

**IDEAS AND POWER: SHAPING MONETARY POLICY IN SOUTH  
AFRICA 1919 – 1936**

**THESIS**

**Submitted in fulfilment of the requirements for the degree of Master of Commerce in  
the Department of Economics and Economic History, Rhodes University**

**By**

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## **DECLARATION**

**Except for the references specifically indicated in the text, and such help as I have acknowledged, this thesis is wholly my own work and has not been submitted for degree purposes at any other university.**

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## ABSTRACT

In the concluding paragraphs of Keynes' *General Theory*, Keynes suggests that vested interests (power) may dominate in the short term, but that "sooner or later, it is ideas, not vested interests, which are dangerous for good or evil" (Keynes; 1936:384). This dissertation seeks to establish whether this is so, and to what extent, in the period 1919 to 1936, insofar as the shaping of monetary policy was concerned.

The context that South Africa found itself in at the time was one in which Britain, the colonising power, was in economic decline. Britain's real economy had lost its lead in the world in the late 1800s, and by our period, 1919 – 1936, she was now struggling to maintain her dominance of the world's financial economy. South African gold flows to London, and a South African monetary policy supportive of British monetary policy, became more important than ever to Britain. On the back of its ascendant real economy, the United States of America was fast developing its financial sector as a rival to that centered on London.

In the broader monetary policy world, the orthodox monetary regime of the Gold Standard, which had worked so well in the period from 1875 to 1914, was firstly difficult to re-establish, and once established, difficult to maintain. Opinion on what should be done was divided between the majority who favoured a return to the orthodoxy, and a much smaller group, including John Maynard Keynes, who argued that the Gold Standard should no longer be the preferred monetary system.

In South Africa, our period starts 17 years after the Second Boer War. Afrikaner nationalists intent on establishing independence from Britain, competed with those, including Jan Christiaan Smuts, who believed that tying our policy up with that of the British Empire was the best for South Africa.

It is in this context that a naturalised Briton, which the research shows was a loyal servant of the London power elite, was appointed by the Empire-friendly Smuts government to advise the South African government on monetary policy, the setting up of the South African Reserve Bank, the appointment of its first Governor and other matters in the period up until the fall of this government in 1924. It is also in this context that an American 'Currency

Doctor' and Professor of Economics at Princeton University, which the research shows was intimately connected with the American government and Benjamin Strong at the Federal Reserve, was appointed by the Pact government later in 1924, and who was anxious to throw off the yoke of British control.

The theoretical paradigm of this study is that developed by John Maynard Keynes and after him by the post-Keynesian economists, particularly Basil Moore and Hyman P. Minsky. Instead of considering the theory chronologically, book by book, the theory section deals with the subject matter in the themes which came up in the monetary policy debates of the time, looking at all the theoretical literature that applied to these various themes.

Aside from the correction of errors of emphasis and errors of fact dealt with in chapter two, chapter five of the dissertation is where most of the original research is reflected. This is the section which deals in depth with the experts that advised the South Africans at the time, how they came to be appointed, whose interests they served, what theories they used in support of their positions, and what was the decision-making process; from their appointment, until their reports were drafted into the law of the Union of South Africa. While Ally's work (1994) is accepted as the principal work on the influence of the Bank of England, and Britain's control of South African gold on South African gold and monetary policy, this dissertation claims legitimacy based on a much closer look at the motives and vested interests of the experts advising the South African government at the time. By the end of this chapter, I believe we are better placed to understand and analyse the relative influence of ideas and power on monetary policy in the period 1919 – 1936.

## **ACKNOWLEDGEMENTS**

I owe two particularly large debts of gratitude relating to this dissertation. The first is to my supervisor, Professor Vishnu Padayachee, whose infectious questioning of the building blocks that make up monetary policy inspired me to undertake this task. His encouragement, guidance, lightning-speed turnaround time and vast knowledge and experience confirmed the value judgement of Professor Adam Habib that, as far as supervisors go, he is “the best”.

My wife Odile, whose own father was an academic, has always encouraged me to pursue this path. Aside from this encouragement, she has had to assume greater responsibility in our business and in raising our children, given the time that I have spent working on this dissertation. For facilitating the process of fulfilling my dream, and for everything else that she is in my life, I shall remain eternally grateful.

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## **TABLE OF CONTENTS**

**Page No.**

<b>Abstract</b>	<b>iii</b>
<b>Acknowledgements</b>	<b>v</b>
<b>1. CHAPTER 1 – INTRODUCTION.....</b>	<b>1</b>
<b>2. CHAPTER 2 – LITERATURE REVIEW AND METHODOLOGY.....</b>	<b>4</b>
2.1.1 Balachandran (1996).....	4
2.1.2 Ally (1994).....	8
2.1.3 Dalgaard (1981).....	12
2.1.4 Kantor (1972).....	15
2.1.5 Gelb (1987).....	21
2.2 Methodology.....	25
<b>3. CHAPTER 3 - SOUTH AFRICA IN A GLOBAL CONTEXT.....</b>	<b>28</b>
3.1 The Rise and Decline of the British Economy.....	28
3.2 British Finance, reliance on Empire 1919-1936.....	34
3.3 The Relationship between Britain and her colonies & Dominions.....	35
3.4 South Africa Economic and Political.....	40
3.4.1 Demographics and Economics.....	40
3.4.2 Industrial policy and Economics.....	43
3.4.3 The Gold Standard, other monetary issues and Economics.....	44
3.4.4 The South African Refinery and Mint.....	46
3.4.5 General Economic conditions 1920-1922.....	48
3.4.6 Monetary causes of the Rand Revolt in 1922.....	48
3.4.7 The consequences of adherence to the Gold Standard 1931-1932.....	49
3.4.8 Recovery 1933-1936.....	50
<b>4. CHAPTER 4 - THE THEORETICAL CONTEXT.....</b>	<b>52</b>
4.1 Introduction.....	52

4.2 From Monetary Orthodoxy through to the Keynesian Revolution.....	53
4.3 Inflation: Cost-Push Inflation arguments against the Quantity Theory.....	56
4.4 Endogenous Money Supply.....	58
4.5 Uncertainty and Banking Instability.....	61
4.6 Central Banks to the rescue.....	67
4.7 Focusing on Internal rather than External Balance.....	70
4.8 Watching for Inflation and deflation.....	73
4.9 Interest Rate Policy .....	75
4.10 Conclusion.....	78
<b>5. CHAPTER 5 – A STORY OF THE EXPERTS AND THE INFLUENCE OF POWER: HENRY STRAKOSCH, EDWIN KEMMERER, GERARD VISSERING AND THE SHADOW OF KEYNES.....</b>	<b>79</b>
5.1 Keynes and his World.....	81
5.2 Keynes, Race and Sex.....	82
5.3 Strakosch’s World.....	88
5.4 Strakosch and Keynes on forming a new gold selling organisation.....	94
5.5 Strakosch’s role as Expert Advisor to the South African Government.....	105
5.6 Strakosch’s ideas in the South African Monetary Policy Debate 1919-1924.....	112
5.7 The appointment of William Henry Clegg as First Governor of the SARB.....	120
5.8 Kemmerer and Vissering, the background.....	121
5.9 Kemmerer’s World.....	122
5.10 Kemmerer’s Relationship with the Fed and the Bank of England.....	127
5.11 Vissering’s World.....	129
5.12 The Kemmerer-Vissering Commission.....	130
5.13 The Kemmerer-Vissering Report.....	144
5.14 Britain leaves the Gold Standard in 1931 .....	147
5.15 The Governor’s correspondence during the crises.....	148
5.16 The Insolvency of the major South African Banks in 1931.....	150
5.17 In Hindsight .....	151
<b>6. CHAPTER 6 – CONCLUSION.....</b>	<b>154</b>

## **7. ANNEXURES**

7.1 Annexure “A” – Primary Source Archival Research Conducted by Major Writers on the Subject.

7.2 Annexure “B” – Professional Dutch/ English Translation of the Diary of Gerard Vissering done by Mr Siegfried Keil.

## CHAPTER ONE

### INTRODUCTION

In the concluding paragraphs of Keynes' *General Theory*, he asks, "Is the fulfillment of these ideas a visionary hope? Have they insufficient roots in the motives which govern the evolution of political society? Are the interests which they will thwart stronger and more obvious than those which they will serve?" (Keynes; 1936: 384). He goes on to suggest that vested interests (power) may dominate in the short term, but that "sooner or later, it is ideas, not vested interests, which are dangerous for good or evil" (Keynes; 1936: 385). This dissertation seeks to establish whether this is so, and to what extent, in the period 1919 to 1936, insofar as it affected the shaping of monetary policy and its impact on the development of the real economy in South Africa.

By monetary policy in this dissertation, I mean to include not just policy concerning interest rates and money supply, but also, and more importantly for our purposes here, wider questions about which monetary system is appropriate for the country concerned (gold, gold exchange, bimetal, sterling standard, or a free floating fiat currency), as well as the institutional mechanisms for managing the system, the most significant being the debate leading up to and following the establishment of the country's central bank, the South African Reserve Bank (SARB) in 1921. Also included are questions about who and what sectors monetary policy serves (the real economy or the financial one), and whether it is aimed at internal or external balance; price stability alone, or output and employment as well.

First ideas are considered. Given that the theoretical paradigm used is that of a post-Keynesian interpretation of the work of John Maynard Keynes, the development of the ideas of Keynes, from his first book *Indian Currency and Finance (ICF)* (1913) through to the *General Theory of Employment, Interest and Money (General Theory)* (1936) and the three 1937 articles; *The General Theory*, *The Ex-Ante Rate of Interest*, and *Alternative Theories of the Rate of Interest* are examined. In mid-1937, Keynes had a heart attack and effectively retired from the debate over the *General Theory*, focusing for the last nine years of his life on other matters.

The international and South African experience of the period 1919 – 1936 is replete with abundant evidence of an investment function, currency regimes and banking systems which are all characterised by inherent instability. Keynes’ warnings on these matters, and his creative attempts to address them so that they were set up to serve the real economy, run like a golden thread through all of his work.

Then chapter five looks at the story of the conception, development, debate, and implementation of, monetary policy in South Africa from 1919 to 1936. Interestingly enough, John Maynard Keynes, who provides the theoretical paradigm, was actively involved in the formulation of South Africa’s monetary policy at the beginning of the period in question.

Throughout this narrative about the development of monetary policy in South Africa from 1919 to 1936, the ideas discussed in Chapter 4 are clearly uppermost in the minds of the main protagonists and antagonists of policy as they battle out the policy debates of the period. Henry Strakosch, the pragmatic servant of British imperial interests, is prepared to argue his case depending on what suited London, sometimes arguing in the unorthodox mode of Keynes, and other times in support of the “Treasury view”, a view of monetary orthodoxy. Samuel Evans, Chairman of a South African based gold mine and an ever-present participant in these policy debates on the side of a Gold Standard and strict enforcement of the shackling of monetary supply to it, is horrified to read Keynes’ *Tract on Monetary Reform* (1930) and equally horrified to hear from Gerhard Vissering, the Governor of De Nederlandsche Bank, that he supports monetary policy favouring “practical men”<sup>1</sup>. William Henry Clegg, the first Governor of the South African Reserve Bank, is less dogmatic on theory, noting to Montagu Norman at the Bank of England that “[Keynes] is a person one must read or pretend to have read”<sup>2</sup>. Edwin Kemmerer, the American Professor of Economics at Princeton University, is an unwavering supporter of the Gold Standard orthodoxy, dismissing those opponents of the Gold Standard wherever he finds them. Many of the opponents to the Gold Standard orthodoxy in the South African debate were picking up on arguments made by Keynes in a British context. This said, the research shows that pure monetary ideas were not considered in isolation, and ultimately,

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<sup>1</sup> Samuel Evans Papers, Barloworld Archives - Box entitled “Politics 1899-1949, Reform Committee, 1895, Reform Committee, Relief Funds” – mainly press cuttings and shorthand notes on gold”.

<sup>2</sup> Montagu Norman Papers, Bank of England Archives, File G1/432.

whether these ideas served the interests of power in London and New York determined whether or not they made it into policy.

If the ideas are in the background in this history, power is very much in the foreground of the narrative of these experts. While Strakosch and Kemmerer argue the merits of the theory to their South African audiences, the power of vested interests in London and New York/ Washington is the real story of chapter 5 of the dissertation.

This is the part of the dissertation which makes the most original contribution to the body of scholarship on the subject. Despite excellent work done by some eminent scholars, which are reviewed in Chapter 2, this dissertation may be the very first to draw on the source material archives, located in all four countries, and which house the original material of Keynes and the three main experts, Henry Strakosch, Edwin Kemmerer and Gerhard Vissering.

## CHAPTER TWO

### LITERATURE REVIEW AND METHODOLOGY

The principal literature dealing directly or indirectly with monetary policy and related gold policy involving South Africa is reviewed in this chapter (2). The literature dealing with the evolution of thinking in monetary theory leading up to and during the formative inter-war years is reviewed in chapter 3, as an integral part of the theoretical overview.

#### **2.1.1 Balachandran, G. *John Bullion's Empire – Britain's Gold problem and India between the Wars* (1996).**

Although Gopalan Balachandran deals only peripherally with South Africa in this period, he shows how Indian monetary policy was managed to suit British interests, which dovetails significantly with our narrative. Therefore, I find his 1996 work the most useful and instructive book covering the broad themes of the subject. There are at least two reasons for this. Firstly, few writers on this subject have done more original archival research than Balachandran, and this is evident in the integrated and coherent narrative that he tells. Secondly, and most significantly, Balachandran (1996:8-9) sets for himself a similar task to the one set by this dissertation, i.e., the exploration of ideas and power in the development of policy. Where I call it a contrast between ideas and power, he refers to 'interest' and ideas. My quest and mandate, as set out in the introductory chapter above, is very similar.

All too often, historians focus predominantly on a particular set of events, in this case for example, commissions of enquiry into monetary policy in a particular country, and fail to place these events in their global context. This usually results in an over-emphasis on the agency of the *dramatis personae* involved, and an under-appreciation of the international forces operating at the time. Balachandran's prodigious primary source research, by far the greatest in terms of its breadth (see Annexure A) and depth, ensures that he is able to contextualise the story of Britain's gold problem and India between the wars with aplomb. Reading Balachandran (1996) and Ally (1994), a picture emerges of just how central the flow of gold and related monetary policy issues was for Britain, particularly during the inter-war years. He also shows that, although the British

were not enamoured of the pace of gold accumulation in the United States, they were able to forge common ground with the United States of America in encouraging the American silver producers to export to India, and thereby mitigate London's hemorrhage of gold to her colony "as U.S. Treasury Under-Secretary R.C/ Leffingwell noted, '... Silver is a pretty poor sort of a reserve... (and) it would be the height of stupidity for us to hold our silver while we are letting our gold go'" (Balachandran; 1996:81).

Brien Cokayne, Governor of the Bank of England at the time of the Babbington – Smith Committee on Indian Currency in 1919, trusted in the orthodox specie-flow theory, developed by Hume, and hence believed that gold flows to New York would result in an inflation of American prices, creating the necessary parity with British prices, which would in turn allow Britain to return to the Gold Standard at pre-war parity. Keynes (1923) pointed out the futility of this belief in the orthodox theory, as the American authorities were hoarding and therefore sterilising these gold flows to the United States, and hence preventing an increase in American prices (see page 56). "Cokayne was also anxious that U.S. gold losses to India would lead to higher interest rates in New York at a time when Britain was hoping for easy monetary conditions in America to ease European deflation" (Balachandran; 1996:82). And so a trans-Atlantic pact was formed to encourage the flow of American-mined silver to India and to discourage gold flows to the sub-continent.

The British Treasury therefore defeated a proposal for a mint in India and India's gold reserves were transferred to London from as early as 1902 and invested in Bank of England gilts. In this way, India was made to pay for the Boer War in the same way that Addis at the Bank of England expected India to pay for "post-war European construction" during the 1920s (Balachandran; 1996:76). India was made to "absorb between £40 million to £60 million of British paper or silver annually" (Balachandran; 1996:30). This eased British interest rates to lower than they would have been in the inter-war period, a period characterised by relative economic decline, during which low interest rates were no doubt a huge help to Britain. Balachandran benefits from Ally's (1994) scholarship, connecting the ban on the sale of South African gold to India up until 1923 with overall British Imperialist policies (Balachandran; 1996:36).

A further British influence on the monetary policy of India, aimed at strengthening the British economy, was that of working to ensure a relatively strong rupee. This had the effect of encouraging imports, the vast majority of which originated from Britain, and discouraging exports. This stimulation of spending (which may otherwise have been spent buying gold), and suppression of earnings on exports weakened India's ability to accumulate gold. That said, in periods such as the 1923-1924 peak harvest season, the inflated rupee provided extra motivation to acquire gold. "Rupee appreciation, by making gold seem cheaper in nominal terms, may have contributed... (to the accumulation of gold) were it not for the general depressed trading conditions" (Balachandran; 1996:120).

Balachandran shows that, despite Britain returning to the Gold Standard in April 1925, Montagu Norman and Charles Addis at the Bank of England opposed stabilising the rupee and supported the floating rupee exchange rate that was the status quo. He concludes that, despite support for European stabilisation of currencies, the Bank of England needed the floating rupee so they could use Indian monetary policy to choke off Indian demand for gold should the need arise (Balachandran; 1996:121-122). However, the fact that India enjoyed four good harvests in the years 1923 – 1926 meant that gold continued to flow into India. 1925, the year of the implementation of the Kemmerer-Vissering report, and the period in which the Pact government encouraged gold exports to countries other than Britain, was also the year of the record importation of gold into India for the period 1890 – 1940, 11 965 000 ounces (Balachandran; 1996:42).

Balachandran shows that, despite the good harvests in the period 1923-1926, the deflationary policies pursued in India at the insistence of the Bank of England "were aimed first at securing exchange appreciation and then at defending an over-valued exchange rate" (Balachandran; 1996:130). This resulted in India missing out on the economic expansion which occurred in other parts of the world during the mid-1920s. Any gold that was imported was largely the result of private purchases. From 1904 to 1914, "a large portion of India's trade was financed through the sale of rupees in the colony against sterling deposited in the Secretary of State for India's account with the Bank of England" (Balachandran; 1996:27), rather than through the acquisition

of gold. This technique for conserving gold would, of course, not have automatically been available to it had Britain been trading with a country which it did not control.

