Slouching Towards Utopia?: An Economic History of the Long Twentieth Century

XIII. Climbing Out of the Great Depression

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To follow the story of human progress, we need to look at the institutions that grew slowly and hesitantly as the North Atlantic began to climb out of the Great Depression in the late 1930s.

13.1. The Course of Recovery

13.1.1. Recovery Was Slow

The Great Depression was not only deep but long. The first reason was workers' unwillingness to risks, but rather to settle for what manner of living they could find that was most secure. The experience of long and high unemployment costs a large and deep shadow on the labor market: a phenomenon that Blanchard and Summers named *hysteresis*, in rather poor analogy with electromagnetism. Thus risky but profitable enterprises had a difficult time attracting the workers they needed, and so investment remained depressed.

The second reason it was long was the memory of and the belief that economies needed to get back to the gold standard. Those kept governments in the 1930s from taking many of the steps to boost production and employment they might have: the gold standard was dead by 1931, but its ghost continued to haunt the world economy. Thus few reflationary measures were undertaken. The one that was was currency depreciation: stimulating net exports by switching demand to and away from foreign-made goods. Commentators disparaged currency depreciation as “beggar-thy-neighbor”. It was. But it was the only thing generally undertaken that was effective.

The third was the lack of a *hegemon* to guide coordinated action in international monetary affairs. The major monetary powers of the world passed up their chances to do anything constructive together. Recovery, where it came, was national only, not global.

That the Great Depression was long meant that the reaction to it shaped nation states’s politics and societies for a long time to come, for the persistence of the Great Depression shook the internal politics of almost every country in the world. In Scandinavia that social democratic parties had more-or-less successfully managed to navigate through the Great Depression put them into power for the succeeding half-century. In much of continental Europe Depression reinforced reaction: one of the gifts that the Great Depression gave the world was Spain’s long-lived fascist dictator, Generalissimo Francisco Franco; a second such gift was Adolf Hitler. In America, by contrast, the Great Depression did not empower reaction but rather liberal and social democratic experimentation the growth of the social insurance state by providing the setting for Franklin Roosevelt’s New Deal.

This is somewhat of a surprise: why did the Great Depression push the U.S. not right but left? My guess is: sheer luck—Herbert Hoover and the Republicans were the right and were in power when the Great Depression started, they were thrown out of office in 1932, and the American political order was not then good soil for growth of a further-right movement.

That Franklin Roosevelt was center-left rather than center-right, that the length of the Great Depression meant that institutions were shaped by it in a durable sense, and that the U.S. was the world’s rising superpower and the only major power not crippled or near-crippled by World War II made a huge difference. After World War II the U.S. had the power and the will to shape the world outside the Iron Curtain.

The principal rule rule to memorize about recovery from the Great Depression was this: the sooner countries went off the gold standard, the better; and the less that gold standard habits of orthodoxy fettered countries thereafter, the better.

The Scandinavian countries bailed first, and did best. Japan was second. Britain also abandoned the gold standard in 1931, but Japan embraced expansionary policies more thoroughly. The U.S. and Germany abandoned the gold standard in 1933, but Hitler had a clearer view that Nazi persistence and success required putting people to work than FDR did with the try-everything-expediency of his New Deal. France stuck it out on the gold standard until 1937, and did worst of all.

More important than that the U.S. was a laggard in recovery was that the U.S., under Franklin Roosevelt, learned this first principal rule about recovery—and then applied it.

13.1.2. The U.S.: The First New Deal

13.1.2.1. FDR at The Chicago Convention

Before the 1930s, U.S. presidential candidates and simply not appeared at the national political conventions. Candidates were supposed to remain at their homes, tending to their private affairs, until informed (a week or so after the convention) by party officials that they had been chosen. They were supposed to emulate the Roman politician Cincinnatus, who mythically remained on his small farm ploughing his crops until told that he had been elected commander-in-chief of the Roman army and dictator of Rome. The conventional pretense was that the man did not seek the office: the office sought the man.

