SUMMARIES OF LECTURES in ECO 303Y1:

the Economic History of Modern Europe, to 1914

for the Academic Year: 2012 - 2013

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Updated: Thursday, 28 March 2013

XXIII: Week no. 23: Lecture Topic no. 29, Part A: 27 March 2013

VII. PROBLEMS OF THE BRITISH AND INTERNATIONAL ECONOMIES, 1870 - 1914:

A. Economic Trends, 1870 - 1914: 'The Great Depression' and After

1. **Introduction: Problems in the British Economy, 1870 - 1914:**

For an overview, we considered four interrelated debates about the British economy, from 1870 to 1914, all of which are major essay topics, for this term:

a) **Industrial Retardation:**

(1) did the British economy experience a decline:
(2) and was it an absolute decline or a relative (to the past, and to other countries)?
(3) 'Retardation' indeed means 'slowing down', slower rates of economic growth;

b) **Was British entrepreneurship responsible for this 'industrial retardation', or relative decline?**

(1) Much of this topic has already been analyzed in studying German industrialization, where evidence was presented to indicate social, economic, cultural, and political reasons with negative effects on British entrepreneurship in this period. Read the lecture notes on Germany
(2) Did British business experience a 'Buddenbrooks' syndrom? Read the lecture notes.

c) **the Era of 'New' or 'Capitalist' Imperialism, and the role of capital exports:**

(1) We discussed the Marxist-Leninist thesis behind this debate: that the export of capital, as it did occur in ever larger amounts from the 1870s, was ipso facto Imperialism,
(2) with economic dominance over new colonies, principally in Asia and Africa, that did not require outright military conquest; but also economic dominance over other areas of the world.
(3) Statistical evidence was presented to show the large increases in British capital exports from the 1870s,
(4) and also evidence to show that the British were investing proportionately far more of their capital abroad than at home.

d) **Did Great Britain also experience a 'Great Depression', during the shorter period of 1873 - 1896:**

(1) was that an international or domestic phenomenon;
(2) and if the latter, was it closely related to the three other problems under examination?

2. **Key aspects of the 'Great Depression' debate: also involving the 'industrial retardation' debate:**

a) **Public Perceptions of a 'Great Depression':** from foreign trade and prices.

b) **Steep Deflation experienced in this era:** unprecedented since the 'late medieval Great Depression', during the later 14th century.

i) **Falling prices is not a trivial phenomenon:** because it generally means, for industrialists and tradesmen, that their product prices are falling, while their real factor costs -- for labour (wages), capital (interest) and land (rent) -- are rising in real terms (even if stable in nominal terms).

ii) **But such price-cost squeezes, resulting from deflation,** can themselves be the vital trigger for productive innovations.

c) **Agriculture:**

i) Certainly British agriculture experienced, if not a 'depression', a severe contraction in the face of a flood of foreign agricultural imports, with a gold-standard base Free Trade regime

ii) unlike most other countries, which had abandoned Free Trade, to restore tariffs to protect their farmers.

d) **Foreign trade:**

i) experienced certainly periodic slumps after 1870-4;

ii) and British exports did not recover that level until 1895-99.

iii) **As Arthur Lewis noted, British trade experienced four problems:**
(1) the loss of foreign markets to industrial growth in those countries, in so far as they established import-substitution industries;
(2) the invasions of those markets by British competitors;
(3) barriers to most foreign markets with rising protective tariffs; and finally
(4) invasion of British home markets by foreign competitors. We had earlier noted the invasion of German steel products, from the 1890s.

e) **Capital investments, domestic and overseas investments:**

i) statistical data was again shown to demonstrate that the British were investing a far smaller share of their national income in domestic capital. than did the Germans, in particular,

ii) and correspondingly an increasingly larger share in foreign capital investments.

iii) Did the British come to rely far too much on overseas earnings at the expense of their domestic economy: i.e., by investing too little in domestic manufacturing and other potential areas of growth?

f) **The Unemployment Question:**

i) most people, rightly or wrongly, associate 'depressions' with high and higher levels of unemployment. Was that the case in Great Britain from 1873 to 1896?

ii) employment statistics, from two sources, were presented:
(1) while unemployment rates did rise, somewhat during the period of the so-called Great Depression,
(2) they did not rise above 6% for any five year periods,

iii) and were far from the truly high rates experienced between World War I and World War II (and were lower than current rates in Canada).

g) **Levels of National Income (NNI and NNP) and the concept of 'Depression':**

i) There is no agreed upon definition of the word 'depression' a term that some restrict to the historically unique circumstances of the world economy, 1929 - 1939.

ii) We all agree on the meaning of the term 'recession': a net decline in real NNI and NNP over two successive quarters of the year – hence a short-term phenomenon.

iii) Possibly we may define 'depression' as a far deeper and far more prolonged recession.

iv) If so, the national income data for the UK do not substantiate a 'depression' thesis, since (as the tables in the notes show) there was no significant decline recorded in NNI, which indeed continued to grow, even if slowly, through the entire period: thus negating any concept of 'depression' (a deep and prolonged recession).

h) **Conclusion:** while there were periodic recessions and trade slumps, there was no 'Great Depression'.