When the Great Depression got underway, largely after the collapse of Credit-Anstalt Bank in Austria in 1931, Britain increased her public debt and other non-industrialised countries defaulted on theirs. India, under the control of the British authorities, took the policy decision to reduce her national debt throughout the Great Depression from 1931 until 1937 (Balachandran; 1996:173, Table 7.2). This was achieved through the export of gold which “lasted until the end of the decade, and totaled over £250 million” (Balachandran; 1996:172). The export of this gold from India greatly relieved Britain’s liquidity position and assisted in the management of sterling (Balachandran; 1996:223).

The huge and unique contribution that Balachandran has made to the study of monetary policy in the inter-war period is due to the volume of primary resource research he conducted in search of motive. This has enabled him to not simply take official explanations at face value, but rather to examine the motives of policy-makers, both in London and in New York, and to “probe their minds more deeply through a synchronic and diachronic study of the records, i.e. examining the text for internal inconsistencies and inconsistencies with earlier texts, and explaining them in terms of a common and unique source of contradiction or divergence” (Balachandran; 1996: 223). In his research, Balachandran found the Indian office bowing to the will of the more powerful, and for the British economy, the more important Bank of England in determining monetary policy in the period of the 1920s and 1930s (Balachandran; 1996:224). Pursuing an essentially deflationist policy in the Indian economy made sense in terms of promoting the British agenda, but it also made it “hard, if not impossible, to justify within the liberal framework” (Balachandran; 1996:226). The more self-serving the policy was, the more fantastical became the official explanation for it.

In keeping with the findings of Cain (1985), Balachandran notes that London’s financial interests managed to exert an influence on India much longer than British manufacturing interests. Britain controlled Indian monetary policy right up until 1947.

Balachandran (1996) contributes enormously to the work of Ally (1994) in placing India and South Africa next to the United States as the pillars supporting British monetary policy in the period 1919-1936. The breadth and depth of his research enables him to tease out geo-political motive in this drama and, as a result, places him just above Ally as the most important supportive text to this dissertation.

### **2.1.2 Ally, Russell *Gold and Empire – The Bank of England and South Africa’s Gold Producers, 1886-1926* (1994).**

Russell Ally’s magnum opus, *Gold and Empire*, preceded Balachandran’s by two years. Ally’s work (1994), like that of Balachandran’s (1996), is a thoroughly researched work discovering motive and vested interest. With the exception of Keynes’ papers in Cambridge and the Barloworld archives in Rivonia, Ally (1994) examines all of the applicable primary source archives in Britain and South Africa in order to understand the importance to Britain of controlling South African gold in the period up to 1926 (see Annexure A).

As a work which uncovers the motive of the ruling elite in the British government, the city of London and the Bank of England, it is almost beyond reproach, with one arguably important exception. Ally’s criticism of Hobsbawm’s statement that the British “motive for the Boer War was gold” was “crudely deterministic” (Ally; 1994:24) may appear to some as excusing the inexcusable. And in a work where motive is so thoroughly researched and examined, failing to acknowledge the British motive for the Boer War means, by extension, failing to understand why Afrikaner nationalists risked economic decline with their monetary policy in the period 1924-1932, in their attempt to escape British control. When Hertzog gambled on South Africa’s return to the Gold Standard independent of London, he no doubt did so with the burning desire to escape British domination. Ally’s failure to acknowledge Afrikaner nationalist indignation caused by the Boer War, robs us of an understanding of the motive of the Hertzog government in the period 1924-1932 in following a policy which was ultimately a mistake.

Although Ally does not examine British industrial decline and the country’s simultaneous financial ascendancy, he does paint a vivid picture of the importance of British financial

institutions to British domination in his period, 1886-1926. At the centre of this domination were “financial institutions which had developed in the city of London over a number of decades: the joint stock banks, the clearing and merchant banks, the insurance industry, the stock exchange and the commodity markets” (Ally; 1994:11). Up until the 1920s, South African mining companies would deliver their raw bullion to the African Bank, Standard Bank of South Africa or the National Bank of South Africa, which then arranged weekly shipments of unrefined gold to London, to be sold by N.M. Rothschild and Son “who, both as refiner and bullion broker, dealt with the bulk of South Africa’s gold” (Ally; 1994:15).

In Chapter 2 of *War and Gold 1914-1919*, Ally sets out how, in terms of the Memorandum of the Bank of England of the 14<sup>th</sup> of August 1914, South African gold producers were forced to sell all of their gold to the Bank of England at the official rate of £3: 17: 9 per standard ounce (Ally; 1994:31). An attempt in 1915 by a South African mining house to sell its gold elsewhere was met with refusal and the threat of force should they not comply (Ally; 1994:34). Ally documents the extent to which the British authorities and British press portrayed this as a “mutual agreement” benefiting the South African producers as much as the British authorities, and also shows the extent to which this benefit was enjoyed exclusively on the London end of the arrangement. Again, the greater the self-interest, the more fantastic the explanations of the hegemon.

This exploitation of South African gold, as documented by Ally, shows the enduring spoils of war from the Boer War to the British state and the tremendous resentment it engendered in South Africa. Norman, on facing an allegation from Clegg that the Bank of England profited from South African gold during this period, protested that the Bank of England “paid over the whole of their profits on gold from whatever source to H.M. Government from November 1915 to August 1919”, as if to suggest that transferring illgotten gains to another British institution somehow cleanses it of guilt.<sup>3</sup> The great thrust of Ally’s excellent research and work on this period enforces Hobsbawm’s observation, as detailed above, and erodes the apology for Imperialism of J.J. Van Helten (1982), quoted by Ally (1994).

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<sup>3</sup> Montagu Norman Papers, Bank of England Archives, File OV37/ 20, SARB File 16/ 12/ 1920 – 31/12/ 1923.

The July 1919 agreement, with which the Bank of England was so happy, and which enforced the supply of South African gold through the London exchange, was the last agreement by which London exercised decisive control over South African gold. After that, indignation in the offices of South African mining companies in South Africa and amongst the Afrikaner nationalists meant that the rest of the period examined by Ally was one of the gradual erosion of British control over South African gold.

Ally notes that the absence of a refinery and mint and the high freight and insurance charges meant an increased cost of between fourteen and fifteen percent to South African gold producers over and above the costs that would apply in the event of gold being refined and minted in South Africa and shipped directly to its final destination (Ally; 1994:75). And so, pressure built significantly in South Africa after the war for the establishment of a refinery and mint and the ability and right to ship gold to whichever shores commanded the highest price (Ally; 1994:80-81). At the same time, Britain's need to control this gold also increased.

Ally shows that after the war, Britain relied more and more on inducements to South African producers to ship to London, rather than the coercion of the First World War period. The October 1919 "agreement" promised that South African gold producers could sell, via London, and with the necessary British permits, to other parts of the world (Ally; 1994:58-59). At the same time, the Bank of England negotiated heavily with the shipping and insurance companies to make these costs competitive (Ally; 1994:51).

Ally highlights an interesting dichotomy between the views of the London-based representatives of South African mining companies and their South African-based counter-parts (Ally; 1994:57, 66 and 69). If the model of economic agents as rational calculators of marginal efficiency is correct, then surely this difference of opinion would either not exist or would be less pronounced than it was. But structure, both in South Africa and in London, was more powerful than the rational expectation school would have us believe. The London managers, relying as they did on their network of City of London financiers, British government officials and other members of gentlemen's clubs, took positions in line with the interests of these groups. South African managers were surrounded by an increasingly vocal group of Afrikaner nationalists as well as

living amongst people who bore the brunt of smaller profits brought on by London's machinations. It is therefore little wonder that this group pushed much harder for independence from British control.

In dealing with the establishment of the SARB, Ally (1994:93-99) shows the length that the Bank of England, and by extension Strakosch, and to a lesser extent Clegg, went to ensure that this institution was independent of the South African government. From his extensive research, it is clear that, while the SARB was to be "independent" of the Union government, Norman envisaged it to be as dependent as possible on the Bank of England. It is a pity that, having garnered so much evidence, Ally fails to make this point explicitly. This tremendous emphasis on reserve bank "independence", which is invariably taken to mean independence from the control of a democratically elected government, but dependent on the policies of central bankers in the hegemonic metropole, is a theme which repeats itself throughout central banking history and one which has not been sufficiently explored. In her thorough work, *The International Political Economy of Central Banking in Developing Countries*, Maxfield's (1997) failure to make this obvious point is a glaring omission in an otherwise well researched book. Ally too has all of the research available to him as ammunition to make this case, but only hints at it peripherally.

If this dissertation was only concerned with the Bank of England and South African gold, there would be very little to add to Ally's 1994 work, save to correct the misconception about the motive for the Boer War, and to emphasise the cultivated dependency of the SARB on the Bank of England. Fortunately, I am saved from an existential crisis by a different focus, that of ideas and power, and by the wider consideration, including New York and India. This is just as well, for the domain of understanding the relationship between the Bank of England and South African gold up to 1926, belongs firmly to Russell Ally.

### **2.1.3 Dalgaard, Bruce Ronald - *South Africa's impact on Britain's return to gold, 1925 (1981)*.**

Bruce Dalgaard's book (1981) is a significantly original contribution to the literature on the subject. He was the first academic to write up the story of the Kemmerer-Vissering Commission and the Report itself using the Edwin Kemmerer Papers, at that stage recently acquired by Princeton University. He is, I believe, also the first academic to show convincingly the role that the South African government's decision in January 1925 to return to the Gold Standard had on the British government's subsequent decision to follow suit a couple of months later. The major writers on the subject that came after Dalgaard (1981), including Ally (1994) and Balachandran (1996), have acknowledged Dalgaard's findings. Dalgaard (1981) can therefore claim credit for correcting an important perception regarding the role of South Africa in influencing Britain's return to gold, a role not properly acknowledged in the literature prior to his important work (Dalgaard; 1981:173-175).

Having said this, Dalgaard's treatment of Kemmerer is imbalanced and somewhat hagiographic. This can be understood, given that Edwin Kemmerer's son, Doctor Donald L. Kemmerer, co-operated in supervising Dalgaard's dissertation and assisted him in his research. Another factor was that he did not conduct research in the South African archives, and when looking through the files of De Nederlandsche Bank, he specifically asked the archivist to get him only the material in English, as he did not speak Dutch<sup>4</sup>. By way of an example, Dalgaard (1981) relying heavily on the Kemmerer papers, notes that "after leaving Southampton, he (Kemmerer) did virtually nothing but eat, sleep and study about South Africa... Kemmerer allowed himself the luxury of an evening of dancing Friday, November the 28<sup>th</sup>, but only after 'studying all day'" (Dalgaard; 1981:73-74 quoting from Kemmerer's diary). This is at odds with how Kemmerer was seen by his fellow commissioner. Vissering notes in his diary entries, 27 November – 2 December: "K. Jokes a lot and even dances every night. A very modern type of scholar."<sup>5</sup> (see Annexure B for the original Dutch). Elsewhere in Dalgaard's work (1981), one cannot put his misinterpretation of Kemmerer's mission to South Africa down to a lack of access to the Dutch

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<sup>4</sup> Gerard Vissering papers, De Nederlandsche Bank Archives, File 23.600 letter from Bruce Dalgaard dated 29 May 1975.

<sup>5</sup> Gerard Vissering papers, De Nederlandsche Bank Archives, File 22058.

and South African archives. Kemmerer's success at dismissing Vissering's suggestion of a Gold Exchange Standard is explained by Dalgaard as some sort of power of personality on the part of Kemmerer (described on page 144). Dalgaard's over-emphasis on agency and the playing down of structure detracts from its original contribution. In this respect, it is similar to Gregory's (1962) account of Sir Ernest Oppenheimer. Innes (1984) notes of Gregory (1962) that "an over-arching admiration for the achievements of ... Sir Ernest Oppenheimer... results in the work being devoid of any serious criticism at all (no mean achievement for a book of over 600 pages)" (Innes; 1984:13-14). Dalgaard (1981) is comparable to Gregory (1962) in the hero worship of their protagonists and the failure to place them in the structure in which they found them. By contrast, Innes (1984) is similar to Ally (1994) and Balachandran (1996) in the masterful placing of the protagonist in the structure. Dalgaard (1981) does not place enough emphasis on the State Department as the source of much of Kemmerer's work and also fails to sufficiently emphasise his position as a representative of American power in determining his popularity with the governments of developing countries.

But Dalgaard's greatest failing is in his single-minded, rigid advocacy of the return to the Gold Standard as proposed by Kemmerer. Despite much evidence, by the time he wrote, of the failure of the Gold Standard to provide monetary stability, economic prosperity or even to advance the interests of the South African gold mining industry, Dalgaard (1981) steadfastly refuses to add any qualification for his support for the Gold Standard. He lists Kemmerer's economic training and extensive experience in numerous countries to motivate for his suitability to head the Monetary Commission in South Africa in 1924 (Dalgaard; 1981: 9). He states that "there was almost universal agreement in South Africa that it was a good idea to refer the question on the return of gold to experts (The Committee on Gold in 1920 had been criticized for not having enough expertise in economic and financial matters)" (Dalgaard; 1981:97). Strakosch's vast experience on monetary related matters, acknowledged by the Smuts government and others in 1920, offers a counter-claim to this unbalanced assessment of Kemmerer compared to his rivals. Rosenberg (1999) offers a much more balanced and critical view. She shows that his "success" in stabilising parts of Latin America with his monetary policy advice coincided with a lending boom "as capital dried up, his missions would lose their luster" (Rosenberg; 1999:163). In addition, Kemmerer was not an impartial advisor as far as advice on loans was concerned, given

the fact that he remained on retainer with the Wall Street firm, Dillon Read. Dalgaard's impression of Kemmerer carefully applying his mind to each problem was one not commonly shared, and Rosenberg notes that a Polish journalist wrote that Kemmerer "applied his ideas from country to country 'as a painter applies a design with a stencil'" (Rosenberg; 1999:192). Given the fact that, in his numerous missions as a money doctor around the globe, Kemmerer invariably advised a return to the Gold Standard, Rosenberg's assessment appears far closer to the truth.

Kemmerer's rigid thinking had a disastrous effect on the South African economy, particularly on South African agriculture in the period 1931-1932, and therefore Dalgaard's support for the Gold Standard is not academically sound. In this dissertation, I hear the numerous voices, including Keynes, Strakosch, Bevan and others who eloquently argued in favour of a more flexible approach to monetary policy. Dalgaard neatly avoids the necessity to consider anything but the arguments for a return to the Gold Standard, stating incredulously that "it is irrelevant for our purposes whether 'faith in a prompt return to 'normal' overlooked the profound changes that war had brought" (Dalgaard; 1981:131). Equally, his summary of the debate in Britain early in 1925 about the return to the Gold Standard includes the unsupportable view that "there was really no alternative but to return at \$4.86" (Dalgaard; 1981:156). As I show in this dissertation, Keynes had, since at least 1913, been active in the public domain, illustrating the danger of a rigid return to the Gold Standard, what he termed the "barbarous relic", and showing how alternative currency arrangements would be better for the health of the real economy. Eichengreen (1992) shows how much damage was done by the return to the Gold Standard in the 1920s, illustrating how those countries who stubbornly remained on the Gold Standard longer than others were the worst economic performers of the 1930s. Given the overwhelming evidence, Dalgaard's stubborn refusal to consider the effects of Kemmerer's bad advice, diminishes his work to an essentially hagiographic account.

#### **2.1.4 Kantor, Brian - *The evolution of monetary policy in South Africa (1972)*.**

Brian Kantor's article (1972) is a good survey of monetary policy in South Africa from 1920 until the then current date (1971). Unlike Balachandran and Ally, Kantor (1972) does not examine in any depth the motives of the various protagonists of monetary policy, but rather considers the development of South African monetary policy purely in terms of the monetary conditions prevailing in South Africa at the time. As a survey of these monetary conditions, Kantor (1972) does an excellent job.

Kantor's (1972) focus is, of course, different to mine, but one wishes that he had made more of the excellent summaries and comments in his article in order to examine motive. Two examples will suffice:

1. Kantor shrewdly comments on Strakosch's select committee on monetary policy in 1920 that "the major issue, whether or not to link the South African pound to sterling or the dollar, was largely ignored by the select committee" (Kantor; 1972:67). This is an important point made by Kantor, prior to the seminal works of Ally and Balachandran, and goes to the heart of the political aspects of monetary policy decisions at the time.
2. Kantor comes down on the side of the post-Keynesians in identifying the nature of money creation in the banking system in South Africa during the First World War and up to 1920. He shows that by 1920 only two banks, the Standard Bank, which by that stage had absorbed the African Bank of South Africa, and the National Bank, dominated the South African banking scene (Kantor; 1972:57). Aside from the gold and silver coins held in reserve in South Africa, the liquid reserves of these banks were held in the London money market, effectively representing the foreign reserves of South Africa at that point in time (Kantor; 1972:58).

Through the signal of increased reserves, and also depending on the differential between the South African interest rates and the London interest rates at the time, credit would be made available in South Africa. Kantor describes the cause of this increase in money supply in

South Africa during and immediately after the war, in sympathy with a post-Keynesian approach: “In the normal way therefore, the South African commercial banks, bolstered by large reserves in London, responded to increased demand for funds in South Africa needed to finance the higher level of war and immediate post-war expenditure” (Kantor; 1972:64). With the important addition of the “large reserves in London” discussed by Kantor earlier, this explanation follows the line of Moore, that “money supply is endogenously both credit driven and demand determined” (Moore; 1989:11).

Kantor fails to note or to explain why the brief of the October 1919 gold conference took such an opposing view to his opinion. Only two pages after his excellent explanation of the increase in money supply, Kantor quotes a contradiction, without explaining its source.

It is clear that by the severance of our connection with the gold basis brought about by the embargo on the export of gold coin has led to inflation, and to the real value purchasing power of the money in the hands of the people being divorced from reference to any concrete value in commodities. The removal of the natural restraint on the banks imposed by the adherence to an effective Gold Standard basis has resulted in an excess increase of paper issues and other forms of commercial currency beyond the legitimate requirements of commerce, thereby creating an excess of money in circulation and an undue increase of the money prices of the necessities of life (Kantor; 1972:66).

From the research at hand, it is clear that Samuel Evans, the nationalists and the Labour party position dominated the October 1919 conference, and this quote is typical of one which would have come from the pen of Evans. It takes an orthodox Gold Standard and quantity theory explanation for the growth of money supply. Kantor fails to explore the dichotomy between his position and that of the October 1919 conference which sets the background for the select committee which Strakosch dominated in 1920. Whereas Evans’ view dominated in October 1919, Strakosch’s position dominated the 1920 select committee and Strakosch’s position, essentially in line with that of Kantor (1972), informed policy from 1920 to the first half of 1924.