Then-Governor of New York Roosevelt broke tradition and flew to Chicago—in part, historian Frank Leuchtenburg says, to disprove whispers that a polio victim with paralyzed legs was too frail to undertake a full-scale American presidential campaign—and spoke:

> breaking the absurd tradition that the candidate should remain in professed ignorance of what has happened.... You have nominated me... I know it... I am here to thank you for the honor.... In so doing I broke traditions. Let it be from now on the task of our Party to break foolish traditions.... I pledge you, I pledge myself to a new deal for the American people…

13.1.2.2. What Was the First New Deal?

Roosevelt's "New Deal" was, first, a unique moment in American political history. Usually American politics is the politics of near-gridlock. The elections of the 1930s would be different. Roosevelt won 59 percent of the vote in 1932—an eighteen percentage-point margin over Herbert Hoover. Congress swung heavily

Democratic in both houses. To an extent never before seen since the Civil War, the president and his party had unshakable working majorities in both houses of the legislature—if Roosevelt could persuade a fractious coalition, including many southern legislators who were Democrats only because the white south remembered that it was Republican Abraham Lincoln who had freed the slaves, to come with him.

The new majority was looking for direction. Roosevelt had a conviction that he could do something important. And he was certain that Herbert Hoover had gotten it wrong. What Hoover had been doing was raising tariffs, maintaining the gold standard, acting aggressively to balance the budget, and block attempts to start employment-promoting public works. Roosevelt was going to do the opposite.

Otherwise?If you had a half-plausible thing, you had a good chance of persuading Roosevelt to try to do it. And Roosevelt was going to try things. He told his congress that if it failed to pass his proposals:

> I shall not evade the clear course of duty that will then confront me. I shall ask the Congress for the one remaining instrument to meet the crisis—broad Executive power to wage a war against the emergency, as great as the power that would be given to me if we were in fact invaded by a foreign foe…

The day after his inauguration President Roosevelt exceeded what a reasonable observer would have seen as his statutory powers by forbidding the export of gold and declared a bank holiday—a nationwide banking shutdown to freeze the then-ongoing banking crisis. The justification? The World War I-era "trading with the enemy" act. But there was no enemy.

Within four days the House and Senate had convened and—the House unanimously—passed Roosevelt's banking reform bill, arranging for the reopening of solvent banks, the reorganization of other banks, and giving Roosevelt complete control over gold movements. The second bill Roosevelt submitted to congress—also passed immediately—was an "economy" bill, cutting federal spending and bringing the budget closer to balance. The third submission was a request for an end to Prohibition—for the repeal of the constitutional amendment banning alcohol. On March 29 Roosevelt called on congress to regulate financial markets. On March 30 congress established Roosevelt's Civilian Conservation Corps. On April 19 Roosevelt took the United States off of the gold standard. On May 12 congress passed Roosevelt's Agricultural Adjustment Act. On May 18 Roosevelt signed the Tennessee Valley Authority bill creating, the first large governmentowned utility corporation in the United States.

Also on May 18, President Roosevelt submitted to congress the center-piece of his first hundred days: the National Industrial Recovery Act, or NIRA. All factions within the newly-constituted administration won something in the legislation:

- Businesses won the ability to collude—to draft "codes of conduct" that would make it easy to maintain relatively high prices, and to "plan" to match captacity to demand.
- Socialist-leaning planners won the requirement that the government—the National Recovery Administration, or NRA—approve the industry-drafted plans.
- Labor won the right to collective bargaining, and the right to have minimum wages and maximum hours incorporated into the industry-level plans.
- Spenders won some $3.3 billion in public works.

The first new deal was: a strong "corporatist" program of joint government-industry planning, collusive regulation, and cooperation; the entire farm sector on the federal dole indefinitely with strong regulation of commodity prices; building and operating utilities; undertaking huge amounts of public works spending; establishing meaningful federal regulation of financial markets; insurance for small depositors' bank deposits; mortgage relief; unemployment relief; plus promises to lower tariffs, lower working ours, and raise wages.

