The History of the Twentieth Century
Episode 277
"The Empire Christmas Pudding"
Transcript

[music: Fanfare]

"When it was winter here, it was summer in South Africa, and the fruits have been ripened ready for you to eat them to-day. Try them!"

This message brought to you by the Empire Marketing Board.

Welcome to *The History of the Twentieth Century.*

[music: Opening Theme]

Episode 277. The Empire Christmas Pudding.

Back in episode 224, I shared with you a story from Mrs. History of the Twentieth Century. Her grandparents were farmers, and she recalls them telling her that in their experience, the Great Depression began as soon as the Great War ended. This was the case for farmers in the United States and many other places: Canada, Argentina, Australia, Brazil. After the war, food prices fell and production costs rose, making it difficult for farmers to make ends meet, especially farmers in countries that relied heavily on agricultural exports.

You could say something similar about the entire United Kingdom—not just the agricultural economy, but the entire British economy. After the Great War ended in 1918, the world experienced the post-war economic slump that lasted until 1921 or 1922. Most of the world's advanced economies recovered afterward and experienced impressive growth beginning about 1924, until the whole house of cards came tumbling down, beginning with the US stock market crash in 1929. But the United Kingdom mostly missed the party altogether. The British economy never fully recovered from that post-war slump. The British GDP of 1928 was actually lower than it had been in 1918, ten years earlier.

Why did this happen? The war had cost Britain close to a million dead, about 2% of the UK population, or 4% of its male population, which would be 5-6% of its working-age male population. And you are by now well acquainted with Britain's post-war debt problems. The UK was heavily in debt to the United States and was in turn owed a great deal of money by other allies, who struggled to pay, or sometimes didn't pay at all.

But there were larger factors that reached beyond the effects of the Great War. At the dawn of the twentieth century, Britain had the world's largest economy, and it maintained this economic supremacy through control of a vast colonial empire and a heavy dependence on exports, especially coal, steel, and shipbuilding. But Britain's aging steel industry was losing market share to Germany and the United States even before the war began.

With regard to coal, let me remind you that in the pre-war days, Russian aristocrats celebrating Christmas in St. Petersburg kept their splendid homes warm through the Russian winter with coal imported from Wales. This was not due to any shortage of coal in the Russian Empire; Russia had plenty of domestic coal deposits. But Welsh coal could be mined and shipped to St. Petersburg by freighter for a lower cost than mining domestic coal and transporting it a thousand miles over Russia's dodgy railroads. After the war, this was no longer the case. The new Soviet Union strove for economic independence, while in Britain the best coal seams had been mined out. Coal production was declining, and the costs of mining it were rising.

World trade generally was down compared to the pre-war era, and that meant less business for British shipyards.

New industries were emerging in Britain that took up some of the slack. The British automotive industry, which before the war had produced only small numbers of premium cars for the luxury market, was embracing American-style mass production, led by the Austin 7, which was for Britain what the Model T was for the United States, not to mention Ford's own British subsidiary. British industry was also producing airplanes and motorbikes. Britain made advances in the chemical industry, which had been a German preserve before the war, and in electrification and consumer electronics. Sales of British phonographs and radios boomed—pardon me, sales of British gramophones and wireless sets boomed. Britain gradually gained a domestic film industry to compete with Hollywood. Britain even saw something like the mass consumerism that had taken hold in the United States, although not to the same degree.

But these economic developments were lopsided. These new industries were cropping up in London, the South East, and the West Midlands regions of England, while the old, declining industries dominated the periphery: Wales, Northern Ireland, Scotland, and the north of England. Many families in the South East had electric lights, gramophones, maybe even cars, while in Liverpool or Glasgow, folks kept their homes lit with kerosene and kept their privies in the back yard.

Unemployment remained stubbornly high, especially in those peripheral parts of the country. Taxes that had been raised to meet the demands of war remained high in peacetime, the money now spent to fund war pensions and unemployment assistance, in keeping with David Lloyd George's pledge to make post-war Britain "a fit country for heroes to live in."