Kantor emphasises that the ability of South Africans to obtain credit depended heavily on the liquidity and interest rates in London, that if interest rates in London were sufficiently high, then credit, which ultimately was derived from the London market, would not be forthcoming (Kantor; 1972:59). In this respect, given the fact that availability of credit was so unreliable, South Africa was in a similar position to that of Latin America. In the case of Latin America, substantial credit was available from the United States in the 1920s, but this dried up in 1928 – 1929, choked off first by higher interest rates in New York and remained unavailable in the 1930s as result of an American contraction in liquidity. Kantor (1972) points out that this unstable supply of credit was one of the main motivations for the group system which developed in the South African mining industry, “to ensure that mining operations can continue independently of unsympathetic capital markets” (Kantor; 1972:62). In terms of this group system, much of the capital needed for South African mining was raised in London, and the share capital of the groups and some of the member mines were quoted on both the London and Johannesburg stock exchanges (Kantor; 1972:63). The integration of these two markets in the capital formation of the South African mining industry limited the ability of the SARB to develop independent monetary policy.

Kantor is perceptive in highlighting the interview which Kemmerer had with Clegg and his deputy Jorissen, in 1924. Kemmerer asked Clegg what he viewed as the role of the SARB and Clegg replied that the role was to achieve external balance, which is parity of the South African pound with that of other currencies, particularly sterling. Kemmerer, by advocating a return to the Gold Standard during the Kemmerer-Vissering commission, was by definition advocating a focus on external balance in the event of a conflict between external and internal balance. Strakosch had argued up to this point for flexibility in the exchanges, with South African monetary policy essentially seeking to achieve parity with the British pound, except in the event where the British pound suffered significant devaluation beyond the level at which it had settled in 1920. Strakosch’s prescription, while given almost certainly for the reason that it suited the British authorities, was nevertheless good advice for the South African economy in that it allowed for flexibility. As he pointed out, it allowed South Africa to focus on internal balance when the need arose. Kemmerer’s prescription, which shackled South African monetary policy to gold, led to a situation where the authorities ended up “allowing the tides of gold to play what

tricks they like with the internal price level and abandoning the attempt to moderate the disastrous influence of the credit cycle on the stability of prices and employment” (Keynes; 1923:172). It is therefore ironic that it is Kemmerer who, leading Clegg away from stated SARB concerns about external balance, suggests “let us forget the exchange rate for a moment. Suppose you just deal with the local situation” (Kantor; 1972:68). Kemmerer goes on to question Clegg about a situation where credit expansion is getting out of control and Clegg responds on cue that, if this was the case, he would tackle it. The point that Kemmerer and Clegg seem to miss at this juncture is the trade off between focusing on internal or external balance, and that once a decision had been taken to commit to external balance through a fixed standard, monetary authorities in pursuit of this external balance are unable to adequately address internal imbalances. This is a point which Keynes (1923) clearly understood.

Kantor notes that, given the situation where both the mining houses and the two major South African banks obtained their capital in London, it was difficult for the Reserve Bank to establish a suitable money market from its inception in 1920 (Kantor; 1972:70). As a result of this situation, the SARB was also unable to control the volume of money supply, given its origin in London.

Kantor recognises that the period 1919-1925 was a difficult one for commercial banks, given the fluctuation between the South African pound and sterling and the havoc that this played on the creation of credit in one market for application in another. As a result, the two main banks kept “abnormally large reserves in London over 1923, 1924” (Kantor; 1972:73). Kantor, in his consideration of the Kemmerer-Vissering Commission, suggests that the question as to whether it is in South Africa’s interest to “tie up definitely either with sterling as Egypt has done, or with gold as Canada is doing” (Kantor; 1972:74) was an open-ended question. It is clear from Rosenberg (1999) that this was not the case and that Kemmerer, without fail, always recommended the Gold Standard. The importance of Dalgaard’s (1981) scholarship is apparent in that most accounts prior to this, including Kantor’s (1972), repeated the fiction that “the issue, however, was to remain academic as Britain returned to gold before South Africa was to do so on the 1<sup>st</sup> of July 1925. South Africa thereafter resumed her link with both sterling and gold” (Kantor; 1972:75). Scholars of this subject owe Dalgaard (1981) a huge debt for correcting the

misperception that South Africa followed Britain back onto the Gold Standard. We now know that it was the other way around.

By 1929, thirty years after Britain went to war in order to obtain control over South African gold, this control was now irretrievably slipping away. “After 1929 the Reserve Bank handled practically the entire South African gold production. The effects of this were to reverse a very important part of the flow of funds between South Africa and London” (Kantor; 1972:75). Kantor documents the increase in the gold reserves of the SARB which followed this arrangement and the transfer of South African government accounts to the Reserve Bank in 1927.

Kantor acknowledges that the arguments of the South African banks in previous monetary policy debates were indeed correct and that, once Britain left the Gold Standard in 1931, South Africa experienced capital flight. The Reserve Bank loans “to the commercial banks and the government increased from £0.893 million in September 1931 to £8.434 million in March 1932” (Kantor; 1972:76), a massive increase. These figures need to be read in conjunction with section 5.17, *The Insolvency of the Major South African Banks in September 1931* (pages 154-155). Henry (1963) and Crossley and Blandford (1975) deal with the pressure which the South African government brought to bear upon these two banks to take responsibility for maintaining the unsustainable Gold Standard which eventually collapsed after Tielman Roos resigned his position as a judge and began a political campaign “against the maintenance of the Gold Standard” (Kantor; 1972:77). The drain of capital following this announcement in September 1932 finally forced South Africa off the Gold Standard on the 29<sup>th</sup> of December 1932.

Following this, the Currency and Exchange Act of 1933 instructed the Reserve Bank to act in a manner so as to “prevent undue fluctuation in the exchange value of Union currency in relation to sterling” (Kantor; 1972:77), the exact opposite of what Hertzog had set out to do in 1924. This did not result in an erosion of monetary policy sovereignty and allowed the Reserve Bank to accumulate foreign reserves in sterling and consolidate its role as “the central repository of reserves and its authority as a banker’s bank” (Kantor; 1972:78). The South African economy, now off the Gold Standard, performed as Keynes suggested it would and not as Kemmerer and

Evans had predicted. With the world now off the Gold Standard, the gold price rose substantially and South African gold producers experienced windfall profits. The favourable effect on the South African balance of payments resulted in an expansion of domestic monetary supply so that “the period 1933 – 1939 saw considerable real expansion of the South African economy. Prices remained relatively stable and gold mining output in particular expanded in response to a higher price and a stable cost” (Kantor; 1972:78). The orthodoxy, represented by Evans, Kemmerer, Norman and others, was proved not to work, not only in South Africa but across the world (Eichengreen 1992) and the minority position which Keynes represented, which claimed that the Gold Standard was an excessively rigid system punishing the real economy in order to maintain parities on the currency exchange, turned out to be valid criticism.

The balance of Kantor’s article deals with the period beyond 1936 and is therefore beyond the scope of this dissertation. I wish to highlight one point from this latter period, given that Kantor’s article first appeared two years after Milton Friedman’s seminal work, *The Optimum Quantity of Money* (1969). In it, Friedman (1969) sets out what he believes monetary policy cannot achieve and what it should achieve, coming to the conclusion that the main prescription is that “the monetary authority... (should publicly adopt) the policy of achieving a steady rate of growth in a specified monetary total” (Friedman; 1969:109). Friedman believed that inflation was “stimulated by cheap money policies” (Friedman; 1969:96) and that by controlling monetary supply, inflation could be controlled, and the free market left to find equilibrium. Kantor, only two years later, in commenting on the South African monetary situation, notes that “it is much more difficult to prove econometrically whether the direction of influence is from changes in the money supply to changes in income or vice versa” (Kantor; 1972:93). He also echoes what would become a post-Keynesian critique of Friedman and other monetarists that bank money, which makes up the vast majority of money supply in countries with established banking systems, was not as subject to control as Friedman would have wished. “As Lewlyn has established ... the authorities do not in fact control the supply of liquid assets. They can, however, control the cash base of the monetary system” (Kantor; 1972:93).

Kantor’s work (1972) is an excellent summary and makes valuable comments on the interaction between monetary theory and policy, as well as monetary conditions in South Africa from 1920

until 1971. It does not set out to critique the motives of those involved in monetary policy or the monetary policy debate, and hence cannot be criticised for failing to do so. This wider task is set by Ally and Balachandran, and having set themselves these aims, they are better placed to achieve them.

### **2.1.5 Gelb, Stephen - *The origins of the South African Reserve Bank, 1914-1920* (1987).**

Gelb (1987) is one of the most quoted articles on the subject and with good reason. The article is a well-researched tour de force on the types of money, monetary problems and related debates in South Africa in the period 1914-1920, paying particular attention to the different segments of the South African economy. If it was quoted for this outstanding contribution, it would have served an excellent educative purpose. Unfortunately, the reason for the article's fame is that, as Gelb states on the first page: "In this paper, I advance an analysis of the reasons for Strakosch's considerable influence over this change in (monetary) policy, by developing, and greatly qualifying, the general thrust" of a group of writers, those using a class analysis approach, who refer to the establishment of the SARB in the context of the broader struggles between 'imperial' and 'national' capital occurring at this time" (Gelb; 1987:48). On the last page, Gelb states that "while a South African central bank was not a necessary outcome of the monetary difficulties, some form of local credit control was desirable. In this sense, the Reserve Bank's establishment was partially 'indicative of the strength of "national" forces"' (Gelb; 1987:65). This analysis is just not true; it is in fact the opposite of the truth.

Strakosch, who led the process, was first and foremost a British capitalist who met with the Governor of the Bank of England forty six times alone, and with an accompaniment more than twenty times in the years commencing 1920. Much of that time was spent planning South African monetary policy so that it suited Britain (Sayers; 1976:202). The extent to which Strakosch managed to ingratiate himself into the British power elite is borne out by the fact that he survived the purging of the Board of Directors of Goerz and Co., (the Union Corporation as it became known after 1918), of the other Teutonic members after the outbreak of the First World War in 1914, despite many other German directors being removed from their positions in various South African mining companies (Phillips; 1924:161). Strakosch visited South Africa "only

twice after 1901”, an extraordinary testimony to the importance of London in the economic affairs of South Africa at the time, and to his allegiances to Britain (Oxford Dictionary of National Biography, 2004)

As dealt with from pages 97 - 114, there existed a web of co-operation in England on drafting monetary policy following the Gold Conference in South Africa in October 1919, and up to and beyond the appointment of the first Governor of the South African Reserve Bank (see pages 122 – 123). This discussion and consensus-seeking took place between Keynes (an advisor to the British government) and Blackett at the Treasury, Keynes and Strakosch, Strakosch and Norman, Strakosch and Hull (the first Minister of Finance of the Union government, Norman and Goodenough (Chairman of Barclays DCO), Strakosch and Goodenough (at Barclays DCO), Strakosch and Smuts and Keynes and Smuts. The memorandum which Strakosch presented to Smuts upon his arrival in South Africa in January 1920 was essentially drafted before reaching South Africa. Gelb’s statement that “even if the state might have been predisposed to accept Strakosch’s advice... there was more involved ... than the ideas of a single individual” (Gelb; 1987:58) suggests that the process was an open one.

This is also not true. From pages 107 to 113, I deal with the fact that, having gained the trust and confidence of the Prime Minister of South Africa, and having been appointed to advise the South African government on monetary policy, including the establishment and nature of the SARB, Strakosch drafts a memorandum, gets Smuts’ support for it and then the support of Smuts’ inner cabinet circle. Strakosch then rams the memorandum through the public participation process, dominating these forums, until his ideas are implemented in law, substantially unchanged. This was essentially also true of Kemmerer and his process four years later. It is not true that decision-making processes determined monetary policy in the period 1920-1925 as open searches for the truth. When it came to selecting Clegg as first Governor of the SARB, the committee of Keynes, Goodenough, Gillett and Strakosch, consisted of all British subjects, all residents of Britain, and none were committed in any meaningful way to South African ‘national’ capital.

Gelb does qualify his finding, but the finding is wrong. In fairness to him, I suspect that he did not benefit from primary source research outside of South Africa. Had he had access to British

archives, or had he been able to read Balachandran (1996) or Ally (1994) who both later conducted thorough research in Britain, amongst other places, he may have come to Ally's conclusion that "even though the call to establish a central bank in South Africa had come from the Gold Conference, it was the Bank of England – through Norman and close allies like Strakosch – which was to play the leading role in the establishment, as well as early functioning, of the South African Reserve Bank" (Ally; 1994:89). Gelb (1987) confuses cause and effect. The cause of the establishment of the South African Reserve Bank was neo-colonialism, the effect was national capitalism. This distinction is important.

Gelb (1987) is famous for cited about the significance of the foundation of the SARB, which is in my view not entirely the correct interpretation. However, the rest of the article is a brilliant summary of the monetary problems and related debates in South Africa in the period 1914-1920, and particularly where the different economic groups stood in these debates.

Gelb notes the dominance of "chequing deposits" (1987:49) and comes to the conclusion that the reason for the substantial increase in bank credit during the First World War was "the difficulties of moving gold, and the need to expand credit to maintain production of export commodities (especially gold) and boost production of manufactures ... to replace unavailable imports" (Gelb; 1987:53). This is in line with the Post-Keynesian analysis, as set out by Basil Moore, that "money supply is endogenously both credit driven and demand determined" (Moore; 1989:11). He shows, with great lucidity, how South African banks, mainly Standard Bank and National Bank were part of the economy of both the City of London and South Africa, and responded to market conditions in both areas. This made it impossible for them to be agents of internal balance (in South Africa) rather than external balance (with the rest of the world) as Keynes (1923) had proposed.

Gelb (1987) excels at tracking the fortunes of the different sectors of the South African economy. He shows how importers, traditionally financed with British capital, and relying on British goods, suffered as a result of the non-availability of British goods during the First World War, and then from the fact that imports were considerably more expensive with the devaluation of the South African currency in 1919 (Gelb; 1987:51). At the same time, this devaluation "provided

important relief to exporters” (Gelb; 1987:51). For the gold producers, this devaluation produced a “gold premium” and a welcome relief from the difficulties which the industry was suffering from, and Gelb notes that “its fall led to the mines to cut costs, which ultimately resulted in the 1922 strike by white mineworkers” (Gelb; 1987:54). In sympathy with a theme considered in this dissertation (see pages 19 – 20, 34 – 35, 59, 66, 147-149, 152 – 153, and 159 - 161), Gelb tracks the relative position of the mining industry and the banks under different monetary conditions, noting how the banks did relatively well while the mines suffered during the First World War, how the banks suffered while the mines prospered in the period 1919 to 1920, but how they both supported the establishment of the SARB, given the plan to establish the refinery and Mint, and given the alternatives.

Gelb also shows how Strakosch stressed the importance of central bank reserves for the stability of the overall banking system (1987:60), and one wonders whether he was impressed on the point by his exposure to Keynes. Keynes (1913) makes the point that centrally held reserves, in order to deal with currency as well as banking crises, are vital to a national economy. As a result of the establishment of the SARB, along the lines prescribed by Strakosch, South African banks were forced to import into South Africa “large amounts of specie through 1920, increasing their holdings by nearly 50%” (Gelb; 1987:63).

Gelb’s analysis of the monetary economy in South Africa does not lead naturally to the conclusion that “national capital” was gaining the ascendancy over “imperial capital” with the establishment of the SARB. Ernest Oppenheimer’s “presentation of himself as an economic nationalist” (Gelb; 1987:52) is taken at face value, where Innes (1984) clearly shows this to be opportunism. In reality, in the early days, Oppenheimer just swapped the Rothschilds, who provided funding for earlier diamond mining, with J P Morgan funding from the USA, hardly great South African nationalism.

Gelb confirms the British rationale for establishing the SARB (Gelb; 1987:61), however his main focus is that the desirability of “some form of local credit control” in South Africa as an indication that the “Reserve Bank’s establishment was partially ‘indicative of the strengthen of

“national” forces” (Gelb; 1987:65). This error means that many who have not read Ally (1994) and Balachandran (1997) are left with a false impression.

## **2.2 Methodology**

Because this dissertation is about the ideas expressed and power exercised by people in a period before the living memory of anyone today, the methodological approach was unobtrusive (exclusively the analysis of primary documents retrieved from archives and secondary sources), qualitative and historical.

The greatest contribution of this dissertation is in the extent of the primary research undertaken. While an intimidating array of first rate academics have tackled the subject of monetary policy in this period, it seems that none have undertaken primary research in all of the archives on which this dissertation has based its research. Whereas other accounts have benefited from a lifetime of academic study, a luxury which I have not had the privilege of enjoying, this dissertation demonstrates how a lack of access to some archival material has resulted in errors of emphasis and errors of fact, in otherwise excellent accounts of the period. This is set out in Annexure A. The primary research involved working through the archives in the periods detailed below, including the correspondence of:

- Edwin Kemmerer Papers, Princeton University June 2011
- Benjamin Strong Papers, New York Federal Reserve, New York June 2011
- Samuel Evans Papers, Barloworld Archives, Rivonia March 2011  
and November 2012
- Smuts Papers, National Archives, Pretoria March 2011
- Keynes Papers, King’s College, Cambridge University January 2012

- Churchill Papers, Churchill College, Cambridge University      January 2012
- Gerhard Vissering Papers, De Nederlandsche Bank, Amsterdam      July 2012
- Montagu Norman Papers – Bank of England Archives, London      January 2012

As I looked for evidence of class, societal and vested interests in the ideas of people who influenced monetary policy in the period 1919 – 1936, I found more evidence of the exercising of “power” in private correspondence than in the public record, where motive is often hidden. As Tosh (1991:34) says, there is no substitute “for the direct day to day evidence of thought and action provided by the letter, the diary and the memorandum... Mark Bloch called this the evidence of witnesses “in spite of themselves”.

The secondary sources detailed in the bibliography were also valuable sources for this dissertation. Checking these sources against the triangulation of the correspondence found in the primary sources detailed above, was very instructive. The opportunity to examine source documents from eight archives in four countries across the globe provided a thorough triangulation of evidence, allowing for, not only the verification of actual events, but also for a better informed opinion of the personalities involved.