13.1.2.3. How Did the First New Deal Work?

What did it all add up to?

The NIRA did break the back of expectations of future deflation. The creation of deposit insurance and the reform of the banking system made savers willing to trust their money to the banks again. It began the reexpansion of the money supply. Corporatism and farm subsidies did spread the pain of the Great Depression to some extent. Taking budget balance off the agenda helped. Promising unemployment and mortgage relief helped. Promising public-works spending helped. All these policy moves kept things from getting worse. They certainly made things somewhat better. And things became substantially better immediately.

But the rest of Roosevelt's "hundred days"? It is not clear whether the balance sheet of the rest of the hundred days is positive or negative. The "economy" bill that cut spending and relief did harm. Much of financial market regulation (save deposit insurance) was simply irrelevant to the Great Depression. Farm subsidies set the American government on a path that would prove expensive and counterproductive for the next sixty years.

The full-fledged policy of monetary inflation and mammoth fiscal deficits that might have pulled the country out of the Great Depression quickly—that did pull Germany under Hitler out of the Great Depression quickly—was not tried. 1934 was a better economic year than 1933, 1935 was better than 1934, and 1936 was better than 1935, but not by much.

Consumers complained that the NRA raised prices. Workers complained that it gave them insufficient voice. Businessmen complained that the government was telling them what to do. Progressives complained that the NRA created monopoly. Spenders worried that collusion among businesses raised prices, reduced production, and increased unemployment. Roosevelt's experiment with "corporatism"—which crusty Democrats like Senator Carter Glass denounced as "the utterly dangerous effort of the federal government at Washington to transplant Hitlerism to every corner of this nation" was over.

The slide in which each year was worse than the one before had been ended by the Depression. Some ground had been regained. But happy days were not here again.

And Herbert Hoover and ilk ranted that Roosevelt's policies were Bolshevist. Hoover and his ilk ranted that Roosevelt's refusal to commit in November 1932 to continue Hoover's policies had killed the economy over the winter, and had created a false baseline relative to which Roosevelt was falsely claiming victory. Hoover and his ilk ranted that recovery would have come of itself, and faster than under the New Deal, if only Hoover had won a second term and had a supportive congress.

13.1.3. The U.S.: The Second First New Deal

Therefore Roosevelt kept trying different things.

If business-labor-government "corporatism" did not work—and was blocked by the Republican Supreme Court—perhaps a safety net would. The most enduring and powerful accomplishment of the New Deal was to be the Social Security Act, which provided federal cash assistance for widows, orphans, children without fathers in the home, and the disabled; and which also set up a near-universal system of federally-funded old-age pensions.

If pushing up the dollar price of gold did not work well enough, perhaps strengthening the union movement would: another enduring accomplishment of the New Deal was the Wagner Act, that set down a new set of rules for labor-management conflict, strengthened the union movement, and meant that the wave of unionization in the United States in the 1930s survived for half a century (rather than being rolled back within half a generation, as had happened to previous expansions of the union movement in the United States. Massive public works an dpublic employment programs restored some self-esteem and transferred some money to households without private-sector jobs—but at the probable price of some delay in recovery, as firms and workers saw higher taxes.

Antitrust policy? The breaking-up of utility monopolies? A more progressive income tax? Finally, a hesitant embrace of deficit spending not just as an unavoidable temporary evil but as a positive good? All were tried. In the end they probably did little to cure the Great Depression in the United States. But they did turn the U.S. into a modest European-style social democracy.

And as the decade came to an end Roosevelt's concerns shifted to the forthcoming war in Europe and to the Japanese invasion of China. Dr. New Deal was replaced by Dr. Win the War.

