THE WORLD ECONOMY BETWEEN THE WORLD WARS

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ment. Hitler conducted a successful balancing act. He reas- that he was not a free-spending radical at the same time as ob-creation programs and tax breaks of his predecessors. Plan embodied many of the new measures and enhanced new policy direction in 1936.

se rapidly in 1933. The new expenditures must have taken full effects. The immediate recovery therefore was the result ations when the Nazis took power. It was the result of antici- tual government activities. Even though the specifics of the not become clear (and in fact were not formulated) until of policy was clear. As we now can see more clearly than d, the Nazi expansion was based from the first on rearming 2006). Hitler had been criticizing the deflationary policies for years, and the commitment of the Nazis to full employ- own. As in the United States, a change in policy regime was he corner, although not to promote full recovery.

s had trouble distinguishing the new administrations in the Germany. Both Roosevelt and Hitler looked like "new men" charge from the paralyzed old guard. But it soon became t at the start—that the two leaders came from opposite ends oosevelt acted to preserve democracy in an economic crisis; t. The evils of the Nazi regime must be accounted among the e Great Depression.

Chapter 7

Unemployment

7.1 The Changing Meaning of Unemployment

In 1909, when William Beveridge, the future mastermind of the welfare state, published his book *Unemployment: A Problem of Industry,* the word "unemployment" itself was relatively new; it had first appeared in the *New English Dictionary* only twenty years back, in 1888. According to Keynes, Alfred Marshall's 1890 book *Principles of Economics*, the definitive nineteenth-century economics treatise, mentions unemployment only once. Before 1913, one finds just a handful of articles dealing with unemployment in serious economic journals; by the 1930s, a constant flow of scholarly publications was produced dealing with the measurement, determinants, and effects of unemployment. More important is the fact that before the First World War, issues such as monetary policy, tariffs, taxes, and the regulation of monopolies dominated political debates and electoral campaigns; in the 1930s, unemployment had definitely taken center stage. Some would say that unemployment was "discovered" in the last decades of the nineteenth century but became a relevant economic, social, and political issue only in the 1920s and much more so during the Great Depression.

There are two reasons why the unemployment received such an overwhelming attention in the 1930s. To be sure, the slump in output, investment, and prices was of a magnitude never seen before. None of the nineteenth-century depressions had produced such a high number of "out of work" persons. At the same time, however, labor markets in the most advanced industrial countries had considerably changed over the previous fifty-odd years, with most changes taking place after 1914. A brief survey of the new labor-market conditions allows us to understand the impact of unemployment on the daily life of the most affected individuals and communities, as well as to intuitively perceive what difference it made to be unemployed in western Europe and North America instead of in less developed, predominantly agrarian societies.

At different times in the nineteenth century, a number of countries made their transition from being an agrarian society to being an industrial society.

Labor markets were also affected by the transition, and they showed two distinct, yet related, features. On the one hand, the seasonal component of the demand for labor declined over time yet remained relatively high. A good number of workers were hired and laid off according to the ebbs and flows of agricultural activity, which remained of paramount importance. When idle, workers would typically consider themselves as "out of work" rather than "unemployed." The difference between the two terms was sociological and psychological rather than just semantic. Workers, particularly unskilled ones, expected to be "out of work" for a certain number of weeks every year, but they also expected to be hired again sometime in the future. During the downward phase of the business cycle, spells of involuntary inactivity were longer than at times of cyclical expansion, but expectations of getting back to work remained. People's lives adjusted accordingly, particularly by savings to cover out-of-work periods and by inter- and intrafamily mutual support (which may be considered as informal insurance). The most enterprising people would travel long distances to find a job when they were out of normal work closer to home. Southern Italian peasants went so far as to take advantage of the different harvest season to temporarily migrate to Argentina for the winter harvest. The term "underemployment" would later be coined for those who could not work full time over the year or even the life cycle.

A second feature of labor markets during the long transition from an agrarian economy to an industrial economy derived from the link many first-generation industrial workers kept with the countryside. Industrial unskilled employment typically began with the expansion of the cities' demand for ever-increasing numbers of construction workers. Construction was also seasonal and highly cyclical, and it suited workers who did not want to risk leaving the security of food provided by the extended family on the farm. Workers would thus typically move either daily, weekly, or seasonally from country to city and back again without severing personal and economic links to either setting. Work time over the life cycle may have increased with industrialization, but "underemployment" remained the key feature of industrialized labor markets, its social cost being somewhat cushioned by the option of going back to the rural environment in idle times. When demand for unskilled work increased in industries other than construction, worker turnover was considerable, making for a continuation of situations of underemployment. When demand for urban industrial work increased to the point of making it reasonable for workers to take the risk of permanently distancing themselves from the countryside in order to take full advantage of higher urban wages, only then did unemployment became a main feature of labor markets as well as a major social problem, due to its duration and to increased uncertainty about if and when it might end.

The nineteenth century did have its chronically unemployed people who were looked down upon with a mix of pity and of the moral stigma that is attached to lazy, immoral, or utterly inept people. It was for churches and charitable institutions to take care of such hopeless cases of long-term unemployment, rather than the government. Things began to change in the last decades of the century, with changing employment patterns as well as the emerging class struggle that would lead to organized labor in the form of trade unions and socialist parties. Both these developments were accelerated by the war. Large factories became common for the mass production of arms, vehicles, and uniforms, while life in the trenches provided a fertile ground for working-class propaganda.

7.2 Measures and Kinds of Unemployment in the 1930s

Even today, unemployment is notoriously difficult to measure, and it is almost impossible to compare unemployment statistics across countries for the 1930s. What we said in the previous section shows that it was not easy to have a uniform definition of unemployment. Underemployment was an even fuzzier concept for statisticians. Moreover, in an era when sample surveys and polls were just making their first timid appearance, one had to rely on official head counts of unemployed workers. Most industrial countries published statistics of the number of people officially registered as unemployed, but registration depended on the amount and duration of benefits, which varied enormously from country to country. Many out-of-work people did not bother to register when they were no longer entitled to the subsidy or when the benefit was too small to bother collecting. Moreover, as we have seen, "unemployment" was a term applied mostly to industrial workers. Only a small minority of those underemployed in agriculture or in the traditional service sector were included in the official head count.