A critique on the conclusions made by the leading academics in our theoretical paradigm who have written on this subject is attempted in chapter 4.

In assessing both primary and secondary sources, I was mindful of Scott’s (1990) criteria, which he lists as:

- Authenticity: checking whether the correspondence being examined is in fact that of the author.
- Credibility: Scott (1990:22) suggests that “one of the most important considerations in assessing sincerity is the material interest that the author has in the contents of the

document, the extent to which he or she seeks some practical advantage which might involve deceiving his or her readers”.

- Representativeness: I have attempted to research a significant volume of correspondence of the various *dramatis personae* so as to eliminate the risk that the sources may not be sufficiently representative of the views of the people involved.
- Meaning: Interpretive understanding requires “an understanding of the particular definitions and recording practices adopted and of the genre and style employed in the text” (Scott; 1990:30). Tosh (1991:33) points out that “Macaulay’s *History of England* is much more interesting in the attitudes and values that it conveys, as opposed to as a record of unbiased recordal of history”. As Scott points out, “texts must be studied as societally situated products” (1991:36).
- Transferability: “The extent to which the findings of research are applicable to other contexts” (Luescher; 2010:5) is not so much a methodological criteria here, as it is a stated goal of this dissertation, given that I hope briefly and finally to elucidate themes from the economic crisis of 1919 – 1936, which would be applicable today.
- Objectivity: Can be defined as “doing justice to the object of study” (Smaling 1998, quoted by Babbie and Mouton; 2001:274). Hence Luescher’s quotes from Kvale and Brinkmann, where “the researchers self-awareness of his/ her subjective contribution to the product of knowledge... involves striving for objectivity about subjectivity”. This “reflexive objectivity” is perhaps all that human researchers are capable of (Luescher; 2010:7).
- Ethical concerns: As no personal contact with any of the *dramatis personae* was possible, ethical concerns are restricted to accurate and complete descriptions of persons and events in an objective fashion.

## **CHAPTER THREE**

### **SOUTH AFRICA IN A GLOBAL CONTEXT**

Given the paradigm of the dissertation, the economic histories described in this chapter are viewed through the lens of monetary economics, particularly that of the Post-Keynesian school.

Minsky describes a process in the financial sector whereby current stability creates the instability of the future. This idea was first expressed by Keynes in book form in 1913, in warning the Indian banking sector that “If the present spell of prosperity lasts too long, she will no doubt lose it” (Keynes; 1913:208-209). The period of 1919-1936 in world economic history was one of instability, due to the over-commitments made mostly in Europe in the preceding period of stability, from about the last quarter of the 19<sup>th</sup> century until 1914. European powers took this stability and prosperity for granted in making and honouring the entangled web of alliances which pulled virtually the whole of Europe into the First World War. This dissertation is set in the period when the world attempted to navigate its way through post-war instability.

#### **3.1 The rise and decline of the British economy**

The course of the world economy ... can be divided into three periods: the early 1800s to the third quarter of the 19<sup>th</sup> century, when Britain was the workshop of the world and dominated the international economy; the last quarter of the 19<sup>th</sup> century until the First World War, which witnessed the relative decline of the British (real) economy due to the rapid economic growth of the United States and Germany; and the interwar years which saw the collapse of the old international economic order, and during which Keynes was actively involved in the economic problems (Hirai; 2007:7).

The rise and fall of the British real economy was followed, with a lag, by the rise and fall of London as the centre of the world’s international money system. With Britain establishing her Gold Standard by 1821 (Kenwood and Lougheed; 1983:119) and consolidating the issuing of bank notes backed by gold with the Bank Act of 1844 (Fetter 1965:196) and with the rise of the dominance of the British real economy, the stage was set for London to be the centre of

international money by the end of the 19<sup>th</sup> century. As Keynes (1913:70-71) pointed out, bank deposit movements were larger and hence more important in relieving disequilibria than gold movements: “the pre-war Gold Standard had already moved in the direction of one with a major role for credit money, both domestically and externally” (Balachandran; 1996:33).

With the passing of the Bank Act of 1844, which also tasked the Bank of England with stabilising foreign exchange rates by means of the bank rate (Hirai; 2007:8), Britain was well on her way to taking the lead in an increasingly global economy. This was achieved by better than average improvements in transport and communication and by an explosion of manufacturing output as a result of its industrial revolution (Kennedy; 1989:143). A couple of decades later saw these new technologies in railways, telegrams, rapid-fire guns and steam propulsion bring massive advantages to the recently industrialised countries over the un-industrialised world (Kennedy; 1989:144). Before the industrial revolution in 1750, Bairoch (1982) estimates that the third world’s share of manufacturing output to be 73%. With the enormous increase in productivity in the industrialising world, this share had dropped dramatically to 11% by 1900 (Kennedy; 1982:149). Also, the relative peace in Europe meant that productive forces could accumulate without the destructive interference of war. Not only was the third world’s share of total manufactured goods falling, but the fall occurred at an absolute level as well, as products from the industrialised world penetrated their markets. With this industrial dominance came physical dominance. Kennedy (1989:150) has the good grace to recognise that with the “roads, railway networks, telegrams, harbors, and civic buildings which (for example) the British created in India, its more horrific side was the bloodshed, raping, and plunder which attended so many of the colonial wars of the period”. In 1800, Europeans occupied 35% of the land of the world, a figure which was to increase to 84% by 1914.

Within this group of Europeans, Britain came to dominate in the 19<sup>th</sup> century. Given its rising industrial strength, Britain kept its military spending in check, spending just 2-3% of GNP per annum on it in the fifty years after 1815 (Kennedy; 1989:153). Kennedy lists three realms, other than its industrial base, which solidified British dominance over her European rivals: its navy, its expanding empire and leadership in finance.

Money made from Britain's industries, which were the most developed in the world in the middle of the 19<sup>th</sup> century, was invested outside of Britain at the rate of £30 million per annum in the mid-century, and £75 million per annum from 1870 to 1875. The fact that the share of investment abroad increased from 4% of national income in the general period 1870 to 1914, to 7% in the years 1905 to 1913, suggests that capital was fleeing a market which it realised had already run its productive course, to invest in foreign markets whose heyday still lay ahead. By 1914, 43% of global foreign investment originated in Britain, more than double its nearest rival France (Kenwood and Lougheed; 1983:40-41). It is little wonder that Keynes (1930) saw the return of British capital to its home market as part of the solution to capital shortage in 1930 (Keynes; 1930: 163).

Yet this money was initially generated in the explosion of productivity which was the British industrial revolution. By the time that monetary debates were resolved in support for the Gold Standard, "the capacity of Britain's steam engines in 1870, some 4 million horsepower, was the equivalent to the power which could be generated by 40 million men" (Kennedy; 1989:147). British industrial production grew by 37.7% per decade in the period 1820 -1870 (Hirai; 2007:7). This partly explains the 80 % increase in the average real wage rates in the second half of the 19<sup>th</sup> century. It is no wonder then that Britain and her colony, Ireland had manufactured goods making up 88.1% of her exports in 1876-80, dominating world trade, given the relative prices that these goods commanded over primary products (Kenwood and Lougheed; 1983:99). But real wage rates did not rise, or rise by the same extent in the different economies of the world. While export-led growth propelled an increase in national income in Britain in the 19<sup>th</sup> century, this was not true of all exporting economies. Feinstein (2005:90-94) identifies two broad types of export economies "distinguished by the technologies used in the staple industry" (2005:90). The first is based on small-scale homestead, family-run farming that typified the USA, Canada, Australia and New Zealand. Although not mentioned by Feinstein, an important component of this economy was that the main participants were not politically powerless. These economies achieved returns to scale which did not require huge production areas or foreign capital. The form of production encouraged mechanisation. "These conditions encouraged the promotion of a high standard of education and advances in human capital and, together with the egalitarian

distribution of income, create a social and political environment in which democratic political systems can flourish” (Feinstein; 2005:92).

Feinstein notes a second type of export economy, one either based on large-scale plantations growing tropical crops, or large-scale mining or oil wells. These economies featured politically powerless labourers employed at low wages in appalling conditions by giant companies dependent on foreign capital and foreign senior management, and a highly unequal income distribution in the society (high Gini co-efficient). They encouraged authoritarian political systems, low standards of education and advances in human capital, in which the system was arranged to benefit the foreign business owners and the local ruling elite. Kenwood and Lougheed note that in Egypt, middlemen handling peasant crops exercised monopoly power to extract the lion’s share of the agricultural export crop. Company factories in Cuba also formed a monopoly in which small farmers were underpaid for their sugarcane (1983:150-151).

By the time my period (1919-1936) arrived in Britain, all adult men, and by 1928 all adult women, enjoyed the vote. This created an impetus towards greater income equality in Britain which was lacking in the above-mentioned countries. The “Labour Party increased its tally from 370 000 in the 1911 election to more than 2 million in 1918” (Eichengreen; 1992:92). The extension of the franchise in Europe in the context of a mostly proportional representation system made it difficult to form lasting and stable alliances. “In Germany, France, Belgium, stabilization was accomplished ... only after financial instability had reached intolerable heights and the costs of inaction reached prohibitive levels” (Eichengreen; 1992:95).

It is easy to come to the conclusion that, because of the dominance of the British real economy, London was able to command internationally mobile capital. As Eichengreen (1992:4) points out, this does not tell the full story. “Kindleberger argues that the stability of the prewar Gold Standard resulted from effective management by its leading member, Great Britain, and her agent, the Bank of England”. What the Gold Standard faithful saw as the inherent strength and stability of their orthodoxy was, as Eichengreen shows, more to do with the two inter-related factors of credibility and co-operation. Credibility relates to the degree of confidence that market participants have in the ability of the authorities to correct imbalances. If this is present, the

authorities have speculators who can bet on the validity of this ability and thus move the markets in the direction of correcting the imbalance. This makes the authorities' job much easier. By contrast, once the authorities are weak and this credibility is eroded, speculators are then tempted to bet against the success of the authorities in closing gaps to reach the official rates. This can destroy attempts to keep a pre-existing order going, as it did in the period in question.

Regarding the second factor, co-operation: Prior to 1914, in a world in which ruling elites did not have to consult and seek compromises with representatives of the working class, and where there was a much greater consensus amongst the ruling elites of different countries on what constituted the common good, co-operation was easier and achieved to a remarkable extent (Eichengreen; 1992:5).

That said, no doubt credibility is easier to achieve, and co-operation easier to enforce when your real economy is the strongest in the world. This position started to erode for Britain by the 1890s and she was substantially weaker, relative to her rivals Germany and the USA, by 1914. In 1880, Britain accounted for 22.9% of manufacturing output, by 1913 it was 13.6%. In 1880, 23.2% of world trade involved Britain, but only 14.1% in 1913. This slowdown in economic performance “involved such complex issues as national character, generational differences, the social ethos, and the educational system as well as ... low investment, out of date plant (and) bad labour relations” (Kennedy; 1987:228). And as the real economy suffered relative decline, gold flows over which London exercised some control became more and more important to what remained as the dominant sector – finance, banking and related services. The number of Westminster parliamentarians with interests in finance and commerce increased from just under 23% in 1900 to almost half by 1906 (Ally; 1994:27).

In the period from 1870 -1913, while Britain's industrial production grew at 2.1% per annum, Germany's grew by 4.1% per annum and the USA by 4.7% per annum (Hirai; 2007:9). Not only was Germany and the USA growing faster than Britain in this period, but new industries which commanded better terms of trade were being developed by Britain's economic rivals. Steel production, using new techniques, shot ahead in the USA and Germany, and Germany in particular developed its chemical industry ahead of Britain, despite “the basic research which

provided the foundations for this industry” being done in Britain (Hirai; 2007:10). As British industry went into relative decline, so British finance assumed a more powerful place in the British body politic. After 1870, when British governments wanted economic advice, “they went instinctively to the City rather than to Manchester or Birmingham (Cain; 1985:16).

Hirai (2007:10-11), as an outsider to British society, notes two fascinating social factors that contributed to the relative British decline: the first being the glorification of the landed gentry and their lifestyle, resulting in the creaming off to the country of successful entrepreneurs and industrialists in their prime. The second was the rising emphasis on the classics and Christianity in British public schools, shaped by Thomas Arnold and others, which took the emphasis off the sciences, at a time when the German education system was taking off. This “created a nation that neither could nor would adapt to technological innovation” (Hirai; 2007:11). This was particularly true of wealthy industrialists who “often betrayed a strong sense of the inferiority of their own position by the rapidity with which they abandoned industry for the gentlemanly life” (Cain; 1985:16). By contrast, banking and finance families enjoyed a greater degree of social acceptability amongst the aristocracy, marrying into their families easily and hence not having to retire early in an attempt to claim respectability (Cain; 1985:11).

J.A. Hobson’s theory, published in his book *Imperialism* in 1902, postulated that under-consumption in Britain, which accompanied the accumulation of capital, produced surplus capital and it was this surplus capital in search of a home which was the “driving force behind British imperialism in the late nineteenth and early twentieth century” (Cain; 1985:1). I am not convinced that it was surplus capital in search of investment in a politically friendly environment which was the cause of imperialist wars, such as the Second Boer War. It could have been the opportunity of control, say for example the gold mined in the Transvaal, which was the stronger motive. What is clear is that Hobson draws a line of causality between British capital and British imperialist subjugation, which is important in order to understand the motives and feelings of Afrikaner nationalists during the period 1919-1936. E. Hobsbawm asserts that “whatever the ideology, the motive for the Boer war was gold”.

Cain (1985), while acknowledging attacks on Hobson's theory, refines it by pointing out the difference between industrial capital and financial capital, and by showing the close relationship between the financial capital controlled by the "City of London" and the imperialism executed by the British government, seated in the same city. It was this capital in search of a home which collaborated with the imperialists in government, more so than those employed in Birmingham or Manchester.

### **3.2 British finance and her reliance on her Empire 1919-1936**

Nathan Rothschild, in correspondence with his French cousin, frequently linked the financial strength of the Bank of England to "regular inflows of gold from the Transvaal... destined specifically for the Bank of England vaults" (Ally; 1994:26).

Balachandran (1996:47-99) points to an important cause of the stability of the pre-1913 Gold Standard. India, run by the British, was made "to settle Britain's deficits with the rest of the world and facilit(ate) her capital exports" (Balachandran; 1996:1), regardless of Indian national interest. He bemoans the lack of attention given to this important fact in the Economic History literature. The importance of this policy, above all others, is evident in the fact that, "while delegating powers to the Government of India on other matters Britain refused to let go of her control over Indian monetary and currency affairs until almost 1947" (Balachandran; 1996:1).

If Britain's centrality to the world economy was slipping by 1913, the First World War irreparably destroyed that dominance. British industrial output may not have declined much during the First World War (Pollard; 1983:25), but the enormous quantity that went into the war effort and the threat of the German submarine fleet, meant that American industry performed even better and American exports replaced British exports into the British Empire and elsewhere. "This expressed one of the most significant permanent economic changes wrought by the war" (Pollard; 1983:38). The "interruption of British textile exports due to the scarcity of shipping space for American cotton stimulated hothouse growth of textile production in India and China ... permanently reducing Lancashire's exports to parts of Asia" (Eichengreen; 1992:89). But this stimulus for the development of manufacturing in South Africa, India and elsewhere was

relatively small and “manufacturing in South Africa remained a small and vulnerable sector” (Feinstein; 2005:115).

The First World War had shattered the fiscal system at a time of the extension of the franchise, so that the working classes and the capitalist classes were engaged in a political tug-of-war over who was going to bear the tax burden of the enormous debt that had accumulated during the war. “France borrowed \$1 billion from the United States and \$555 million from Britain, she lent \$514 million to other countries. Britain, while borrowing \$1 billion from the United States and \$329 from other neutrals, lent \$3.8 billion to her allies” (Eichengreen; 1992:84). The liquidation of foreign assets and the accumulation of new liabilities set up a line of dominos just waiting for one to fall, setting off the others. In the event that anyone in the system who failed to meet their commitments, be it German reparations to France, French debt to Britain and the USA, British debt to the USA, Latin American debt to the USA dependent on commodity prices, or continued growth in the American economy sufficient to keep the dominos from falling the world economy was in trouble (Eichengreen; 1992:66-99).

### **3.3 The Relationship between Britain and her colonies and dominions**

After 1914, with serious rivalry from New York, and gold not freely flowing to London as it had done up to a decade earlier, Britain’s empire of finance was shrinking. A result of the new challenge for financial supremacy from New York was that Britain was thrust into “greater dependence upon the formal empire for finance and trade; and a sterling area, centred on the empire, began to emerge in the 1920s” (Ally; 1994:89). This dependence on co-operation with the empire, as a crutch to replace the naturally dominant position which Britain previously held, is highlighted by the shift away from South Africa’s trade dependency on Britain. South African imports from the USA, which in 1914 stood at less than 10% were 25% after the war. Exports to the USA had jumped from less than 1% in 1914 to 17% by 1918. Britain on the other hand, now took only 62% of South African exports in 1918 as opposed to 89% before the war (Henry; 1963:175). Given London’s need to economise on gold as a result of her weaker position, the British authorities hoped that sterling, through cooperation with her empire, would become the leading reserve currency, and the Gold Exchange Standard the formal mechanism.

South Africa's contribution to the war effort was thus not just to be measured in soldiers. The effort to conquer the Boer Republics, and commandeer their gold in the Boer War now paid off for Britain. The Bank of England entered into the "August Agreement" in 1914 with South African gold producers, by which all South African gold was sold exclusively to the Bank of England at a fixed price of £3:17:9 per standard ounce and 97% of the set value was to be paid to the producers upon receipt of the gold in South Africa, the balance to be paid once it reached the Bank in London (Ally; 1994:33-34). The fiction about this being a "voluntary agreement", as claimed by the Bank of England, is revealed when in 1915, one of the mining companies made arrangements to ship their gold, for a considerably better price, to America. When the British authorities discovered the attempt to get the best price, an "ultimatum was issued to the company to hand over its gold to the British representative in Cape Town" (Ally; 1994:34). From a Bank of England Memorandum, it was clear that if the company had not complied, "the British government would have done what it did in Australia, it would have commandeered the gold" (Ally; 1994:34). By "commandeering" the 3% which it owed upon receipt of gold in London, by loading the shipping and insurance charges and by sticking to an official price considerably less than what the gold producers could get on the world market, the Bank of England took a not inconsiderable share of South African gold revenue during the war (Ally; 1994:41).