13.2. Patterns of Recovery Outside the United States

13.2.1. National Patterns

13.2.1.1. Those That Did Well

In one region of the North Atlantic alone was the Great Depression shallow, short, and followed by a decade of strong economic growth: Scandinavia.

In the interwar period the Swedish socialists won enough votes to exercise power. In sharp contrast to their counterparts in Britain and France—who had no idea of what a left-wing exercise of political power would be (in large part because they bought their own propaganda that the cruelties of interwar capitalism were an inevitable part of the functioning of a market economy)—Sweden's socialists knew: things like housing subsidies, paid holiday and maternity benefits, expanded public-sector employment, government loans to the newly-married—all made possibly by a monetary policy that early cut loose from the gold standard and pursued the goal of domestic balance through easy money and stimulated exports through the consequent low value of the real exchange rate. The Swedish socialists turned into social democrats: they lost their commitment to the apocalyptic doctrines of socialism, lost their belief that all private property was inherently evil, lost their belief that only a great and sudden revolutionary transformation could bring about a better society. Democracy became a goal rather than a tactic.

Close behind Scandinavia in having a mild Great Depression was Japan. Fiscal orthodoxy and budget balance were abandoned in 1931. The Great Depression was not deep, and was over by 1932. It was due to Takahashi Korekiyo, not one of the "Meiji Six" but in the next rank of Japanese modernizers. At 72 he became Minister of Finance for the third time in 1931, and he had little tolerance for European models of "sound finance". Japan adevalued its currency in order to boost demand by making its export industries hyper-competitive and generating an export boom, and embarked on a massive program of armaments. Industrial production in Japan in 1936 was half again as much as it had been in 1928. Good short-run economic policy. Bad long-run strategy: The armaments boom and the loss of civilian control over the military led to getting involved in a land war in Asia and then launching pin-prick attacks on the world's two superpowers, Britain and the United States. Takahashi Korekiyo did not live to see World War II. He was one of three senior politicians successfully assassinated on February 26, 1936, when the Imperial Way faction of the army attempted to seize power. He had not pushed the military budget high enough to please the coup plotters.

Third to recover was Nazi Germany, once Hitler had taken power and broken adherence to monetary and fiscal orthodoxy. With the Gestapo in the background and with strong demand from the government for public works and military programs, unemployment fell rapidly in Germany in the 1930s. Hitler appears to have been focused on employment and weapons, not adding to industrial capacity and increasing national wealth. Build national highways, yes—but build them not by building individual city-to-city or resources-to0-industry links, but by building as much as possible first where it would be seen as many as possible. Political effectiveness and military capacity were the priorities.

Political effectiveness we understand. But weapons? Armies? Hadn't World War I taught the Germans, and even the Nazis, and even Hitler, not to do *that* again? No, it had not.

13.2.1.2. Those That Did Poorly

Close to bringing up the rear in the race for recovery was Britain. Great Britain was forced off the gold standard in September 1931. But Britain's abandonment of the gold standard was not followed by large-scale reflation. The Bank of England did its part, cutting back on its short-term discount rate. The National-Conservative government did not do its. In October the Conservative Party swept the general election, winning 78 percent of seats in the House of Commons. The government that followed was Conservative. Conservative Stanley Baldwin ran things, with ex-Labourite Ramsey MacDonald as an initial figurehead Prime Minister. Britain's recovery from the Great Depression was slow and painful.

The United States's recovery lagged both Germany's and Britain's. But it was France that brought up the rear. France's undervalued exchange rate parity meant that, when the Great Depression began, it had little *initial* effect on France. But as exports dropped, country after country devalued to try to regain some foreign demand. Increasingly, countries that had not devalued found their industries uncompetitive, their payments in deficit, and their maintenance of convertibility a source of domestic unemployment because they had to maintain higher interest rates and apply further deflation to keep foreign exchange speculators' greed in balance with their fear. A fragmented electorate produced unstable coalition governments. From the crash of 1929 to 1936, the French Prime Ministers were, in succession: Briand, Tardieu, Chautemps, Tardieu again, Steeg, Laval (remember him?), Tardieu yet again, Herriot, Boncour, Daladier, Sarraut, Chautemps again, Daladier again, Doumergue, Flancin, Bouisson, Lavel (again), Sarraut (again), and finally Leon Blum, Popular Front Prime Minister who grasped the nettle, and France and the rest—the Netherlands, Switzerland—abandoned their gold parity in 1936.