And in addition to the bleeding of the British economy through war debts and a shrinking market for British exports, you have to add in the self-inflicted wound of the decision to restore convertibility between sterling and gold at the pre-war exchange rate. I told you that story back in episode 240 and pointed out then that restoring gold convertibility meant subjecting the UK to a painful period of deflation. To achieve deflation, you want the government budget to be in surplus, which in turn means cutting back on the unemployment and pension support that makes Britain "a fit country for heroes to live in." A more expensive currency meant more expensive exports just at the time the British government was trying to increase exports; it means cheaper imports just at the time the British government was trying to reduce imports.

One possible solution to this balance of trade problem would be a tariff, but tariffs are a touchy subject in the UK, which had a tradition of free trade policies that many credited with making Britain an economic superpower in the first place. Also in episode 240, I told you how the government of Stanley Baldwin called a general election in late 1923 that was meant as a referendum on the tariff question; that election took Mr. Baldwin right out of Number Ten and replaced him with Ramsay MacDonald, Britain's first-ever Labour PM, which everyone took as a resounding "no" on the tariff question. Efforts to cut government spending and lower wages as part of the necessary deflation led to a bitter general strike in 1926.

With the pound back on the gold standard, the British economy still sluggish, the balance of trade still a problem, and tariffs off the menu, came the introduction of the Empire Marketing Board, also in 1926. The Empire Marketing Board funded a public campaign to encourage British consumers, women especially, to "Buy Empire," as the saying went; that is, to favor imported goods from other parts of the Empire. The idea of an Imperial tariff goes all the way back to Joseph Chamberlain and episode 38. It would raise revenue while discouraging imports from outside the Empire and encouraging them from within, which would build economic ties among the constituent nations of the Empire.

But the British public had made clear its opposition to a tariff, so the Empire Marketing Board hoped to start a voluntary campaign that might achieve many of the same goals. At this time, Britain imported more than half the food it consumed, so agricultural imports in particular were targeted by the "Buy Empire" campaign, like the pitch to buy South African fruit that I read to you at the top of the episode. The Empire Marketing Board advised the public that "The Good Shopper" shops Empire and "The produce of the home country crowns the Christmas feast." You could send to the Board for a free recipe booklet that included items like "The Empire Christmas Pudding," for which the ingredients included apples from Canada, sugar from Barbados, eggs from Ireland, cinnamon from India, raisins from Australia, and rum from Jamaica. The public was assured that this was the very recipe used at Buckingham Palace and made available with the gracious consent of Their Majesties.

The British general election of May 1929 resulted in another hung Parliament. The Conservatives got the most votes overall, but Labour got the most seats for the first time ever.

Even in the 1923 election, which put Ramsay MacDonald into Number Ten with the aid of the Liberals, Labour had come in with slightly fewer seats than the Tories.

We can attribute this 1929 Labour surge to the widespread unemployment. Votes for the status quo were concentrated in a relatively smaller number of constituencies. The Liberal Party, still under the leadership of David Lloyd George, increased its seat total to 59, running on a manifesto titled “We Can Conquer Unemployment,” which was written by friend-of-the-podcast John Maynard Keynes.

As in 1923, MacDonald formed a minority government with Liberal support and assumed the premiership for a second time. The British financial world in the City saw a major scandal and a collapse in the stock market just after MacDonald’s Cabinet was seated, episode 258. The accusation was made at the time that it was the threat of a socialist government that induced the lack of confidence in the City that followed, but that seems a stretch. The City was perfectly capable of inspiring a lack of confidence all on its own, as indeed it did.

I already told you about the Simon Commission, which had been created under the Tories and was meant to find a formula for increasing self-government in India. The Tories also meant to use it to restrain a future Labour government from going too far with Indian autonomy. In the event, as we saw last week, the Labour government all but ignored the Simon Commission and forged ahead into negotiations with Indian political leaders, with the blessing of the Tory Party, or most of it, but certainly not including Winston Churchill.

The 1929 stock market crash in Britain and then in the US induced the MacDonald government to form a committee under the leadership of Scottish jurist Hugh Macmillan to look into the depressed economy and the role of the British banking system. This Macmillan Commission would include among its members the banker Reginald McKenna, the trade union leader Ernest Bevin, and economists Lord Bradbury and John Maynard Keynes.

The following two years were dire ones for the British economy. The British stock market crash had not been so big a blow to Britain as the Wall Street one had been to the United States, but as we have already seen, the aftermath of the American crash saw a further decline in world trade, tariff increases in many countries, and banking crises in the US and Germany. These developments all hurt the UK economy, which was much more dependent on exports than the US was.

