister, Trade and Employment Conference', Press Release, 17 January 1947, NAA A1976/34/1, Box 2.

<sup>583</sup> Notwithstanding this, according to Dedman the 'prevalent opinion' at the Conference was 'that Dr. Coombs was the outstanding personality at the Conference' ('International Trade Organisation and General Agreement on Tariffs and Trade', speech by the Minister for Post War Reconstruction, J.J. Dedman, 3 March 1948, NAA A1976/34/1, Box 2). In an interview with this author on 2 October 1992, Sir Arthur Tange (who was also a member of the delegation) affirmed Dedman's assessment and added that it was equally true at Havana.

*details* of international economic negotiations had accelerated since the death of Curtin and the accession to the Prime Ministership of Chifley. Much more interested in economic matters than his predecessor, it was often Chifley himself who was the most intimately involved minister. Of course, with the war over, ministers now had much more time to devote to such matters. Interestingly, the role of international economic negotiations in domestic ‘politics’ had also become elevated for the same reasons. Throughout 1946 and beyond, Government Ministers were attacked by the opposition parties for the concessions they were offering in international forums and, not least, for the expenses incurred in travelling to them.<sup>584</sup>

The employment and other ‘macroeconomic’ Articles of the Draft Charter survived Geneva mostly intact, whereupon the negotiations moved, finally, to the United Nations Conference on Trade and Employment, held in Havana, Cuba, from November 1947 to March 1948.<sup>585</sup> Though the conflict between the United Kingdom and the United States over imperial preferences once more flared, compromises acceptable to the Australian delegation (once more including Coombs and led by Dedman) were reached before the end of the Conference.<sup>586</sup> In 1948 the Australian Government successfully introduced the International Trade Organisation Act, which authorised the Government to ratify both the Charter of the ITO agreed at Havana and the GATT. The GATT was already being applied provisionally by Australia and most countries present at Havana, but formal ratification of the ITO would not, in the Australian legislation, take place until the Governments of the United Kingdom and the United States had done so. In this Australia was not alone and, apart from Liberia, no country ratified the ITO Charter before its consideration by the United States Congress.<sup>587</sup>

Guided by Clayton, the Truman Administration accepted the ITO Charter and submitted it to Congress in early 1949. It did not reach a vote in 1949, however, and it was not until 1950 that Congress began to hold hearings on the matter.<sup>588</sup> By 1950, however, events had begun to move rapidly against the entire underlying philosophy from which were created international institutions such as the ITO. Protectionist sentiment in the United States was rising, particularly in relation to agriculture, but also within the context of a ‘general disenchantment with the Administration’s major war-time assumptions’ (Gardner 1956, p.373). The ability to sell multilateralism as the engine for world peace, for example, seemed less relevant with the advent of the ‘Cold War’ with the Soviet Union - a war which had become ‘hot’ with the opening of hostilities in Korea in 1950. The confrontation with the Soviet Union took the focus away from ‘international’ institutions and their possibilities (Gardner 1956, pp.369-380).

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<sup>584</sup> See, for example, the instances cited in ‘International Trade Organisation and General Agreement on Tariffs and Trade’, speech by the Minister for Post War Reconstruction, J.J. Dedman, 3 March 1948, NAA A1976/34/1, Box 2.

<sup>585</sup> Australia, Parliament (1948).

<sup>586</sup> *ibid.*

<sup>587</sup> ‘Notes on Australia’s Position in Relation to the General Agreement on Tariffs and Trade and the Havana Charter for an International Trade Organisation’, undated memorandum, NAA A1976/34/1, Box 1.

<sup>588</sup> *ibid.*

Just as countless United States delegations had warned, American business groups also balked at many of the provisions of the international institutions, not least those which related to the full employment obligations contained in the Charter of the ITO. Something akin to hysteria seemed to pervade the (many) commentaries of groups which thought they had an interest. Representative of these was the 'National Foreign Trade Council' which declared that the employment provisions of the Charter 'would operate inexorably to transform the free enterprise system of this country into a system of planned economy, with consequent initiative-destroying regimentation, reduction in productive output and standards of living, and threat to the free institutions and liberties of the American people'.<sup>589</sup> By late 1950, the Truman Administration had quietly given up on the ITO, and on 6 December issued a press release:

[T]he interested agencies have recommended, and the President has agreed, that, *while the proposed Charter for an International Trade Organization should not be resubmitted to the Congress*, Congress be asked to consider legislation which will make American participation in the General Agreement [GATT] more effective...(emphasis in original).<sup>590</sup>

The GATT was to be 'provisionally' applied by Australia, the United States and all the other Havana signatories for the next forty years. The ITO, however, was no more.

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<sup>589</sup> Quote cited from Gardner (1956, p.376), which provides a good survey of this commentary.

<sup>590</sup> Cited from Gardner (1956), p.380.

## **Chapter Nine**

### **The Employment Approach Reconsidered**

#### **9.0: Theoretical Coherence**

Gottfried von Harberler opened his monumental *Theory of International Trade* with the observation that '[t]he only really systematic theory of international trade we possess is the so-called classical theory' (Harberler 1936, p.3).<sup>591</sup> Largely the product of Smith, Ricardo and Mill, the classical theory of trade was, in Harberler's analysis, little more than a discrete application of what he referred to as a 'general economic theory' - comprising the theory of marginal utility on the one hand, and the propositions of price theory ('the laws of supply and demand') on the other (Harberler 1936, p.8). Simply aggregated, these propositions made for the characteristic features of the classical trade story that Harberler recounted as the doctrine of comparative costs and accompanying it, the operation of the 'gold standard'. The former was the motive behind trade and the latter the mechanism through which 'prices, exchange rates and money flows...[linked] together the monetary systems of different countries and ensure[d] the automatic adjustment of the balance of payments' (Harberler 1936, p.3). Harberler acknowledged that classical trade theory had its critics, particularly in his native Germany, but these had 'not succeeded in substituting for it anything that deserves to be called a new theory of international trade' (Harberler 1936, p.3).

An implicit assumption of classical trade theory was initial full employment - both within each country and hence in the global trading system as a whole. Full employment was then maintained at all times in the presence of exogenous shocks by the operation of the gold standard and the other mechanisms of the classical story noted above. If, for example, a country suddenly experienced a reduced demand for its exports this would, *ceteris paribus*, lead to deterioration in its balance of payments position. Under the 'rules' of the gold standard, and assuming for simplicity that the country did not possess any external assets or borrow from abroad, this would cause an outflow of gold from the deficit country to the countries enjoying a surplus with it. In its strictest form, the quantity of gold possessed by a country was directly related to the quantity of money in circulation. In fact, the assumption did not need to be as strict as this, for as long as the banking system's ability to create credit was somehow linked to gold, then the result of the outflow would be to reduce the money supply of the country in question. This, given a fully employed economy and including, as the classical story did, the most basic form of the 'quantity theory of money', would result in a reduction in the general price level. With nominal wages flexible to ensure full employment this would in turn mean that the prices of the exports of the deficit

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<sup>591</sup> More correctly, of course, this was *neo*-classical theory that Harberler had in mind. In the inter-war years Harberler's was the most comprehensive rendering of the orthodox free trade approach.

country would similarly fall. With the deficit country's trading partners similarly fully employed and 'inflating' through their imports of gold, the result was that the exports of the deficit country would increase. On the import side, the reduction in nominal income from the initial export disturbance would reduce the volume of imports. This process of adjustment would continue in both the deficit and surplus countries until the trade imbalances were removed. At this point, gold would flow no longer and (full employment) equilibrium would once more prevail.<sup>592</sup>

Numerous 'imperfections' in the real world meant that the classical story of international trade was never seen as representative of real world conditions, even in the nineteenth century. But there was equally no doubt that Harberler's declaration of its dominance (in the English-speaking world especially) was entirely justified. Even in Australia, where the pragmatism of nation-building outweighed the injunctions of theory in the advocacy of economists, these same economists nevertheless carried with them what they believed to be the fundamental truths of the classical story until well into the 1930s. The Brigden Report, for example, an almost archetypal statement of trade in the cause of nation-building, contained an appendix titled 'The Principles of International Trade' which both defended protectionism in practice, but noted (like von Harberler) that the

simple principles of international trade would be more easily understood if they were thought of as principles which apply to individuals engaged in personal trading. ...the complexities which seem to give them a different character are due to distance, to differences in languages and currencies, and to the fact that international trade has to pass over national boundaries...<sup>593</sup>

That the classical model did not fit the 'facts' of the world was not a barrier to the loyalty to which most economists adhered to its message. Indeed, as Harrod (1938, p.112) noted, the existence of price and wage rigidities and the unwillingness of countries to play by the 'rules' of the gold standard only added to the ardour of its adherents, since all of these could 'explain why the theory of the balance...[had] not been precisely fulfilled'. As has been noted throughout this study, the great majority of economists throughout the inter-war years were unable to escape the mindset of comparative full employment equilibrium states and, to this end, were mostly concerned with identifying deviations from the theoretical ideal and thereafter to exhort countries to eliminate them.<sup>594</sup>

The employment approach explicitly rejected the full employment assumption of the classical model, and with it the theoretical underpinnings behind the claims that multilateralism on its own would act as a self-equilibrating mechanism in the international economy.<sup>595</sup> Take, for example, the case most feared by the Australians -

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<sup>592</sup> There are, of course, a myriad of sources detailing the workings of the 'classical' model, but a particularly worthy exposition is contained in Harrod (1938).

<sup>593</sup> Brigden *et al.* (1929), p.214.

<sup>594</sup> Such exhortations were made regularly whenever economists were in a position to comment upon the state of international economic relations, and exemplified by the economists employed at the League of Nations (de Marchi 1991).

<sup>595</sup> The United States proposals were never about reinstalling a new gold standard, but their arguments nevertheless had their intellectual base in the classical story. As it turned out, the monetary structure created at Bretton Woods, together with what the United States had *initially* proposed in the way of

the failure of a large country (though the principle would be the same whatever the size of the country) to maintain full employment.<sup>596</sup> According to the classical story, such a scenario, though never an object of analysis under its assumptions, would be corrected as a consequence of the balance of payments surplus in the depressed country, which would be a direct result of its slump in domestic income. The gold flows which would be induced by this surplus would increase the money supply of the depressed country and, according to the quantity theory, increase nominal income (via a reduction in the bank rate). The difference now, though, was that this increase in nominal income would also include an increase in *real income*, since in the depressed country the assumption that only prices would respond to changes in the money stock no longer held. The end result of the application of the classical model to this scenario, with only the assumption of *initial* full employment removed, was that full employment was restored anyway, with the exogenous imposition of unemployment being automatically rectified by the resultant surplus in the balance of payments.

Unfortunately for the classical story, however, this process was flawed. In the classical model the depressed country enjoyed its balance of payments surplus via an income effect (the reduction in imports as a consequence of unemployment) upon the traded goods sector. But all of this depended on the conditions of the classical story remaining valid *everywhere* else. In the story above, the rest of the world had balance of payments deficits with the depressed country and, as a result, lost gold to it. This in turn, caused a contraction in their money stocks, a rise in bank rates and, assuming all were fully employed to begin with, a decline in prices. With price and wage flexibility, the balance of payments of the rest of the world was restored in turn by the increased demand for their exports via this price effect. What was missing from the classical analysis, however, was a consideration of any income effects upon these exports. With the depressed country initially at less than full employment (the reason, after all, for its surplus) what was the source of the effective demand for the exports of the deficit countries? If it was the depressed country, then the reason for its own recovery via a balance of payments surplus would be removed, and once more unemployment would prevail. At the same time, however, the effective demand could not come from anywhere else. All other countries had experienced a deflationary shock and each required an improvement in their own balance of payments if internal and external equilibrium was to be restored. All would depend upon the relative price and *income* elasticities of the exports of both the depressed economy and the rest of the world. Thomas Balogh, writing at the same time as the Australians were advancing their thesis, noted as follows:

The effects on the demand for any one country's produce of a fall in price are highly conjectural. They will depend on the reactions of competitors in other countries and also on the state of expectations in each of the countries which...are inter-connected. *All countries may well sink and rise together without their international balance, in distinction to the volume of total trade, altering in a significant manner* (Balogh 1944, p.139, emphasis added).

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'multilateralism' were, though there were many safeguards, not all that removed from a gold standard framework in any case.

<sup>596</sup> This is not the only way one could go about demonstrating the centrality of the full employment *assumption* for the free trade story. It has, however, the virtue of being the theoretical apparatus the Australian economists were pitched against. A fixed exchange rate story is therefore chosen because it was the regime on offer, but the story holds regardless of the exchange rate mechanism.



Within the classical model there existed, in short, the possibility that in the absence of the assumption of full employment no automatic mechanism existed for restoring balance of payments equilibrium in response to an exogenous deflationary shock. Rather, in the attempts to restore balance, the classical model posited that countries were required to respond via further deflation. But since this would not assuredly work, still further deflation had to follow. There was no reason to suppose that this situation would not continue *ad infinitum*, and the only assured phenomenon was the creation of a global deflationary spiral.

It is important to note that at no stage in the questioning of the self-equilibrating nature of the classical model above, was there any reliance placed upon the ‘imperfections’ of the real world which were of such concern to the pre-*General Theory* economists. Each of the actors in the drama were not assumed to be anything other than the individual maximising agents identified by von Harberler as those of ‘general economic theory’ (Harberler 1936, p.8). They were ‘national’ agents, but certainly they were not protective nation states with conscious policy ends, nor were they the aggregations of anything other than entirely frictionless internal markets. In this context then, the analysis above was analogous to the behaviour of economic agents in the closed economy of the *General Theory*, in which the phenomenon of balance of payments surpluses arising in less than fully-employed countries could be considered as ultimately analogous to the ‘paradox of thrift’. The overall story was one in which it was effective demand, rather than prices, which determined income and equilibrium both in individual countries and globally.