3. **The Deflation of 1873-1896: monetary or real causes?**

a) I**n terms of the Fisher-Friedman quantity theory of money,** we can argue that this deflation was essentially the product of monetary stagnation, on the monetary side, and cost-cutting, thus price-reducing technological changes on the real side:

b) **consider the Friedman equation of exchange:** $M.V = P.y$, in which 'y' stands for real net national product,

i) 'y' or real NNI steadily grew, thanks to technological changes, capital investments, and a vast expansion in world trade

ii) we reviewed the extent of technological changes in both production and trade (transportation) that led to world-wide falls in most commodity prices

iii) and NNI grew to a much greater extent than did the volume of money payments.

c) **The Gold problem:**

i) at the same time, world gold mining slumped (with no new mining booms), so that available world gold supplies did not increase to keep pace with increased volume of world production and trade.

ii) In era of gold-backed currencies, the declines in world gold mining and transfers of gold for various purposes (monetary and industrial), inhibited monetary expansion, to explain the deflation, but one in which real factors were just as important, indeed more important, as indicated above.

4. **The World Inflation of 1896-1914:** the pre-War boom

a) **here, the real factors do not provide a convincing explanation of this pre-war inflation:**

i) we can hardly argue that the tempo of technological changes slowed down

ii) Arthur Lewis: rising marginal costs in world agriculture, leading to rising food prices: but than can hardly explain an overall rise in prices, i.e., genuine inflation.

iii) Rostow's Keynesian thesis, as an exception: on the changing nature of capital investments:
(1) with far longer periods of gestation, in technologically more complex forms of industrial growth,
(2) combined with economically wasteful investments in rearmament,
(3) so that capital expenditures created incomes not matched by an immediate increase in consumer goods, etc. [that is, an increase in both I and G, in terms of the formula, Y = C + I + G + (X-M).

b) **Money and Gold:**

i) For this inflationary era, the prime cause must be sought in monetary factors:

ii) especially the major new gold mining booms -- of South Africa and the Yukon -- along with substantial increases in gold mining in much of the rest of the world.

iii) Graphs were shown to demonstrate the exponential increase in gold stocks from the 1890s to World War I.

5. **Productivity changes in the British economy, 1870 - 1914:**

a) **Three sets of data, based on the researches of Charles Feinstein and Arthur Lewis, were presented:**

i) with sometimes conflicting results for individual decades within the overall era of 1870 - 1914.

ii) But they all conclude, in all forms of comparisons, that British productivity, and especially industrial productivity, was lower in the period 1896 - 1914 than it had been in 1873 - 1896, which in turn was lower than the preceding era, back to the 1840s.

iii) All sets of data, with no exceptions, show that the period the poorest productivity performance was from 1900 to 1913

iv) Do these negative productivity data, indicating rising marginal costs, help to explain the rise in prices?

b) **As Deirde McCloskey had earlier contended,** the British economy fared better in the Victorian era (to 1901) than in the Edwardian era that followed (to 1914).

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Section VII. PROBLEMS OF THE BRITISH AND INTERNATIONAL ECONOMIES, 1870 - 1914:

B. British Banking Institutions, 1870 - 1914: experiments in investment banking

1. **Did the British adopt and take up investment banking after 1870:**

a) **The central question to be asked is:**

i) did the British, after witnessing the success of investment or Universal Banking on the continent, decide to follow suit: to engage in investment banking as well?

ii) While there are numerous examples of important investment banks to be found in London, from the 1870s, most of them were internationally-focused merchant banks,

iii) principally engaged in acceptance banking, to finance foreign trade and foreign governments,

iv) and most of them were foreign in origin.

b) **There was some minimal investment banking undertaken:**

i) by these foreign merchant banks, along with some London-based joint stock banks,

ii) they did occasionally engage in forms of investment banking:
(1) in financing overseas railroads and governments,
(2) especially in North America. Some also tried investing in domestic British firms,

iii) but generally without much success.

c) **In general, these investment banks were too small-scale, to be cost effective:**

i) especially the family oriented banks,

ii) far smaller in scale than German investment banks,

iii) to be successful in an area of enterprise that involved very high fixed costs, especially start up costs.

d) **Not until after World War II:** would British banks gain the economies of scale and large capitalizations to become successful in investment banking.

2. **Late 19th century financial disasters:**

a) **The last part of the lecture focused on some financial disasters:**

i) the failure of the City Bank of Glasgow (1878) and

ii) the near collapse of the Baring Brothers bank in the 1890s (lending to bankrupt South American gov'ts)

b) **that also dissuaded British banks from investment banking:**

i) and thus encouraging them to remain wedded to traditional and very conservative deposit and transfer banking,

ii) principally, with short term discounting and short-term loans.