Shrinking exports meant increasing balance of trade difficulties and higher government expenditures for unemployment relief, which made it all the more difficult to maintain the exchange rate between sterling and gold. The conventional view, sometimes known as the Treasury View because it was widely held among officials in the British Treasury, was that the only solution was to cut government spending.

You might expect that idea would be poorly received by a socialist Cabinet, but this is 1931, when the Treasury View was widely accepted, even by socialists. Government budget deficits were regarded as always and everywhere a bad thing, regardless of the state of the economy, and doubly bad when the economy was ailing. Even in our time, when we know this view not to be true, it is still commonly voiced. The prime minister, Ramsay MacDonald, ardent socialist though he was, fully accepted the Treasury View, and even more firm in his belief was the Labour Chancellor of the Exchequer, Philip Snowden. Snowden was a Liberal turned Labourite who still believed strongly in free trade, sound money, and low tariffs and would hew to those positions even in the darkest depths of the Great Depression.

But by February 1931, it had become painfully clear that the British government was still in the red, and the deficit was growing larger all the time. The House of Commons passed a resolution to form a committee to advise the government on ways to reduce expenditures. This committee was chaired by Sir George May, a financial expert, and was known as the May Committee.

As you already know, the first half of 1931 saw a banking crisis arise in the United States that spread to Austria and Germany, and then to a number of smaller countries in Europe, the Near East, and Latin America. As banks failed and governments began defaulting on their foreign debts, pressure rose on British banks and on the Bank of England. We've seen how London was the world center for finance at the beginning of the century. After the Great War, New York assumed that role, but British banks remained heavy engaged in international lending. Leaders in British government and finance believed British international lending to be both lucrative and a useful instrument of British foreign policy. Beyond that, it was also a matter of national pride.

But as banks failed on five continents and governments suspended debt repayment, the position of British banks grew increasingly insecure. In July, at the height of the banking crisis in Germany, officials at the Bank of England learned that the international investment house Lazards was insolvent. This had nothing to do with the banking crisis; a trader in the Brussels branch of the firm had made a risky bet, shorting the French franc, which backfired and lost the firm £10 million. He'd concealed the loss for years, but it had recently come to light. The trader in question killed himself when this was discovered, and it seemed likely the firm would follow him into the next world.

At the Bank of England, they feared that the failure of Lazards would panic the City, and bailed out the firm. Within a week, two other merchant banks revealed that they too were underwater. This was getting to be more than the Bank of England could handle on its own, so it arranged a bailout by a consortium of private banks.

Then came the report of the Macmillan Committee on British banking. The report itself was not earth shattering. It largely endorsed the Treasury View, with some dissenting opinions, notably that of Keynes, who recommended restrictions on imports and nationalizing the Bank of England.

The real news, though, was buried in the fine print. British banks had nearly three billion US dollars in loans to borrowers in foreign countries, including half a billion in Germany alone, and another half billion in the Americas. With some countries defaulting, and others—including Germany—restricting the flow of money abroad, British banks were unlikely to recover any of this money soon. Maybe not at all. And unlike the way things were done during the salad days of the British Empire when British industry was flush with cash, most of the money lent had been in the form of short-term deposits, meaning the grand old dependable British banking system had now become vulnerable to the same kinds of bank runs that had been plaguing the United States and Germany.

Britain had been back on the gold standard for six years now, but the Bank of England's gold reserves were still very thin, much smaller than those of the United States or France, hardly any larger than the German Reichsbank, in fact. Foreign investors began selling off their pounds and the Bank of England was forced to pay out US$250 million in gold in the last two weeks of July, half of the Bank's reserve.

[music: Elgar, "Warrior's Dance" from *The Crown of India*]

The last day of the month, July 31, 1931, was also the last session day before Parliament adjourned for the summer. That same day, the report of the May Committee was made public. The May Report came down hard on government spending; the Committee estimated that the budget deficit would reach £120 million by the next fiscal year. That amount was less than 3% of the British GDP. In our time, this would not be considered a grievous level of national debt, but the authors of the May Report thought it catastrophic and rang the bell as loudly as they could. They called for steep budget cuts, including wage cuts for public employees such as teachers, police, and military personnel and cuts to job subsidies and unemployment benefits. It recommended only modest tax increases, on the argument that Britain was already overtaxed. As for cuts to unemployment expenditures, the programs introduced by the Lloyd George government to make Britain "a fit country for heroes to live in," the May Report argued that Britain had not had such programs twenty years ago but had had a strong economy, therefore they "cannot be essential" to economic prosperity.