William Henry Clegg, a couple of months after arriving in his post as the first Governor of the SARB writes to Montagu Norman, the Governor of the Bank of England, on the 31<sup>st</sup> August 1921 informing him of the considerable anger in South Africa, both amongst the gold miners, and amongst the nationalists at this pillage. "It is believed that the Bank makes about £50 million to £60 million per annum merely as commission". Clegg notes that these figures come from public statements by Samuel Evans. Evans was Managing Director of Crown Mines, Chairman of the October 1919 Gold Conference in South Africa, and a rigid, near fanatical, supporter of the Gold Standard. He also complains about the "statutory price" paid by the Bank of England for South African gold, less than the going price in America<sup>6</sup>. Although Norman corresponded with Clegg on other matters in the interim, he only responded to Clegg's allegations in his letter of the 21<sup>st</sup> October 1921, protesting that the "Bank of England ... paid over the whole of their

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<sup>6</sup> Montagu Norman Papers, Bank of England Archives, File OV 37/20 SARB file 16/12/1920-31/12/1923.

profits on gold from whatever source to H.M. government from November 1915 to August 1919”<sup>7</sup>, as if taking what does not belong to you is somehow legitimised by handing it over to someone else! Clegg also asked Norman why he did not allow South African producers the freedom to sell their gold where they chose. Norman, fully aware that London’s position as the centre of the gold market could now only be maintained by coercion, replied: “It would be one thing if we could restrict such “freedom” to South Africa, but whatever arrangements were made with South Africa would necessarily have to be extended to India, to Australia, and to a half-a-dozen other colonies or countries”<sup>8</sup>.

This coercion was extended in the July Agreement of 1919, which was already in place by the time of the exchange of letters detailed above. In terms of this agreement, again all South African gold would be sold and transported to the Bank of England in London and then the South African producers “would be issued with special licences for its re-export to any country” (Ally; 1994:58-59). These licenses were not easy to obtain and “neither the gold producers nor the Union government were to display the same enthusiasm for the new selling arrangement as was the Bank of England” (Ally; 1994:67). This fact, and the political capital made on it by the nationalists, meant that the October 1919 Gold Conference passed the motion “That the establishment of natural exchanges and of a free market for gold in the Union is desirable” (Ally; 1994:63).

The Bank of England desperately needed someone to step into the breach, and that someone was Henry Strakosch (see pages 89 - 123). After installing his trusted accountant, William Henry Clegg, as first Governor of the South African Reserve Bank, Norman thought of extending this blueprint to other colonies and dominions. This was made attractive by the fact that leading British economic figures, including Norman, Keynes, Blakett, Strakosch, Goodenough and others had defined the terms of South African monetary policy including the setting up of the South African Reserve Bank (see pages 97 -122) in 1919 and 1920. Clegg responded to Norman’s *Principles of Central Banking*, commenting in his letter dated the 12<sup>th</sup> April 1921 that

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<sup>7</sup> Montagu Norman Papers, Bank of England Archives, File OV 37/20 SARB file 16/12/1920-31/12/1923.

<sup>8</sup> Montagu Norman Papers, Bank of England Archives, File OV 37/20 SARB file 16/12/1920-31/12/1923.

“Your scheme of a Central Bank for each economic unit of the Empire – all acting together in co-operation – is a practical one”<sup>9</sup>.

Norman took a decision to “visit only those countries having an established Central Bank” (Sayers; 1976, Vol 1:160), declining an invitation to Canada in 1927 because it did not have one. In addition to the co-operation detailed above, Norman wished that Central Banks would develop standard practices so that gold could be conserved in the world. This conservation of gold excluded the “Gold centres required, London being one” (Sayers; 1976, Vol 1:158). By rigging the system so that everyone conserved gold, London could perhaps manage to hold onto hers. And of course, the most important criterion for Norman as a leading member of the London financial elite was central bank “independence”, which meant independence from local political pressure and subservience to the Bank of England. “Norman’s ideal, preached in season and out of season, was that there should be both formal autonomy and substantial independence in action”. “He was always glad to meet central bankers, but would refuse all contact with foreign Ministers of Finance or their officials” (Sayers; 1976, Vol 1:158).

Despite preaching Central Bank independence from the pulpit of the temple of orthodoxy at the Bank of England, Osborne Smith, the Australian first Governor of the ‘white and sensible’ Reserve Bank of India (RBI) was pushed out “18 months after he joined and two years before his term was due to expire” (Chandavarkar; 2000:3048). “‘White and sensible’ was how a Treasury official described the type of central bank the British Authorities had in mind for India” (P.R.O., T177/16, Waley’s minute, 3 April 1933 – quoted in Balachandran; 1996:21). Smith’s crime was not so much that he slept with the wife of the manager of the Calcutta office of the RBI, but rather that, although he was thought to be “a person on whom the Bank of England could rely and of whom they could expect unquestioning cooperation” (Chandavarkar; 2000:3050), Smith turned out to be sympathetic to Indian business concerns. Threatened with being fired if he did not resign, Osborne Smith finally did resign in 1936. Chandavarkar assesses that “in retrospect, Smith stands out as a competent and independent minded governor of the RBI” (2000:3059). It is

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<sup>9</sup> Montagu Norman Papers, Bank of England Archives, File OV 37/20 SARB file 16/12/1920-31/12/1923.

telling that this story had to wait until 2000 to be told. Maxfield (1997) who wrote an important book on Central Banks in developing countries fails to mention it<sup>10</sup>.

When considering the British relationships with her colonies and dominions, it is useful to think of them in two categories; those where the majority of inhabitants were of European extraction, or in the case of South Africa, where the white minority firmly held political and economic power, and those where the indigenous people made up the majority. Although Australia, New Zealand and Canada had less political independence than the USA, their basic structure was closer than those colonies where the majority of the inhabitants remained disenfranchised. This is not to suggest that Australia, Canada or New Zealand were more compliant with London, but London did have to consider countries in which the population exercised the franchise differently to say India, in which they had a more direct control.

Further evidence of the lie of central bank “independence” and the truth of a coordinated Empire wide central banking co-operation came in a telegram exchange between Clegg and Norman in 1922. Clegg started by telegraphing Norman on the 9<sup>th</sup> June 1922, enquiring about the progress of loan negotiations between the Bank of England and the Mozambican authorities. Clegg told Norman that “the Prime Minister’s (Smuts) hand would be greatly strengthened if loan efforts (by Mozambique) are unsuccessful”<sup>11</sup>. Norman responded immediately on the same day, asking whether Clegg wanted him to discourage the loan<sup>12</sup> and, on the 14<sup>th</sup> June 1922, Clegg stopped being obtuse and directly asked Norman to stop the loan. Again, on the same day, Norman telegraphed back to inform Clegg that the loan was not going to be granted<sup>13</sup>. Smuts needed to weaken the Mozambican hand while he was negotiating with Portugal over new terms for South African use of the port at Lourenco Marques (Ally; 1994:92-93).

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<sup>10</sup> In fairness to her, she limits her study to Thailand, Mexico, South Korea and Brazil, an unfortunate collection in that it excludes examples of developing countries far from the apron strings of Washington.

<sup>11</sup> Montagu Norman Papers, Bank of England Archives, File OV37/20.

<sup>12</sup> Montagu Norman Papers, Bank of England Archives, File OV37/20.

<sup>13</sup> Montagu Norman Papers, Bank of England Archives, File OV37/20.

### 3.4 South Africa: Economic and political

#### 3.4.1 Demography and economics

Feinstein (2005:16-17) notes two major linguistic groups who made their way from the Great Lakes region into current day South Africa at least 1500 years ago. Because they “entered two very different ecological habitats in the eastern and western parts of South Africa”, two different forms of economy evolved. The Nguni-speaking ancestors of today’s Zulu, Swazi and Xhosa people’s environment grew millet and sorghum in the summer rainfall areas. The Sotho-Tswana speakers migrated to the area north of the Orange River and later settled in what became Lesotho. “The poor quality of the grassland, and the great distances between sources of water necessitated pastoral farming, with seasonal movements of livestock over a large area” (Feinstein; 2005:17). In both groups, cattle represented the origin of the word “capital”, which is head of cattle, in that these animals represented money, both as a store of value but also as a means of exchange for large purchases. “Not only do the English words ‘*capital*’ and ‘*cattle*’ share the same root, the Hebrew word for ‘*herd/flock*’ – *ashtoroth* – is closely related to its word for ‘*wealth*’ – *ashiruth*” (Power, 2002:235).

European settlement in South Africa started in Cape Town in the mid-17<sup>th</sup> century as a refreshment station for a (Dutch) monopolist company, the VOC, which also governed The Cape. The expansion of Dutch farmer settlement away from government control started under the VOC rule as the “Vry Burger” movement and developed later in an attempt to escape British control in the middle of the 18<sup>th</sup> century. From the time when they recaptured the Cape in 1806, British rule was tolerant of domestic trade and manufacturing and a separate branch of the government owned Lombard Bank provided new facilities to Cape commerce. “The first private banks started operations in the 1830s, typically ... owned by local merchants” (Feinstein; 2005:27).

The 1820s saw a severe depression in Britain following the collapse of farm prices at the end of the Napoleonic wars, which coincided with the Cape colonial government’s requirement of a buffer between the Colony and the Xhosa settlements on the other side of the Fish River. The

British government assisted five thousand British settlers to commence farming in what became the Eastern Cape. “The main gain to the economic life of the colony from its absorption into the British Empire was the stimulus given to wine farms” which enjoyed imperial tariff preference, this was followed in the second half of the 19<sup>th</sup> century with wool, demanded by the British textile industry (Feinstein; 2005:28).

Feinstein (2005:33) introduces a fascinating model to explain the particular exploitative and dispossessing nature of what became the South African economy. He attributes to Domar (1970) a description of a specific economic organisation when, in an agrarian economy, a country has an abundance of land and a relative scarcity of labour. In this situation, “owners of land will be unable to profit from it” as hired labour would be better able to make a living by cultivating or grazing their cattle on surplus land. The only way for politically powerful landowners to make a profit, in excess of subsistence levels, is to cut off access to the surplus land, tie labour to the farms of the politically favoured in a system of servitude, and/or otherwise discourage alternative employment.

When gold mining got underway in South Africa in the 1880s, the fact that the nature of the operation required the mining of low grade ore at great depths meant that mine owners now joined white farmers in the challenge of attracting and maintaining a labour force. Their challenge was not dissimilar to that of the landed gentry of Tsarist Russia, as described by Domar’s model. In the South African case, this challenge was originally met by slave labour imported into South Africa to work on white-owned farms. After the slave trade was abolished, a missionary noted that the Boer tactic against the Sotho in the 1860s seemed to be to add farm to farm, pasture to pasture “to force the natives against some impassable range or drive them back into arid deserts ... that it becomes impossible to subsist on the produce of agriculture and livestock and to be compelled to offer their services to the farmers in the capacity of domestic servants and labourers” (Feinstein; 2005:34).

After slavery was abolished, the servitude was maintained by the Masters and Servant Ordinance (1841) and later Act (1856), pass laws, vagrancy law (1879), Native (Urban Areas) Act (1923), and by access to government sponsored capital, particularly strong in our period (1919 -1936). In

order to maintain white business, additional measures were imposed to weaken black agriculture through the imposition of hut taxes, first levied in Natal in 1849, and through the confiscation of fixed property, and the prohibition of acquiring any land in areas designated for white people, culminating in the Land Act of 1913.

The discovery of diamonds in the 1870s and gold in the 1880s, saw a large influx of white immigrants into South Africa, and by “1911 some 260 000 Africans were employed on gold and other mines compared to 360 000 on commercial, white owned farms” (Feinstein; 2005:63). Both forms of mining involved key features; a strict demarcation between the skilled jobs reserved for whites and unskilled, low paying, manual work for African workers recruited as short-term migrants, and housed in closed compounds (Feinstein; 2005:63). The number of black South African mineworkers in our period steadily increased from 38.7% in 1921 to 52.2% in 1936. At the start of the mining industry, companies competed briefly against one another for the required African labour, but soon realised the profit limitations of the laissez faire business philosophy which Lipton (1985) describes them as great proponents of. Mine-owners were faced with a political environment in which they had to overpay and/or overemploy white workers in skilled/managerial positions because of the political power that they yielded, but the same political environment disenfranchised black workers, and so provided the perfect excuse for mine-owners to abandon the liberal paradigm and collude with each other in having a single black labour recruitment agency, setting a “‘maximum permissible average’ on daily earnings” (Feinstein; 2005:67). Lipton (1985:410, Table 11) shows that the worst income inequality of the first half of the 20<sup>th</sup> century was 1921, where thanks to an enormous increase in average white wages, a white worker earned 15 times more than a black worker. That multiple was reduced to 11.2 in 1922 following the crushing of white organised labour, but the political environment, following the period in office of the National Party, with different partners, from 1924, meant that the multiple of average per capita personal income in 1936 was up to 13.1 times greater for a white worker than for a black one (Feinstein; 2005:11).

Given the above, it is clear that a liberal model does not adequately explain the development of the South African economy up to and including my period, particularly as it relates to the economic welfare of black South Africans. Another explanation, along the lines of Domar (1970)

detailed above, but with a mining twist, applied in South Africa. Wolpe (1972) shows that, not only did the mining industry drive down black wages to the bare minimum necessary for reproduction, but relied on the “reserve” or homeland subsistence economy to provide social services, which allowed the mine-owners to set the wages at below subsistence levels. This Marxist analysis fits the South African economy much better than it does an economy like Western Europe or the United States in the 20<sup>th</sup> century, where, as workers received the vote, they were able to push for better working conditions and pay. Notwithstanding the brief success of the ICU, this was not the case for black workers in our period 1919-1936. Black wages at obscenely low levels were the one variable which the mine-owners could control in order to make profitable low-grade ore mining at great depths.

### **3.4.2 Industrial policy and economics**

Feinstein (2005:114) notes that there was no concerted industrial policy in the Boer republics, and none of note under British administration. Manufacturing received a small boost from the relatively lower level of competition during the First World War, but in 1923 “when the Board of Trade and Industries again suggested increased tariffs, it drew only a half-hearted response from the Smuts government” (Feinstein; 2005:117). This changed with the election of the Pact government in 1924 and the revised Customs and Tariff Act of 1925 (Feinstein; 2005:119). The Smuts government can claim credit for state ownership and the extension of the railways and for the establishment of ESCOM in 1923. The Pact government was the promoter of ISCOR, established in 1928 which was producing steel by 1934 (Feinstein; 2005:121). This boost to industrialisation in the period 1919-1936 was engineered to benefit white workers, with the percentage of white workers in industry peaking in the middle of the period (1932/3) at 45.3%.

From 1933, with the gold price rocketing, manufacturing in support of mining, surged. This shows the truth of Fine and Rustomjee’s (1996) basic hypothesis that by “taking account of the systematic linkages between ... different economic activities, the direct and indirect dependence of the entire economy on the MEC (Minerals-Energy Complex) is exposed” (Fine and Rustomjee; 1996:71). An example of this linkage is the success of “the development of the uses for boart, which was then (in the 1930s) essentially a by-product of the mining of gem diamonds

... At its peak in the early 1980s, Boart International controlled 100 companies and employed 17 000 people in twenty-eight countries” (Fine and Rustomjee; 1996:144).

While the arguments of Davies et al (1976), Freund (1989), Yudelman (1983) and others discussed by Fine and Rustomjee (2005:121-146) in Chapter 6 on *The Political Economy of the Inter-war Period* approach the economy from a different perspective, and in a different paradigm to that of this dissertation, they do highlight the strength of economists such as Fine and Rustomjee, schooled in a Marxist framework, and the weakness of those schooled in a general equilibrium one (a liberal political framework). Fine and Rustomjee (1996:4) summarise: “One of our broad conclusions is that the political economy and economic and social history of South Africa has unduly suffered from the exclusive attention that has been paid to economic and political agencies ... In classic Marxist terminology, the forces of production have been overlooked in a one-sided emphasis upon class or other relations”.

### **3.4.3 The Gold Standard, other monetary issues and economics**

In chapter 5, I consider in detail the role of the experts in determining monetary policy in South Africa in the period 1919-1936. However, the period of involvement of these experts was mainly 1919-1921 in the case of Strakosch and Keynes, and 1924-1925 in the case of Kemmerer and Vissering. In this section, I consider the rest of the period and other aspects of the story.

When the Liberal government of Lloyd George took power in Britain at the beginning of 1919, they feared the hardship and disruption which would come from returning to the Gold Standard and the pain that deflation would bring. And so the Cunliffe committee rightly recommended setting aside “fiscal, financial, commercial, and monetary orthodoxy in order to hasten the revival of industry and employment” (Boyce quoted in Ally; 1994:104). Britain abandoned the Sterling/Dollar peg in March 1919 and Sterling depreciated as did the South African pound, but not by as much. As a result of this depreciation, the content of gold coin was now significantly higher than the official gold coin price. “While a sovereign was still only worth 20s in the Union, in places like the Indian Bazaars it could fetch as much as 38s 9d”. And so from 1 April 1918

until the 31 March 1920, specie to the value of £2 945 435 had left the country, most of it after March 1919 (Ally; 1994:105).

The burden of this drain was felt heavily by the banks who appealed to the South African authorities to be relieved of their obligation to exchange their notes for sovereigns at par, given that they were paying more for gold than they were receiving (Ally; 1994:105). In response, the South African government convened a special Gold Conference in October 1919 to essentially answer two questions: Should the embargo on the export of gold be lifted, and should the South African pound break the link with sterling and establish a direct link to gold? Obviously, the bankers preferred a sterling link, given the huge cost to them of the then current link to gold. In the opposite camp were the nationalists, who wanted an independent link to gold in order to gain independence from Britain, and the white Labour Party who had an obsession with the eroding power of inflation, oblivious to the economic damage which comes from deflation. The Conference resolved to reject a fiat currency and committed to return to a full Gold Standard, a victory for the nationalists and Labour, and a defeat for the banks. Smuts supported this resolution, support he was to withdraw once Strakosch had worked his magic on him a couple of months later (see pages 97 - 108). Perhaps Smuts' support came from his lack of understanding of economics. Smuts' vast education and reading does not seem to have extended much into the fields of Economics and Finance. His extensive library at Irene has very few books on economics, and Smuts himself writes in a letter to his friend Margaret Gillett (nee Clarke) from the Treaty of Versailles, where economic data was being discussed: "I wish I had Arthur here to help me as I am quite ignorant of finance"<sup>14</sup>.