Table 7.1, taken from Eichengreen and Hatton (1988, 9), reflects the statistical problems involved in comparing rates of unemployment in the 1930s by showing two estimates made by sophisticated historical statisticians. The first column (Galenson and Zellner) provides statistics for the industrial sectors, while the second column's figures (Maddison) are adjusted to the overall size of the labor force. However, the figures in the second column typically understate underemployment. By only taking into account industrial underemployment, one of us has shown that in the case of a relatively backward economy (Italy), official statistics underestimated unemployment possibly by more than half (Toniolo and Piva, 1988).

Even when all this is taken into account, table 7.1 suggests a huge variation of unemployment rates across countries. This variation is caused by a number of variables, the most important of which is the level of economic activity. Table 7.1 also shows the huge proportion of unemployed workers relative to the total registered work force.

Table 7.1 Average unemployment rates, 1930–1938

Country	Galenson and Zellner	Maddison
Australia	17.4	n.a.
Belgium	14.0	8.7
Canada	18.5	13.3
Denmark	21.9	6.6
France	10.2	n.a.
Germany	21.8	8.8
Netherlands	24.3	8.7
Norway	26.6	n.a.
Sweden	16.8	5.6
UK	15.4	9.8
USA	18.2	26.6

Source: Eichengreen and Hatton (1988), 9.

The increasing amount of labor and unemployment statistics that appeared after the First World War, difficult to compile and compare as they are, is in itself an indicator of the policy makers' interest in labor issues, a fact shown also by the creation in 1919 of the International Labour Organization (ILO), based in Geneva. Besides promoting international conferences and conventions, the ILO was a major source of statistical and economic research on labor issues, among which unemployment figured prominently. In most countries, the theoretical and empirical study of unemployment attracted an increasing amount of intellectual energies both academic and governmental. Pioneering inquiries such as those described in the next section stem from the growing interest in the social consequences of unemployment, as stimulated by the swelling dimension of the phenomenon.

One of the most innovative and complete surveys of unemployment was compiled in the United Kingdom by a group of high-profile international scholars under the auspices of the Royal Institute of International Affairs. As a rough estimate, the study put total unemployment worldwide to be about three times higher at the end of 1932 than it had been in 1929. The study also argued that while traditionally full unemployment depended either on workers' "displacement" (e.g., by technical change or relocation of production) or on "temporary business fluctuations," a new form of unemployment had emerged in the 1930s called "depression unemployment" that had "been a matter of vital concern to Government in the last four years" (Royal Institute of International Affairs, 1935, 28). The Great Depression, it was argued, produced "hard core unemployment" consisting of persons who "have been out of work for long periods and are unlikely to obtain work unless the total demand for labour relative to available supply is very much increased" (Royal Institute of International Affairs, 1935, 30).

Outside of Europe and North America, unemployment during the 1930s largely took the form of increased underemployment, for which no statistics are available. It is possible to speculate that within individual countries and areas, three factors affected the rise in underemployment: the composition of output, the severity of the depression, and the tariff and monetary policies followed by the government. In India, falling grain and rice prices resulted in widespread social unrest in the countryside during 1930–1931, indicating that peasant conditions had deteriorated almost to the breaking point and, most likely, that underemployment was on the rise. The subsequent imposition of a tariff on wheat import provided only limited and temporary relief to the peasantry. China was peculiar in that the onset of the depression and increased underemployment was somewhat delayed until 1933, probably due to an unintended but beneficial early devaluation of the silver-based currency. In Japan, unemployment in the 1930s was contained by the early devaluation of the currency, war with China, and the spree of military-related government spending. In Latin America, particularly in Argentina and Brazil, the fall in price of the main export staples resulted in large increases in underemployment in the countryside.

7.3 The Personal Experience of Unemployment

Aggregate statistics tell something about the overall extent and pattern of hardship experienced by those who experienced loss of work during the Great Depression, but averages do not tell enough about who suffered most and how. Aggregate statistics have the virtue of generality, but they miss the detail of individual lives. As already mentioned, the magnitude of the relatively "new" phenomenon of unemployment attracted a wave of scholarly interest, not only by economists and statisticians but by sociologists as well.

Unemployment in Marienthal: A One-Factory Village

One of the most fascinating studies of the impact of unemployment on individual lives was conducted by a group of sociologists who studied an industrial village in Austria during the winter of 1931–1932 (Jahoda, Lazarsfeld, and Zeisel, 1971). First published in 1933, the results of their research provide a close look at the intimate lives of those living in an industrial village in which the factory had closed.

Marienthal could be reached from Vienna by a half-hour train ride to a neighboring village and then another half-hour walk over the flat countryside. Its population numbered about five hundred families in 1931. A cotton mill had furnished the chief opportunity for employment in the village since its founding almost a century before. The mill had progressed from cotton to rayon after the First World War. Despite industrial strife and a slowdown in demand in the mid-1920s, employment was at its peak in early 1929. By February 1930, however, production had ceased in the mill. The mill owners must not have expected business to pick up again, for they started to demolish the mill almost immediately. In the early 1930s, workers in Marienthal looked out over the rubble of their former place of employment.

Unemployment relief was governed by a 1920 law. Workers were entitled to relief if they had worked at least twenty weeks in the previous year and had no other income. Aliens were not eligible. The amount of relief varied with the worker's work history, wage, and family situation, and relief lasted for twenty to thirty weeks. A worker's claim to relief was voided if any work at all was undertaken. Workers lost their benefits for activities as limited as cutting down trees in return for firewood, delivering milk in return for some of the milk, and playing the harmonica in return for a little money. The result was idleness supplemented by minimal illegal activity, such as stealing coal from the railroad or potatoes from farmers.

Emergency assistance was available after unemployment relief ended. This aid was only slightly less generous and lasted for an additional twenty to fifty weeks. After that, assistance ceased. By the winter of 1931–1932, therefore, most families were still on some kind of relief, but they were approaching the end of it. Fewer than one hundred families in the village had income from work in Marienthal, neighbouring villages, or Vienna. The other four hundred families subsisted on relief of some sort, with the exception of nine families with no relief or assistance and eighteen with railroad pensions.