If, however, ‘imperfections’ *were* allowed into the story, the scenario painted above only worsened. The deflationary spiral would remain, but to this would be added the *certainty* that changes in quantities and employment, rather than prices and wages (if these were no longer supposed to be perfectly flexible), would be the *primary* avenues of adjustment. In the situation above, for example, the initial deflationary shock from the unemployed country to the rest of the world would produce not just a change in the terms of trade, but immediate unemployment in the rest of the world. The depression, in short, would automatically spread. Countries thus affected could counter this external deflation by internal measures designed to expand effective demand, but these would also exacerbate the balance of payments difficulties. Of course, all of this pointed in the direction of measures to protect the domestic economy from external deflation, and allow it to pursue internal policies which were, at least to a degree, free from the constraints of the external sector. These measures, which could operate via prices (as in the form of tariffs, subsidies, competitive devaluations and so on) or more directly (quotas, reciprocal trade agreements, licensing, bulk purchase and the like) could also be used to enable countries to maintain domestic demand and employment via a positive external balance. This occurred at the expense of other countries in the form of the ‘beggar-my-neighbour’ policies which had destroyed the global trading and financial system in the inter-war years.

### *International Lending*

The existence of international lending was a phenomenon which, in the classical framework, permitted countries to maintain trade imbalances but allowed for global equilibrium to prevail at the same time. The country which enjoyed a trade surplus, but which matched this surplus with an equivalent amount of lending, would impose no deflationary force on any other. Moreover, so long as it was of a long term and productive nature, international lending provided the prospect for an increasing rate of growth of the world economy as a whole. In the frictionless world of the classical model, international lending would continue for as long as capital returns (net of risk) were differentiated geographically and would cease only when factors were allocated in such a way that growth rates for individual nations converged. To re-use the analogy with the *General Theory*, international lending was to balance of payments surpluses what investment was *meant* to be to saving if internal equilibrium was to be achieved.

Unfortunately, again, for the classical story, international lending did not provide an escape from the above critique. This was because full employment was also a requisite assumption for the conclusions regarding international lending. That this is so can be seen when the issue of repayment is considered. Repayment requires the lending country, when in receipt of loan repayments, to be in trade deficit. This was necessary for it to maintain overall balance of payments equilibrium, and for it to be a net supplier of its own currency. This, in turn, implied that the country enjoyed a level of domestic demand sufficient not just to maintain full employment but, indeed, at a level beyond that.

The issue of international lending, and its inability to provide for international balance of payments equilibrium *in the absence of full employment*, was an issue which had exercised Michal Kalecki, who (like Balogh) wrote a number of articles on the subject around the time that Australia's efforts were reaching their apogee.<sup>597</sup> Kalecki, too, propounded the idea that international lending would be a force for equilibrium only if full employment was maintained in the creditor countries, but he offered in this context an explanation of why this had to be so which focussed much more on dynamics and on expectations in the lending country than the account above. According to Kalecki, the volume of international lending was, in the absence of full employment, not likely to be at a level necessary to provide for 'workable multilateralism' (Kalecki 1946, p.415). Its volume, rather, was 'limited by anticipation, on the part both of the lender and of the borrower, of future difficulties arising in connection with interest and amortization payments...' (Kalecki 1946, p.415). This anticipation would vary according to the level of employment in creditor countries since this would also determine the capacity of the borrower to repay. It would also vary according to the degree of *stability* of employment in creditor countries, a fact which Kalecki concluded meant that if international lending was to

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<sup>597</sup> Kalecki's initial work in this area came in a special issue of the Oxford Institute of Statistics Bulletin published in August 1943. The special issue was devoted to an analysis of the respective virtues of the Clearing Union and Stabilisation Fund proposals. Kalecki, with E.F. Schumacher, wrote a paper, *International Clearing and Long-Term Lending*, in which they argued for an international investment body to be attached to the Clearing Union. Kalecki continued his arguments in his 1946 *Multilateralism and Full Employment* which was first published in the Canadian Journal of Economics and Political Science. The paper is reproduced in Osiatynski (1990). Balogh (1944) draws heavily on Kalecki and Schumacher's 1943 paper for his section devoted to international lending.

be an equilibrating force it would, though this was hardly likely, have to ‘vary counter-cyclically’ (Kalecki 1946, p.415).<sup>598</sup>

### *A Body of Theory*

Keynes’s *General Theory* was concerned for the most part with the analysis of a closed economy but, as the above has indicated, its central insights were adaptable to the open system. As such they were used by the Australians in the employment approach, and by other contemporary theorists. In the *General Theory*, Keynes himself explicitly used the type of reasoning central to the above and to the employment approach pursued by Australia. Confined to the final two chapters of the work, Keynes warned that the ‘laws’ of comparative advantage applied only *after* domestic demand was at a level sufficient for full employment. In a seminal passage which outlined the lessons of his message for the international economy, he wrote of the hope that

if nations can learn to provide themselves with full employment by their domestic policy...there need be no important economic forces calculated to set the interest of one country against that of its neighbour. There would still be room for the international division of labour and for international lending in appropriate conditions. But there would no longer be a pressing motive why one country need force its wares on another or repulse the offerings of its neighbour, not because this was necessary to enable it to pay for what it wished to purchase, but with the express object of upsetting equilibrium in the balance of payments so as to develop a balance of trade in its own favour. International trade would cease to be what it is, namely, a desperate expedient to maintain employment at home by forcing sales on foreign markets and restricting purchases, which, if successful, will merely shift the problem of unemployment to the neighbour which is worsted in the struggle, but a willing and unimpeded exchange of goods and services in conditions of mutual advantage (Keynes 1936, pp.382-383).

Keynes’s contributions to the application of *General Theory* reasoning to the international economy continued (most notably, as we have seen, in the Clearing Union proposal) for the remainder of his life. But Keynes was not the only theorist interested in the question, and theoretical contributions consistent with the employment approach were reasonably common in the 1940s, particularly in the United Kingdom. The work of Kalecki and Balogh has already been mentioned, though as noted, their work was part of a coherent set of studies in applied economics

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<sup>598</sup> In a longer term sense, Kalecki was also concerned that international lending was a force for the continuation and propagation of imperialism. According to Kalecki, international lending provided the creditor countries with an ever-increasing source of external profits, providing the fuel for ever higher levels of investment in their own productive capacities and entrenching still further their trade advantages in a ‘virtuous circle of cumulative causation’ (Kriesler and Halevi 1995, p.14). The debtor nations, by contrast, faced a scenario in which external profits were negative, investment and productivity declined and their ability to compete was much reduced - in short, ‘a vicious circle of increased indebtedness and reduced competitiveness’ (Kriesler and Halevi 1995, p.16). The seeds of imperialism, and future conflict, were sown in this process as capitalists in the creditor nations scrambled to divide foreign markets in the drive for the export of capital and goods, collectively ‘the classical source of “external” profits’ (Kalecki 1965, p.52).

sponsored by the Oxford University Institute of Statistics, in which they were often joined by E.F. Schumacher. Schumacher himself produced a Fabian Society pamphlet, *Export Policy and Full Employment*, which had at its core the message that a 'rational international system can only grow out of national full employment in all...national systems' (Schumacher 1943, p.33). Schumacher's work was influential within the British Labour Party, but this particular paper also managed to find its way to Melville in 1944, who regarded it highly. Other works which either explicitly or implicitly adopted the employment critique of the classical story in this era included Arndt (1944), Robinson (1937), Meade (1951), Harrod (1938), as well as the United Nation's report on the subject by Clark, Kaldor, Smithies and Walker in 1949.<sup>599</sup>

Notwithstanding the above deficiencies in orthodox trade theory, its role as the theoretical core of the approach of the United States and other countries to trade and other policies was deeply entrenched. Keynes's analysis, even to the extent it was accepted by policy makers and theorists for domestic policy, scarcely touched the theoretical assumptions of most economists working in the *trade* field. The (neo)classical paradigm had rocked inexorably back into place by the time of Bretton Woods and the ITO, and in the post-war era economic theorists and policy-makers quickly re-adopted the Hecksher-Ohlin model, took on the Stolper-Samuelson extensions and moved on to monetary theories of the balance of payments, even if, at the same time, a non-trade theory literature flourished around issues of international policy co-ordination. None of these trade models took up the issue of employment beyond assuming as a starting point that it was always *full*. More recently 'general equilibrium' trade theories have removed thinking on the international economy to an altogether new level of abstraction, in which the assumption of full employment mostly remains inviolate. Pockets of dissent remain, however, and in the work of Kregel (1998), Di Ruzza (1998), Bhagwati (1989), Kriesler and Halevi (1995), Harcourt (1995), Arestis (1996), and Davidson (1997) to note but some, there is confirmation of the centrality of full employment for the conclusions of much that is called modern trade theory, and justification for the argument that Australia's employment approach was consistent with an alternative *theoretical* discourse which resonates to the present day.

## **9.1: The Approach as Political Economy**

In their peerless official history of Australia's war economy, Butlin and Schedvin (1977, pp.672-673) acknowledge that, in the employment approach, Australia had a policy which was both 'intelligently conceived and directed towards the fundamental problem'. The product of 'young economists newly recruited to government service', and of a government 'equally quick to absorb the political attractions of the message', it was a policy that was important in linking trade and employment in the discourse of international post-war reconstruction (Butlin and Schedvin 1977, p.273).

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<sup>599</sup> This report, *National and International Measures for Full Employment*, was commissioned by the Economic and Social Council. The team was headed by Australia's E.R. Walker. Of course, this is by no means an exhaustive list of works in this era which made the point that employment levels were important for trade, but it is indicative of some of the more significant works which explicitly took up the idea that *full employment* was a required assumption of classical trade theory.

Butlin and Schedvin's broad tick to the employment approach was qualified, however, by what they regarded as the 'rigidity' in which it was pursued - a rigidity which was based on an 'undue suspicion' with which the motives of the United Kingdom and the United States were viewed by Australia. According to Butlin and Schedvin (1977, p.273), although 'caution' was warranted, the Australian approach made 'insufficient allowance... for the need to build the framework of collaboration from the grass roots'.

It is the view of this study, as in the discussion of trade theory above, that the 'rigidity' with which Australia pursued the employment approach was justified. Australia was being asked to surrender policy control to a promise, that of multilateralism, the only benefits of which could be unambiguously specified with the equally rigid assumption of full employment. Pursuing the employment approach, therefore, was in this context no more than an exercise in calling the intellectual bluff of a programme whose central objective - the multilateral reduction of trade barriers - was no less rigidly pursued. It is also the view of this study that, certain excesses of some of its political representatives aside, Australia was also correct in the degree of suspicion it entertained with regard to the major economic powers. As noted by Butlin and Schedvin, these suspicions were perhaps unduly harsh with regard to motives, since the same socio-political forces which would no longer tolerate unemployment of the Depression variety in Australia were equally as strong in these countries, but it was surely appropriately held with regard to *actions*. If the United States could have been expected not to allow for large scale unemployment within its own borders (though the Australians had received no surety on this), the suspicion that it would attempt to achieve this by exploiting its enormous advantages relative to the rest of the world in trade was surely a justifiable one. Full employment in the United States, in other words, could very likely be achieved at the expense of full employment elsewhere. This was less true for the United Kingdom, whose policy makers were more in line with the employment approach than Australian representatives often cared to admit, but its actions would always be circumscribed by the same constraints that the employment approach was trying to eliminate. Once the equilibrating force in the world economy, the United Kingdom was never to regain that role in the post-war period.

The question of the appropriateness of policy many years after it was relevant will always be difficult to determine and, in the context of the employment approach, even counter-factual, since for most of the post-war period the countries concerned in this study enjoyed a period of unparalleled prosperity.<sup>600</sup> The employment approach was not formulated, however, in the light of the long post-war boom. Rather, it was developed in the light of the experiences and the theoretical developments of the 1930s, and it was concerned to influence policy in a period when the circumstances of the post-war world economy were not known. This period, which extended from the war years and until the early 1950s, was one in which the suspicions entertained by Australia as to the actions of the economic powers appeared to be well justified.

### *United States Employment Policy After 1945*

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<sup>600</sup> That is, the 'Bretton Woods' era, from 1945 to about 1973.

A consistent thread running throughout Australia's advocacy of the employment approach, was the fear that a downturn in the United States could once more plunge the rest of the world into depression. For this reason, and given that the United Kingdom had committed itself in its employment White Paper, the 'binding commitment' so central to the employment approach was largely directed at the United States.

The lack of success in having such a binding agreement incorporated into the emerging international economic institutions was partly ameliorated, as far as some of Australia's economists were concerned, by the introduction in 1945 of a 'Full Employment Act' into the United States Senate.<sup>601</sup> Sponsored by a group of 'liberal' senators, the Act was, in fact, little different in its policy advocacy from the Australian and British White Papers.<sup>602</sup> The Act was explicitly Keynesian, reasoning like its Australian and British counterparts, that national income was determined by various components of aggregate spending. Should private spending fall short of that required for full employment, the Act mandated that public spending increase accordingly. At the centre of the policy process under the Act was the National Production and Employment Budget, a device through which full employment could be defined and measured and compensating public expenditure could be made. More broadly, the Act was unambiguous in its vesting with government the responsibility for economic welfare, and employment in particular (Goodwin 1989 p.100, Hamby 1973, p.60, Patterson 1996, p.143).