The May Committee had six members, two each from the Conservative, Liberal, and Labour Parties. The two Labourites dissented from the final report. They argued that the deflation caused by the decision to put the pound back on the gold standard was the main culprit and called for higher taxes on holders of British debt as a more equitable solution.

The May Report was intended to put the fear of God into the Labour Cabinet—maybe I should say the fear of the Invisible Hand. But coming as it did in the midst of a banking crisis, in only added to the sense of panic in the City. The Bank of England raised its interest rate from 2.5% to 4.25%, but that did little to slow the demand for gold, so the Bank borrowed $250 million from the Banque de France and the New York Federal Reserve Bank, then ran through that money in another two weeks.

The Bank of England was now down US$500 million in gold in one month. Its gold reserves were depleted, its credit had run out, and the Bank was loathe to raise interest rates any further in the middle of a depression. The only plausible borrower left was the British government itself. In August, the government queried the New York Fed on the prospects of another loan, but US law prohibited the Federal Reserve from lending directly to a foreign government. So the query was forwarded to J.P. Morgan and Company.

There followed delicate negotiations. When bankers loan money to foreign governments, it often comes with conditions, and the conditions are usually raise taxes, cut spending, and reduce the budget deficit. And those were exactly the terms in this case as well. But here we have a particularly sensitive situation. This isn't just any government to which the bankers are dictating terms. This is not a Haiti or a Peru or a Romania, or even a Japan. This is the United Kingdom we're talking about, the nation that, until recently, had the largest economy and largest banking sector in the world.

It was therefore necessary to keep the negotiations over the terms of the loan a closely held secret. Not even the Cabinet was informed. Over the weekend of August 22-23, the Cabinet remained in session, the first weekend session since the war ended, while the King cut short his summer holiday at Balmoral and returned to Buckingham Palace. On the other side of the Atlantic, the J.P. Morgan partners met at a home on Long Island to debate the loan package. On Sunday afternoon, they sent a telegram agreeing to the terms.

When the telegram arrived in London, it was 8:45 Sunday evening. Sir Ernest Harvey, deputy governor of the Bank of England, personally delivered it to Number Ten and handed it to the Prime Minister, who rushed it into the Cabinet room. Shortly thereafter, angry shouting could be heard.

The Labour Cabinet split by the narrowest possible margin, 11-9, in favor of accepting the bankers' terms. With his Cabinet so sharply split, Ramsay MacDonald went to the Palace that night to offer his resignation. With the nation in a financial and now a political crisis, the King asked MacDonald to form what was called a National Government of all political parties. Conservative Party Leader Stanley Baldwin agreed, as did the acting leader of the Liberal Party, Sir Herbert Samuel. Liberal Party Leader David Lloyd George was at the time recovering from prostate surgery.

The National Government was conceived as a government of all parties that would pool their talents to lead the nation out of its current crisis. This was in principle no different from the coalition government that had led the country from 1915-1922, but that government having broken down following the embarrassment of the Chanak Crisis just nine years ago, episode 196, it was felt that the term "coalition government" evoked unhappy memories, so the National Government it became.

Only, the Labour Party refused to go along with the National Government and went into opposition. MacDonald himself, along with Philip Snowden and the other Labour members who supported the National Government were expelled from the Labour Party. They formed the National Labour Organization and continued to support the National Government, in defiance of the larger Labour Party.

The new Cabinet of the National Government, with Ramsay MacDonald still prime minister and Philip Snowden still chancellor of the exchequer, but now with Liberal and Conservative support, approved the budget cuts that had split the Labour government. King George insisted the government also reduce the Civil List, the annual grant to the Royal Household, by the same 10% cut that was applied to unemployment benefits.

There are those who would argue that the Civil List *was* an unemployment benefit, but let's not go there.

With the new budget in place, the government received a $200 million loan from a consortium of US banks and an equal amount from a consortium of French banks. By the end of the following month, September, it was all gone out the door. The demand to exchange pounds for gold had not decreased one bit.