Blum promised to restore pensions and public-sector wages to the levels they had held before the budget cuts of the preceding two years. Blum promised to greatly increase unemployment benefits. Blum had promised to defend the franc—no devaluation. Blum promised to balance the budget. Blum promised to cut back on military spending. Blum promised to share the work and the wealth by cutting back on working hours and supporting strikes. It did not add up. Blum abandoned the gold standard. But that did not mean substantial expansion of aggregate demand: the government's belief that the government *should* be trying to balance the budget led to the scaling-back of its non-military spending programs. The investing public's fear of socialism more than offset the positive, stimulative effects of a late devaluation. France entered 1938, the last year before the beginning of World War II in Europe, with its level of industrial production still less than the level attained in 1929.

13.2.2. Global Patterns

The major monetary powers of the world regularly passed up their chances to do something constructive to help the world monetary system as late as 1933, when the London Economic Conference collapsed in disagreement. The French believed that they should try to maintain the gold standard. The British, who had long since abandoned the gold standard, were unwilling to, in Eichengreen's words, "…tie their policies to those of a foreign partner [the United States] of whose intentions they were unsure." Coordinated reflation was the first obvious strategy. But it was never tried. Fiscal expansion was the next obvious thing to try. But it was not attempted until the very end of the decade, when the threat of war made governments realize that spending public money building weapons was more important than trying yet again to balance the budget.

13.3. The Depression as Defining Moment

13.3.1. Social Democracy Comes to America

In the long run Franklin D. Roosevelt's policies mattered not because they cured the Great Depression, but because they left behind a different—a much more social democratic—America. In sector after sector, the Great Depression encouraged and allowed to do things that brought the U.S. government much closer to the social democracies of Europe.

The most important social programs of twentieth century America all started in the 1930s. The Social Security system, supplemental support for the elderly even outside the contributory system, a framework for labor unions to bargain with their employers, aid to families with dependent children—although that "right" is now long gone: in today's America poor children receive government support only to the extent that their parents' behavior is pleasing to not the federal but the local state government—unemployment insurance, the peculiar American farm subsidy system, and our system of financial regulation. More important, the Great Depression produced and solidified the idea that the *government* was responsible for the health of the economy.

Some historians interested in continuity trace the roots of New Deal programs back to World War I or to the Progressive Era. But steps toward social democracy in Minnesota or Wisconsin or Massachusetts had not attracted large-scale support across the country. The Great Depression taught a painful lesson about how private might fail, and how public might succeed in ameliorating if not resolving problems. Michael Bordo, Claudia Goldin, and Eugene White ask: "Did the Great Depression alter the public's view concerning the functions of government, particularly those at the national level?" And they answer: "It would certainly appear that it did." Capitalism had failed—at least partially failed—and it was hard to argue to workers without jobs (or who remembered that they or their parents had been without jobs), to farmers who had lost their farms (or to those who remembered that they or their parents had lost their farms) that government intervention would inevitably destroy a near-utopian near-*laissez faire* economy.

Thus the Great Depression called forth a substantial increase in the government share of the economy, both in the scale of programs started during the New Deal and in people's willingness to consider other possible roles for the government.

13.3.2. Income Distribution and Societal Well-Being

The usefulness of market systems as social allocation and control mechanisms—as instruments to guide economic activity in ways that promote the general welfare—depends on the distribution of income. Markets carry out their implicitly assigned tasks with ruthless efficiency. The key to managing systems of markets is to determine what instructions the market is being implicitly given, and how to alter those instructions.