The Full Employment Act was supported by organised labour, a core group of mainly Democratic Party politicians, the representatives of various agricultural interests, 'liberal' groupings more generally and, initially at least, by the Truman Administration. The Act also encountered substantial opposition from the majority of Republicans and from most business organisations. Within the latter group there were those who saw the Act as creeping socialism to be resisted at all costs, while other more 'moderate' business organisations sought merely to modify the Act to make it more business 'friendly'. These organisations recognised the benefits to business of the maintenance of effective demand, but tended to stress tax cuts as the mode for fiscal expansion (Griffith 1989, pp.68-69, Goodwin 1989, p.135).

By 1946, the Full Employment Act had been passed in the Senate but had stalled in the House of Representatives, and from here it evolved into something less pleasing to the advocates of the employment approach. Anxious that the Act be passed in some form, the Truman Administration agreed to 'modify' the Act in a way which was to emasculate it of its explicitly Keynesian aspects. The new version of the Act, which

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<sup>601</sup> Crisp (1965, p.19) suggests that the publicity generated by Australia's advocacy of the employment approach gave much needed 'aid and comfort' to the framers of the 1945 Act, a view which was sympathetically acknowledged in Tange (1996). Whether this was the case or not is almost impossible to judge, but in August 1945 the Australian Legation in Washington reported back to the Department of External Affairs that the 'State Department has asked us for eight copies of the Commonwealth Government's White Paper on Full Employment, which...was arousing considerable interest in the Department'. 'Australian Legation Washington to Department of External Affairs', 25 August 1945, NAA A1066/1, ER45/2/3/2.

<sup>602</sup> The Act was introduced into the Senate by Robert F. Wagner of New York whose interest in Keynesian economics had been aroused through Alvin Hansen, the most influential importer of 'Keynesianism' into the United States (Hamby 1973, p.60).

was now merely called the Employment Act and entirely eschewed the words ‘full employment’, asserted that government should only attempt to achieve ‘maximum’ employment. There was no reference to mandatory public spending. The Act was also broadened to make employment merely one of a number of responsibilities of government, which now included price stability and the improvement of productivity. References to public works expenditure in the Act were also accompanied by exhortations that such works be consistent with the maintenance of ‘sound finance’. The National Production and Employment Budget was replaced in the Employment Act by a three person Council of Economic Advisers, a Joint Economic Committee of Congress and an annual economic report to the President. The Employment Act was passed by Congress in February 1946 (Goodwin 1989, p100, Griffith 1989, pp.69-70, Patterson 1996, p.143).

As events transpired, with the exception of a brief (though significant) episode in 1949, unemployment in the United States was not a serious problem in the immediate post-war period. Once more, however, this could only have been of limited comfort for the Australian advocates of the employment approach. If the twists and turns over the Full Employment Act had demonstrated anything to outside observers, surely it must have been that full employment in the United States would always be subject to the slings and arrows of its domestic fortune. In 1946 ‘New Deal’ policies were in retreat. With a relatively affluent population anxious to preserve their purchasing power, the issue of employment policy was a fast receding priority amongst policy-makers and, in this context, a less than guaranteed objective should the good times end.

### *Loss of Interest in Multilateralism*

Multilateralism has been portrayed throughout this study as the single catch-all policy of the Roosevelt Administration. The guarantor of external balance, it was also viewed as the means to internal balance, expanding overseas markets being the preferred alternative to countercyclical fiscal policy to ensure full employment. For a government anxious as any other not to return to the unemployment of the Depression, but equally less willing to undertake many of the interventionist measures acceptable to others, multilateralism was a particularly attractive creed that promised to reconcile many of the contradictions between the political and economic realities prevailing in the United States. This, coupled with an idealism in which multilateralism was also seen as a harbinger of peace, went a long way to explaining the zealotry by which it was pursued in the international conferences concerned with post-war reconstruction. If the United States was not likely to provide guarantees with respect to its employment policies, it was surely reasonable for its trading partners and allies to expect that multilateralism could be relied upon as firm Administration policy. By 1945, however, even multilateralism began to fall from favour (Bennett Woods 1990, pp.304-306).

The dramatic turnaround in United States commercial policy that spelled the end of multilateralism began with the renewal of the Reciprocal Trade Agreements Act (RTAA) in June 1945. The RTAA, passed in 1934 as Cordell Hull’s counter to ‘Schachtism’ in Germany, was originally developed as a device to expand United States trade with Latin and South America. Under the auspices of the RTAA, the

administration could, without prior congressional approval, lower United States' tariffs by up to 50 percent so long as comparable reductions could be negotiated in tariffs on United States' exports. With the most-favoured-nation principle applying to all items subject to negotiation and to all countries with whom the United States had signed a trade treaty, the RTAA was trumpeted before the war (as noted previously in Sections I and II) as an important device for reducing trade barriers around the world. In reality, it was always something less than this, since the RTAA provided that advance public notice had to be made before any agreement was concluded, which allowed United States industries to declare their objections and apply a veto (Bennett Woods 1990, pp.212-219).

The RTAA, as renewed in 1945, was much more destructive to the ideals of multilateralism than the old Act had been. Passed by large majorities in both houses, Congress had added to the original Act the requirement (long feared by the Australian economists) that each new reciprocal treaty promote American exports while endangering no existing domestic industry. Congress also added a 'peril point' provision which allowed *higher* tariffs to apply to particular industries deemed to be in danger. At a time when the United States already held the large part of the world's gold stock and had by far the world's most productive industries, the renewal of the modified RTAA was a most unwelcome development (Bennett Woods 1990, pp.220-226). The RTAA was, in short, a 'mechanism whereby a basically self-sufficient nation could bargain for those few items it needed to import and export' (Bennett Woods 1990, p.305). Its substitution of product-by-product bilateral bargaining for universalism and non-discrimination was a long way removed from the structure the architects of multilateralism had so recently tried to build, and upon whose guarantees the trading partners of the United States had sacrificed much of their protective devices.

The problems inherent in the unequal divisions of wealth and productive capacity did not take long to show themselves in the post-war global economy. In 1946 the United States had a trade surplus of \$8.2 billion, a figure which increased to \$11.3 billion the following year and marking the high point of what became the world-wide 'dollar shortage' (Gardner 1956, p.294). Europe, its productive capacity devastated by the war and its markets reduced via the Soviet occupation of Eastern Europe, was importing in 1947 seven times the amount of goods from the United States it could collectively export to that country (Cairncross 1996, p.102). The United Kingdom, nominally one of the victors of the war, took 43 percent of its imports from the United States but sent only 14 percent of its exports there (Morgan 1984, p.341). The Anglo-American loan in 1946 allowed, however, the newly elected Labour Government in the United Kingdom to pursue policies of social reform and full employment in the short run, with the key to the latter being a policy of 'cheap money' - referred to by Hugh Dalton, the Chancellor of the Exchequer (with due deference to Keynes) as the 'euthanasia of the rentier' (Morgan 1984, p.339).

Dalton's policies came undone in the 'convertibility crisis' of 1947. A condition of the Anglo-American Loan, the convertibility of sterling came into force in July 1947 and from the outset exposed the imbalances not only between the United Kingdom and the United States, but also between the rest of the world and the United States. Sterling remained for a great many countries the currency of international commerce -



indeed, given the dollar shortage, a great many countries sought the shelter of sterling trade in order to save dollars. This, coupled with the large debts it had acquired during the war, posed huge problems for the United Kingdom as these sterling earnings and sterling debts could now be converted into dollars. Put simply, the United Kingdom did not have sufficient dollars to allow these conversions to take place. In August 1947, a mere five weeks after it had been implemented, convertibility was suspended (Cain and Hopkins 1993, p.272). The optimistic policies of expansion which characterised Dalton's tenure was replaced by policies of retrenchment, rationing and austerity. The faltering moves towards multilateralism in the United Kingdom were replaced by closed trading within the sterling area and with certain countries in Europe. In September 1947, Ernest Bevin, the Foreign Secretary, even proposed an 'Empire Customs Union' as the solution to Britain's economic difficulties. As it was, imperial preferences, which had been the target of much of United States policy during the wartime negotiations, did not disappear in the post-war world, but remained a symbol of disappointed hopes (Gardner 1956, pp.358-360).

The role of the new IMF and World Bank during the 'reconstruction' period was left ambiguous at Bretton Woods. Again, however, United States policy during the period did little to alleviate the exchange crises endemic the world over. Because both institutions were seen by many in Congress as simply the vehicles through which other countries could drain dollars from the United States, the Bretton Woods Agreement Act, which formally expressed the American government's acceptance of the two institutions, was a conservative document which removed various features which provided the modicum of expansionary inclination sought by Australia and others. The Congress also established an 'Advisory Council' to instruct the United States Executive Directors of the Fund. The first act of this Council was to require the Directors to ensure that the Fund did not 'provide facilities for relief or reconstruction on the part of any member' (Gardner 1956, p.263). Keynes, who had hoped for an 'internationally minded' board of directors for the Fund, was profoundly disappointed in what he saw as the replication of national interests into the operations of the 'children' of Bretton Woods. Should this national/political dimension dominate their existence, he told the first meeting of the Fund in Savannah in March 1946,

the best that could befall...would be for the children to fall into an eternal slumber, never to waken or be heard of again in the courts and markets of mankind.<sup>603</sup>

The conservative lending policies subsequently practiced by the Fund and the Bank did not endear the institutions to many countries. Even the much trumpeted safeguards failed before the scale of the disequilibrium and the Fund's aloofness from the problem. The celebrated 'scarce currency clause', for example, made little difference in a situation in which the Fund was not dispensing dollars, even though it was not short of dollars and the rest of the world was (Gardner 1956, p.331). In the end, the Fund's inactivity meant that in most countries post-war policies were much the same as which had held sway before the war - exchange restrictions, tariff barriers and those other protective measures designed to save scarce dollars. In 1948, Harry White admitted that '[a] candid appraisal of the contributions which both institutions have so far made toward the stated objectives would force us to the conclusion that

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<sup>603</sup> Keynes's address is cited in Harrod (1951), p.632.

achievement has been much less than anticipated'.<sup>604</sup> The following year his assessment was joined by that of the Executive Directors of the Fund themselves, who noted in their annual report for 1949 that 'dependence on bilateral trade and inconvertible currencies is far greater than before the war'.<sup>605</sup>

The post-war period did not end on this gloomy note, however, largely because politics intervened. In 1948, fearing that Western Europe's survival as a non-communist entity was at stake, the United States launched the famous Marshall Plan. Conceived by Clayton, now Undersecretary of State, and the new Secretary, George C. Marshall, the Marshall Plan (officially the Economic Recovery Program) provided unencumbered grants, loans and conditional aid. Importantly, it also made provisions for the payment for United States imports to be made in local currencies. Like Lend-Lease, the Marshall Plan has been portrayed as a 'most unsordid act' but, also like Lend-Lease, it was not without accompanying strategic, political and economic advantages for the United States. A condition of Marshall aid was the removal of many of the trade and exchange restrictions *between* European countries, a condition which meant the application of multilateralism if not to the whole world, at least to a region. Supplemented and then later replaced by military spending, the Marshall Aid allowed for that 'crucial margin' which enabled European recovery while maintaining external balance.<sup>606</sup> Writing many years after the events in which he had participated, the distinguished British economist, Alec Cairncross, delivered of the Marshall Plan a valedictory which could easily have been said of the Australian employment approach had it been applied:

[T]he Marshall Plan prolonged and underpinned European economic recovery when it was in danger of collapsing for lack of the necessary finance. It tided over an awkward period and helped to establish confidence in the continuity of recovery. What was of almost equal importance, it created confidence in American leadership and participation. In these ways it helped to establish the full employment which was the driving force in postwar prosperity. It did not guarantee full employment in the fifties - *that depended on American domestic policy* - but by establishing a high and rising level of GNP it generated investment requirements that carried the world economy upwards without a major setback. It was indeed a key element in the 'Golden Age' (Cairncross 1996, p.104, emphasis added).

### *Australia*

Contrary to the expectations of the Australian economists, Australia did not run into balance of payments difficulties in the early post-war years. High prices for Australian exports, in fact, meant that the traded goods sector was a net contributor to

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<sup>604</sup> White cited in Gardner (1956), p.305.

<sup>605</sup> International Monetary Fund (1949), p.3.

<sup>606</sup> Cairncross (1996), p.109. Accounts of the Marshall Plan are, of course, legion, but Cairncross's account, written with all the benefits of hindsight by someone who participated in the negotiations at the time, is particularly illuminating.

the extraordinary growth of the Australian economy during this period.<sup>607</sup> Like other countries, though, Australia suffered from a chronic ‘dollar shortage’, a situation which meant continued rationing for a range of ‘dollar sourced’ products well beyond the end of the war. Dollars were rationed by the Government according to a quarterly budget amongst private firms and public enterprises, a process which meant that only certain essential raw materials, high-priority capital equipment and petroleum imports were granted significant dollar allocations (Crisp 1961, pp.309-311). The Marshall Plan, which was so important to the maintenance of internal and external balance in Europe, did not include Australia or any of the sterling countries outside of Europe.