That was because the government budget was beside the point. The problem was that British banks were overextended. The Bank of England and the British banking industry had attempted to ease the world banking crisis by serving as the world's lender of last resort. But neither the UK nor its banking sector had the same clout in the twentieth century that they'd had in the 19^{th}, though neither the government nor the bankers had yet absorbed that lesson.

The pay cuts infuriated workers. In the Royal Navy, the pay cut had been administered as a flat reduction of one shilling per day from the pay packet of each sailor, from the admirals to the lowest seaman. Naturally, the sailors at the bottom resented this. In September, one group of sailors in the Atlantic Fleet refused orders to put out to sea. This was a minor incident, but the foreign press labeled it a "mutiny," which only added to the sense of panic. If even the Royal Navy was coming apart, surely the apocalypse is at hand.

The only solution was to abandon the gold standard. John Maynard Keynes was already writing articles advocating this, but it was a bitter pill for British bankers to swallow. The weekend following the "mutiny," the British government asked the Hoover Administration in Washington to come to its aid. Secretary of State Stimson told the British Ambassador, Sir Ronald Lindsay, that America had already done everything in its power.

That same weekend, Ramsay MacDonald met with the directors of the Bank of England and they agreed that gold convertibility had to end.

Montagu Norman, the governor of the Bank of England, had been on holiday in Canada and at this moment was aboard a passenger liner en route back to England. The emergency was too great to wait for his ship to dock and he needed to be informed. Unfortunately, he had neglected to take his code book with him. On Sunday, Sir Ernest Harvey sent him a telegram in the clear that read, SORRY, WE GO OFF TOMORROW, AND CANNOT WAIT TO SEE YOU BEFORE DOING SO, and hoped Norman would put two and two together. Norman did not, and thought Sir Ernest was merely saying he would be away on holiday himself when Norman returned to London. When the ship docked and Norman learned what had actually happened, he was shaken, and angry the decision had been taken without him, although it's difficult to see what he could have done differently.

By the end of the year, the pound sterling had dropped from US$4.86 to around $3.50, a 28% drop, and this triggered a similar drop in two dozen other countries with close commercial and financial ties to the UK: Austria, Portugal, Norway, Denmark, Sweden, and of course the currencies of British Dominions and Imperial possessions: Ireland, Canada, Egypt, Palestine, Malaya, and of course India, as I mentioned last week. The rupee was devalued proportionately to the pound, even though rupees were not under the same selling pressure as sterling. You'll recall I described in episode 219 how in the 19th century, the British benefited from cheap imports from India when India suffered a famine. Now, when the shoe was on the other foot, the British Raj would not allow Indians to benefit from cheap imports from Britain, but instead decided that Indians would share Britain's financial pain.

And generally speaking, the Second Round Table Conference, which I told you about last week, took place in the shadow of this deteriorating economic situation in Britain. That conference reached no agreement, partly because the Indian delegates couldn't agree on a shared set of demands, but also because the British side was unwilling to make more than modest concessions. Some of the blame for that has to fall on the National Government, which had replaced a sympathetic Labour government with a more hardline government that included the Tories, but even more on the political difficulty the new government faced in offering bold concessions to Indian nationalists at the same time it was forced to make unpopular budget cuts at home.

Under pressure from the Conservatives, Ramsay MacDonald agreed to call a general election in October, in which the new National Government would stand together, as the old coalition government had done in the Coupon Election of 1918, episode 173. MacDonald and his National Labour group stood alongside the Tories, against the opposition Labour Party. David Lloyd George, now recovered from his surgery, called on the Liberals to leave the National Government for the election. Some did, but other Liberal MPs opted to support the government.

The election resulted in an overwhelming victory for the National Government, which won an astonishing 554 seats. The Tories had by far the largest share of these seats, with 470, with pro-government Liberals winning 67 and MacDonald's National Labour winning just 13. The official Labour Party took 52 seats to become the chief opposition party, while Lloyd George's Liberal opposition faction carried only four.

The new National Government would keep Ramsay MacDonald on as prime minister, but the Tories would be running the show, with Stanley Baldwin as Lord President of the Council and Neville Chamberlain as the new Chancellor of the Exchequer.