Systems of markets can indeed promote the general welfare under certain conditions. These required conditions are that property rights be well-defined, and that spillovers be small—thus market systems will be good at activities like allocating labor or finding and exploiting minerals (where property rights in land are set), and will be bad at activities like directing the proper amount of resources to research (for one firm can receive powerful benefits from another's research) and controlling pollution (for no one polluter benefits directly and immediately from his own pollution reduction).

There is another required condition: that the general welfare be defined in a way that weights the material well-being and utility of each individual in an appropriate manner that depends on his or her wealth. Suppose each doubling of material consumption adds an equal amount to individual utility—that the first dollar of income is more valuable than the second, the second more valuable than the third, and so on. Then theoretical economists' formulas and theorems take on a particularly simple form: the market maximizes the general welfare if and only if the general welfare weights each person's well-being by the market value of his or her wealth.

With unequal distribution a market economy will generate extraordinarily cruel outcomes. If my wealth consists entirely of my ability to work with my hands in someone else's field, and if the rains do not come so that my ability to work with my hands has no productive market value, then the market will starve me to death.

13.3.3. The Eclipse of Market Ideology

13.3.3.1. George Orwell's Take

The failure of "orthodox" economics to have anything constructive to say about the Great Depression paved the way for the emergence of social democracy. *Laissez-faire* had been supported by habits of mind. Social Darwinism, the benefits of free competition, and the rest seemed much less reasonable, and must less worthwhile during the Great Depression. As George Orwell put it: "the thing that horrified and amazed me was to find that many were *ashamed* of being unemployed. I was very ignorant, but not so ignorant as to imagine that when the loss of foreign markets pushes two million men out of work, those two million are any more to blame than the people who draw blanks in the Calcutta Sweep." And few had a reply in the depths of the Great Depression.

But once unemployment is no longer seen as the fault of the unemployed, any belief that the market order of income and work unpleasantness is the result of personal responsibility becomes vulnerable as well. Thus someone like Orwell could reframe coal miners not as unskilled workers with a union who were probably overpaid, but benefactors whom the rest of us had not properly acknowledged:

> Practically everything we do, from eating an ice to crossing the Atlantic… from baking a loaf to writing a novel, involves… coal…. It is only because miners sweat their guts out that superior persons can remain superior. You and I and the editor of the *Times Lit. Supp*., and the Nancy Poets and the Archbishop of Canterbury and Comrade X, author of *Marxism for Infants*—all of us really owe the comparative decency of our lives to poor drudges underground, blackened to the eyes, with their throats full of coal dust, driving their shovels forward with arms and belly muscles of steel…

Orwell's touchstone for judging a social system was a combination of honesty, decency, prosperity, and liberty, but with the accent on decency. The social and economic system had a moral obligation to treat these men-its most productive resource-well. It was not decent that they should be without work. And since the system did not live up to the obligations it had undertaken, it did not deserve to survive.

13.3.3.2. A Real Third Way?

With the coming of the Depression, it was impossible not to conclude that the old order was bankrupt. And as it fell it took representative democracy down with it. By 1939 representative democracy was to be found only in Great Britain and its Dominions, in the United States, in France, and in the arc of small northwestern European countries: Switzerland, Luxembourg, Belgium, the Netherlands, Denmark, Norway, Sweden, and Finland.

Few would claim that market economies had delivered, or could reasonably promise that they would deliver Everywhere else the combination of democratic representative governments and market economies had been tried and been found wanting. It seemed quite likely that you had a Hobson's choice: You could abandon the market economy, and hope that an as-productive and more-equal socialism could deliver human freedom and something like political democracy (although the example of the internal politics of the Soviet Union gave no confidence). You could abandon political democracy, and so hope then, under the guidance of a wise leader to provide purpose, preserve the market economy and private property and the choice, autonomy, and inequality—for most a bug, for some a feature—that it brought (although the examples of Mussolini and Hitler gave little hope for avoiding regimentation and preserving freedom of thought and discussion).