As a result, "faced with a rapid depletion of their specie reserves, the banks proceeded to restrict their advances and exchange purchases" (Henry; 1963:181). At the Bank of England, Norman was shocked by the bad news from the Gold Conference in South Africa and met regularly with Strakosch to change the South African monetary policy decision, as set out from pages 90 to 91.

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<sup>14</sup> Smuts Papers, National Archives Pretoria, Originally Vol 22 (renumbered 206), 226. Arthur Gillett was a personal friend of Smuts and the husband of Smuts' friend Margaret Clark and her sister Alice, to whom he was also attracted (Schwartz 2011:312). See also Smuts Papers, Vol 24 no.96.

### **3.4.4 The South African Refinery and Mint**

Added to the October (1919) conference, came the decision in South Africa to build a refinery and a mint for her gold. The Mint Act of 1919 provided the legal basis, and the gold producers were tasked with building the refinery. The refinery started operating in December 1921 and the mint at the end of 1923. The operation of the refinery earlier in 1922 and the mint by the beginning of 1924 brought pressure on the Bank of England to loosen its control of South African gold, with amendments to the July (1919) agreement in 1922, and in April 1925 it was amended so that only gold not sold by producers elsewhere, had to go to London (Ally; 1994:70). On the 25<sup>th</sup> January 1926, it was formally ended by the South African gold producers.

Contrary to the concerns of the Labour Party, South Africa continued to suffer from deflation, not inflation, with CPI declining by 9.5% in 1921, and 16.6% in 1922. In fact, it was only when South Africa was forced to abandon its obsession with the Gold Standard at the end of 1933 that this destructive deflation stopped and prices stabilised for the rest of the decade (Statistics SA, annual inflation rate measured as changes in CPI).

In the inflationary environment caused by the stimulus of war expenditure, “a spirit of reckless competition had tended to reduce progressively the quality and security of bank advances”, (Henry; 1963:227), so the official biographer of Standard Bank tells us. In this environment, the National Bank was particularly guilty, showing “a dramatic speed in opening branches”, opening 100 new offices during the year ending March 1920 (Crossley and Blandford; 1975:10). This classically destabilising behaviour fits neatly into the description of the nature of banking described by Minsky (1986) and as dealt with in section 4.5, pages 62 – 68.

As predicted by Keynes, this all too common reckless behaviour by the banking sector required firm regulation by a Central Bank (see pages 68 - 79), and this became clear to Clegg at the SARB in 1923. Given the political pressures on Smuts following his suppression of the white miners’ strike in 1922, Clegg telegrammed Norman on the 23<sup>rd</sup> May 1923 with his concern that Smuts might buckle to nationalist pressure, nationalise the National Bank and turn it into a State

Bank while amalgamating it with the SARB<sup>15</sup>. Norman recognised the threat and the opportunity and telegraphed back on the 11 June 1923, offering in the strictest confidence that the Bank of England would assist with any rescue of the National Bank on the strict condition that the independence of the SARB was maintained. This, he said, was to promote co-operation among Central Banks (read “in the Empire”), to prevent the establishment of State Banks, as opposed to Central Banks in the Empire and to maintain the prestige of British and Colonial Banks<sup>16</sup>. National Bank continued to suffer with deposits falling by £5.5 million in the year ending March 1924 (Crossley and Blandford; 1975:11). Little wonder then that F.C. Goodenough, the chairman of Barclays Bank Limited since 1916, who was intimately involved with Strakosch and Norman in choosing Clegg for his position, and from whose office this selection process was run<sup>17</sup> (see pages 122 - 123) should be ready to pounce when, in April 1924 the “Governor of the South African Reserve Bank visited London” and Goodenough entertained Clegg “at lunch at the National Bank’s London office” (Crossley and Blandford; 1975:12). Of course, the National Bank was struggling with a “lack of capital together with the restrictions imposed on the bank’s freedom of action, necessitated by the close supervision of the Reserve Bank” (Crossley and Blandford; 1975:11).

Barclays were anxious to get South African government approval for the takeover of the National Bank, and following the offer to the National Bank shareholders, Leisk secured the approval of Hertzog and his finance minister, Havenga in April 1925 (Crossley and Blandford; 1975:17). The National Bank changed its name to Barclays Bank (Dominion, Colonial and Overseas) later that year.

Concerns about the incestuous relationship between banking regulators and the banks which they are tasked with regulating, which are so relevant today, were obviously very valid in the 1920s. The fact that Norman and Goodenough were central to the appointment of Clegg, and Norman and Clegg were involved in the rescue, regulation and sale of National Bank, allowing Barclays an instant national presence in South Africa, is problematic. Although a causal relationship does

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<sup>15</sup> Montagu Norman Papers, Bank of England Archives, file OV37/20.

<sup>16</sup> Montagu Norman Papers, Bank of England Archives, file OV37/20.

<sup>17</sup> Montagu Norman Papers, Bank of England Archives, file OV37/20.

not exist, it is interesting that Strakosch's £5 000 cheque supporting Smuts' 1924 election was drawn on National bank<sup>18</sup>.

The difficult banking environment caused by deflation also saw African Banking Corporation Ltd lose its independence when it was absorbed by Standard Bank in 1921 (Henry; 1963:232).

### **3.4.5 General economic conditions 1920 - 1922**

South Africa's balance of trade for 1920 moved from a deficit of £21million to a surplus of £3.5 million in 1921 as a result of the post war depression (Henry; 1963:223). Deflation brought depression in 1921, as Keynes (1923) predicted in the *Tract* (see pages 74 - 76). "In 1920 10 097 motor cars were imported; in 1921 only 2 093"(Henry; 1963:221). By 1922, insolvencies were up to almost 2 500 (Henry; 1963:223).

### **3.4.6 Monetary causes of the Rand Revolt in 1922**

Although the direct cause of the 1922 white miners' strike, which became the Rand Revolt, was the decision by the Chamber of Mines to change the Status Quo Agreement and lower white wages and increase the number of black workers, Ally (1994:140-141) looks at the deeper monetary causes. Although South African mines benefited from the devaluation of sterling in 1919, Britain began a process of depreciating prices to re-establish pre-war gold parity, as a result of which the gold price began to fall, precipitating the crisis. This, together with an inability at the time to refine, mint and ship the gold to the highest bidder (see pages 10 and 24), left the producers with the only option of squeezing white miners.

Contrary to the conventional wisdom espoused by Samuel Evans, Edwin Kemmerer and others, the Gold Standard was not the saviour of the gold miners as they had hoped. As mentioned in Chapter 2 above, South African producers received the official price, far less than the open market price for gold in India or America, throughout the First World War and the first half of

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<sup>18</sup> Smuts Papers, National Archives, Pretoria, File 30 (renumbered 214 in National Archives) number 38, Strakosch's letter dated 16<sup>th</sup> April 1924.

1919. Then in 1920-21, when the world was largely off the Gold Standard, the price received jumped 28% to £5.45 per ounce. The restoration of the Gold Standard saw the price received by the South African producers fall back to the official £4.25 per ounce during the period 1925-1929, and climb again once Britain left the Gold Standard in 1931, climbing further during the period when South Africa and the USA was forced off in 1933-34. The period in question ends with the world off the Gold Standard in 1936 and with the price received by our gold miners up 69% on that which they received at the beginning of the period in 1919 (Feinstein; 2005:105, Table 5.3 sourced from the Chamber of mines 1985 Annual Report, p.58). And so this quasi-religious belief that the Gold Standard was good for the gold miners, turned out to be not only untrue, but the opposite – once the world was unshackled from the Gold Standard, the South African miners did significantly better.

By 1925, the economy was improving with the production of gold and coal substantially increased (Henry; 1963:225). Also, the weather was kind to agriculture, and with the new protective environment, which included trade protection, “Employment in manufactures ... improved greatly” (Henry; 1963:226). Up to 1928, agriculture, mining and manufacturing did well, as the deflation of the period 1919 – 1923 was now clearly in the past and prices were now relatively stable (Statistics SA South African annual inflation rate measured as changes in CPI). Export prices for agricultural products had actually risen in 1928 (Henry; 1963:229). For the year up to September 1929, the newly branded Barclays DCO opened 12 branches and ten sub-branches (Crossley and Blandford; 1975:45).

Then came the decline. By 1930, the average price of wool, sugar and other agricultural products was just over half what it had been in 1926, but the currency was, thanks to the Pact government, stubbornly fixed to gold. Although a greater volume was shipped, the wool exported netted 31% less.

### **3.4.7 The consequence of adherence to the Gold Standard, South Africa 1931-1932**

If the rigid thinkers in the Bank of England and Whitehall received their comeuppance in 1931, the stubbornness of Pretoria meant that South Africa dragged on with its Gold Standard until the

end of 1932, before being forced off it. As Fine and Rustomjee so brilliantly show, “class agencies”, which are described here as the will of “vested interests” does not automatically translate into economic welfare. We need to pay attention to “actual and potential economic linkages” (Fine and Rustomjee; 1996:144-145), or in other words, the structure of the world in which we live. They point out the “extreme example”, which is the subject of this dissertation, which “proved so disastrous that it had to be dropped” (Fine and Rustomjee; 1996:125), namely the decision to return to the Gold Standard, and worse, to stubbornly refuse to leave the Gold Standard while it destroyed South African agriculture. I cannot think of a better illustration of the power of structure, or “linkage” as Fine and Rustomjee (1996) call it, and the weakness of agency in explaining economic performance than this example.

There could be no greater constituency for Hertzog, the Prime Minister of the Pact government, than white farmers, and no greater adversary than the English mine-owners. And yet, in his ill-conceived attempt to struggle free from British control, and to align South Africa with the gold-rich USA, agriculture went from contributing over 20% of South African GDP in 1924 to about 13% in 1934. This was the fault of Hertzog’s disastrous decision. At the same time, mining went from contributing less than 17% in 1924 to over 20% of GDP in 1934 (Fine and Rustomjee; 1996:72), a fortune made purely thanks to the structure/linkage of the international economy as it spiralled into the great depression, and as the gold price rose as a result thereof, and not because of the agency of any South African politician or businessman. In this way, *ideals* have their last laugh over *power*. For regardless of how powerful those in control are, if the ideas which underpin that exercising of power turn out to be misaligned with the structure of the world in which they find themselves, then “sooner or later, it is ideas, not vested interests, which are dangerous for good or evil” (Keynes; 1936:385).

### **3.4.8 Recovery 1933-1936**

By 1934, having cast off its gold fetters just over a year ago, South Africa was “both commercially and industrially one of the more prosperous countries in the world (Henry; 1963:254). Gold continued to do well for the economy “with output increased by 45per cent” (Henry; 1963:255), thanks to the higher price since the destruction of the Gold Standard. By

1936, world commodity prices were rising and South Africa was experiencing a building boom (Henry; 1963:257).

## **CHAPTER FOUR**

### **THE THEORETICAL CONTEXT**

#### **4.1 Introduction**

The monetary orthodoxy before Keynes can be summed up as arguments in favour of “sound money” principles. These arguments were almost always supported by the institutions of internationally mobile capital, and invariably these institutions profited from “sound money” policies. Alternative to this orthodoxy was a line of thinking which this dissertation picks up at the end of the 18<sup>th</sup> century, which argued for a monetary policy in service of the real economy.

This dissertation seeks to locate Keynes in this paradigm, rejecting the notion that the “sound money” or Gold Standard policies were finally also good for the real economy “in the long run”. As this dissertation highlights, the world and South Africa during the period 1919-1936 was one in which “sound money” failed the real economy.

Those active in the monetary policy debates of the time had to face the failures of orthodox theory. They had to admit that Hume’s specie-flow mechanism was not working in the United States or in India; that money was not neutral, as shown by the war time inflations in South Africa and elsewhere. Contrary to the advice of Gold Standard supporters like Samuel Evans and others, they had to consider Henry Strakosch’s advice that growth in money supply, fuelled by increases in bank money, was cost-push inflation, as discussed in section 4.2. If war expenditure demanded increased production from South African industries, they needed to understand that bank money is endogenously created, as set out in section 4.3.

Furthermore, the experience of the period 1919-1936 made a laughing stock of the idea that the banking and investment market was stable and tending towards equilibrium as the orthodox theorists implied. The African and National Banks got into trouble in South Africa, necessitating two take overs; and banks collapsed spectacularly in Europe, Britain and the United States. With this evidence, the Pact government soon discovered the inherent uncertainty of investment decisions and the instability of the banking sector that is discussed in section 4.4.

## 4.2 From Monetary Orthodoxy through to the Keynesian Revolution

“The history of the Keynesian revolution is largely a story of Keynes’ escape from the quantity theory of money” (Skidelsky; 1983: 214). By 1875, the Gold Standard, and related to that, the Quantity Theory of money, was the dominant orthodoxy. The monetary debate, particularly in Britain, which was relatively rigorous in the 19<sup>th</sup> century up until 1875, was largely “resolved” by that time. “Defense of the Gold Standard had become, by the 1850s, a matter of faith rather than analysis, and in trying to find out its basis it is hard to get much beyond the idea of the law of nature and the sanctity of contracts” (Fetter; 1965:232).

The strands of this debate can be traced far back. In this case, I will start with the “Bullion Controversy” of 1779-1815, which came about as a result of the divergence of the silver-gold price ratio as the London Exchange was essentially a gold exchange and its principal currency trading partner was Hamburg with a silver exchange (Fetter; 1965:28). The bullionists blamed the rise in the price of silver relative to gold, and the depreciation of the British pound in the foreign exchange market, on the expansion of the monetary base by the Bank of England - a monetary phenomenon. John Wheatley (1803) and David Ricardo (1810-11) represented the “extreme bullionist position that the decline in the exchanges, and the increase in the price of bullion, were solely due to an excess issue of Bank of England notes, an excess issue which could not have taken place under convertibility” (*Palgrave*; 1986, Volume 1:290).

Although at this time the Quantity Theory of Money “was usually associated with the case for bi-metalism and was treated with much hostility by the advocates of “sound money” (Laidler; 1991:50), it came to embody orthodoxy, thanks largely to Irving Fisher who was responsible for its development in America, and to a lesser extent, thanks to Alfred Marshall who developed a version of it at Cambridge. This early Cambridge school of the Quantity Theory did not place much importance on velocity (in what came to be the Quantity Theory equation  $MV = PQ$ ) (Laidler; 1991:59).

Shocks to the money supply were held to work their way through the real economy, leaving real variables unchanged in the long run. Money was believed to be neutral as a long term influence. As far back as Ricardo, the Quantity Theorists' Achilles heel was this focus in the debate on "giving answers relevant to the long run outcome of particular situations, to questions having to do with the interim stages whereby long run equilibrium is achieved" (Laidler in *Palgrave*; 1986, Volume 1:291). A corollary of the Quantity Theory and Gold Standard orthodoxy was David Hume's specie-flow mechanism which specified that in a Gold Standard international system, price differentials between countries would be eliminated. If a country lost gold, say as a result of an unfavourable balance of trade, money stock would be constricted by this loss and prices would deflate. This would result in a stimulation of exports and a constriction of imports, resulting in gold flows into the country until a new equilibrium was achieved (William R. Allen in *Palgrave* 1987 vol 4:431).

Keynes' critique of this thinking occurs in Chapter 3 of the *Tract* dealing with "The Theory of Money and of the Foreign Exchanges", and particularly in the sub-section dealing with the Quantity Theory of money (1923:74 – 87). With a rhetorical technique which repeats itself in the *Tract*, Keynes starts off by praising the orthodox position: "1. *The Quantity Theory of Money*, This theory is fundamental. Its correspondence with fact is not open to question" (Keynes; 1923:74).

But then he identifies the weakness in Quantity Theory: He starts off by tracing the neutrality of money assumed by Quantity Theory, as disturbances make their way through the system without affecting real variables. "Now "in the long run" this is probably true... But this *long run* is a misleading guide to current affairs. *In the long run* we are all dead. Economists set themselves too easy, too useless a task if in the tempestuous seasons they can only tell us that when the storm is long past the ocean is flat again" (Keynes; 1923:80).

In the *Tract*, Keynes attacks Hume's specie-flow mechanism. He attacks the inflexibility of shackling one's country to an external monetary standard, robbing that country of the tools to work towards internal balance. His example turns out to be prophetic of British and South African monetary policy in the period up to 1931 in the case of Britain, and up to the end of 1932

in the case of South Africa. In both countries, the currency was shackled to the Gold Standard, “allowing the tides of gold to play what tricks they like with the internal price level and abandoning the attempt to moderate the disastrous influence of the credit cycle on the stability of prices and employment” (Keynes; 1923:172).

But scepticism of this specie-flow mechanism was not common in the Bank of England. Witnessing the enormous in-flows of gold into the USA after the First World War, it relied on orthodox specie-flow theory, hoping that the monetary base would swell in America. Orthodox theory held that this inflow of gold would cause a weakening of the dollar relative to sterling and hence make the British task of pre-war parity easier. Keynes shows the naïveté of this blind faith in orthodoxy by pointing out that the Americans were sterilising in-flows. “In practise the Federal Reserve Board often ignores the proportion of its gold reserve to its liabilities and is influenced, in determining its discount policy, by the object of maintaining stability in prices, trade and employment. Out of convention and conservatism it accepts gold. Out of prudence and understanding it buries it” (Keynes; 1923:197). This section of the *Tract* is interesting in how it relates to the central question of this dissertation, concerning the relative influence of power and ideas. The theory which underpinned the international Gold Standard dictated that this specie-flow mechanism should operate. The American authorities on the other hand were not going to allow the niceties of theory to get in the way of domestic priorities. Power trumped theory in this case.

Keynes points out that “the depreciation of the dollar through inflation in the United States, is that on which many have based their hopes. But it could only come about by a reversal or defeat of the present policy of the Federal Reserve Board” (Keynes; 1923:201), something which was not likely to happen.

Keynes saw the faith in the Gold Standard in Britain in the same way that he viewed Victorian religion, as a “barbarous relic” (Keynes; 1923:172). “Keynes habitually referred to Victorian moral discourse as ‘medieval’ or ‘barbarous’” (Skidelsky; 1992:xx). Keynes urges his reader not to rely on the solutions of the recent past when thinking about the solutions of the present.

The advocates of gold, as against a more scientific standard, based their cause on the double contention that in practise gold has provided and will provide a reasonably stable standard of value, and that in practise, since governing authorities lack wisdom as often as not, a managed currency will, sooner or later, come to grief. Conservatism and scepticism join arms – as they often do. Perhaps superstition comes in too; for gold still enjoys the prestige of its smell and colour (Keynes; 1923:164).