And I should mention here that December 1931 saw the new Parliament enact the Statute of Westminster, which I've mentioned a couple of times before. This law formalized terms already agreed to between the UK government and the self-governing Dominions of the British Empire: Canada, Newfoundland, Ireland, South Africa, Australia, and New Zealand. Under this act, Parliament surrendered the power to legislate for the Dominions. Henceforth, the UK and the Dominions would be equal sovereign powers, united by a shared allegiance to the Crown. With the Dominions, it's sometimes hard to draw a line and say exactly, "This is the moment when this nation became fully independent." But the enactment of the Statute of Westminster may be as good a place as any.

These months of crisis and alarm and political and economic turmoil were bewildering to ordinary Britons, few of whom fully understood what was going on. But the news of the pound going back off the gold standard came as a shock, just six years after the return to the gold standard had been announced as a triumph of British monetary policy. The newspapers solemnly declared it the end of an era and warned that the international financial system that had served the world so well for more than a century, had been broken by the Great War, and then rebuilt with considerable sacrifice, was now lost again, perhaps this time for good.

British economic and financial supremacy was indeed gone for good, but at least in the short run, the news got better. With the end of gold convertibility came the end of deflation, and 1932 actually saw wages and prices in the UK rise modestly. This was in contrast to much of the world, especially the United States, where wages and prices continued to fall.

Among socialists and Labour Party supporters, the name Ramsay MacDonald became anathema, seldom uttered except when preceded by the word *traitor*. It was accepted wisdom among British socialists that J.P. Morgan and the American bankers had imposed those harsh economies on the UK government for the specific purpose of bringing down the government and discrediting the Labour Party and the socialist movement.

British economist and socialist Sidney Webb, one of the founders of the London School of Economics, had served in the Labour Cabinet as Colonial Secretary. He had been one of the nine members opposed to the bankers' conditions. His wife, Beatrice Webb, herself an economist, also a founder of the LSE and the Fabian Society, condemned the system under which the very same bankers who had crashed the world economy in the first instance were now seizing the authority to decide who paid the consequences for their own folly. “The dictatorship of the capitalist,” she called it.

One class of Briton definitely felt the change devaluation made: Britons traveling overseas, especially those who had the misfortune to be abroad when the change was announced. *Time* magazine reported the story of a well-to-do English gentleman in New York that September, who was infuriated when a local bank would only offer him US$3 to the pound. He gave the bank teller a good scolding and announced he would take his money back to England, where a pound was still worth a pound.

We’ll have to stop there for today. I thank you for listening, and I’d especially like to thank Ed for his kind donation, and thank you to Peter for becoming a patron of the podcast. Donors and patrons like Ed and Peter help cover the costs of making this show, which in turn keeps the podcast available free for everyone, so my thanks to them and to all of you who have pitched in and helped out. If you’d like to become a patron or make a donation, just visit the website, historyofthetwentiethcentury.com and click on the PayPal or Patreon buttons.

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And I hope you’ll join me next week, here on *The History of the Twentieth Century,* as we return to the topic of atomic physics. The year 1932 saw multiple breakthroughs in understanding of atomic structure. These insights at first seemed subtle, mostly of interest to other physicists. But there would be ripple effects that would change the course of history. You might even call it the beginning of a chain reaction. That’s next week, here, on *The History of the Twentieth Century*.

Oh, and one more thing. Winston Churchill was still on the outs with the Conservative Party, because of his stubborn opposition to concessions in India. When Britain abandoned the gold standard, the man who had led the move to restore it six years earlier saw his reputation suffer still further. The very weekend that the decision to leave the gold standard was taken, Churchill was at Chartwell, his home, entertaining a very special guest, Charles Chaplin, the Hollywood film star on a visit to his native England. To Churchill’s dismay, Chaplin opened the conversation by berating him over his role in the 1925 restoration of gold convertibility. The following Monday, the very day the Bank of England announced the end of gold standard, Churchill had lunch with John Maynard Keynes. The two of them had become friends, but even so, Keynes could not resist using the occasion to gloat. Later that week, Keynes would publish an article about the policy change, in which he would declare, “I believe that the great events of the last week will open a new chapter in the world’s monetary history.”

In the October general election, Winston Churchill was easily re-elected to his own seat, but, still on the outs with his own Party, he was not offered a Cabinet position.

[music: Closing Theme]