The dollar shortage, Australia’s traditional ties and the on-going fear that in the absence of a commitment to full employment the United States could drag the rest of the world into depression, meant that Australia became a leading member of the post-war sterling group. A net drawer of dollars under the sterling group’s dollar ‘pooling’ arrangement, Australia nevertheless contributed to the group’s solvency by direct aid to sterling countries, by the sale of its annual gold production to the United Kingdom and by its restrictions on United States exports (Lee 1990, p.185). In 1949, however, all of this was of little avail when a mild recession in the United States brought about a dramatic reduction of sterling country exports, including Australia’s. The fear long expressed by Australian economists and the government alike had come to pass, and prompted Evatt, with Chifley’s approval, to work on a proposal that the sterling area form a ‘self-sufficiency’ bloc.<sup>608</sup> The proposal was subsequently advanced at a financial conference of sterling countries in London in July 1949, but formulated as a multilateral non-dollar bloc committed to maintaining full employment. The proposal did not go anywhere at the conference, not least because in these politically charged times the British Government was anxious to avoid a split in the non-communist world.<sup>609</sup>

In November 1949, and in the absence of a recovery in its export income, the British Government devalued sterling by 30 percent (Pressnell 1986, p.367). The Australian Government, after some hesitation and after having taken out an IMF loan to maintain the minimum of dollar imports required by Australia, followed suit.<sup>610</sup> Significantly, Chifley also felt forced to re-introduce rationing on petrol, a deeply unpopular and courageous move one month before an election. With an opposition committed to the removal of this and other restrictions, the Chifley Government was subsequently defeated in the December elections (Crisp 1961, pp.313-314). The government which had launched the employment approach in 1942 as a way of liberating the nation’s political economy from the constraints of the external sector was brought down by difficulties in the very same sector. With the Labor Government’s defeat came the end of the employment approach. The Korean War, beginning the year after Labor’s defeat, heralded for Australia the beginning of the same ‘Golden Age’ the Marshall Plan had delivered for Europe. In the following decades, the application of the same

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<sup>607</sup> See, for example, the tables of Australia’s terms of trade and export price indices in Dyster and Meredith (1990), pp.186-187.

<sup>608</sup> Evatt’s proposal is outlined in ‘Memorandum of Conversation Between Chifley, Evatt, Dedman and Wheeler’, 29 June 1949, NLA, Dedman Papers, MS 987.

<sup>609</sup> ‘Memorandum of Discussions’, 7 July 1949, London Financial Discussion, NAA A4311. J.J. Dedman represented Australia at these discussions.

<sup>610</sup> The loan, which was taken out in October 1949 with great reluctance, was for \$US 20 million (Lee 1990, p.192)

theories which had been behind the employment approach enjoyed widespread application and, for quite a while economists and governments remembered that the gains from trade and full employment were *complements* in an interdependent world.

## Section IV

### *Keynesian ‘Revolutionaries’*

## **Chapter Ten**

### **The Keynesian ‘Revolution’ in Australia**

In relatively recent times, a burgeoning line of research has opened up which has attempted to examine the questions of the existence, initiation and propagation of a ‘Keynesian revolution’ in Australian economic policy-making and theorising.<sup>611</sup> Though confined initially to the recollections of the surviving protagonists, the literature devoted to the topic has grown to include a broad church of work ranging from institutional histories, biographies, inter-disciplinary accounts with an accent on politics and sociology and, latterly, the adoption of models which attempt to formally distinguish mechanisms through which economic ideas are propagated. Broad as it is, however, this literature is comparatively weak in identifying the threads through which the consistency of much Australian economic thought can be identified - a thread which this study has attempted to highlight by focussing upon the framework which informed the advice of economists regarding the international economy. It is the purpose of the following chapter to examine the extent to which this advocacy sheds light on the success of the ‘Keynesianising’ of Australian economics immediately before and after World War Two, providing along the way no succour to revisionist accounts which seek to downplay Keynes’s centrality. At the same time, it also draws attention to the fact that, for many Australian economists, the *General Theory* generated, as it had for Keynes himself, the means by which that long ‘struggle of escape from habitual modes of thought and expression’ could be realised.<sup>612</sup>

The chapter does not attempt to offer an alternative holistic explanation for the Keynesian revolution in Australia. Rather, it highlights how important the ideas and issues examined in the preceding sections would be in the construction of such an explanation, and how the existing literature on the subject needs to be recast in this light. The chapter also examines some of the most influential frameworks employed to consider the evolution of economic ideas. While not arguing for any particular sociology of economic knowledge, it finds that the Keynesian revolution in Australia is made more explicable in each of these frameworks by the inclusion of the international advocacy of Australian economists.

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<sup>611</sup> The term ‘revolution’ has been employed in this study in the loose meaning of the term as widely applied to the history of economic thought. It is not used necessarily in the very specific meaning prescribed to it by Kuhn (1970) and others concerned with the processes of change in scientific thought. A revolution in economic thought requires fundamental or comprehensive change in the discipline, but this study does not take the view that this has to take place in an especially rapid period of time. Thus it agrees with Hutchison (1978, p.286) that there is nothing contradictory in writing of a ‘long revolution’.

<sup>612</sup> In this quote Keynes is referring, of course, to his own ‘long struggle’ which he retrospectively identified in his prior works (Keynes 1936, p.viii).

## **10.0: The Existing Literature**

Coombs 1981 autobiography, *Trial Balance*, and its clarion declaration that (p.3) '[t]he publication in 1936 of John Maynard Keynes's *General Theory of Employment, Interest and Money*, was for me and for many of my generation the most seminal intellectual event of our time', has been cited in almost every study devoted to the question of the influence of Keynesian economics in Australia. An example of what might be called a 'revelatory' approach to the question, but one which acknowledged the extent of the intellectual journey already undertaken by Australian economists before 1936, it was an approach common to the recollections of Australian economists who 'came of age' during this period. Crisp (1961; 1965), for example, highlighted the excitement of 'young' economists to the message of the *General Theory*, an excitement which he suggested was complemented by the accession of the Labor Party to office during the war and by Chifley, a Keynesian of the 'first hour' following his exposure to the Banking Royal Commission in 1936. For Crisp, as for Coombs, the success of *General Theory* reasoning in initiating a *policy* revolution lay in the combination of the influx of young economists already imbued with a Keynesian *joie de vivre* into influential government positions during the war, and the extent to which this was in sympathy with the underlying philosophy of the Labor Government. Other accounts, such as Tange (1996), Copland (1960) and Melville (in Cornish 1993), together with private interviews with other relevant players, present a similar story of an economics profession in Australia that was quickly and comprehensively 'Keynesianised' after 1936.

### *Five Modern Accounts*

In the last two decades the literature on Keynes's influence on Australian economics has grown beyond the accounts of those personally involved in implementing his ideas. Though now a vast literature encompassing a range of disciplines, five accounts particularly stand out. These five are surveyed below. Differences and similarities to the present study are highlighted.

Whitwell (1986), the most prominent of recent academic writings on the subject, charted the rise and fall of Keynesian economics via an intellectual history of the Treasury - the department which, more than any other, has been the primary source of economic advice to Australian governments. Relating a story in sympathy with Coombs and his contemporaries, Whitwell suggested that the ready and wide acceptance of *General Theory* reasoning was the 'outstanding feature' of the Australian economics profession immediately before and after the Second World War (Whitwell 1986, p.53). Defining 'Keynesian' economics along the lines taken by Kaldor - giving primacy to effective demand as the general determinant of production and highlighting the inherent tendency in capitalist economies for instability and underemployment equilibrium - Whitwell emphasised the new conception of the role of the government's budget in maintaining macroeconomic stability.<sup>613</sup> This new conception reached a high point, according to Whitwell, in the 1945 Full Employment

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<sup>613</sup> An understandable emphasis given the central actor of his study.

White Paper, a 'remarkable document' and the 'outstanding symbol of the change in attitude' (Whitwell 1986, p.52).

Whitwell explained the acceptance of Keynesian economics in Australia in terms of the predispositions of the ruling Labor party (its leaning towards 'interventionism', and the role of Chifley as a 'Keynesian-of-the-first hour'), the legacy of the depression and war in creating a public demand for a more activist role of government, and the part played by young economists, sympathetic to the Keynesian message, in infiltrating government departments (Whitwell 1986, pp.58-59). Amongst the latter, Whitwell highlighted the F&E Committee, quoting Coombs that 'it was the work of this committee which gave to the economic planning of the war an essentially Keynesian character' (Whitwell 1986, p.66).

In terms of the economists themselves, and the reasons for their embrace of Keynesian economics, Whitwell stressed the 'personal' links to both Keynes and Cambridge. In this context, the connections between King's College and Giblin have already been noted, but just as important, Whitwell suggested, was Cambridge's influence upon E.R. Walker. A graduate of Sydney University and Cambridge, Walker participated in the meetings of Keynes's 'Political Economy Club' in 1931-33 in which many of the nascent ideas which were to form the *General Theory* were discussed. Walker was the only economist to employ *General Theory* reasoning in his evidence before the 1936 Royal Commission into Money and Banking and, according to Whitwell (1986, p.72), 'the first of the F&E economists to embrace a Keynesian attitude to the role of the budget in dealing with economic instability'. Others with a link to Keynes and Cambridge highlighted by Whitwell included W.B. Reddaway and Colin Clark. Reddaway had been supervised as a student by Keynes over 1936-37, was subsequently appointed a research fellow at the University of Melbourne and wrote a well-regarded review of the *General Theory* for *The Economic Record* before returning to the United Kingdom. Clark's extensive contacts with Keynes via their membership of the Economic Advisory Council and at Cambridge have already been noted.

Whitwell also focused on the social philosophy of the F&E economists more generally, and in Whitwell (1986 and 1994) he took Wilson, Coombs, Copland, Melville, Walker, Giblin and Bridgen, to suggest that all (in varying degrees) shared an outlook conducive to Keynesian economics. This included a view that 'human ignorance and myopia' were the root causes of economic misery - a misery which in part could be ameliorated by the actions of the state and by education 'from on high' (Whitwell 1987, pp.78-79). More specifically, there was a profound scepticism as to the ability of competitive markets to achieve a self-regulating economy and a predilection for various types of 'planning'. Curiously, Whitwell had little to say on the *theoretical* development of the Australian economists before 1936, although his contribution on social philosophy was undoubtedly valuable in explaining the broad appeal of the *General Theory* to the members of the F&E.

Whitwell returned to the question of the adoption of Keynesianism in Australia in 1994 when he examined, in the context of Australia, the three analytical approaches identified by Hall (1989) as being generally common to the attempts of researchers to explain the embrace of Keynesian economics in various countries. These three



approaches, which were canvassed by Hall as editor of an influential book, *The Political Power of Economic Ideas: Keynesianism Across Nations*, were labelled the 'economist-centred' approach, the 'state-centred' approach and the 'coalition-centred' approach. Each had particular strengths and weaknesses and were more or less relevant according to the particular circumstances of individual countries. Hall's own view was that conditions had to be favourable in all three areas for both the adoption and longevity of a Keynesian economic framework.<sup>614</sup>

The economist-centred approach was in many ways simply a re-statement of Keynes's own assessment of how revolutions in economic thought occurred - an expansion on his oft quoted lines in his concluding notes to the *General Theory* about economic ideas being 'more powerful than is commonly understood' and the world being 'ruled by little else' (Keynes 1936, p.383). To Hall this approach had the virtue of focusing attention on the *ideas* of Keynes, and the revolutionising of an intellectual discourse, but it also had the potential vice of attributing excessive influence over policy by the economics profession (Hall 1989, p.10).

According to Whitwell (1994, pp.126-130), an economist-centred approach is particularly useful in examining the adoption of Keynesian economics in Australia because of the extent and unanimity of its acceptance amongst the nation's economists and, importantly, the degree to which he thought that they *were* subsequently able to influence policy. On these questions, Whitwell largely reiterated his earlier work, but he also emphasised to a greater extent than before the demonstration effect of the war in validating a Keynesian approach. On the issue of influence, Whitwell again advanced the idea of the infiltration of economists into government departments and the emergence of a coherent line afforded by the F&E. In this context also, the war experience emerged as a more important influence than in the earlier account, and Whitwell appropriated for the Australian circumstance Skidelsky's (1975) claim for the United Kingdom that the war had stimulated experimentation due to the replacement of official personnel by others less bound by past convention.

Hall's 'state-centred' approach highlighted the role of state institutions, especially the economic policy bureaucracies, as the vehicles or inhibitors of the spread of ideas. Emphasising the 'permeability' of the civil service and/or the degree to which 'outsiders' could be appointed as important prerequisites to the early acceptance of Keynesianism, Hall also noted that the *lack* of permeability and the extent of centralisation of economic advice was thereafter critical to its longevity (Hall 1989, pp.10-12). In this context Hall, and the earlier work of Weir and Skocpol (1985), drew attention to the differing experiences of the United States and the United Kingdom. The system in the United States by which a large proportion of its officials were appointed by each successive administration meant that Keynesian ideas made their way relatively early into the halls of government. At the same time, however, the flows of economists into or out of government according to changes of administration meant that these ideas did not become entrenched. In the United Kingdom, by contrast, economic policy advice was very largely in the hands of the Treasury, a body hierarchical in structure with full time career paths and slow to embrace change.

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<sup>614</sup> Hall's framework is outlined in the introduction to Hall (1989), pp.7-26.

This meant that once adopted, Keynesian ideas survived numerous changes of government.

