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HSS4 — Keynesian Economics
02/07/20

The Rise of a Dynamic Monetary Policy
Response to Keynes' Essay "The End of the Gold Standard"

Since ancient times, gold and money have been virtually synonymous. However, in 1931, Britain broke free of the gold standard that implemented the correspondence between money and gold, and John Maynard Keynes argues in his essay, "The End of the Gold Standard," that the gold standard only created "an intolerable strain" on national economies, motivated only by a historical "obligation of *honour*" to couple currencies with gold. He welcomes the change, citing its use in combating economic stall and the problematic concentration of gold in trade-surplus nations.

Keynes believes the gold standard is only "quixotry" — a romantic, old-fashioned want to keep money at its original worth; thus he cites contemporary and logical evidence to debunk its importance, such as the revitalization of the Stock Exchange in the weeks following the separation from the gold standard. He also reasons that the resulting decrease in national purchasing power is not detrimental to trade: a currency depreciation of 25% offers protectionist restrictions on imports, *and* a greater return on exports (i.e., a "bounty of the same 25 per cent"); benefits the economy bidirectionally and bilaterally; contrastly, tariffs are unidirectional. Keynes believes that becoming "the cheapest producer in the world in terms of gold" is of no consequence: maintaining an equivalent value in gold is not as important as keeping the economy flowing.

Then what are the fiat standard's downsides? For the countries following this new standard, Keynes presents no disadvantage, as each country may adjust their exchange rate to match their needs. However, the two major proponents of the gold standard — namely, France and the U.S., which had amassed much of the world's gold supply from trade or war reparations, and whose hoarding of gold led to its global deficit — are disadvantaged as their high-valued gold-backed currencies discourage trade.

Despite Keynes' optimism, the gold standard protected against hyperinflation, which plagued the Weimar Republic in 1921 after it left the gold standard in 1914; a prior and potential mishap Keynes fails to mention. Secondly, the fairness of currency manipulation is an activate debate, especially between inflated currencies in large national producers such as China, leading to the two-way benefits Keynes describes; this led to IMF regulation of currency exchange rates which

> "ensure that such countries regularly and promptly adjust the rate of exchange between their currencies and the United States dollar to permit effective balance of payments adjustments and to eliminate the unfair advantage" (United States, Dept. of Treasury, 1988).

One of the factors of the "trade war" between the U.S. and China, currently the two largest national economies, is that the IMF does not consider China as a currency manipulator while President Trump's administration does (United States, Dept. of Treasury, 2019). Now that the success of currency fluctuations as government policy has established it as an international norm, the legacy of the separation from the gold standard is how to determine when these measures go too far, and how to prevent against the possibility of the massive inflation that it promotes.

Works Cited

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7. The End of the Gold Standard
(Sept. 27, 1931)[29]
[29][On Sept. 21, 1931, the Gold Standard in Great Britain was suspended.]

There are few Englishmen who do not rejoice at the breaking of our gold fetters. We feel that we have at last a free hand to do what is sensible. The romantic phase is over, and we can begin to discuss realistically what policy is for the best.

It may seem surprising that a move which had been represented as a disastrous catastrophe should have been received with so much enthusiasm. But the great advantages to British trade and industry of our ceasing artificial efforts to maintain our currency above its real value were quickly realised.

The division of inside opinion was largely on a different point. The difficult question to decide was one of honour. The City of London considered that it was under an obligation of honour to make every possible effort to maintain the value of money in terms of which it had accepted large deposits from foreigners, even though the result of this was to place an intolerable strain on British industry. At what point—that was the difficult problem—were we justified in putting our own interests first?

As events have turned out, we have got the relief we needed, and, at the same time, the claims of honour have been, in the judgement of the whole world, satisfied to the utmost. For the step was not taken until it was unavoidable. In the course of a few weeks the Bank of England paid out £200,000,000 in gold or its equivalent, which was about half the total claims of foreigners on London, and did this at a time when the sums which London had re-lent abroad were largely frozen. No banker could do more. Out of the ashes the City of London will rise with undiminished honour. For she has played the game up to the limits of quixotry, even at the risk of driving British trade almost to a standstill.

No wonder, then, that we feel some exuberance at the release, that Stock Exchange prices soar, and that the dry bones of industry are stirred. For if the sterling exchange is depreciated by, say, 25 per cent, this does as much to restrict our imports as a tariff of that amount; but whereas a tariff could not help our exports, and might hurt them, the depreciation of sterling affords them a bounty of the same 25 per cent by which it aids the home producer against imports.

In many lines of trade the British manufacturer to-day must be the cheapest producer in the world in terms of gold. We gain these advantages without a cut of wages and without industrial strife. We gain them in a way which is strictly fair to every section of the community, without any serious effects on the cost of living. For less than a quarter of our total consumption is represented by imports; so that sterling would have to depreciate by much more than 25 per cent before I should expect the cost of living to rise by as much as 10 per cent. This would cause serious hardship to no one, for it would only put things back where they were two years ago. Meanwhile there will be a great stimulus to employment.