Four-fifths of the families had allotments in the common land owned by the village and the factory. Each allotment consisted of five plots of about two by six meters each. The plots were used to grow vegetables, varying with the season. Many families grew flowers as well, choosing cheerfulness over sustenance. About thirty families also bred rabbits. Despite the homegrown vegetables, diets were very monotonous. Meat was eaten only once a week by half the families, on Sunday. Very few families had meat more than twice a week, and what they had was usually horsemeat. In the language of economists, horsemeat in Marienthal was an "inferior good"; its consumption rose as income fell. Starches were the basis of most diets, and the flour used had changed from wheat to the cheaper rye. Sugar was replaced by cheaper saccharine. The evening meal typically was either coffee and bread or leftovers from the noon meal.

This poor diet consumed almost all the incomes of the families in the village. Families with children also bought milk, and most families bought coal for heat. But there was little money left over for clothes and other expenses. Shoes in particular were a problem. Families typically could not afford to replace shoes that had worn out, so they were patched and patched again. Some families even restricted the activities of their children to save the wear and tear on their shoes. Almost nothing was left over for recreation or capital expenses.

While spending collapsed back into food, and food into bread and coffee, movement collapsed back into the village. Trips to Vienna had been frequent during the 1920s, to go to the theater, do Christmas shopping, or attend school. With unemployment, the money to undertake these journeys vanished. The train fare was no longer affordable, and people relied more heavily on their bicycles. The isolation of rural villages that had been reduced by the railroad and by prosperity after the First World War reappeared in the depression.

The isolation was deepened by a decline in newspaper subscriptions. Subscriptions to the Social Democratic paper, which contained intellectual discussions as well as news, dropped by 60 percent from 1927 to 1930. This was not entirely a matter of money, because the paper had a cheaper subscription rate for unemployed workers; subscriptions to another paper with more entertainment value fell only by 30 percent. Detachment was hardly complete, however. Political organizations continued, albeit with reduced passion. Votes in the 1932 elections were almost identical to those in the 1930 election, and the National Socialists started organizing in the village.

Politics, like other leisure activities, should have benefited from the increased availability of time. But this advantage was heavily outweighed by an increase of apathy that reduced all forms of recreational activity. Library usage also declined; both the number of borrowers and the books checked out by each borrower fell. Card playing became a popular way to pass the time. One striking aspect of this lethargy was the fate of a park that formerly belonged to the village manor and had become a focal point for village life. In more prosperous times, villagers sat on its benches and walked on its paths on Sundays, and the grass and shrubs were neatly tended. In the depression, despite the increase in leisure time, the park fell rapidly into disuse and disrepair. The paths became overgrown; the lawns deteriorated; the park became a wilderness.

Villagers became suspicious of each other as they reduced their activities. There always had been denunciations of people seen or suspected of doing illegal activities, such as working while receiving relief. The number of denunciations rose dramatically in 1930 and 1931, but the number that stood up under investigation did not.

The observing sociologists classified most families as resigned to their condition. The families were hanging on, preserving as much of their life as they could on their meager budgets. All their activity was dedicated to getting by; little thought was given to the future. Some families still planned as before, but others collapsed entirely in mental and physical neglect and conflict.

The unemployed men passed their time doing essentially nothing. They sat around the house, went for walks—walking slowly—or played cards and chess at the Workmen's Club. They could not even recall much of any activity during the day when asked. In a compilation of time cards, more than half of the men's time was idle or unaccounted for. Another quarter was occupied in minor household tasks like shopping and getting water. Less than a quarter of the time was used in major household work, looking after children, or handicrafts.

Women were far more active. Although no longer working, they had the responsibility of keeping the household running and caring for the children. They spent time cooking, mending clothes to make them last longer, and managing their budgets. The men contributed less to the running of the household than before—sometimes not even turning up on time for meals—and the women had the full responsibility. Even though the women often had had a hard time completing their housework after working, they uniformly would have preferred being back at work.

One revealing key to the meaning of time for unemployed workers was their bedtime. While working, people generally went to bed around 11:00. They came home from work, ate, put the children to bed, went to a political meeting or had some other activity, talked a bit, and then went to bed. In the early 1930s, the women still went to bed late in the evening, taking the time to complete their household tasks, but the men went to bed before 9:00. There simply was no reason to stay awake; sleep expanded to take up the extra time.

The Life of the Unemployed Worker in London and Wigan

Another classic survey conducted a few months earlier, in the summer and fall of 1931, examined the experience of unemployed workers in Greenwich, a suburb of London (Bakke, 1934). In this study, a lone investigator lived among the workers, recording his observations and conversations. The results are less systematic than those from Marienthal, but they are similar in spirit.

The experience of a 28-year-old mechanic and lorry driver was reported in this Greenwich study. Three days after being out of work, the mechanic was very optimistic about finding another job. After all, he had never been out of work for much more than a week before. Three weeks later, he was not so sure. He had answered all the ads in the newspaper, but he was getting discouraged. "You feel like you're no good, if you get what I mean," he said.

After eight weeks, he was reduced to walking to seek jobs to save the bus fare, even though he was living with his parents to avoid paying rent. He had begun to lie about how long he had been without a job, to avoid being lumped in with the long-term unemployed. After eleven weeks, he was still actively searching, but now only randomly; answering ads did not seem promising any more. His comment at this point: "There's one of two things, either I'm no good, or there is something wrong with business around here."

By the seventeenth week, the mechanic was thoroughly discouraged and depressed. He was described as "sullen and despondent." Although not as depressed or idle as the workers in Marienthal, because there was evidence of work nearby that might be found, this English worker nonetheless saw his experience as similarly hopeless: "It isn't the hard work of tramping about so much, although that is bad enough. It's the hopelessness of every step you take when you go in search of a job you know isn't there" (Bakke, 1934, 64–67).

As in Austria, unemployed workers were eligible for unemployment assistance in Britain. Assistance was set up with the same restrictions: any work disqualified the recipient from further aid. The rules were policed by competing workers who reported real and suspected infractions.

Unlike Marienthal, productive activity in the whole city had not closed down in Greenwich. Workers consequently continued to search for work. The observer formed an early judgement on the effect of unemployment assistance on the willingness to search for work. He asserted that there was no effect at all; the benefit did not retard or reduce efforts to find jobs. Instead: "It has removed the cutting edge of the desperation which otherwise might attend that search" (Bakke, 1934, 143).