Whitwell placed the Australian experience somewhere between those of the United States and the United Kingdom. Before the Second World War, bureaucratic economic advice and policy enactment in Australia was highly diffuse, with Whitwell nominating the treasuries of the Federal *and* state governments, the Tariff Board, the Commonwealth Bank, the Arbitration Courts and the Loan Council as all having a say and none of them being particularly interested in new sources of ideas. The Second World War and the growth in power of the Federal Treasury (infused with new recruits of a Keynesian disposition) turned matters around and, according to Whitwell, was the principal cause for Keynesian ideas becoming ‘an entrenched component of the policy process’ (Whitwell 1994, p.132). Hall had also identified a strong central bank as usually an impediment to the spread of Keynesian ideas, but in Australia the Commonwealth Bank - certainly a negative force against expansionary policies in Australia in the 1930s - was, unusually under Coombs as Governor, a focal point of a Keynesian approach (Whitwell 1994, pp.133-134).

The ‘coalition-centred’ approach, as identified by Hall, argued that economic policy ultimately depended upon the political mobilisation of various interest groups (Hall 1989, pp.12-13). The ability to forge coalitions of groups that identified Keynesian economic policies as relating to their interest, therefore, was a factor which differentiated their successful adoption across countries. Hall regarded Keynesianism as uniquely possessing, in the context of the times, elements attractive to both capital and labour. He also observed that the adoption of Keynesian economic policies tended to be associated with governing political parties which had ‘particularly strong ties to the working class’ and had some history of favouring government intervention in the economy (Hall 1989, p.376).

It was under the Labor governments of Curtin and Chifley that Keynesianism was adopted in Australia but, as Whitwell (1994, p.136) pointed out, after the fall of the ineffectual conservative coalition governments of the early war years and despite some initial hesitations, the Keynesian framework came to be accepted by *both* conservative and Labor parties in Australia in the postwar years. Like Hall, Whitwell noted the appeal of Keynesianism for both capital and labour in Australia, quoting Coombs’s comment in *Trail Balance* that

it was one of the most attractive features of the Keynesian analysis that it seemed to by-pass the most divisive issues within our society. It seemed in everybody’s interest that expenditure should be pitched at levels adequate to sustain business activity close to capacity and so to maintain high levels of employment.<sup>615</sup>

Of course, from the time of first settlement, Australia had had a tradition of government intervention in the economy in any case, much of it in the form of detailed regulation at the microeconomic level.<sup>616</sup> Whitwell argued that in this

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<sup>615</sup> Coombs (1981, p.146) cited in Whitwell (1994), p.136.

<sup>616</sup> Whitwell noted Noel Butlin’s term ‘colonial socialism’ to describe the relations of state and market in Australia in the nineteenth-century. Butlin, N.G. *et al* (1982), p.10, cited in Whitwell (1994), p.137.

context, Keynesianism was a mild regime, being at heart an indirect mode of intervention which left the private sector largely free to pursue its own interests.<sup>617</sup> Seen in this light, the apparent success of Keynesianism as an instrument for building political coalitions favourable to its acceptance was perhaps less surprising in Australia than in countries whose national traditions were less predisposed to state intervention.

Hall's triad approach to the promulgation of a Keynesian revolution provided one of the few systematic attempts to account for the interaction of economic ideas and economic policy. In the specific context of the Keynesian story, it provided a corrective to the early historiography which placed a somewhat naïve emphasis upon the triumph of ideas over entrenched interest - what Winch (1972, p.24) described as the 'rationalist fallacy of believing that ideas alone are powerful enough to determine the course of events'. At the same time, however, it avoided the equally distorted interpretation of what might be called a 'revisionist' literature which removed the agency of economic ideas almost entirely and instead emphasised a pragmatic, atheoretical response by institutions to changing circumstances.<sup>618</sup> This was 'an excessively passive, even deterministic view of policy making' according to Winch (1989, p.117), who also noted, in the context of the United Kingdom, that 'the presence of Keynes and other economists in government significantly shifted the nature of Treasury discussions and priorities in Keynes's direction'. In Australia, such extremes of interpretation were never really present; the scene set by the accounts of Australia's economist-administrators were clear not only concerning their decisive theoretical shifts 'in Keynes's direction', but also the administrative and political complexities of their task as well. Whitwell's timely introduction of Hall's triad, however, offered a structure in which such issues could be profitably considered.

The external sector did not loom largely in Hall's framework - except as the source of potential difficulties in initiating Keynesian policies - for he viewed the ideal national economic structure as 'a closed industrial economy with rigidities in the labour market and a well-developed financial system' (Hall 1989, p.372). In this sense, countries such as Australia were least suited to a Keynesian approach - small, still in the process of industrialising, and dependent on prices in world markets for a small range of primary commodities. This point was amplified by Whitwell, who added to the list of limitations the fact that Australia was also heavily indebted. This developed in Australia, according to Whitwell, a fatalistic belief that whatever policy was undertaken 'economic recovery depended much less on official policy than on the movement of commodity export prices' (Whitwell 1994, p.130). This was true up to a point, of course, but Whitwell overplayed matters somewhat when he also declared that it 'was taken for granted that there was little that anyone could do about the latter...[I]t was simply a matter of waiting and praying' (Whitwell 1994, p.130). Waiting and praying was undoubtedly part of the plans of Australia's delegations of economists abroad in the 1930s but, as this present study has sought to demonstrate, they went well beyond that.

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<sup>617</sup> Of course, this was not to say that, in practice, Keynesian macroeconomic policies could not be accompanied by administrative controls of various forms.

<sup>618</sup> The most extreme examples of which, according to Winch (1989, p.118), were Tomlinson (1981) and (1984), to which could be joined, amongst the recent Australian literature, Cornish (1994).

Like Whitwell, Smyth (1994) was concerned with the broad philosophy behind Australian economists' views on the correct relationship between the economy and the state, and in particular what he regarded as their generally socialist underpinnings. This philosophy was fertile ground for a Keynesian 'revolution' but, according to Smyth (1994, p.67), the 'social vision' of Australian economists was much more radical than the motivation of 'a liberal desire to save capitalism' that he attributed to Keynes. The vision of the Australian economists rather was one which, citing Crisp (1961) and McFarlane (1968), was 'part-Keynesian, part-socialist', and the general movement was less strictly Keynesian than simply one divorced from orthodox stories. In this context, Smyth cited Seymour Harris's comparative study of the various official government statements on employment made during and after the war in Britain, the United States, Canada, South Africa and New Zealand, and his conclusion that the 'strongest' statement of the Keynesian position was to be found in the Australian White Paper.<sup>619</sup> That the White Paper was subsequently regarded as a disappointment by many of its authors - a function largely of the deletions required by its political authors to make the document saleable to a populace tired of wartime controls - was proof of the 'radical bias of Australian economic thought at this time' (Smyth 1994, p.64).<sup>620</sup>

Smyth nonetheless acknowledged that the *theoretical* framework of the White Paper, and of the Australian economists' advocacy generally in the post-war period, was essentially Keynesian and that this framework was compatible with a variety of socio-political arrangements (Smyth 1994, p.55). In this sense he provided something of a repudiation to accounts, Black (1984) and Jones (1995) among them, which questioned the existence of a Keynesian revolution by comparing the work of Australian economists with various programmes (notably Beveridge's *Full Employment in a Free Society*) which went much further in the direction of social policy than that which was strictly necessary under a Keynesian economic framework. Germane to this point, Smyth cited Butlin's (1946) obituary of Keynes for *The Economic Record* in which Butlin, though in no sense a Keynesian neophyte, noted that

all see full employment through Keynes's eyes and lean towards his methods of attaining it. Thousands of economists throughout the world think in Keynesian terms about Keynesian problems, even when they believe themselves to be reacting against him; and, diluted, and sometimes far from pure, the Keynesian stream of thought has become part of public opinion.<sup>621</sup>

Smyth's citation of Butlin also provided a rebuttal to Cornish (1994) who, while acknowledging that it was 'doubtless true that the economics profession in Australia and some of the nation's principal economic advisers had accepted the Keynesian dispensation by the outset of the Second World War', suggested that a similar

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<sup>619</sup> Harris (1948), p.20, cited in Smyth (1994), p.64.

<sup>620</sup> This disappointment was acutely felt over Curtin's decision to remove references in the paper to institutions concerned with planning and controlling investment. Melville (1946) and Firth (1945) are both cited in this context.

<sup>621</sup> Butlin (1946, p.17) cited in Smyth (1994), p.57.

conversion had not taken place amongst politicians and, as such, a Keynesian policy revolution was stillborn (Cornish 1994, p.44). Of course, this is partly true - politicians are never likely to slavishly follow economic doctrines at any time - but it somewhat missed Butlin's broader point. Cornish also provided a curious assemblage of evidence for his thesis, using, for example, the Australian Government's reluctance to join the IMF from the outset as proof of a simultaneous reluctance to adopt Keynesian economic policies. According to Cornish, this was so because of 'the various international preparations regarding external economic policy after the war, probably no other structure bore so heavily the imprint of Keynes than the International Monetary Fund' (Cornish 1994, p.57). A principal finding of this study is to the contrary - Australia's objections to the IMF came from the fact that it was *not Keynesian enough*.

Smyth's acknowledgment of the Keynesian underpinnings of the work of Australian economists after the war was not accompanied, however, by a tracing of the development of their thought either before or during the conflict - and led him to the rather surprising conclusion that, based on their '*published literature*', the period 1939 to 1945 showed no signs of a theoretical acceptance of Keynes (Smyth 1994, p.67, emphasis added). An examination of the unpublished work, however, much of which has been cited in this study in the context of the international negotiations, disavows such a conclusion. The pre-war advocacy of Australian economists in international forums likewise rejects the notion that Keynesianism came to Australia as a revelatory doctrine ushered in by a new generation of economists in 1945.<sup>622</sup>

By far the most comprehensive project attempting to trace the development of Australian *economic* thought up to, and including, the 'take-off' phase of its Keynesian dominance, has been that of Neville Cain. In a series of published articles and working papers, Cain (1980, 1983, 1984, 1985, 1987a, 1987b, 1988a, 1988b) moved through monetary thought in the 1920s, the Depression years, and the advocacy of relative cost adjustment up to a point just before the Second World War - from when, 'the framework within which Australian war and post-war economic planning were conceived was unabashedly Keynesian' (Cain 1984, p.380).

Cain's work brought with it a number of important contributions to the history of Australian economic thought, not least of which was the identification of a more or less consistent 'expansionary' inclination in the advice of sections of the economics profession throughout the 1930s. This inclination, which was apparent in the work of what Cain referred to as the 'Melbourne School', was founded principally upon the personalities of Giblin and Copland at the University of Melbourne (hence Cain's label) and Mills, Walker and a group of younger economists (including Hermann Black and W.C. Wentworth) at the University of Sydney. Other economists who have featured in this study, Wilson, Brigden and Shann particularly, joined or opposed this rough grouping according to the issue. Melville (except, as highlighted by this study, when it came to international advocacy) and Arthur Smithies were more or less constantly opposed. Other economists who were to be important for the subsequent

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<sup>622</sup> This is not meant as a general criticism of Smyth's admirable research, however, which was not primarily concerned with accounting for the Keynesian revolution in Australia.

Keynesian era such as Coombs, Firth, Phillips, Swan, Tange, and Wheeler generally appeared on the scene too late to appear in the debates of concern to Cain.

As noted earlier in this study, Giblin generally took the lead in setting the agenda of inquiry of Australian economists throughout the 1930s and as such, his work looms large in Cain's research. Beginning with the advice of relative cost adjustment in the Premiers' Plan, Cain moved on to document Giblin's developing conviction (noted in this present study from 1933) that expansionary measures would be required if unemployment was not to lead to social breakdown. Giblin's subsequent advocacy of treasury-bill financed public works, exchange rate devaluation, the formulation of his multiplier, and his attacks on the conservatism of the Commonwealth Bank are presented by Cain as proof of a general recognition by Giblin (and others of the Melbourne 'School') of the interdependence of macroeconomic variables and, as a policy consequence, the importance of public spending in stimulating recovery (Cain 1983). That these faltering steps were self consciously regarded by the Australian economists themselves as being representative of a decisive, though undefined, shift away from orthodox thought was apparent in Giblin's favourable review of Keynes's *Means to Prosperity* in *The Economic Record* in 1933 (Section I above). Giblin's claim in this work that Keynes's scheme was 'a systematic co-ordination and generalisation for world use of the successful steps that have been taken in Australia' was somewhat self-deceptive perhaps, and carried with it the caveat anyway that the Australian efforts were 'piecemeal', 'accidental' and 'without any general acceptance of principle'.<sup>623</sup> It was, nevertheless, a revealing identification before the emergence of the *General Theory*.

Sharing the most conspicuous billing with Giblin in Cain's narratives was E.R.Walker. Much more than Whitwell, Cain was concerned to trace the development of Walker's theoretical position from his arrival back in Australia to his prominent appearance at the 1936 Money and Banking Royal Commission.<sup>624</sup> Walker's first book, *Australia in the World Depression*, was published from his Cambridge Ph.D thesis and was presented by Cain as demonstrating the exposure of its author to the transition of Keynesian thought from the *Treatise* to the *General Theory*. In this work and in others around the same time (notably Mills and Walker (1935) and Walker (1936)), Walker used a multiplier concept (an extended amalgam of Giblin's and Kahn's), elevated the importance of uncertainty in investment decision making, and suggested a saving-investment equilibrium below full employment, but stopped short of many of the other theoretical innovations soon to appear in the *General Theory*. In all of these, flexibility of exchange rates was supposed to maintain external balance (Cain 1984). It was at the 1936 Royal Commission that Walker first employed *General Theory* reasoning - the only economist to do so - and the first in any forum in Australia. Five months after the publication of the *General Theory* in the United Kingdom, Walker referred in his evidence to the Royal Commission to a liquidity preference theory of interest, the propensity to consume, the ex-post equilibration of planned saving and investment through changes in income, the determination of investment along the lines of a marginal efficiency of capital and the determination of national income and employment via aggregate demand (Cain 1988b). Beyond the Royal Commission, Walker continued to advance Keynesian ideas in the remaining

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<sup>623</sup> Giblin's review is cited in Cain (1983), p.215.