### **4.3 Inflation: Cost-Push Inflation arguments against the Quantity Theory**

As we have seen in section 4.1 above, the Quantity Theorists, its predecessors and successors laid the blame for the *cause* of inflation on an excessive increase in money supply, mainly by banks. Likewise, opponents of this approach, those who focus on cost-push causes of inflation, span an equally long period of time. The anti-bullionists attributed the rise in bullion prices primarily to “wartime disruption of trade and to foreign war expenditures by the British government; and they rejected or minimised any monetary explanation of these movements of prices and of exchange rates” (Fetter; 1965:28). In defense of the anti-bullionist position, the rise of food prices at the turn of the 19<sup>th</sup> century was so obviously the result of a small crop and the difficulty of importing food that hardly any mention was made of a possible monetary cause of this inflation in the pamphlets of the period. Malthus takes up what would be a Post-Keynesian response to Quantity Theory when he states in this period that “He would be inclined to consider an increase of paper rather as the effect than as the cause of the high price of provisions” (Fetter; 1965:30).

In a different attack on the Quantity Theory, Keynes in the *Treatise* discusses different price levels, sharing with Sraffa a concern not to treat all price levels equally. Having previously questioned the validity of purchase power parity in the *Tract*, he now goes on to state that “in its purest form (purchase power parity theory is) no more than a re-statement of the proposition given above to the effect that the rates of foreign exchange between two currencies move in the same way as the ratio of an international index expressed in the prices of one country to the same index expressed in the prices of another country” (Keynes; 1930:72). Keynes however warns that while the wholesale index “was moving rapidly into adjustment – as an international index

necessarily must”, it was misleading to say that “therefore the same thing was true of ‘prices generally’” (Keynes; 1930:75). Keynes continues with this theme in Chapter 6 dealing with currency standards, criticising Edgeworth and Jevons’ attempts to find a measure of “general prices”. In step with Sraffa, Keynes notes that “there is no moving but genuine centre, to be called the general price level or the objective mean variation of general prices, around which are scattered the moving price level of individual things. There are all the various, quite unique, conceptions of price levels of composite commodities appropriate for various purposes and enquiries which have been scheduled above, and many others too. There is nothing else. Jevons was pursuing a mirage” (Keynes; 1930:85-86).

Having criticised the simplistic Quantity Theory model, based on the assumption of a single price level, Keynes then goes on in Chapter 7 of the *Treatise* to build a more complex model. He notes that if there is an increase or decrease in the amount of money “the increase or decrease... is not spread evenly and proportionately over the various buyers. It will, in general, be concentrated in the hands of particular classes of purchasers” (Keynes; 1930:92). Sraffa’s influence on Keynes is fascinating. Sraffa’s graduate thesis (1920) was in the field of monetary economics and considered “differentiated trends shown by the various price indexes... in particular the social classes of workers and entrepreneurs” (Roncaglia; 1979:6). Following this concern by Sraffa, Keynes suggests a workers consumption price index in the *Treatise*. He notes that “the working out of the social and economic consequences of the new distribution of purchasing power will end up establishing a new equilibrium” (Keynes; 1930:92). He then goes on to develop his idea of the stickiness of wages as a reason of “the failure of different price levels to move together” (Keynes; 1930:94).

On both sides of the fundamental equation (Keynes; 1930: 133 – 157), Keynes points to two types of inflation (four in total). Profit and income inflation on the one side and commodity and capital inflation on the other. He states that his concern is income and profit inflation. It is by the anticipated profit or loss that entrepreneurs affect prices and it is by anticipating this that “the banking system is able to influence the price level” (Keynes; 1930:159). Sraffa’s efforts to “solve certain analytical problems – in particular the link between relative prices and distribution of income” (Roncaglia; 1979:50) is another theme picked up by Keynes. The arguments by

Evans and Strakosch about the increase in money supply and inflation during and just after the First War point to the relevance of these arguments.

#### **4.4 Endogenous Money Supply**

Keynes' approval for the fact that most money is created in the banking system starts in his first book *Indian Currency and Finance (ICF)*. It is in a way one of two archetypal monetary systems which loom large in Keynes' psyche and inform his approach to monetary economics. The first is the backward, uncivilised world where trust is at its lowest, no banking system of note is developed, no-one trusts bank loans, no-one trusts cheques or other negotiable instruments and wealth is held in a base and heavy metal, such as gold, hoarded as it might have been by a troglodyte, far from any useful application by a clever entrepreneur or existing business owner. "Keynes was fascinated by the legend of King Midas, whose hunger for money was such that his food and wine turned into gold. Perhaps he started to see himself in legendary terms – as a Dionysus come to turn Midas' gold back into food and wine" (Skidelsky; 1992:175).

In Keynes' mind, there is a clear connection between the distrust involved in not accepting paper currencies or the instruments of an advanced banking system and the primitive instinct to hoard wealth. It was in Keynes' first book, *ICF* that he discusses hoarding, and of course, the negative effects of hoarding were to be developed in his later books, particularly in his last book, *The General Theory*. "The extent to which the people resorted to hoarding ... during the Balkan War was very remarkable, and has exhibited a danger to which the banking systems of those countries are still subject, although some have begun to forget it. .... Some banking failures, a hint of political trouble, - and the old habits will come back, whatever progress banking may seem to have made in a time of prosperity" (Keynes; 1913:165). I would argue that Keynes had in his mind ideas about advancing financial civilisation, not always a stable thing, away from the "barbarous relic" of the Gold Standard and away from the primitive urge to hoard, towards a well regulated and stabilised banking and financial system which would afford, what he called in another context, "that degree of civilisation which we have already attained" (Keynes; 1963:324).

Keynes redirects the cause of Britain's monetary success away from the "barbarous relic" of mistrust represented by the Gold Standard and towards the trust, co-operation and shared resources of the British banking system, the London capital market and the use of cheque books by businessmen. "In England the use of a cheque currency has grown so universal that the composition of the metallic coin has become a matter of secondary importance" (Keynes; 1913:69-70). Later in *ICF*, he points out that "The 'sound currency' maxims of twenty or thirty years ago are still often repeated, but they have not been successful, nor ought they to have been, in actually influencing affairs... It has been found that the expense of a gold circulation is insupportable and that large economies can be safely affected by the use of some cheaper substitute" (Keynes; 1913:71-72).

This theme of civilising progress detailed in *ICF* continues in the *Treatise*. Keynes includes "debt contracts" in the definition of money, noting that if the narrower definition of "a convenient medium of exchange" is only allowed "we have scarcely emerged from the stage of barter" (Keynes; 1930:3). As a dig at those seeking a metallic base for money, Keynes notes that state sponsored money constitutes "all civilised money" today (Keynes; 1930:5). He points to the mistake of Milton Friedman's monetarists forty plus years later "in the futile attempts to ignore the existence of bank money and consequently the inter-relationships of money and bank credit" (Keynes; 1930:17). Having identified the inclusion of bank-created money in the definition of money, Keynes goes on to show how not only do banks create money, but that the extent of the money created is demand driven and credit determined (Keynes; 1930:25-26), a theme picked up by Basil Moore almost sixty years later (Moore; 1989:11).<sup>19</sup> Keynes points out that this system of bank-created money relies on a system where money supply by individual banks is in step with those of their colleagues in the banking system.

As if to support his fundamental equations detailed in the *Treatise* (Keynes; 1930: 133 – 157), Keynes notes that ninety percent of money in the USA and Britain is bank money. Not to take into account this predominance results in the "essential characteristics" of total money supply "being treated as anomalous or exceptional" (Keynes; 1930:33).

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<sup>19</sup> An excellent summary of Moore's views and his debate with Charles Goodhart can be found in "Has the demand for money been misled? A reply to 'Has Moore become too horizontal?'" in *Journal of Post Keynesian Economics*. 14(1), pp.125-133.

Unfortunately while many, and perhaps even most, theoretical shifts in the *General Theory* can be considered improvements on previous articulations by Keynes, his insistence on the exogeneity of money in the *General Theory* is, I believe, not one of them. It is difficult to see why, when he was so aware of the power of the banking system to expand monetary supply in *ICF*, and where similar articulations of endogenous money supply by the banking sector are found in the *Treatise*, he now reverts to a simplistic exogeneity of money. This is ironic, as the economist most responsible for slaughtering Keynes' reputation, Milton Friedman, held the power of the central bank to control money as the one act allowed to non-market forces. And it is doubly ironic, given the failure of monetarists to successfully target money supply, and the fact that it was left to the post-Keynesian economist, Basil Moore, to point out the futility of the central bank directly targeting monetary supply.

Also endogenous are the separate and unrelated motives of savers and investors. In the *Treatise*, Keynes points out that “the increase or decrease of capital depends on the amount of investment and not on the amount of savings” (Keynes; 1930:173). “The performance of the act of saving is in itself no guarantee that the stock of capital goods will be correspondingly increased” (Keynes; 1930:175). In chapter 12, Keynes goes on to illustrate this point by his famous example of a single product economy producing bananas.

With Keynes' banana economy showing how easily an economy can go out of balance as a result of a shortfall of investment, once again (as in the case of *ICF*), he places the banking system, the provider of the appropriate level of credit to business, as the equilibrator “thus the first link in the causal sequence is the behavior of the banking system, the second is the cost of investment... and the value of investment..., the third is the emergence of profit and loss, and the fourth is the rate of remuneration offered by the entrepreneurs to the factors of production” (Keynes; 1930:182).

## 4.5 Uncertainty and Banking Instability

Having established that bank money constituted the majority of total money, I will now look at the Achilles heel of capitalism, the banking and investment systems. I do so, firstly considering the uncertainty which all bank clients and investors face, then building on that, consider banking and investment instability. Once this Cassandra-like task is done, I look at how Central Banks can remedy this undesirable situation.

Keynes understood the problem of uncertainty in decision-making early in his career. In *A Treatise on Probability* (1921), he considers two types of probabilities: those whose chance of occurrence can be calculated with a degree of precision, and which Keynes called “subjective probabilities”, something he later named “uncertainty”, based on “insufficient knowledge and which can change quickly and substantially as a result of changing circumstances” (Minsky; 1975:62-63). In addition, *A Treatise on Probability* considers the “confidence attached to a proposition” (Minsky; 1975:63). As Minsky points out, “decision-making under uncertainty, which Keynes had treated in his *A Treatise on Probability* is central to the *General Theory*” (Minsky; 1975:63).

In his article, *The General Theory of Employment* (1937), known as “the answer to Viner”, Keynes could not be more explicit:

By ‘uncertainty’ knowledge, let me explain, I do not mean merely to distinguish what is known for certain from what is only probable. The game of roulette is not subject, in this sense, to uncertainty... Even the weather is only moderately uncertain. The sense in which I am using the term is that in which the prospect of a European war is uncertain, or the price of copper and the rate of interest twenty years hence, or the obsolescence of a new invention, or the position of private wealth owners in the social system in 1970. About these matters there is no scientific basis on which to form any calculable probability whatever. We simply do not know. Nevertheless, the necessity for action and for decision compels us, as practical men, to do our best to overlook this awkward fact and to behave exactly as we should if we had behind us a good Benthamite calculation of a series of

prospective advantages and disadvantages, each multiplied by its appropriate probability waiting to be summed up” (Minsky; 1975:64).

In this same article, Keynes could not be clearer: “The theory can be summed up by saying that given the psychology of the public, the level of output and employment as a whole depends on the amount of investment” (Minsky; 1975:65). Minsky sums up the differentiation between Keynes and classical economists, noting that Keynes’ focus “revolve around portfolio preferences, financing conditions and uncertainty” (Minsky; 1975:65).

In the *General Theory* this uncertainty takes centre stage. Keynes again speaks profoundly: “Or perhaps, we might make our line of division between the theory of stationary equilibrium and the theory of shifting equilibrium – meaning by the latter the theory of a system in which changing views about the future are capable of influencing the present situation. *For the importance of money essentially flows from it being a link between the present and the future*” (Keynes; 1936:293). The fact that Keynes emphasises the second sentence in italics suggests his theory is more one of instability, uncertainty and complexity. For if money is indeed a link with the future and the future is by definition uncertain, then instability is inherent in the economic system.

Keynes, the astute investor, notes that “our conclusions must mainly depend upon the actual observation of markets and business psychology” (Keynes; 1936:149). His thorough knowledge of investment markets, through his position on the board of an insurance company and through his own investments and those which he directed on behalf of Cambridge University, gave him an insider view of investment markets not common amongst theoretical economists (stockbroker David Ricardo being the one exception that springs to mind). Skidelsky (1992) hones in on Chapter 12, noting that it is “the best account in the economic literature of the psychology of panics” (Skidelsky; 1992:556).

All of this uncertainty, tied up as it is within the psyche of money, particularly bank money, provides the background to the discussion on inherent banking instability. In *ICF*, when Keynes is discussing the bank finance of Indian trade, he notes that “India is now enjoying the fruits of past disasters and of conditions in which the struggle for existence was too keen to allow any but

the fittest to survive. If the present spell of prosperity lasts too long, she will no doubt lose it” (Keynes; 1913:208-209). This is a fascinating sketch of a cycle in banking, which had to wait another 73 years to be fully explored by Hyman P. Minsky in *Stabilizing an Unstable Economy* (1986). As Keynes shows here, financial crises and bank failures cause the banking system to be generous in providing reserves and to be prudent with their loans. If a period of prosperity and calm in financial markets extends too long, banks fail to correctly price the risks involved and the seeds of future failure are sown. As Minsky (1986) put it, “stability creates instability”. And whatever level of reserves are customary “the bank will then be... unwilling to see its reserves rise above it, since this generally means that it does less profitable business than it might” (Keynes; 1930:29).

“A monetary system of this kind would possess an inherent instability”, Keynes points out, because this herd mentality in the supply of money “would be capable of setting up a violent movement of the whole system” (Keynes; 1930:27). The instability of banking and investment systems was the subject of articles which Keynes persuaded Pierro Sraffa to write for both the *Economic Journal* and the *Manchester Guardian* commercial reconstruction supplements (Moggridge; 1992:435). Sraffa’s articles on the instability and nepotism within the Italian banking system can be read along similar lines to Keynes’ comments on the Indian banking system in *ICF*.

In chapter 13 of the *Treatise*, Keynes introduces a model of how investment goods are produced, which shows how investment flows like water from a fire hydrant, in theory it can vary incrementally, but in practice it is usually gushing, or not flowing at all. At the start of describing the genesis and life history of a credit cycle, Keynes again notes that “the decisions which determine saving and investment respectively are taken by two different sets of people influenced by different sets of motives, each not paying very much attention to the other” (Keynes; 1930:279). Again, this sets the tone for a Sraffian approach, eschewing a general equilibrium model and focusing separately on the constituent parts of the credit cycle. “The business of saving is essentially a steady process... Investment in fixed capital, on the other hand, has been accustomed to proceed irregularly and by fits and starts” (Keynes; 1930:280).

By the time we get to the *General Theory*, this model, now in chapter 11 (on the Marginal Efficiency of Capital), has become more stable, although its basic structure is very similar to chapter 13 of the *Treatise*. Skidelsky (1992) points out that chapters 11 and 12 (on Long Term Expectations) contain the two contrasting spirits of the *General Theory*. For the investor, this contrast involves on the one hand the calculated decisions of making sure that the expected return on an investment is greater than the Marginal Efficiency of Capital, and also greater than the cost of finance (interest), and on the other hand, by contrast, being aware of the brittle foundations that long term expectations are based on.

In Chapter 22 of the *General Theory*, Keynes dismisses the idea that interest rate policy *causes* a boom or a slump. In a boom, we have a situation “in which over-optimism triumphs over a rate of interest which, in a cooler light, would be seen to be excessive” (Keynes; 1936:322). When the turn comes, as a result of a revision of expectations at a time when investors notice that asset prices are inflated, the fall comes “with sudden and even catastrophic force” (Keynes; 1936:316). Skidelsky notes that the collapse is aggravated rather than caused by a rise in interest rates due to increased liquidity preference (Skidelsky; 1992:568). In the modern world of course, with activist central banks, the lowering of the rate of interest in a recession might soften the blow, but does not alleviate the fall in asset prices and the concomitant debt deflation linked to it.

The extent to which the *General Theory* is read as an annexure to classical economics is the extent to which the special nature of the banking and investment sectors are ignored. Minsky (1975) sets himself the task of bringing investment finance back into Keynes’ analysis. Keynes, in chapter 24 of the *General Theory*, called for a decrease in capital’s share of total income, for socialisation of investment, and for the driving down of interest rates thereby eliminating the scarcity of capital and achieving full employment. By contrast, the neo-classical synthesis promoted private investment. “Rather than reducing inequality, public policy actually promoted it. Rather than achieving full employment through job creation, policy offered welfare and social security to remove people from the labour force. As Minsky argued from the late 1950s, this combination of policies would inevitably promote inflation, rising inequality, and financial fragility” (Minsky; 1975:xiii).

The interference in the pricing mechanism of the real economy by an over powerful financial sector is something which Keynes deals with in the *Tract* and in the *General Theory*. After discussing the income deposits and business deposits that make up industrial circulation in the *Tract*, Keynes goes on to discuss financial circulation, noting that “the pace at which a circle of financiers, speculators and investors hand round one to another particular pieces of wealth, or title to such, which they are neither producing nor consuming but merely exchanging, there is no definite relation to the rate of current production. The volume of such transactions is subject to very wide and incalculable fluctuations” (Keynes; 1930:47). He goes on to comment that trying to detect the economic fundamentals of signals from the real economy amongst the noise of the “large and variable factor of financial transactions is a serious obstacle to reaching reliable inductive results concerning modern monetary problems” (Keynes; 1930:48).

Minsky’s summary of the *Treatise on Money* makes one realise that, in some respects, the ideas of the *Treatise* are finer than that of the *General Theory*. Firstly, Minsky notes that in the *Treatise* Keynes worked with “more natural concepts of money than the standard theory admitted, in that money as created by banks indirectly represented business debt... (That) money changes to the price level ... operates first by affecting business financing of investment” (Minsky; 1975:8). In the *General Theory*, the speculative nature of asset holding and financing choices dominates production function characteristics in determining investment output (Minsky; 1975:9). He proposes to blend the institutional analysis of the *Treatise* with the more holistic theory of the *General Theory* (Minsky; 1975:10). Minsky rejects the policy of merely rescuing private investment institutions when they get into trouble, noting that “the stability that this will cause, even if it is the result of policy, is destabilising” (Minsky; 1975:11). What he proposes in its stead is to shift investment towards the public sector so that the instability of financial markets and private investment is reduced.