Our third report was made by the famous writer George Orwell. Orwell was commissioned by the Left Book Club to report on the condition of workers in northern England in the mid-1930s and went to a small town called Wigan, near Manchester (Orwell, 1958). He reported that there was little evidence of extreme poverty in the industrial north. Everything, he said, was poorer and shabbier than in London, but there were fewer beggars and derelicts than in the metropolis. The communal nature of life in the smaller communities enabled unemployed workers to pool their resources and scrape by.

Orwell did, however, comment on the dreadful condition of single unemployed men. They lived in depressing furnished rooms in which they could not stay all day. Outside, their main concern in the winter was to keep warm. The cinema, the library, even a lecture offered refuge from the cold. Orwell said he was taken to hear the "silliest and worst-delivered lecture I have ever heard or ever expect to hear," but while Orwell fled in the middle, the hall remained full of unemployed men.

The diet of unemployed families was based on white bread, margarine, corned beef, sugared tea, and potatoes. Orwell commented (1958, 95): "The peculiar evil is this, that the less money you have, the less inclined you feel to spend it on wholesome food. . . . There is always some cheaply pleasant thing to tempt you. . . . Unemployment is an endless misery that has got to be constantly palliated, and especially with tea, the Englishman's opium."

More recent authors have amplified these observations and provided details of unemployment in other countries. The general patterns are similar to those described here. Unskilled workers suffered more than skilled workers, idleness and discouragement abounded, and unemployment relief often provided the margin between some semblance of the previous life and disruptive poverty.

7.4 The Social and Demographic Pattern of Unemployment

Unemployment was not evenly spread among all classes of workers when considered by age, sex, and occupation. Unfortunately, not much is known about this important problem for most countries. One exception is Britain, where more studies have been conducted than elsewhere.

In relation to age, Thomas (1988) found that the risk of becoming unemployed was very much the same for all adult age groups, but that after about age 45 it was increasingly difficult to find a new job after losing the old one. In the words of a pioneering investigator (Beveridge, 1937, 13): "The older man has less power of recovery industrially, from loss of unemployment, as he has less power physically, from sickness or accident." The results were higher unemployment and higher long-term unemployment among older workers.

On the other hand, there is evidence that it was young workers who were most liable to be without a job. According to a group of contemporary observers, "The difficulty in retaining or securing employment appears to arise at the point when the change-over takes place between the juvenile and the adult wage" (Royal Institute of International Affairs, 1935, 62). If they did find work, trade-union customs and their lack of experience generally made them the most vulnerable when employers needed to dismiss workers.

Women accounted for only a small proportion of all those who were out of work, less than 14 percent in 1933. This was largely a reflection of the fact that they were a smaller proportion of the labor force, but it was also the case that women were less likely than men to lose their jobs. Surveys also found that women were more easily discouraged than men after losing their jobs and therefore were more likely to leave the register than to continue to search for employment.

As far as occupation was concerned, unemployment was heavily concentrated in semiprofessionals and manual workers, the unskilled workers being the harder hit. As Thomas put it (1988, 123), "In general terms, the risk of unemployment fell as social class rose. Unskilled males were the most vulnerable, female higher professionals the least."

The authors of the 1932 Royal Institute for International Affairs report also demonstrated that the increase in unemployment in the 1930s was not the result of increased job leaving. Rather, it was that workers were not being reemployed as rapidly as before. Some were not rehired at all, or at least not for a long time. The proportion of the unemployed in Britain who were out of work for more than a year rose from about five percent in 1929 to more than twenty percent during the 1930s. The result was a bifurcated labor market: one group went in and out of work with some frequency, while the other remained unemployed.

The workers who were unemployed for long periods or permanently and those who suffered the highest rates of unemployment were predominantly located in the areas dominated by Britain's traditional activities: coal mining, iron and steel, shipbuilding, and textiles. The problems of these industries were considered in section 4.2. Here we note that declining production in particular industries as well as in nations as a whole meant declining employment. While it is true that greater aggregate demand would have reduced British unemployment (as it did after 1939), it also is true that even with higher demand, many workers in traditional industries would have had to move to jobs in newer industries.

For various reasons, such workers may well have been the last to be hired in those industries. Their skills may not have been transferable across industry lines. Also, employers may have wished to recruit younger workers or those without a previous history of employment in the declining industries with their specific trade-union traditions and work practices. Workers also may have been reluctant or unable to move to newer industrial locations. The result of these structural factors was that unemployment in Britain between the wars was particularly concentrated in certain areas. For instance, the male unemployment rate in 1932 was 36.5 percent in Wales, compared to 13.5 in London, and the gap tended to widen as the recovery got under way (Thomas, 1988, 124).

In France, unemployment was neither as high nor as concentrated in specific locations and industries as it was in Britain. This was in large measure a reflection of the different pattern of economic activity in France. The proportion of the labor force occupied in agriculture was much larger in France (see section 4.1), and although peasant farmers suffered in other ways during the depression, they were not deprived of all sources of income and were not forced into the ranks of the unemployed workers dependent on state assistance or charity for their survival. Within industry and trade, the structure of employment was also different, with a much larger proportion of small shopkeepers, outworkers, part-timers, and self-employed workers in small establishments. Many of these workers were also able to retain some sources of income during the downturn.

Two other factors contributed to France's more favorable position. First, compulsory conscription eased the problem of youth unemployment, but much more important was the fact that a substantial part of the burden was shifted onto foreign workers by controlling the influx of immigrant labour. Admission from abroad fell from 221,000 in 1930 to 60,000 in 1933 (Royal Institute of International Affairs, 1935, 74). Thus, when asking who the French unemployed were, it is possible to reply: the Algerians, the Italians, the Polish, the Portuguese, and the Spanish.

As for the United States, a survey taken at the end of the depression (March 1940) showed that 11.1 percent of male heads of household in the labor force were still unemployed (Margo, 1988, 329). "Unemployed experienced workers were often middle-aged or older (over age-45), foreign born, single, urban, less geographically mobile, and living in the north-east or west rather than in the north central states or the south. The unemployed had 1.2 fewer years of schooling than the employed, and far less wealth, as measured by the value of owner-occupied housing" (Margo, 1988, 330–31). Overall, unskilled laborers in such industries as construction faced a higher probability of becoming unemployed and a lower probability of finding a new job once unemployed. On the other hand, individuals who possessed higher-than-average human capital (as measured by years of schooling) and who were geographically mobile were more likely to be reemployed (Margo, 1988, 343). Women were more likely to work if their husbands were unemployed. The strength of household bonds proved in many cases crucial in mitigating the effects of unemployment.