<sup>624</sup> Walker features especially prominently in Cain (1984, 1988a, 1988b).

pre-war years, though tempered by his growing concern for Australia's external position.

A little-known but interesting paper which drew on Cain for interpretations of Australian economists was Markwell (1985).<sup>625</sup> Not so much concerned with the development of Keynesian thought in Australia as it was with the role of Keynes *personally* in Australian economics (which meant, for example, that Markwell dwelt on the interactions between Keynes and the Australian Prime Minister, W.M. Hughes, over the Versailles Treaty), it was a work which nonetheless added much to the scholarship concerned with the Keynesian 'revolution'. Markwell surveyed most of the economists included in this study but placed particular emphasis on the Federal Treasurer in the Scullin Ministry, E.G. Theodore, as an important *political* conduit through which Keynesian ideas were disseminated. Theodore's place in Australian political history has been much examined, of course, but Markwell was concerned with Theodore's long-standing regard for Keynes, whose work he used (more or less accurately), from *The Economic Consequences of the Peace* through to the *Treatise on Money*, to support his own monetary ideas.

Using the research of Cain and others, Markwell concluded, much as this study has done, that it was 'into an Australian economics profession reasonably familiar with the policy prescriptions Keynes championed that the *General Theory* came in early 1936'. Markwell noted, too, (as this study has also done), that the pages of *The Economic Record* throughout the 1930s were redolent with references to Keynes - a phenomenon which only increased following the publication of the *General Theory* - the majority view seeming 'almost to take for granted that Keynes was basically right'. Markwell was also one of the few writers to touch on the story of the employment approach - appropriately enough in a section of the paper he titled 'more Keynesian than Keynes' (Markwell 1985, pp.43-51). His account of the employment approach was, however, relatively brief, and he did not draw on the unpublished writings of its advocates.

A most recent attempt to account for the rise of Keynesian economics in Australia, though this was not its primary purpose, was Battin (1997). Concerned rather with the decline of the 'Keynesian consensus' in Australia in the 1980s, Battin nevertheless provided a number of insights into the initial embrace of Keynesian economics. His central theme in this context was that the adoption of Keynesian economics in Australia was a function of political factors more than economic - more particularly, that Keynesian economics fitted well the social democratic tendency of the Labor Party leadership in the 1940s. This leadership was greatly influenced by its experiences during the short-lived Scullin Government. The all pervasiveness of underconsumptionist and non-orthodox monetary doctrines through its ranks in the 1930s provided, as Battin emphasised (1997, p.35), theoretical predecessors to Keynes. Keynesian economics also provided key leaders of the Party, Evatt and

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<sup>625</sup> Markwell's work, a Reserve Bank of Australia Seminar Paper, was not subsequently published, and appears not to have circulated far beyond that institution.

Chifley being highlighted, with a theoretical basis which allowed their policies concerned with full employment and social welfare to be expressed in ways which could counter their traditional critics. All of this was perhaps fairly obvious, but like Whitwell (1994), Battin used the propagation model of Hall (1989) to demonstrate that Keynesian economics provided the means for the necessary coalition of disparate political forces essential for its successful implementation. Battin was also critical of revisionist accounts that attempt to downplay the Keynesian nature of Australian economic thought and policy in the 1940s, noting with regard to the Full Employment White Paper that to 'say that...[it] was Keynesian in character is to *understate* the case' (Battin 1997, p.39, emphasis added).

### **10.1: The Contribution of this Study**

A primary aim of this study has been to examine the advocacy of Australian economists to the international economy with a view to shedding light on their theoretical development. More particularly, given that the 'Keynesian revolution' was by far the most important event in this development during the period under consideration, it is concerned with examining the international advocacy of Australian economists in order to better account for the wide acceptance of Keynesian economics after 1936. Still comparatively small, the existing literature concerned with the question of Keynes and his influence in Australia has yielded many insights into the interactions of economic theory and policy. It is, however, a literature that has a number of shortcomings, some of which have been identified above. Primary amongst these, with the exception of the work of Neville Cain, has been the neglect of many of the economic writings of Australian economists (especially, but not exclusively, concerned with international matters) before the publication of the *General Theory*, from which the seeds of their later thought can be readily identified. In the absence of detailed work on this period, perceptions of economic thought in Australia have tended to be drawn from a number of high profile episodes (the 'Premiers' Plan' is a notable example), the consequence of which have been incomplete and distorted accounts.

A point made throughout this study is that a focus on the international advocacy of the period is important in that it exposes the researcher to the economic thought of Australian economists free from the ubiquitous constraint of the current account. It is possible to trace a path through the work of the Australian economists at Ottawa and the World Economic Conferences, through the work of McDougall and through the advocacy of Australian economists in international forums up to and during the Second World War to reveal an incremental progression of a constant theme of policy expansionism. To some extent this is due to the fact that, as a country dependent on overseas markets for its survival, Australia could be expected to be in the vanguard of movements calling for expansionary policies to be applied beyond its shores. Right up to the present day, Australian Governments and their economist-advisers have taken positions which have called for policies overseas that they would not have countenanced at home. Nevertheless, the advocacy outlined in this study reflects more than merely a merchant's interests in obtaining customers. The study has emphasised that, throughout this advocacy, there existed a profound scepticism of orthodox neoclassical theory, a tendency to view the economy in macro as well as micro terms, a recognition of the implications of 'money' in the economy and conceptual novelty



(if undeveloped) in the recognition of multipliers and marginal propensities to consume. In short, a world view which evolved from 'proto-Keynesianism' in the 1920s and 1930s to a more explicit and developed Keynesianism in the 1940s.

### *The evolution of economic ideas*

Implicit in the motivation for this study is the proposition that changes in economic thought, and changes in the way such thought is received and implemented, do not occur as inexplicable events, or as acts of revelation after which a new world dawns free from the shibboleths of the past. This is not to say that the process of change in economic thought is necessarily or wholly incremental, but rather that typically it occurs in a context that has evolved in such a way that it is ready to receive something which may be regarded as revolutionary. This is perhaps not such a controversial point - it is implicit, for example, in most texts concerned with the history of economic thought which attempt to connect with at least a rudimentary sociology of knowledge for economics. In such accounts, the process of change in economic thought is often divided into two competing ideas - a 'relativist approach' which highlights historical, sociological, political and economic forces which provoke the investigation of certain economic problems, and an 'absolutist approach', which is more concerned with intellectual developments within the economics profession itself as being the promoter of change.<sup>626</sup> Within this latter idea there is a tacit belief that the process of change in economic thought is one in which logical error is progressively eliminated and greater areas of truth are gradually opened up. Both of these approaches have been more or less influential at various times, but most texts and general histories of economic thought have tended to employ elements of both and to neglect somewhat the question of a sociology of knowledge for economics. In either case, change in economic thought and its acceptance is a gradual, if not necessarily linear, process.

### *Implications of the Inclusion of International Advocacy*

This section examines the implications of including the advocacy of Australian economists internationally for the Keynesian revolution in Australia. This is done by employing some of the most influential frameworks used to consider the evolution of economic ideas - those of Schumpeter, Thomas Kuhn and, more recently, Douglass North. This present work does not attempt to critique these frameworks in any comprehensive way, but simply demonstrates how each could be consistent with the evolution of thought as contained in the international advocacy of Australian economists. Upon the broader question of the evolution of economic thought, this author could only agree with the argument of Hutchison (1978), that any worthwhile explanation of fundamental changes in economic thought will be complex and inclusive of accounts that are probably more complementary than they are contradictory. This will leave explanations that are 'untidy and indecisive', but a 'neatly exclusivist or monistic account will not do justice to the complexity of the actual processes' (Hutchison 1978, p.317).

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<sup>626</sup> These approaches are also sometimes labelled 'external' (highlighting the historical, sociological, economic and other forces from outside the discipline) and 'internal' (the rational construction of thought within a discipline). For a critique of these labels, see Hutchison (1978), pp.295-306.

## Schumpeter

Joseph Schumpeter was a pioneering scholar of a sociology of economics whose work accounting for the evolution of economic ideas is consistent with the above.<sup>627</sup> In his monumental *History of Economic Analysis*, Schumpeter advanced a ‘primitive’ but ‘not...misleading statement of the process by which we grind out...scientific propositions’ that highlighted the role of the pre-analytic ‘vision’ that preceded changes in more formal theorising (Schumpeter 1954, p.41). This vision, which Schumpeter regarded as providing the ‘raw material for the analytic effort’, consisted firstly of the recognition (by an individual or society more generally) of a set of phenomena which may or may not have been considered within the boundaries of established science (Schumpeter 1954, p.41). Out of this recognition came the verbalising or labelling of the phenomena in a way which facilitated ‘recognition and manipulation in a more or less orderly schema or picture’ (Schumpeter 1954, p.41). From this stage there subsequently emerged ‘theoretical’ work and ‘scientific models’ in a process in which the original vision was transformed by the application of ‘more rigorous standards of consistency and adequacy’ (Schumpeter 1954, p.42).

In support of his conception of the evolution of economic ideas, Schumpeter cited the development of Keynes’s own thought. As the ‘outstanding success of the 1930s’, Schumpeter regarded the *General Theory* as a plausible ‘apparatus designed to give convenient expression to certain facts of “the world in which we live”’ (Schumpeter 1954, p.41). It ‘antedated all the analytic efforts that Keynes and others bestowed upon it’ and was the final formulation of a vision, ‘as yet analytically unarmed’, which Schumpeter identified in Keynes’s *Economic Consequences of the Peace* (Schumpeter 1954, p.42).<sup>628</sup> According to Schumpeter then, ‘the whole period between 1919 and 1936 was...spent in attempts, first unsuccessful, then increasingly successful, at implementing the particular vision of the economic process of our time that was fixed in Keynes mind by 1919 at the latest’ (Schumpeter 1954, p.42). Schumpeter wrote that other theorists at other times had demonstrated analogous processes of intellectual development, but that in the example of Keynes, this thesis stood out as one of ‘unsurpassable clearness’ (Schumpeter 1954, p.42).

As for Keynes, so as for the Australian economists. In the case of the professional economists, the *General Theory* did not fall upon virgin soil but upon a profession that to a large extent had been both consumers and synthesisers of the economic thought of Keynes and others for many years. This being the case, their acceptance of Keynesian economics, in the context of Schumpeter’s framework, was perhaps little different than the process of *innovation* had been for Keynes himself - less a sudden realisation of the ‘truth’, than an acceptance of a more plausible expression of what they saw around them. Even for the amateurs like McDougall, the Schumpeterian model has much to recommend it. McDougall did not pre-empt or even necessarily subsequently *follow* the theoretical contributions of Keynes, but his voice was one of

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<sup>627</sup> Schumpeter’s approach, notwithstanding the breadth of his scholarship but reflective of the contemporary intellectual fashion, was quite unambiguously biased towards an ‘absolutist’ interpretation of the development of economic ideas.

<sup>628</sup> In the view of this author, this is far too early with respect to Keynes’s most significant insights. The *Tract on Monetary Reform* and the *Treatise of Money*, neither of which carried his full vision, were still six and eleven years away respectively in 1919.

a number to articulate a 'pre-cognitive vision' of economic phenomena - that 'less completely systemized sets of opinions on economic subjects that, at any time and place, "float in the public mind"' (Schumpeter 1954, p.41). Though such opinions might have been analytically unarmed, and though largely derivative the advocacy of Australian economists abroad might have been, they were suggestive of a more fertile environment within which Keynesian ideas could take root than that suggested by concentration upon domestic advocacy alone.

### *Kuhn*

One of the best-known attempts to construct a theory of change in scientific ideas, and one of the very few to have been applied by scholars to economics, was the 'paradigm switch' hypothesis of Thomas Kuhn. According to Kuhn, 'normal' scientific work proceeded within paradigms - a term which he appropriated to describe the 'universally recognised scientific achievements that for a time provide model problems and solutions to a community of practitioners' (Kuhn 1970, p.vii). Paradigms defined and limited what was acceptable in the way of a discipline's methodology and the types of problems which it could examine and hence provided the terrain in which 'normal science', the actual work undertaken by the majority of practitioners of a particular discipline, was undertaken. Intellectual discovery within the boundaries of normal science was incremental and was seldom, if ever, concerned with novelties, 'conceptual or phenomenal' (Kuhn 1970, p.35).

This did not mean that the progress of scientific *ideas* was incremental. According to Kuhn, the incremental advance of normal science was punctuated by incidents of scientific revolution that Kuhn called 'paradigm switches'. Such switches were the result of anomalies - 'crisis-provoking problems' for which existing science had no answer or even any conception (Kuhn 1970, p.144). Eventually though, some practitioners in a discipline would confront such anomalies and in the process 'subvert the existing tradition of scientific practice' (Kuhn 1970, p.6). Such a process would not occur overnight since it was preceded by an attempt to assimilate the anomaly within existing science. Then 'the extraordinary investigations' would lead the profession at last 'to a new set of commitments, a new basis for the practice of science' (Kuhn 1970, p.6). A paradigm switch necessarily involved the replacement of one set of theories with another. This was a dynamic process rather than an instantaneous one, and was 'seldom completed by a single man' (Kuhn 1970, p.7). This dynamic story caused problems for historians though, whose vocabulary, according to Kuhn, conditioned them to view such revolutions 'as an isolated event' (Kuhn 1970, p.7).

