FACULTY OF ECONOMICS STUDY AIDS 2019

ECT1 Paper 5 British Economic History - EXAM

The Faculty Board has agreed to release outline solutions to the 2019 examinations as a study aid for exam revision. They are abridged solutions, and not 'definitive', and should therefore not be considered as an exemplar for 'complete' answers.

Note that the Faculty will not respond to any queries regarding these solutions.

Answers:

British Economic History 1850-1914

Output and productivity evidence suggests that Britain was outperformed by other industrialising nations, such as Germany and the USA, between 1850 and 1914. Consider whether this relative decline originated in the manufacturing or the service sector of the economy. Discuss whether this period witnessed the beginnings of Britain's long term relative decline.

- Output and productivity evidence: Matthews, Feinstein and Odling-Smee – poor performance in this period relative to earlier C19th. Feinstein – growth in output per capita lower than in other industrial nations. Overtaken by USA around 1890.

- Broadberry. Manufacturing sector, no steady relative decline in output per person employed (labour productivity) in sector. But consistently outperformed by USA – better natural resources, use of mass production. Catching up at whole economy level in part due to sectoral shift from agriculture into more productive services.

- Broadberry. Service sector, inefficiency can persist here, some protection and collusion. See American overtaking in output per person employed in this sector, Germany catching up. America introduces new managerial hierarchy on railways, 'mass produces' some financial services and steam liner voyages, Britain sticks to small scale, based on networks and tramp shipping. Germany – more efficient in transport and distribution, but not elsewhere at this time. Service sector performance explains whole economy catching-up and overtaking.

- Broadberry, Crafts: argue certain institutions in this period constrain future growth, particularly lack of competition in some industries (exacerbated in interwar period), lack of shareholder power, and power of craft skilled labour to protect type of work through unions. These things persist and prevent Britain adopting some of the American mass production techniques.

Poor entrepreneurship has been cited as a cause of late Victorian decline. Outdated technology in staple industries and the small size of British firms relative to their American counterparts bear witness to this. Does the evidence on these aspects of British business support the accusation of failing entrepreneurship?

- Technology in staple industries can be defended (McCloskey and Sandberg, Harley). Cotton: use of mule rather than ring spinning due to expense of raw material and abundance of skilled labour in UK. Coal: mechanical cutting less used because geology of coal seams different – require capital in drainage rather than cutting. Steel: technological hold up which needs to be overcome to use domestic iron ore and most up-to-date process.

- Size of firm certainly smaller in UK. Small, family run, where have mergers tend to be horizontal and not improve efficiency of the process. America – vertical integration and hierarchical management, attain larger size and mass produce. But mass production may not be suited to British conditions. Mergers/ oligopolies have cost to consumer. Competition, both with industry and from overseas (as a free trade nation) should ensure efficiency of British firms in the industries in which they operate. Also successful industries that do show entrepreneurship and mass production, but tends to be in light industries rather than old staples.

Entrepreneurs who organize corporations worry about losing control of their businesses. But the attempts they make to ensure their ongoing control increase investors' worries that profits will disproportionately be captured by insiders. Discuss the extent to which corporate governance practices in Britain assuaged or exacerbated these opposing worries. Do you think bad corporate governance contributed to British economic decline in the late nineteenth and early twentieth centuries?

- Parliament imposed reasonably strict governance rules on statutory companies (such as railroads and utilities), but corporations formed by registration under the companies acts could write their own rules, and most wrote rules that enabled entrepreneurs to maintain control (sometimes even by formally entrenching themselves). The London Stock Exchange's listing rules prohibited formal entrenchment but allowed most other ways of ensuring control. Moreover, most companies whose securities traded on the exchange were not formally listed.
- If the difference between statutory and registered companies mattered, we should observe small investors displaying a preference for the former. The relative capitalization figures (and data on the choices of small shareholders) certainly favour statutory companies, but the numbers could also be explained by other factors, most notably differences in risk.
- Companies organized for overseas ventures do not seem to have had better governance rules than companies operating domestically, so, contrary to Kennedy, it is unlikely that poor corporate governance explains the flow of funds out of the country.
- Companies compensated investors for their lack of power by maintaining dividends at high levels and by ritual performance at shareholders' meetings. There is quantitative evidence suggesting the former mattered and anecdotal evidence for the importance of the latter.
- The rules governing securities issues became stricter at the turn of the century, but most companies chose to raise funds privately rather than through public offerings of shares. As a result, data on publicly traded companies is a misleading indicator of economic activity in the corporate sector. More general macroeconomic indicators offer better metrics.

How does the idea of a "bifurcated labour market" help to explain the features of unemployment during the 1930s?

- Discuss the bifurcated British labour market in terms of short-term unemployment, high turnover and long-term unemployment and duration dependence. The short-duration group experienced high turnover and high re-employment opportunities, whereas the long-term unemployed group experienced low re-employment probabilities and duration dependence
- A feature of the 1930s was that the amount of long term unemployed was increasing. In 1929, 4.7% of males who were unemployed had been unemployed for more than a year. This figure rose in the early 1930s and settled around 25% in 1938. A discussion of the measurement of the long-term unemployment problem (as a ration of the unemployed) would allow for a more refined essay.
- Insider-outsider effects may be important in determining this bifurcation. The Insider-outsider model suggests that the real wage is set by insiders and that outsiders cannot influence the wage bargaining process. Since the outsiders have no effect of the wage level, the level of unemployment shows no tendency to return to the pre-shock level. The wage equation estimates of Crafts helps us understand this effect in the context of the 1930s
- The bifurcated labour market is a good way of explaining the features of unemployment during the 1930s. It helps to account for the apparent paradox of unemployment rates falling during the recovery period of 1932-37 whilst workers that were long term unemployed became a new problem in the 1930s.

Evaluate the effects of Britain's return to the gold standard at the 1913 gold parity on trade and economic growth.

- Effects on real effective exchange rate and recession 1920-1
- Effects of real exchange rate on trade adjustment in the depression 1920-1
- Effects on trade during the exchange rate correction 1921-29 –short run some favourable effects
- Analysis of exchange rate shock and trade hysteresis effects in 1920s.
- Price deflation effects and debt burden in 1920s
- Possible long term effects via the output gap arising in 1920-1
- Possible negative effects from deflation, public debt and public debt service –linking the fiscal discussion in the lectures

Evaluate the evidence as to whether the 1932 General Tariff impacted adversely on Britain's economic recovery during the 1930s.

- Import Substitution effects –Richardson, Kitson Solomou, Broadberry Crafts evidence

- Resource Allocation -Effective Protection Rates (Capie, Kitson-Solomou-Weale)

- Macroeconoimic impacts – Foreman Peck, Kitson Solomou, and Tariff-Growth literature. Broadberry's analysis of floating exchange rates contrasted to evidence of a managed exchange rate under the exchange equalisation account,

- A discussion of Imperial Preference will also allow us to evaluate the effects on trade creation and trade diversion in the context of trade collapse in the 1930s.