7.5 The Cross-Country Pattern of Unemployment

As already mentioned, data on unemployment in this period are imperfect, but a rough indication of the pattern of industrial unemployment for countries for which acceptable statistics are available is shown in table 7.2, which shows unemployment rates in the 1920s and 1930s.

The countries in Table 7.2 fall into two groups. The first group, consisting of the United Kingdom, Belgium, and the Scandinavian countries had high unemployment throughout the interwar years. The contrast between the 1920s and 1930s was not very pronounced; the later decade was only slightly

Table 7.2. Unemployment rates, 1920s and 1930s

	1921–1929	1930–1938
Group I		
Denmark	18.7	21.9
Norway	16.8	26.8
Sweden	14.2	16.8
United Kingdom	12.0	15.4
Group II		
Australia	8.1	17.8
Belgium	2.4	14.8
Canada	5.1	18.5
France	3.8	10.2
Germany	9.2	21.8
Netherlands	8.3	24.3
United States	7.7	26.1

Source: Galenson and Zellner (1957).

worse than the 1920s had been. Japan may be seen as belonging to this group, with the qualification discussed below. The second group consists of France, the Netherlands, the United States, and Australia. Germany and Italy (not included in the table) also belong to this group, but they staged a more rapid reduction of unemployment in the second part of the 1930s. The countries in this second group had much higher unemployment in the 1930s than in the preceding decade.

Aggregate unemployment roughly reflects aggregate growth in the two decades, which in its turn depended to a considerable extent on monetary and exchange-rate policies. In fact, the two groups of countries in table 7.2 roughly correspond to the groups of nations to be identified in Chapter 8 as belonging to different trading areas. The sterling area—that is, the countries that followed Britain off gold in 1931—was afflicted by relatively high aggregate unemployment, partly due to the high rate of exchange at which the gold standard was reintroduced after the First World War (this applies both to the UK and to Scandinavia). On the other hand, countries in Group I devalued early in the depression and had the least severe increase in unemployment in the 1930s. Japan, for which no comparable statistics exist, can be seen as fitting within this group. In Japan, however, the deflationary targets of successive governments aimed at reintroducing the gold standard in the 1920s had to be repeatedly put on hold to deal with exogenous circumstances, such as banking crises and earthquakes, that required the creation of additional liquidity (Faini and Toniolo, 1992). Japan remained on the gold standard only for a handful of months and was quick to abandon it when the sterling area did.

Group II countries did not undertake violent deflationary policies in the 1920s (Belgium, with the lowest unemployment of all, actually pursued a competitive devaluation of the currency). In the 1930s, however, they remained on longer on the gold standard longer than any other country. These countries, therefore, suffered high and protracted unemployment in the 1930s after being able to contain it in the 1920s. Germany and Italy also fall within this group, but after 1934, they pursued much more aggressive expansionary policies (largely but not entirely related to rearmament) than the other countries in the group, with notable positive effects on employment. Toward the end of the 1930s, the German labor market was quite close to full employment.

The United States is peculiar within this group in that, unlike most European countries, they did not have to face the trade-off between deflation and currency stabilization, having effortlessly gone back to gold convertibility in 1919. The 1920s were among the fastest-growing periods in the history of the country and unemployment, while not negligible, was contained within acceptable boundaries. In the 1930s, on the other hand, the United States and Germany were the large countries with the highest levels of unemployment. However, unemployment remained exceptionally high much longer across the Atlantic than across the Rhine.

7.6 Unemployment, Benefits, and Real Wages

Earlier in this chapter we reported the unemployed Greenwich worker's comments on the effects of unemployment assistance on his willingness to search for a new job. In a highly controversial article, Benjamin and Kochin (1979) argued that the increase in British unemployment in the 1930s was essentially due to the increase in the level of these benefits. In other words, workers remained unemployed because they had little incentive to find a new job. Benjamin and Kochin attempted to demonstrate this proposition econometrically, by estimating an equation that explained the unemployment rate by the ratio of the unemployment benefit to the wage and the deviation of national income from its trend. Although a number of authors have shown that the evidence adduced by Benjamin and Kochin in support of their thesis is deficient, their hypothesis has not been completely demolished, and it is now generally accepted that some weight should be given to the role of higher unemployment benefits in increasing unemployment (Crafts, 1987; Eichengreen, 1987).

A further issue closely related to the question of unemployment is the behavior of real wages. Keynesian explanations of the depression start from the observation that workers bargain over nominal wages. When prices fall in a depression, real wages rise. The resultant profit squeeze intensifies the depression. This mechanism was evident during the Great Depression. As documented by Eichengreen and Sachs (1985), higher real wages in the mid-1930s were associated with higher unemployment.

This finding has created a problem for macroeconomists who conceptualize the wage bargain as the result of negotiations between highly sophisticated agents. These agents, particularly those acting for the workers, should have seen the demand for labor fading away and should have thus accepted lower nominal wages. The question for macroeconomists is, "Why did nominal wages not adjust to the rise in unemployment?" (Bernanke, 1993).

One answer that has been proposed in the context of discussions of European unemployment in the 1980s is that the labor market does not work in the atomistic fashion of other markets. In the market for apples, for example, the trader who has apples left over at the end of the day will lower their price to clear his stand. But the unemployed worker in this story does not have the ability to force down wages. Instead, the worker has become an "outsider" to the wage-setting process. Wages are determined by agreement between the employers and the unions, which represent employed workers—the "insiders." If the workers' agents care only about insiders, then in the bargaining process, they tend to settle for a combination of high wages and high unemployment, rather than the opposite. This could explain why increasing unemployment in the Great Depression failed to force nominal wages down faster than prices.