If choices boiled down to Hitler or Stalin, how should people choose? Many—including thinkers and politicians who would play major roles in the 1940's in setting the foundations of the post-World War II liberal democratic industrial capitalist order—chose Stalin for at least a little while, doubting the survival (or the value) of the old order, and hating Hitler more. Many others chose Hitler for at least a little while, hating Stalin more. But it turned out people did not have to choose.

13.3.3.3. The Voice in the Air: An "Academic Scribbler"

We assign this third way to John Maynard Keynes: his is the name we use to label it. But, truth be told, William Beveridge and A.C. Pigou played as large a role in formulating the ideas on the level of economics and political economy. And many, many others contributed mightily in thought, in institution building, and in practice. Building a political-economic order that repaired the flaws of while grasping the opportunities of the market system was a very broad current. It had been dammed by ideology and plutocracy before the Great Depression. The Great Depression made the dam break.

Keynesianism and the "mixed economy" had become the dominant ideology in the world economy's North Atlantic industrial core. It provided North America and western Europe with a Keynesian escape hatch from what had been insoluble crises and contradictions in the years up to 1939: solid ground between *laissez faire* on the one hand and some form of Total State on the other. You could avoid the waves of mass unemployment and the extremes of relative wealth and poverty of the first without risking the dangers of the second. One way to read Keynes's *General Theory of Employment, Interest, and Money* is as a confident prediction that all that was needed were relatively minor reforms, and that such relatively minor reforms could successfully stabilize the economy with nearly-perpetual full employment. An activist welfare-state government with a commitment to full employment had the tools to level the distribution of income, eliminate Great Depressions, and could put economies back onto the road to utopia.

If governments would only lower interest rates and spend money freely (without raising taxes) in times when total demand was low and raise interest rates and raise taxes (without spending) in times when total demand was high, Great Depressions could be avoided. Gross inequality was produced by mass unemployment and the fear of mass unemployment. Mass unemployment was produced by the extreme severity of the business cycle. And the extreme severity of the business cycle were "the fruits of risk, uncertainty, and ignorance". The cure was straightforward: "partly to be sought in the deliberate control of the currency and credit by a central institution, and partly in the collection and dissemination on a great scale of data relating to the business situation". Call it minimal central planning: "society in exercising directive intelligence… yet it would leave private initiative and enterprise unhindered".

But, as Pigou pointed out, that private initiative and enterprise needed to be properly channeled. The *laissez-faire* market was rife with externalities—positive and negative—and monopoly. The government needed technocrats who could nudge, via taxes and subsidies, prices away from where the *laissez-faire* market put them to levels where they provided proper incentives to induce the crowdsourcing of solutions to societal problems. And, as Beveridge points out, a market system not only allocates resources, it also distributes incomes and then makes its decisions by giving those with the larger incomes much larger voices. Egalitarian redistribution and income support are as key toward making a market economy work for societal purposes as are Keynesian demand management and Pigovian nudges.

Stabilize the macroeconomy, adjust prices for eternalities, properly manage income distribution, and all of a sudden political democracy, human liberty and freedom from regimentation, and the productivity and growth benefits of a (largely) market economy could be grasped. Humanity could then awaken from the nightmare of 1914-1945 to what had been reality before 1914, when humanity had been progressing fitfully—slouching—towards utopia. Or, it turned out, humanity could awaken to an even better daylight than that of the years before 1914, in the North Atlantic at least.

From the left, Keynes and the Keynesians, the compromisers, the ideologues of the "mixed economy" were denounced somehow unfairly stealing the future. Capitalism contained *fatal and irresolvable* contradictions that could not be forever avoided by Keynesian sleight-of-hand. Authors like Paul Sweezy would confidently predict socialism and government planning would deliver a more efficient allocation of productive forces and a faster rate of economic growth: we will outlive you, and so have to preside at your funeral, in the Russian proverb that Nikita S. Khrushchev used in the late 1950s.