I make no forecast as to the figure to which sterling may fall in the next few days, except that it will have to fall for a time appreciably below the figure which cool calculators believe to represent the equilibrium. There will then be speculation and profit-taking in favour of sterling to balance speculation and panic selling on the other side. Our authorities made a great mistake in allowing sterling to open so high, because the inevitable gradual fall towards a truer level must sap confidence and produce on the ignorant the impression of a slide which cannot be stayed. Those who were guilty of undue optimism will quite likely succumb to undue pessimism. But the pessimism will be as unfounded as the optimism was. The equilibrium value of sterling is the same as it was a month ago. There are tremendous forces to support sterling when it begins to fall too far. There is no risk, in my judgement, of a catastrophic fall.

These, in brief, are the consequences in Great Britain. How will the rest of the world be influenced? Not in a uniform way. Let us take first the debtor countries to whom Great Britain has in the past lent large sums in sterling, and from whom interest is due in sterling, such as Australia, Argentina, and India. To these countries the depreciation of sterling represents a great concession. A smaller quantity of their goods will be sufficient to meet their sterling liabilities. The interest due to Great Britain from abroad, which is fixed in sterling, amounts to about £100,000,000 a year. In respect of this sum Great Britain now plays the part of a reasonable creditor who moderates his claim in view of so great a change in the situation as the recent catastrophic fall in commodity prices.

When we try to calculate the effect on other manufacturing countries, whose competition we are now in a better position to meet, the effect is more complex. A large part of the world will, I expect, follow Great Britain in reducing the former gold value of their money. There are already signs in many countries that no great effort will be made to maintain the gold parity. In the last few days Canada, Italy, Scandinavia have moved in our direction. India and the Crown Colonies, including the Straits Settlements, have automatically followed sterling. Australia and the whole of South America had already abandoned the effort to maintain exchange parity. I shall be astonished if Germany delays long before following our example. Will Holland deal final ruin to the rubber and sugar industries of the Dutch Indies by keeping them tied to gold? There will be strong motives driving a large part of the world our way. After all, Great Britain's plight, as the result of the deflation of prices, is far less serious than that of most countries.

Now, in so far as this is the case, we and all the countries following our example will gain the benefits of higher prices. But none of us will secure a competitive advantage at the expense of the others. Thus the competitive disadvantage will be concentrated on those few countries which remain on the gold standard. On these will fall the curse of Midas. As a result of their unwillingness to exchange their exports except for gold their export trade will dry up and disappear until they no longer have either a favourable trade balance or foreign deposits to repatriate. This means in the main France and the United States. Their loss of export trade will be an inevitable, a predictable, outcome of their own action. These countries, largely for reasons resulting from the war and the war settlements, are owed much money by the rest of the world. They erect tariff barriers which prevent the payment of these sums in goods. They are unwilling to lend it. They have already taken nearly all the available surplus gold in the whole world. There remained, in logic, only one way by which the rest of the world could maintain its solvency and self-respect; namely, to cease purchasing these countries' exports. So long as the gold standard is preserved—which means that the prices of international commodities must be much the same everywhere—this involved a competitive campaign of deflation, each of us trying to get our prices down faster than the others, a campaign which had intensified unemployment and business losses to an unendurable pitch.

But as soon as the gold exchange is ruptured the problem is solved. For the appreciation of French and American money in terms of the money of other countries makes it impossible for French and American exporters to sell their goods. The recent policy of these countries could not, if it was persistently pursued, end in any other way. They have willed the destruction of their own export industries, and only they can take the steps necessary to restore them. The appreciation of their currencies must also embarrass gravely their banking systems. The United States had, in effect, set the rest of us the problem of finding some way to do without her wheat, her copper, her cotton, and her motor-cars. She set the problem, and, as it had only one solution, that solution we have been compelled to find.

Yet this is quite the opposite of the note on which I wish to end. The solution to which we have been driven, though it gives immediate relief to us and transfers the strain to others, is in truth a solution unsatisfactory for every one. The world will never be prosperous without a trade recovery in the United States. Peace and confidence and a harmonious economic equilibrium for all the closely interrelated countries of the globe is the only goal worth aiming at.

I believe that the great events of the last week may open a new chapter in the world's monetary history. I have a hope that they may break down barriers which have seemed impassable. We need now to take intimate and candid conference together as to the better ordering of our affairs for the future. The President of the United States turned in his sleep last June. Great issues deserve his attention. Yet the magic spell of immobility which has been cast over the White House seems still unbroken. Are the solutions offered us always to be too late? Shall we in Great Britain invite three-quarters of the world, including the whole of our Empire, to join with us in evolving a new currency system which shall be stable in terms of commodities? Or would the gold standard countries be interested to learn the terms, which must needs be strict, on which we should be prepared to re-enter the system of a drastically reformed gold standard?