The exceptions to this story are Germany, and possibly Italy, where the fascist government repeatedly intervened to curb monetary wages. In Germany, alone among European countries, wages fell faster than prices. In Italy, real wages declined from 1934 onward. Except for Germany, real wages in 1933 were higher than in 1929 in every country for which data have been collected. For the many countries with rising real wages, the range in 1933 (1929 = 100) was between 104 and 119. For Germany, by contrast, real hourly earnings in manufacturing, mining, and transport in 1933 were 5 percent below their 1929 level (Eichengreen, 1994).

This quantitative evidence has intriguing implications for the Borchardt debate, referred to in section 4.2. If wages were too high in Weimar Germany (though this has not yet been firmly established), the problem was erased in the contraction. The conditions that allowed German wages to rise rapidly in the Weimar Republic evaporated with the onset of the depression.

Some writers have suggested an alternative explanation for the rise in real wages. In their view, it was not the result of an independent fall in prices without a corresponding adjustment in money wages, but of an autonomous increase in nominal wages. In either case, the rise in real wages would lead to higher unemployment, but there would be two quite different interpretations of why this had occurred. In the first case, it would be necessary to explain why there was a fall in prices; in the second case, it would be necessary to explain how workers were able to obtain the higher nominal wages. It is thus important for an analysis of the causes of increased unemployment to establish which of these two versions was correct.

Dimsdale et al. (1989) attempted to do this by means of an elaborate econometric study of the British experience. They concluded that both the recession and the recovery in the 1930s were consistent with the consequences of a large exogenous demand shock (such as we have described in our account of the depression) accompanied by a large fall in the real price of imported goods. This led to higher unemployment because wages and prices were sticky, so that real wages rose when import prices fell, making it unprofitable to employ workers at that level of remuneration. Autonomous changes in wages were not an important factor.

Our search for an explanation of the mass unemployment of the depression thus leads back to the causes of the large demand shock, which we have attempted to analyze in the preceding chapters. It cannot be said that workers were themselves responsible for their own plight because they had initiated the process by exerting pressure for higher wages.

The fact that high real wages could be one of the causes of high unemployment did not escape policy makers. In order to solve the problem, countries that had devalued their currencies in 1931 implicitly counted on inflation, assuming some kind of upward rigidity of money wages. The governments of gold-bloc countries, particularly Italy and France, tried to impose nominal wage cuts. Mussolini's Italy had adopted this policy as early as 1927 at the time of the stabilization of the lira at a revalued parity, and they introduced it again in the first part of the 1930s. In the same vein, Lavalle attempted to make French workers take a cut in their nominal wages. Such attempts, however, met with strong opposition from the organized labor movements and proved to be difficult to implement on a sufficiently large scale, even for dictatorial or authoritarian governments.

7.7 Work-Relief Policies

It was recognized at the time, as it is today, that much of the reason why unemployment and underemployment remained stubbornly high for so many years was that the depression lasted so long. As long as demand remained depressed—for the host of reasons we have discussed in previous chapters—so did output and employment. By and large, only macroeconomic policies capable of ending the slump would cure unemployment.

Policy makers, however, saw unemployment as a major social and political problem, and some of them sought means to alleviate it in the short term by means of ad hoc policies and particular public-work programs intended to create new jobs. As early as January 1931, the Committee for Unemployment of the International Labour Organization spoke in favor of "a concentrated implementation of large-scale international projects" (Schneider, 1986, 166). International pressure for governments to act on public works programs remained high, and these were eventually undertaken in several countries.

At the micro level, steps were also taken to reorganize the labor market. In some cases, these included attempts at improving employment-exchange offices in order to ease the possible mismatch between demand and supply of labor and to organize seasonal and casual labour more effectively. In the same policy category fall efforts to provide better vocational guidance to new entrants in the labor markets, and retraining for those who had lost their jobs.

Government intervention in these areas was variably active in many countries, but seldom was it really able to make much of a difference. Nevertheless, in this as in many other areas, the interventions signaled a new interventionist stance shared by most governments worldwide, albeit with different intensities, a stance that was to take root and develop on a much wider scale during and after the end of the Second World War. The 1930s created a widespread belief in the electorates of most countries that the Great Depression had highlighted a gigantic market failure, that unmitigated laissez-faire economics could not cure mass unemployment, and that only appropriate state policies could deliver full employment. Post-World War II reconstruction and much policy making in the 1950s and 1960s was based on these assumptions.

Keynes and the Campaign in Britain

The attempt to persuade the government to adopt a large-scale public works program funded by borrowing was conducted most vigorously in the United Kingdom. It is worth spending more than a few lines on the British case, not only because England was Keynes's own country but also because many of the arguments advanced in London against unemployment-relief programs were shared in many other capitals.

The issue first emerged in the 1920s, when unemployment soared after the collapse of the postwar boom, and it gathered strength in the trade-union and labor movements, with support from the Liberal Party. By the time of the general election of 1929, unemployment had become the dominant issue dividing the parties, and the election was notable for the active participation of Keynes. He penned a brilliant pamphlet in support of the Liberal leader's proposals for a vast public-works program, *Can Lloyd George Do It?*, originally written with Hubert Henderson in 1929 and collected with his other *Essays in Persuasion* two years later. In spite of Keynes's sparkling prose and his brilliant critique of the Conservative Party's opposition to such expenditure, neither the electorate nor the government were at the time persuaded.

The issue remained at the center of political and intellectual debate as the depression deepened. In 1931, Keynes gave a detailed elaboration of his ideas in evidence to a Royal Commission but was once again unable to overcome the resistance of those whose views were still rooted in orthodox economic thinking. The theoretical breakthrough was not to come until he had completed his great work, *The General Theory of Employment, Interest and Money*, published in 1936; and even then the process of conversion was slow and partial, particularly in Whitehall and in the City (respectively, England's governmental and financial centers).

The government ministers and their advisors in the Treasury had a number of different reasons for their steadfast rejection of all proposals for state public-work spending aimed specifically at reducing unemployment. Some of their objections were practical and administrative: it took time to draw up plans for road-building, land had to be acquired, it was the responsibility of local authorities and not of central government, and so on. These were convenient debating points to make in political campaigns, but they could not be sustained when unemployment persisted for so long.

A second line of attack was that the causes were structural and long term—the problems of the declining industries discussed in section 4.2—and would not be alleviated by short-term measures. There is more merit in this argument, but inability to solve a problem completely is not sufficient justification for not doing what can be done. With unemployment rising to about three million by 1932, even the removal of a few hundred thousand workers from the dole queues would surely have been worthwhile.