Kuhn's paradigm shifts were confined to 'persuasive argumentation' within expert groups and though seldom brought to fruition by individuals, were provoked by individuals 'who first learn to see science and the world differently' (Kuhn 1970, p.144). Such individuals may or may not be on the right track towards the new paradigm since, according to Kuhn, a period of 'paradigm breakdown' was one in which there was typically a proliferation of new theories in an environment of 'profound professional insecurity' (Kuhn 1970, p.67). The majority of these theories were 'speculative and unarticulated' and though they could 'point the way to discovery', were not themselves sufficiently inclusive of the scientific corpus or

revolutionary enough to be the paradigm shift itself (Kuhn 1970, p.61). In Kuhn's framework, it took a relatively fully articulated paradigm to replace another. He also speculated that the individuals behind change would more than likely be young, and therefore less committed than established practitioners 'to the world view and rules determined by the old paradigm' (Kuhn 1970, p.144).<sup>629</sup>

### *Applications and Extensions of Kuhn*

The potential for the application of Kuhn's hypotheses to economics was recognised relatively early by economists with an interest in such matters.<sup>630</sup> Coats (1969 [1993]), for example, regarded it as an appropriate framework within which to consider change in economics - not least because throughout its history economists had 'persistently striven to emulate the natural scientists' methods' (Coats 1993, p.58). The paradigm concept was also regarded as being readily applicable to economics, dominated as its history had been by one single paradigm - 'the theory of economic equilibrium via the market mechanism' (Coats 1993, p.60). Scientific revolutions of the sort painted by Kuhn had been apparent in economics, though, such as the rise of classical economics itself, the *Methodenstreit* between Austrian and German economists in the nineteenth century and the 'marginal revolution' (Coats 1993, p.93). Kuhn's framework did not always provide an exact fit in these and other circumstances, but it gave, according to Coats, 'precision' to the process identified by Schumpeter and protection against overly 'deterministic' sociological theories (Coats 1993, p.61). For Coats, the clearest example of a paradigm shift in economics, however, was the Keynesian revolution - a 'unique event' which demonstrated almost all the features of profound change identified by Kuhn - from the unrecognised and incomplete precursors, the crisis in orthodox economics which meant that it could not even conceive of the real problem, to the fact that the change, when it came, was mostly led (Coats noting the exception of the 'Pan-like' figure of Keynes himself) by a younger generation of scholars (Coats 1993, p.61).

Deane (1978) was also impressed by the possibilities suggested by a Kuhnian approach to economic thought. In a thorough application and critique of Kuhn's ideas in relation to several episodes in the history of economic thought, Deane noted the various objections which had been raised against the concepts of paradigms and paradigm shifts. Most significant of these were those raised by philosophers of science (including Karl Popper) concerned with the implied irrationality of scientific practitioners in adhering to paradigms for reasons not necessarily exclusively to do with logic. This was not a difficulty for the history of economics, studded as this history was with the adherence to theory for reasons 'beyond the range of logical evaluation of its explanatory power' (Deane 1978, p.xiii).<sup>631</sup> Despite 'rhetorical exaggeration' in the concept of paradigms (which implied for economics a knowledge of their discipline which probably went beyond that understood by the average economist), Deane thought that the Kuhnian framework brought out more effectively

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<sup>629</sup> Kuhn (1970, p.156) did not neglect what he regarded as a likely greater aesthetic appeal of new ideas to younger practitioners of a discipline.

<sup>630</sup> The first attempt to apply Kuhn's ideas to economics was probably Gordon (1965).

<sup>631</sup> This is not to say that Kuhn's ideas were ever unanimously accepted by the economics profession as being relevant to their 'science'. Colander (1998) for but one example of a number of similar critiques, regarded the economics discipline as too pluralistic to ever have been a perfect fit for Kuhn's conception of a paradigm.

than any other ‘the connection between the socio-historical development of professional schools of thought and the intellectual development in the theoretical content of a discipline’ (Deane 1978, p.xii). Moreover, while there were dangers in using such terms as ‘paradigms’ and ‘revolutions’, it was ‘scarcely in dispute that there have been ruling paradigms in economics in that the textbooks describe a related set of theories, concepts and analytical techniques accepted as authoritative...by a majority of economists, and that there have been radical changes in the structure of economic doctrines which determine the generally accepted problem situation’ (Deane 1978, p.xii).

Like Coats, Deane also regarded the Keynesian revolution as the quintessential example of a paradigm shift in economics. According to Deane, the endemic unemployment in all capitalist economies in the 1930s rendered the existing paradigm of orthodox economics an anachronism, its assumptions nevertheless maintaining a ‘stranglehold on conventional economic analysis’ (Deane 1978, p.175). The *General Theory*, by contrast, asked and attempted to answer the question of moment - the determination of employment and output - a question which existing theory did not seem to address. Of course, as Deane noted, Keynes himself was quite aware of the revolutionary nature of his work and, in a Kuhnian sense, his account of what constituted ‘classical’ economics (however self-serving this might have been) was an attempt to define the currently dominant paradigm (Deane 1978, pp.175-179). Deane was clear that the publication of the *General Theory* signified the arrival of a new paradigm, but she regarded Keynes own revolution as beginning as early as 1924 with his essay *The End of Laissez-Faire*.<sup>632</sup> That this personal revolution became a more universal one from 1936 was simply because the ‘time was ripe’. The *General Theory*’s

abstractions seemed more relevant to the conditions of the 1930s than the competing theories. Its analysis gave a theoretical basis for policy prescriptions that were more in tune with existing political trends in a world that was already in massive retreat from a *laissez-faire* ideology. (Deane 1978, p.184)

It is my contention that an analysis of the Keynesian revolution in Australia which includes the international advocacy of these economists provides a better fit for a Kuhnian story of paradigm change than analyses that overlook this work. As noted above in the brief review of works concerned with the Keynesian revolution in Australia, a focus upon domestic advocacy alone can leave the researcher with the impression that Australian economists were reluctant advocates of expansionary economic policies because of theoretical commitment, rather than what was perhaps an overriding concern for the country’s external position. None of this is to say that the domestic advocacy was free of the sort of paradigm crisis which precedes paradigm change, for clearly it was not, but equally such a crisis is so much more apparent when the full picture, including the balance of payments constraint, is considered. In this context, the work of McDougall once again could be likened to the pre-paradigm experience when ‘speculative and unarticulated theories’ pointed the way, suggesting something of the *zietgiest*, but not themselves representing paradigm

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<sup>632</sup> As we have seen, Schumpeter dated its beginning as 1919 and the publication of *The Economic Consequences of the Peace*.

change. The advocacy of the Australian economists at Ottawa and the WMEC likewise were suggestive, not only of professional insecurity but also of the ‘ad hoc modifications’ to existing theory of the variety identified by Kuhn. Since it took a new paradigm to replace an old one in the Kuhnian framework, the Australian efforts would have to await the appearance of the *General Theory* before they could be caught up in a genuinely revolutionary movement. Such movements require that the ground be first prepared. The advocacy of Australian economists abroad in the interwar years was in the Australian context, as in the rest of the world, indicative that the time was ripe for something new.

Deane’s judgement as to the applicability of Kuhn’s framework for economics was not shared by a number of others in the profession in the years in which its impact was being most strongly felt. Hutchison (1978, p.314), though noting that it provided some useful parallels and analogies, believed that it would be ‘misleading and presumptuous to assume’ that what might apply in the natural sciences could ‘also yield accurate and significant lessons in the case of economics and the social sciences’. The structure and behaviour of the physical world was immutable, this was not true of the economic universe. Friedman (1970), Hicks (1975), Blaug (1976), Kunin and Weaver (1971), took similar positions, arguing that changes in economic thought were fashioned by changing external circumstances rather than rational progression within the discipline itself. Stigler (1973) and Johnson (1975) equally took an historically relativist position, albeit with an emphasis on the sociology of shifting values and conventions of the discipline, but where the ‘success for a new theory...depends upon its fitting appropriately into the intellectual climate of its time’ (Johnson 1975, p.305).

In recent times, meta-theoretical analyses of how scientific ideas change have fallen out of intellectual fashion.<sup>633</sup> Modern scholarship concerned with the history, philosophy and sociology of science has become disdainful of approaches suggesting the universality of theories and principles in favour of approaches which are more local and defined in their scope and much less willing to advance generalities. Instead of exploring scientific ideas from principles to practice, they have attempted to examine exactly what it is that scientists do in certain circumstances and analyse these efforts relative to the localised criteria of their objectives, rather than against some set of universal norms or theoretical attachments. Overly reductionist perhaps, these modern approaches are, in the view of one of the few economists to have considered them in relation to economics, more ‘genuinely historical in [their] goals and methods’ than those of earlier generations (Coats 1993, p.38)<sup>634</sup>.

However, such modern scholarship concerned with the evolution of scientific ideas has yet to be systematically applied to economics, and hypotheses such as those advanced by Kuhn remain influential in the sociology of economic knowledge (Coats 1993, p.37). The application of more recent approaches would make no difference to

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<sup>633</sup> In the context of studies of scientific progress more generally, Kuhn’s own work by now is regarded as a classic - that is, an out of date but seminal work that is rarely used or read.

<sup>634</sup> For a survey of this modern scholarship, and its possible uses for economics, see Coats (1984) and Coats (1985).

the central idea advanced in this study, however, and its conclusions regarding the advocacy of Australian economists abroad and the implications of this for the Keynesian revolution in Australia. Indeed, this study is an example of a localised and contextualised research project. Australian economists, it has been argued, had a predilection throughout the interwar years for expansionary policies (as manifested in their advocacy overseas) but were prevented in applying these at home because of the particular constraints of Australia's external position. In the absence of the global expansion for which they were arguing they were forced to advance contractionary policies for the domestic economy. Similarly, that the economists were able to advocate expansionary policies at home after the publication of the *General Theory* and *after* the beginning of the Second World War was likewise to do with particular events rather than theoretical adherence.<sup>635</sup> One of these events was simply the war itself, which created the circumstances for a great number of domestic institutional changes (the influx of young economists into the public service, the empowerment of the Federal Government in the economy, the existence of controls and so on) conducive to the application of Keynesian economics. Another, equally important, factor was that Keynesian economics itself provided for an alternative framework for the global economy (the Clearing Union and related proposals) which promised the potential at least for the alleviation of the traditional systematic external/internal balance dichotomy. Too often relegated to the shadows by the preliminary closed economy analysis of the *General Theory*, such international considerations had always been part of Keynes's schemes but had been blunted by political forces in the years before war provided the necessity for the reconstruction of the international economy.

### *North*

The emergence of 'new institutional' political economy, and in particular the work of 1994 Nobel Laureate Douglass North, has introduced new methodologies within which to consider the evolution of economic ideas. North, who was chiefly concerned with finding out the reasons for the evolution of efficient markets, economic *and* political, began as a theorist convinced of the efficacy of neoclassical theory as a tool for examining economic history. This conviction, which was at the heart of the so-called 'new economic history' often identified with him, was subsequently abandoned by him in favour of a growing, contrary, conviction of neoclassical economics *inability* to account for change.

According to North, markets (including those of ideas) evolve through the interactions of 'institutions' and 'organisations'. By institutions North meant 'the rules of the game of a society'. They consist of formal rules (common law, statute law, government regulations and so on) as well as the much broader set of informal rules, conventions, and norms which regulate social behaviour (North 1995, p.10). Institutions then, are 'constructs of the mind' which collectively form the 'belief system' of a society (North 1990, p.107). Organisations, on the other hand, operate within the institutional setting and are groups bound by a common purpose. These groups could be political (political parties, bodies representing particular interests,

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<sup>635</sup> Even then, of course, the policies employed and the general approach was decidedly local - to which the repeated attempts of Australian economists to modify Keynes international schemes to suit Australia's interests also bore witness.

political entities such as legislatures and local government), economic (corporations, cooperatives, trade unions), social (religious, sporting, cultural) or educational. In North's schema, it is the attempt by organisations to advance their interests that is the primary motor for institutional change (North 1995, p.10).

The attempt by organisations to further their ends is tempered, however, by the institutional framework. Institutions, as constructs of the mind, will necessarily shape the direction of intellectual inquiry and, as such, knowledge and skills (if these are the outcomes desired by an organisation) will be acquired only to the extent 'tolerated' by society (North 1990, p.75). Such acquisition is a two-way process, though, for just as perceptions of what is possible will be shaped by the institutional setting, so will knowledge shape perceptions of what is possible. The implications of this for the evolution of economic ideas (and especially their application in policy) is that change will be largely incremental. Revolutions will occur when new organisations emerge which have different interests - 'typically as a result of dissatisfaction with the performance of existing institutions' - and the resultant conflict between the old and the new which cannot be accommodated within the existing institutional setting (North 1995, p.11). Even revolutions will not be as 'revolutionary' as they might at first appear, however, for while formal rules can be changed immediately, the informal rules and constraints will change much more slowly:

It is essential to change both the institutions and the belief systems for successful reform, because it is the mental modes of the actors that will shape choices...the degrees of freedom that policy makers possess to alter the direction of economies are constrained by the intellectual matrix and the belief systems of the players. Of all the implications of institutional analysis for policy, this is the most important (North 1995, p.12.)