From the right, Keynes and the Keynesians would be denounced because an economy could not forever by government financial legerdemain live beyond its means on its wits, in words that we have noted from Churchill's Private Secretary P.J. Grigg put it. The most incisive if not the shrewdest critic of Keynes, the University of Chicago's Jacob Viner, said that Keynesianism worked only if "volume of employment, irrespective of quality, is considered important", and only as long as "the printing press could maintain a constant lead" in an inevitable race with "the business agents of the trade unions" could it avoid inflationary self-destruction. They continued to burble underground, and would resurface to dangerous effect in 2008. That year saw a revival of the Schumpeterian claim that mass unemployment was an essential part of the process of economic growth, and attempts to artificially keep the unproductive at work from experiencing it would only store up more trouble for the future. Witness the University of Chicago's John Cochrane's claim in November 2009 that he welcomed recession because "people pounding nails in Nevada need to find something else to do", and thought recession unemployment would be a welcome spur.

Keynes snarkily cast shade at his then-present and future intellectual opponents. He highlighted that his escape hatch would seem to a "nineteenth-century publicist or to a contemporary American financier to be a terrific encroachment on individualism”. He told such people to shape up and get with the program: he had “the only practicable means of avoiding the destruction of existing economic forms in their entirety”. Moreover, if his critics were even half-smart, they would understand that successful capitalism needed the support of an activist government ensuring full employment, for without it only the lucky innovators would survive, and only the mad would attempt to become innovators, and growth would be much slower than necessary:

> If effective demand is deficient… the individual enterpriser… is operating with the odds loaded against him…. Wealth has fallen short of… savings… [with] losses… [for] those whose courage and initiative have not been supplemented by exceptional skill or unusual good fortune.”

13.3.3.4. Keynesianism Worked

Those countries that had attempted to exit through the Keynesian escape hatch (largely by fortunate accident) during the Depression did indeed do relatively well. World War II provided further proof: in the United States unemployment that had been called “structural” or “permanent” during the 1930s and had appeared immune to the self-adjusting forces of the market as well as to the entire armament of the New Deal vanished entirely in the 1940s under the pressure of vastly expanded government spending. The United States fought World War II *without* reducing the real value of civilian consumption: all U.S. war production came from new capacity, or from capacity that stood idle at the end of the 1930s.

The magnitude of Depression-era unemployment shifted politicians’, industrialists’, and bankers’ beliefs about the key goals of economic policy. Before the Depression a stable currency and exchange rate were key. But after the Depression even the bankers recognized that a high overall level of employment was more important than avoiding inflation: universal bankruptcy and mass unemployment were bad for workers, but they were worse for capitalists and bankers.

Thus entrepreneurs, the owners and managers of real capital—industry—and even the bankers found that they gained, not lost, from a commitment to maintain high employment first. High employment meant high capacity utilization. Rather than seeing tight labor markets erode profit margins by raising wages, owners of property saw high demand spread fixed costs out over more commodities and so increase profitability.

There is a sense in which Christian and social democracy, the twin political powers of the post-World War II world, evaded class-conflict based dilemmas of the interwar and pre-World War I politics *because* the shock of the Great Depression shifted politics from a concern over redistribution to a concern over production. All would lose heavily from another Great Depression. It seemed much more worthwhile to compromise, and to pursue policies that would enlarge the pie to be distributed rather than for either side—either the left or the right—to engage in substantial redistribution. For all parties the post-World War II mission became, in Charles Maier's words:

> one of expanding aggregate economic performance and eliminating poverty by enriching everyone, not one of redressing the balance among economic classes or political parties. The true dialectic was not one of class against class, but waste versus abundance.

It is very hard to argue that accepting the "mixed economy" was a mistake for anyone. Had either owners or workers tried to hold out for more—as they did in the interwar period—they might well have ended up with far less.