This was not done because within the Treasury and in the financial and business community, there were deeper levels to the opposition to deficit government spending, which, it was believed, would undermine the reputation and reliability of London as a financial center. Still more fundamental, though probably too technical to be appreciated by more than a minority, was the argument that a program of government expenditure would not actually be an effective cure for unemployment. This proposition rested on a concept that has since come to be known as "crowding-out": any spending by the government would simply displace a corresponding amount of spending by the private sector, even if the increased government spending was not matched by an equivalent increase in taxation but instead was funded by borrowing. There would thus be no net gain in output or employment. At a time of mass unemployment and idle factories, this negative prospect could scarcely be attributed to shortages of labor or other physical resources. Rather, the argument was psychological and financial.

The source of the psychological crowding-out was the private sector's belief that budget deficits were a sign of financial profligacy and irresponsibility. If the government committed such sins, financiers and industrialists would lose confidence in the future stability and prosperity of the economy. Businessmen would refuse to invest in their enterprises, and bankers at home and abroad would refuse to buy the securities the government must sell if it was to cover its deficit. Such views might have been irrational given the prevailing conditions, but they were deep-rooted and powerful.

Financial crowding-out was a more abstract proposition and was the most fundamental determinant of the view held by the Treasury and their supporters among academic economists. According to these theorists, displacement of spending would occur because there was a limited supply of savings. If more of this finite fund were drawn on for public investment, less would be available for private investment. A possible escape from the logic of this doctrine might be available if there was a compensating reduction in investment overseas. That aside, public spending could only be effective in increasing total spending if it was associated with a relaxation of bank credit and lower interest rates. However, if the authorities wanted to take that route, it was not necessary for them to accompany it by public works. In the words of the original and most influential proponent of this doctrine (Hawtrey, 1925, 48), "The original contention that the public works themselves give additional employment is radically fallacious."

But, as we have seen, the Treasury and the Bank of England did not want to relax credit in the 1920s. On the contrary, it was an imperative requirement of the restoration and preservation of the gold standard that interest rates should be kept high. It was not until the country finally abandoned the gold standard in 1931 that they could begin to think in terms of a different strategy. From mid-1932, the fact that it was no longer necessary to defend sterling made cheap money a possibility for the first time since the war.

Before we leave this topic, we should note that recent research indicates that even if the program of public works advocated in 1929 had been adopted, the impact on employment and output would have been somewhat less than

Keynes and his colleagues had anticipated. We now know that the value of the multiplier—the expansion of expenditure as a result of the initial increase in spending—was not as great as they had thought. The benefits in increased activity at home would have been rapidly curtailed by higher imports, and an outlay of the magnitude proposed by Lloyd George would probably have created jobs for only about 300,000 of the more than one million who were out of work in 1929 (Thomas, 1981; Hatton, 1987). Those who would have found work if the program had been adopted would no doubt have welcomed even this modest increase.

At the onset of the depression, in 1931, the attitude of the Swedish government was similar to that in the United Kingdom, and they were not willing to adopt measures that required deliberate budget deficits. In 1933, however, a new government was elected, based on a coalition of the Social Democrats with the Farmers' Party. They were more responsive to proposals from a group of distinguished Swedish economists, notably Myrdal, Lindahl, and Ohlin, for a deliberate countercyclical fiscal policy, with deficits to be financed through government borrowing. A policy of this nature was implemented from 1933 to 1935, but only on a modest scale, and its effects were relatively limited. In 1933, however, unemployment had already began to decrease due to the more expansionary monetary policy inaugurated a year earlier.

The German Case

The system of welfare provision for those without a livelihood created in Germany during the war was developed in 1918–1919 into a form of social insurance for the unemployed. In 1927, the fortieth German Welfare Conference adopted the slogan "work not welfare," advocating the transition from financial support to support through labor (Homburg, 1987, 93). Therefore, there existed at the onset of the Great Depression a political and social context that favored public works as a means for unemployment relief. As we have seen, however, the Brüning government inherited three main problems: budget deficits, heavy reparations, and rising unemployment. The government focused on the first two problems, assuming that once those problems were solved, unemployment would be taken care of. For the time being, even unemployment benefits had to be partly sacrificed as tax revenues declined.

The conflicts within German policy can be seen in the discussions that took place in early 1932. The depression was at its worst, and unemployment was extremely high. The General German Trade Union Federation (ADGB) sponsored the WTB plan of job creation, as described in section 6.5. Vladimir Woytinsky was the chief source of the ideas in the plan. The ADGB requested a meeting with Chancellor Brüning to present this plan, but the government was only willing to undertake a work-creation program if the budget was balanced. Brüning insisted that expenditures for unemployment relief, welfare, and job creation had to be cut rather than increased as tax revenues declined. Brüning actually linked job creation to the effects of his deflationary policy on wages.

The labor minister nevertheless proposed a plan for work creation in several areas, chiefly government enterprises and agriculture. The Reichsbank vetoed this plan, on the grounds that it required undesirable credit expansion. The plan was leaked to the press, which did not help its progress in the Cabinet, but it provided a fig leaf for the labor minister when he appeared at an emergency ADGB congress on unemployment in April 1932. The only initiative taken by the Brüning government for work creation was a program approved by the Cabinet in May 1932, under the pressure of increasing public-opinion approval for work-relief programs. It allocated a relatively limited amount of government funds to road works, waterworks, and job creation.

Brüning was replaced by Papen in May 1932, and a month later the new government issued an emergency decree that contained "alongside measures for social contraction, which generally corresponded with the ideas of representatives of industry, public works projects in the area of transport and water as well as schemes for agricultural improvement" (Schneider, 1986, 173). The decree was issued at the time when the Lausanne Conference was deliberating the final and official status of reparations (see section 8.1). Only in September, after the conference had ended reparations for good, was an expanded program introduced. It emphasized incentives for private employers to hire workers and de-emphasized direct government employment. Among these incentives were lower wages for new employees, which the trade unions saw as being against rather than for the workers' interests. Although this program was relatively modest and had no discernible immediate effects, it was the model for succeeding plans.