In the context of the evolution of economic ideas, North's framework in many ways is simply a more systematic rendering of Schumpeter's conception of the development of economic theory. Schumpeter's idea of the pre-analytic vision which precedes formal reasoning, for example, is analogous to the collective 'belief systems' out of which formal rules must emerge. In the specific example of the Keynesian revolution - the political side of which was a revolution of formal rules (policy) via the agitation of a number of 'organisations' - ultimate success was the result of a process in which the new formal rules were a better fit for an institutional setting which had been evolving in a favourable direction for some time. The fact that Keynes himself, through many previous unsuccessful attempts at formal rule changing, had been a part of this change in the institutional setting is, in terms of North's framework, perhaps the greatest of his achievements.

As with Schumpeter, North's framework provides considerable support for the proposition advanced in this study as to the nature of the Keynesian revolution in Australia. As with the Keynesian revolution more generally, the adoption of Keynesian ideas in Australia can be considered a part of a longer process through which the institutional settings (and the possibilities for policy) were slowly evolving. The institutional framework was not favourable at the time of the economists' forays at Ottawa or the WMEC, nor was it favourable when McDougall was attempting to hawk his ideas to the centres of economic power. All, like Keynes's advocacy before



1936, were organisational attempts to change the rules in times less predisposed to allow their admittance. Nevertheless, all were indicative of a frame of mind, and all helped to prepare the ground for riper times. These arrived with the Second World War. The employment approach, a campaign 'more Keynesian than Keynes', was the theoretical edifice of the earlier efforts.

## **Section V**

### **Concluding Comments**

## **Chapter Eleven**

### **Conclusion**

It has been the purpose of this study to make a contribution to the history of economics in Australia by examining the thought of its prominent economists relating to international questions from 1925 to 1950. This was a period in which hegemonic instability was the prevalent feature of the international economic order. Their advocacy, across generational and professional/amateur divides, contained within it a strong expansionary theme in its policy propositions. It also represented a theoretical context within which the macroeconomic revolution instigated by Keynes was capable of being quickly assimilated and propagated. Held to be distinctive of Australian economists by foreign observers, this advocacy deserves to hold a significant position in that pantheon of views that have come to be regarded as characteristic of Australian economics. The pantheon, hitherto dominated and represented by the 'defensive' posture of Australian economic thought as manifested in 'New Protection', 'protection all round', and associated philosophies, is challenged in this study which takes a more comprehensive and positive view. This view is one in which Australian economists were not simply passive and contractionary in the face of external constraints but, indeed, were energetically engaged in policies of global expansion, which by alleviating these constraints, would permit domestic expansion and the maintenance of full employment.

The absence of much of the advocacy outlined in this study from the established discourse of Australian economic thought is unfortunate because it leads to a misleading portrayal of events of recent years in which, once more, Australia has been active in international economic debate. This recent engagement, which has concerned Australia's efforts since the early 1980s to assemble a global coalition of countries committed to free trade in agriculture and a free trading bloc in the Asia-Pacific region, has taken place without reference to earlier campaigns.<sup>636</sup> Indeed, it has sometimes been regarded as representing a newly independent and assertive Australia making its mark in the world free from the subservience of traditional alliances. The efforts of Australian economists in propagating the employment approach, the nutrition approach and expansionary monetary policies, made use of Australia's traditional relations with greater powers, but they were hardly representative of supine genuflection to external authority which is sometimes used to caricature Australia in that era. The fact that the latest of Australia's efforts to influence international economic policy making has been concerned with *free trade*, moreover, and with deliberately subordinating domestic policy to the requirements of the external sector, says much about the dramatic changes in Australian economic thought over the previous half century. That this turnaround has been largely ignored within mainstream economic literature, or even been presented as simply the natural

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<sup>636</sup> That is, Australia's leadership of the 'Cairns Group' of commodity exporting countries and its high-profile involvement in the regional Asia-Pacific Economic Cooperation (APEC) initiatives.

outcome of a 'getting of wisdom' of the 'true model', also says much about the paucity of current understanding of our national history and the dominance of the North American discourse within the economics profession.

Nor were the efforts of Australian economists outlined in this study wrong or merely self-interested. The overwhelming problem of the world economy of the interwar years was not, as the doctrines in opposition to those presented here so constantly asserted, the growth of barriers to trade, but the collapse of international aggregate demand. This collapse in demand, precipitated in the United States and exacerbated by counterproductive policy responses in most countries and the deflationary bias of the prevailing gold exchange standard, was the greatest economic problem of the interwar years. The growth of trade barriers and the collapse of international trade were prominent symptoms and effects. The loss of national income from countries failing to take advantage of international specialisation must have been large, but it could only have been a tiny fraction of that lost as a consequence of the extraordinary levels of unemployment experienced by most countries during the Depression. Attempting to 'export' unemployment through the erection of trade barriers only made things worse globally, but it was an understandable response in a system which allowed for little else. As documented in this study, the Australian efforts to promote global expansion were generally unsuccessful, but contrary to their opponents, they at least identified the real problem.

The advocacy of Australian economists outlined in this study was also theoretically sophisticated. As demonstrated, the gains from specialisation which are the *raison d'être* for free trade, are based upon an explicit assumption of full employment. The gains from free trade are gains that arise from expansion of aggregate supply supported by a concomitant and necessary increase in aggregate demand. However, in the absence of sufficient domestic demand, and with the adoption of the doctrines of 'sound finance', export-led growth *at the expense* of one's neighbours is the only option for domestic prosperity. This is what happened in the interwar years, and it continues to occur up to the present day. The lesson was learned for a time when, because of political, military and other accidental reasons, the United States provided the global effective demand that alleviated the deflationary bias implicit in an international monetary arrangement that continued to *assume* full employment. Although lasting from around 1949 to 1973, this period could not endure because of the temporary circumstances prevailing in one country alone, but it was at least a reminder of what was possible.

It may help the reader draw the threads together if the main arguments of this study are briefly reviewed. In the four sections of the study, continuity has been a strong theme, not only through the central theses but also the re-appearance of particular participants.

Section I focussed on the first generation of professional economists in Australia in terms of their advocacy of expansionary monetary policies by the major creditor countries as the solution to the global Depression. An advocacy hitherto ignored in considerations of Australian economic thought, its inclusion here, based upon often overlooked archival resources, is a major contribution of this study to the existing literature. The first episode was the advocacy at the 1932 Imperial Economic

Conference in Ottawa for 'cheap money' policies propagated from London. This was the natural outcome of a theoretical posture developed over a number of years as Australian economists absorbed the ideas of writers such as Fisher, Hawtrey and, especially, Keynes. Newly freed from needing to protect the sterling/gold exchange rate, the United Kingdom was committed to a policy of cheap money but its concomitant advocacy of restriction schemes to raise agricultural prices meant that the Australians left Ottawa disappointed. Ottawa was followed up in 1933 by the World Monetary and Economic Conference, at which Australian economists again pursued their monetary line. This advocacy was again unsuccessful and the Conference, the last such attempt for a co-operative global solution to the Depression, ended in ignominious failure. The World Monetary and Economic Conference and its failure prompted a certain theoretical introspection amongst the Australian economists who attended it, and led to a (mostly private) discussion redolent with theoretical innovation. This revealed them to be much less theoretically orthodox than sometimes supposed. In this context, an assessment radically different from existing accounts was offered regarding the contributions of certain economists during the interwar period, in particular Edward Shann and Leslie Melville.

Section II broke with strict chronology to document Australia's foreign economic diplomacy as advanced primarily by F.L. McDougall, an 'amateur' economist who provided in the international sphere a contribution to match that of the long-standing tradition of domestic 'cranks and scribblers' to Australian economic thought. Section II began this exploration of McDougall's proposals for 'sheltered markets' - a post World War One version of the imperial trading bloc. McDougall's model was less about notions of empire building than it was of creating a structure within which the 'anarchy' of the market could be replaced by the application of 'scientific planning' and other devices consistent with 'progressive' opinion during this era.

The next stage in McDougall's advocacy was the 'nutrition approach'. From 1934, disillusioned with regard to the possibilities of empire markets, McDougall, in conjunction with S.M. Bruce, the former Australian Prime Minister and then High Commissioner in London, launched a campaign for improved nutrition via a reorganisation of world agricultural production and trade. Propagated at the League of Nations and by personal advocacy with many political leaders and officials of various countries, the nutrition approach broadened into a campaign to improve living standards more generally. This was advocated not only for its own sake, but also as a device to alleviate the trade cycle. The nutrition approach also expanded into the campaign for 'economic appeasement', taking up that most persistent idea amongst economists that it was in economic prosperity that the solution to conflict between nations lay. The nutrition approach was partially successful in establishing certain international institutions, and was consistent with other movements in a *zeitgeist* providing for an expanded role for the state. As with McDougall's earlier advocacy, the nutrition approach was essentially part of a proto-Keynesian discourse which would prepare the way for the theoretical revolution still to come. The nutrition approach, and McDougall's efforts generally, were by far the best known aspects of what came to be seen as Australia's economic diplomacy in the interwar period. Notwithstanding this, McDougall and his works have been largely ignored by economic historians and historians of economic thought in Australia. This study has attempted to redress this oversight by the use of archival resources in Australia and

overseas which help paint a picture that departs from the conventional view of Australia's role in the world.

Section III concerned itself with Australia's economic diplomacy from 1941 to 1950, that is, after the Keynesian revolution in macroeconomics to the period immediately following the Second World War. The largest section of the study, it explored Australia's 'employment approach' to the reconstruction of the international economy. Developed initially by the economists who had been at Ottawa and the World Monetary and Economic Conference in response to American pressure for the reduction of trade barriers and the elimination of imperial preference, it was quickly taken over by a 'new generation' of Australian economists who were enthusiastic users and proselytisers of Keynes's work. The approach evolved over time according to the issues confronting successive delegations of Australian economists to various international conferences.

In the existing literature, the employment approach had never been comprehensively examined. It was, of course, broadly outlined in a volume of the official history series of Australia's involvement in the Second World War, and various episodes in the campaign have been recalled by their participants, but no comprehensive examination of it had been undertaken. This study explores for the first time its theoretical nature in terms of Keynesian analysis and the application of contemporary trade theory. This exploration found that the approach was theoretically coherent and 'correct' within the parameters of a Keynesian analysis of the international economy. It was also concluded that the approach was correct in a broader political economy sense in that the suspicion with which Australian economists tended to view the actions of other nations turned out to be justifiable. The examination of the employment approach was pursued according to primary documents preserved in Australia and overseas, many of which do not figure in the existing literature. This led to a number of interesting revelations, including the extent of Keynes's personal involvement in the advocacy outlined. It also reaffirmed the finding of earlier Sections that accorded Australia a quite prominent and independent role in international economic affairs.

Section IV joined various threads from previous Sections in examining the Keynesian revolution in Australia. The existing literature which accounted for (or denied) this revolution was criticised as almost universally falling short of a complete picture of the theoretical positions of Australian economists because of a concentration on their domestic advocacy alone. This had the effect of portraying Australian economists as much more theoretically 'orthodox' in their opposition to expansionary policies than was in fact the case. Their opposition to expansion, however, assumed the continuation of a severe balance of payments constraint, a chronic problem for Australia made acutely worse in the Depression years. But this portrait of Australian economists changes once their international advocacy is taken into account, advocacy that reveals them to be more than just theoretically receptive to Keynes's message in 1936. The take-up of Keynesian economics in Australia was not some sudden Pauline conversion, but a continuous process. It was also noted that this explanation of the Keynesian revolution in Australia is much closer to existing explanations of the evolution of economic (and other) ideas, than alternative tales of blinding revelation.

## **11.1 Extensions of This Research**

The most obvious extension of this work is to relate it to more recent times. That is, to trace developments from the cessation of the employment approach in 1950 to Australia's economic diplomacy with regard to the emerging markets of the Asia-Pacific in the 1980s and 1990s. The search for, or promotion of, expanding markets has, as this study has noted, been the *leitmotif* of Australia's economic engagement with the rest of the world. By the early 1950s, attention was already beginning to shift (as indeed, the prescient comments by Coombs noted in Chapter 9 attest) to our immediate region as an area of trade growth. In this context, the Colombo Plan, the Treaty with Japan in 1957, Australia's support for various decolonisation movements as well as the more recent Cairns group and APEC initiatives would feature.

Conversely, another desirable extension of this research would be backwards in time. Schedvin's (1970) call for more work to be done on the activities of Australian economists in the latter half of the 1930s has, remarkably, yet to be taken up in any comprehensive way. It is this period from which most can be discovered as to the nature of any take-up of Keynesian analysis prior to the Second World War. This study has examined the international policies of certain economists and the extent to which they developed along these lines, but a comprehensive treatment of the profession as a whole in the period is sorely needed.

Finally, there is a need for a critical examination of what might be called the great 'turn-around' of Australian economic thought with regard to trade policy. The last fifty years, and in particular the last two decades, has seen a remarkable reversal in protectionist sentiment in Australia. A foundation stone of Federation, protection today is anathema to the majority of the economics profession, if not necessarily to the community as a whole. The reasons for this extraordinary change would yield much in understanding the transformation of economic and political ideas, and might throw light on the nature and continuing existence of an identifiably *Australian* tradition of economic thought.

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