Schleicher followed Papen in December and built on the existing plan. A Reich Commission for Work Creation was established. This policy was seen as a move to the left and a departure from the principle of a free-market liberal ideology. Schleicher's plan entailed the extension of loans on very favourable terms to those undertaking projects for work creation. Government agencies were to issue and supervise the loans, provided by advances from the Reichsbank on security from the Reich. This turned out to be the blueprint for the larger work-creation program introduced under Hitler.

Hitler was not bound by either reparations or foreign-exchange constraints, eased by tight controls. In contrast to the short-lived Schleicher cabinet, after a brief period of diffidence, Hitler enjoyed the support of big business and large landowners. The work-creation program initiated in 1932 entered full operation in 1933. A new, more extended plan, the Reinhardt Program, was approved in June. Soon afterward, the Law for the Creation of Motorways was passed. In September, additional funds were made available to prevent a seasonal slump, including provisions for grants and further tax cuts. Signs of economic recovery clearly appeared in 1933, as the number of jobless

decreased. But the real breakthrough in the fight against mass unemployment did not occur until increases in military spending provided a major stimulus to aggregate demand.

The same can be said of Italy, if on a much smaller scale. In the summer of 1931, Mussolini launched a public-works program to enhance existing schemes aimed at creating jobs for seasonally unemployed agricultural workers. Such schemes were based more on social philosophies that inspired similar nineteenth-century programs (i.e., idleness is morally evil and socially dangerous) than on the ideas that Keynes was beginning to disseminate at around the same time. At its peak in 1933, the program created some 200,000 new jobs (Toniolo and Piva, 1988, 237). As in the case of Germany, however, it was only the large spree of military spending for the Abyssinian adventure that led to a substantial increase in industrial output and employment (Toniolo, 1980).

The New Deal

The American New Deal was probably the most comprehensive and (at least in principle) organic "plan" enacted in any market economy to lift a country out of the Great Depression. At the macro level, it focused on monetary, exchange-rate, fiscal, and financial policies, while at the same time seeking to modify the incentive structure at the micro level. It went through at least two major phases, the second one being modified in light of the experiences (and the mistakes) of the first, which had been enacted in haste during the spring of 1933. Scholars still disagree about the impact of New Deal policies on levels of activity and unemployment. Currently, however, the prevailing view is that the New Deal's overall impact was relatively modest. It is likely that a number of measures might actually have been counterproductive. For instance, Roosevelt's high-wage policy is seen as restricting the creation of new jobs (e.g., Temin and Wigmore, 1990; Temin, 1990). Most of the New Deal measures fall in the broad category of reflationary policies and are not discussed in this chapter, which is only concerned with actions directly aimed at immediate unemployment relief.

The Hoover administration had intervened, on a rather small scale, to support "poor relief" at the state level. But by 1933, even this modest form of support was in a state of collapse. Intervention on a larger scale was envisaged with the creation in 1933 of the Federal Emergency Relief Administration (FERA), which immediately made $500 million available to states in the form of grants rather than loans. Roosevelt, however, was opposed to dole payments, as he felt they lowered the morale of the recipient and led to an erosion of work skills (a socially more modern view than the one underlying Mussolini's distaste for the dole). FERA, therefore, directed states to set up useful public-work schemes to provide employment rather than dole payments as far as possible (Fearon, 1987, 236). A scheme for fair pay was developed based on estimates of the weekly needs of households. However, the federal government was unhappy with the seemingly disappointing progress of the FERA schemes, and as a further unemployment crisis was looming in November 1933, a new agency was created—the Civil Works Administration (CWA)—for the immediate creation of four million jobs, leaving FERA to care only for unemployable people. A third agency, the Civilian Conservation Corps (CCC), was also created to set up work camps for young people and war veterans.

By January 1934, the CWA had been able to create the targeted four million new jobs in road creation and repair, public-building construction, and park construction. It was the largest and perhaps the most successful work-relief program in the depression. However, it was relatively expensive, and it created political difficulties with those unable to get the CWA's relatively well-paid jobs, so the program was terminated in the spring of 1934.

FERA took over again, and in 1935 the agency developed five new emergency-relief programs, two of which focused on educational content, one was directed to the so-called "interstate" transient who did not qualify for relief support in any state, and the remaining two focused on rural America.

As work-relief programs made little impact on the roots of unemployment, they may perhaps be better seen as steps in the development of the American welfare state. According to Fearon, "in February 1934, FERA, CWA, and CCC together gave aid to eight million households or some 22 per cent of the population" (1987, 243). But this form of emergency relief was not an appropriate permanent arrangement. In 1935, Congress passed the Social Security Act, one of the most important and long-lasting New Deal reform laws. The act provided for old-age pensions and unemployment compensation. These provisions were not to be seen as relief to destitute people but as a general insurance scheme paid for by taxes on both employers and employees.

Chapter 8

The Fragmented World of the 1930s

The two central themes in this chapter are the disintegration of the international economy that followed the onset of the depression and the more or less successful path to recovery in the main areas of the world. We look first at the extent of the disharmony and rivalry displayed by European nations and the United States at the World Economic Conference of 1933. Cooperation was desperately needed to mitigate the effects of the slump, but it was not forthcoming. Each country had its own agenda, its own economic and political priorities, and its own preferred solutions. The next sections examine the operation of the different trading areas that emerged in this decade, the economic policies followed by the main participants in each area, and their growth and employment outcomes.

Table 8.1 summarizes in a nutshell (with a good dose of oversimplification) the relation between exchange rate and domestic policies on the one hand and economic performance on the other, as measured by GDP per person. (This relation is discussed in more detail in the second part of the chapter.) By and large, recovery from the depression was faster and more robust in countries that, by an early dismissal of convertibility, were free to put in place fiscal and monetary polices apt to stimulate domestic aggregate demand.

England and the sterling area are the textbook case in point. By ending gold convertibility of the pound in September 1931, England was able to lower interest rates, thereby stimulating investment, particularly in the construction sector. The depreciation of the exchange rate stimulated both exports and the substitution of domestic products for foreign products. A somewhat muddled and inefficient way of getting rid of gold-standard constraints on domestic demand management without formally suspending convertibility (a move that some governments saw as a political suicide) was to introduce administrative controls on capital movements. For all practical purposes, this amounted to a devaluation of the currency. This policy was followed by Germany and later by Italy.