Minsky takes Keynes’ arguments about the instability of the investment function to the next logical level, examining business cycles in the economy by taking into account the “instability of portfolios and of financial inter-relations” (Minsky; 1975:55). He defines a “portfolio” as assets owned or controlled and liabilities put out to achieve this ownership and control (Minsky; 1975:67). The portfolio composition is the area in which decisions about the future play out most dramatically. “To understand Keynes it is necessary to understand his sophisticated view about

uncertainty, and the importance of uncertainty in his vision of the economic process. Keynes without uncertainty is something like *Hamlet* without the prince” (Minsky; 1975:55). Minsky points out that classical economics, including the new-classical synthesists, are based on the barter paradigm; the image of a producer trading in the village market comes to mind. Keynesian theory (particularly that developed by Minsky) rests upon a speculative/ financial paradigm, with the image of a banker making deals on Wall Street being more appropriate.

Minsky claims that the concepts which are de-emphasised in interpreting Keynes, the cyclical perspective, the relationship between investment and finance, and uncertainty are central to his contribution to economics. In Marshall, the economic system’s tendency towards equilibrium is a “tendency towards rest” with population change, innovations, political and institutional changes being exogenous to the system. Minsky points out that the “equilibrium” in Keynes is a transitory system of variables where endogenously determined change is ever-present. “Each state, whether it is boom, crisis, debt deflation, stagnation or expansion is transitory” (Minsky; 1975:58-59). He sets himself the task of completing Keynes’ theory, which is “incomplete without a model of endogenous generation of booms, crises and debt deflations”, specifically those linked to the debt structures of investments (Minsky; 1975:61).

In attempting to build a model to establish the pricing of capital assets which have been subject to finance, Minsky (1975), starts with an overview of capitalist financial relations in terms of cash flows, considers the liquidity preference function in equation form, and examines how asset valuation and the financing of these assets are related. This is of profound importance to the stability of the banking system. His models of the investment process in which debt finance is involved, build upon Keynes’ models of chapter 13 of the *Treatise* and chapter 11 of the *General Theory* and explain the collapse of the financial system in 2008, arguably better than any model since.

Keynes also deals with “the industrial circulation and the financial circulation”. Industrial circulation being the process of maintaining normal current output, distribution and exchange and paying the factors of production income for the various duties which they perform from the beginning to the final satisfaction of the customer. “By *finance* on the other hand, we mean the

business of holding and exchanging existing titles to wealth... including stock exchange and money market transactions, speculation and the process of conveying current savings and profits into the hands of entrepreneurs” (Keynes; 1930:243). In considering the industrial consequence of a change in money supply, Keynes notes cheerfully that the “injection of an increased quantity of cash... into the monetary system will increase the reserve/ resources of the member banks, it will, ... render the latter more willing lenders on easier terms; that is to say, the new money stimulates the banks to put resources at the disposal of those borrowers who are ready to employ them” (Keynes; 1930:263). It is noteworthy that Keynes has yet to develop his understanding of the liquidity trap which he describes so eloquently in the *General Theory*. In the year or so after the 2008 banking crisis, despite enormous injections into the banking system, loans could not be said to be placed in the hands of “those borrowers who are ready to employ them”.

#### **4.6 Central Banks to the rescue**

It was obvious to Keynes that central banks had an important role to play in an economy. Someone in authority needed to deal with excessive money supply at the time of the harvest and chronic shortages of it in the growing season (Keynes; 1913:258). In advanced countries with banking systems, pro-cyclically determined money supply added to the instability of the business cycle. Both scenarios required the steady hand of a monetary authority. “The ultimate solution probably lies in the establishment of a central bank for India which shall be the government bank and shall hold the banking and currency reserves at the same time” (Keynes; 1913:161). “Something must be said for proposals for a state bank. This is a proper subject for inquiry by a royal commission. I am not prepared to discuss it here in detail” (Keynes; 1913:232-233). It is clear that the *ICF* arguments in favour of a central bank in India would have been even more forthright had the political environment been more sympathetic towards it. In a confidential memorandum to Foxwell at the Treasury, Keynes “went well beyond the brief discussion of the pros and cons of a state bank in *ICF*”. Keynes pushed in private for the establishment of a central bank in India in this document (Moggridge; 1992:227).

The function of lender of last resort was one something much talked about in monetary debates. Until Walter Bagehot raised the issue as editor of the *Economist* newspaper in the 1860s, it was

virtually undiscussed. It points to the power of a particular theoretical paradigm in which the lender of last resort concept did not neatly fit. Yet in a world of regular bank crises, it is a wonder that it took so long for someone in the debate to have the courage to raise it (Fetter; 1965:200-206).

The function of lender of last resort was very much in Keynes's mind in *ICF*: "We now come to the much more important question of the adequacy of the sterling reserves. I do not think it has ever been thought out quite clearly for what precise purposes these reserves are held. The difficulty can be put shortly in this question - are they held purely as a currency reserve, or are they to fulfill also the purpose of a banking reserve?" (Keynes; 1913:147-148). In Keynes' correspondence with Foxwell, he clearly indicates that he would have argued more stridently for full reserves to be held by an Indian central bank to be used in the event of both a currency and a banking crisis, had the support for an Indian central bank been greater. The difficulty of getting past vested interests in order to set up a central bank was well understood by Keynes.

The government is naturally afraid of so troublesome a proposal – and one so far removed from that which they are used to; while there is no important body which is sufficiently interested in forcing it on their attention. The banks fear a possible rival; merchants are content with present prosperity; and no one else knows anything about it. I shall be astonished, therefore, if action is taken while times are good. Perhaps we may have to wait for the lessons of a severe crisis. Only under some such strong influence as this is it likely that the responsible government will nerve itself to the task, or the business community acquiesce in it (Keynes; 1913:238-239).

This "crisis" is exactly what caused the establishment of the SARB. Retaining these profits in the reserves of a proposed central bank was an integral part of working towards this stability. The above quote is a brilliant description of the interplay of ideas and power. Twenty three years later, Keynes would end the *General Theory of Employment, Interest and Money* with a chapter which begins "Are the interests which they will thwart stronger and more obvious than those which they will serve?" (Keynes; 1936:383).

In the MacMillian Committee, one of the seven possible remedies which Keynes suggested for monetary disequilibrium, which started with Britain's return to the Gold Standard in 1925 and was now being exaggerated by the development of the Great Depression, was a co-ordinated effort between the central banks of the world to drive down interest rates in the interest of stimulating investment.

Ironically, given the straitjacket of rules which central bankers have been subject to in the post-Milton Friedman world, Keynes hoped that a central bank staffed by educated and competent monetary authorities could be trusted to use their *discretion* in applying their minds to the monetary problems which they faced from time to time. "Keynes' characteristic preference for discretionary arrangements as opposed to fixed rules emerges very clearly, as does its condition: expert management shielded from political interference" (Skidelsky; 1983:280). He railed against rigid rules for monetary policy. "The 'independent Treasury system' and the traditional aloofness of the government from the money market was seen at their worst. Millions of rupees were lying idle in the government treasuries at the time of year when there was most work for them to do outside" (Keynes; 1913:258).

Keynes was also well aware that bankers could not be trusted to regulate themselves.

New banks are springing up with alarming rapidity... The fear is that if one of these mushroom growths fail, others will follow, and the timid depositor, unable to discriminate between the sound and the unsound concerns, will make haste to get his money back from whatever bank it is in, and his confidence in banking institutions thus rudely checked will take years to win back... various suggestions have been made as to what restrictions would be proper. It has been proposed that it should not be permitted to combine banking operations with other businesses... and that capital and reserves should bear a certain proportion to liabilities before dividends may be paid (Keynes; 1913:231-232).

#### 4.7 Focusing on Internal rather than External Balance

Central to the arguments of those in South Africa, Evans, Kemmerer and others, who favoured a return to the full Gold Standard, was the belief that external balance – maintaining Gold Standard parity – was a panacea in and of itself, and that internal balance would follow. Contrary to this, the *Tract's* principle aim was to argue for a focus on achieving internal, rather than external, equilibrium when pursuing monetary policy.

Put differently, the question was whether the policy should be directed towards the stabilisation of prices or, alternatively, the stabilisation of the currency exchange. And if there arose a conflict between these two aims, “monetary policy should be used to stabilise the price level” (Skidelsky; 1992:153). This suggests a disconnection with the concerns of the real economy, and perhaps a better way to explain this would be that “exchange rate policy should be subordinate to the needs of the domestic economy” (Skidelsky; 1992:158). Pierro Sraffa’s graduate thesis (1920) was in the field of monetary economics. Its most important contribution lay in “the distinction between the stabilisation of the internal and of the external value of money, or in other words between stabilisation of the average level of domestic prices and the stabilisation of the exchange rate” (Roncaglia; 1979:6). Given that Keynes and Sraffa met in 1921 (Moggridge; 1992:435), and given the fact that this distinction between internal monetary equilibrium and external monetary equilibrium was the central theme of Keynes’ *Tract on Monetary Reform*, the speculation of Sraffa being the inspiration for the main theme of the *Tract* is interesting.

In the *Tract*, Keynes employs his rhetorical technique to deal with seasonal fluctuations, a theme which he dealt with in *ICF*. Keynes notes that the exchange rate can be raised to a target level by the “lowering of its internal price level relative to the internal price level of the other country... The conclusion is generally drawn that budgetary deficits covered by a progressive inflation of the currency render the stabilisation of a country’s exchanges impossible” (Keynes; 1923:106). He goes on to state the orthodox corollary that “if a country’s budget, currency, foreign trade and its internal and external price levels are properly adjusted, then automatically, its foreign exchange will be steady” (Keynes; 1923:107).

Keynes then highlights the weakness in this approach by showing that, while there may in fact be equilibrium over the long run, say a period of a year, the seasonal nature of agricultural trade causes disequilibrium during the year (Keynes; 1923: 108). He goes on to show that, for bankers to play their role as equilibrators of the seasonal agricultural trade imbalances, they require the expectation of stability, which needs to be “backed up by a guarantee on the part of the central authority (bank or government) to employ all of their resources for the maintenance of the level of exchange at a stated figure”. Hence, Keynes’ theme, developed in *ICF*, of a money market requiring the support of the authorities in order to assist in the establishment of equilibrium, finds further expression: “If, therefore, the exchanges are not stabilised by policy, they will never come to an equilibrium of themselves” (Keynes; 1923:114).

In the *Tract*, Keynes first states the conventional orthodox view: “When by adopting the Gold Standard we could achieve stability of exchange with almost the whole world, whilst any other standard would appear as a solitary eccentricity, the solid advantages of certainty and convenience supported the conservative preference for gold” (Keynes; 1923:158). He then introduces a weak point into this edifice, noting that it may be a coincidence that in previous years, the Gold Standard had achieved a “stable price level”. He notes that, as a result of the supply of massive amounts of gold by South African mines, at a time where expansive monetary supply was required, a situation arose where “the choice between stable exchanges and stable prices had not presented itself as an acute dilemma” (Keynes; 1923:158). Finally, he shows that, in the situation which had developed after the First World War, “when fluctuations are large and sudden, a quick reaction is necessary for the maintenance of equilibrium; and the necessity for quick reaction has been one of the factors which have rendered the pre-war method inapplicable to post-war conditions, and have made everyone nervous of proclaiming a final fixation of this exchange” (Keynes; 1923:159). Again, Eichengreen (1992) confirms that those countries in the inter-war period which left the Gold Standard early, and were able to work quickly on achieving internal equilibrium, fared better than those, like South Africa, who lumbered on trying to maintain the fixed exchange of the Gold Standard to which they had committed.

In looking at the conditions of external equilibrium in the *Treatise* (Keynes; 1930: 163), Keynes is mindful of the reality in Britain at a time where a lack of investment in British industry was accompanied by large British investments abroad.

He goes on to point out that with an international monetary system such as the Gold Standard, the central bank is forced to focus on external equilibrium, often at the expense of internal disequilibrium. He notes that, since 1924, France and the United States ignored external disequilibrium to focus on their own “internal equilibrium” while Britain had been stoically holding up its reputation as the great standard bearer of international equilibrium while at the same time suffering internal disequilibrium. At this point, it is worthwhile considering that the Pact Government also foolishly believed their salvation lay in shackling the South African currency to an international equilibrium, which it turned out was at the cost of great internal disequilibrium, particularly in the period 1931-1932/3. Keynes points out that orthodox equilibrium analysis assumes that the volumes of foreign lending (balance on the capital account) of the foreign balance (balance on the current account) and the “internal money costs of production are all... very susceptible to small changes in interest rates, prices and the volume of employment respectively” (Keynes; 1930:165). He points out that the evidence is against confidence in these orthodox assumptions, reiterating the central point in the *Tract*, namely that in a world of monetary disequilibria, the authorities should focus on achieving internal equilibrium. In highlighting the causal direction of change of price levels, Keynes states that “the most usual and important occasion of change will be the action of entrepreneurs under the influence of the actual enjoyment of positive or negative profits” (Keynes; 1930:157).

Keynes ends the *Treatise* still in the section on international disequilibrium, considering the case of restoring disequilibria in the absence of an “effective international standard”. In 1930, this is very prescient, given that it was written about a year before Britain was forced off the Gold Standard. Here for possibly the first time, certainly it is rarely admitted in the *Treatise*, Keynes admits that “when a disparity between  $B$  (the foreign balance), and  $L$  (the volume of foreign lending), cannot be cured by allowing gold to move... the operative machinery for preserving external equilibrium is no longer, primarily, a change in bank rate, but a change in the rate of foreign exchange” (Keynes; 1930:357). By allowing this disequilibrium, the bank rate can

perform its task as primarily an “instrument for internal equilibrium” (Keynes; 1930:357). Deflation as a cure to the ills of the real economy finally gets a mention.

#### **4.8 Watching for Inflation and Deflation**

One of the grave errors made during the period 1919-1936 was the excessive focus on the evils of inflation, all the while ignoring the destruction to the economy which comes with deflation. This was understandable given German hyper-inflation, and other inflation in Europe. But this ignored British and other deflations in this period. Connected with this concern only for inflation, and not deflation, is the useless national pride in a “strong” (uncompetitive) currency, and the distaste for a weaker (more competitive) one.

While orthodox economists railed against inflation, deflation, particularly if it was necessary to establish a previous parity of the currency, was accepted as necessary for economic health “in the long run”. Thomas Attwood (1783-1856), a Birmingham banker, who advocated for a flexible, managed currency aimed at achieving full employment (*Palgrave*; vol 1:135), attacked this thinking brilliantly: “If human wants could stand still during the action of this fatal principle; if men could live without food and clothing for two or three years, until the reduction of the circulating medium had acted alike in reducing the prices of all kinds of industry and commodities, then the social system might go on again” (Fetter; 1965:76).

The *Tract* looks at the relative damage done by inflation and deflation, noting that for the worker, deflation is much worse: “Labour is in a better position to protect itself from over-exertion in good times (in an inflationary environment) than from underemployment in bad times” (Keynes; 1923:39). This truism is grasped rather fully by COSATU in its approach to monetary policy over the last decade, much better than it was by Frederick Creswell representing the Labour Party in the mid-1920s. Keynes ends the discussion of inflation and deflation on a pro-development note: “Thus inflation is unjust and deflation is inexpedient. Of the two perhaps deflation is, if we rule out exaggerated inflations such as that of Germany, the worst; because it is worse, in an impoverished world, to provoke unemployment than to disappoint the rentier” (Keynes; 1923:40).

Later in the *Tract*, Keynes points out that, in order to re-establish the Gold Standard, countries had a choice of devaluation of their currency from the pre-war period so that their weaker currencies would be the new point of entry into an international Gold Standard. “Stabilisation at the existing level has been recommended by international conferences; and the actual value of many currencies tends to fall rather than to rise” (Keynes; 1923:142-143). He does not say too much further about devaluation as an option, but spends the rest of this section of chapter four showing the damage done by the deflation of prices so as to maintain a relatively strong currency. Many countries were motivated, as is so often the case in the world, including today, by some nebulous and naïve idea that a strong currency is some sort of indication of prowess and a source of national pride. He shows that Mussolini was caught up in this testosterone-fuelled hubris in seeking to deflate prices so as to re-establish the lira at an artificially high level: “Fortunately for the Italian tax payer and Italian business, the lira does not listen even to a dictator and cannot be given castor oil” (Keynes; 1923:145). Keynes brilliantly parodies Mussolini’s approach: “My policy is to halve wages, double the burden of the national debt, and to reduce by fifty percent the prices which Sicily can get for her exports of oranges and lemons” (Keynes; 1923:146).

Keynes then goes through the main arguments for re-establishing the value of the national currency at its previously stronger (higher) level, picking holes in each argument. We are shown the fallacy of the idea that it would be a breach of honour to do an injustice to the rentier class by devaluation, when Keynes points out that, by not committing this breach and allowing devaluation, is to do an injustice to entrepreneurs and employment in the real economy. He shows that arguments in favour of artificially inflating the currency to give the country financial prestige in order to build future confidence involves “pinning ourselves ‘in the past’” (Keynes; 1923:150). The third argument was one which seduced Frederick Creswell of the Labour Party, but of which Keynes is particularly forceful in his rebuttal. This is the idea that “if the gold value of a country’s currency can be increased, labour will profit by a reduced cost of living, (and) foreign goods will be obtainable cheaper” (Keynes; 1923:151). Keynes points out that the cost of this fool’s paradise is that “exports, which pay for the imports, will, measured in francs, fall in value just as much as the imports” (Keynes; 1923:151).

In concluding this section on the relative merits of deflation or devaluation, Keynes chooses Gibbon, the author of the multi-volume set *The Decline and Fall of the Roman Empire*, which graced the homes of “all respectable” Victorians, to represent the then erroneous conventional wisdom. He chooses the genius Jewish stockbroker, and hence outsider, David Ricardo, to represent the meritorious position, not popular at the time. “Gibbon deems incredible a story of how in AD 274 Aurelian’s deflationary zeal to restore the integrity of the coin excited an insurrection which caused the death of 7000 soldiers”. By contrast to this foolish view, which he puts in the mouth of a great Victorian icon, Keynes chooses the genius outsider to present the wise advice, with Ricardo noting that with the pound devalued in 1813, “it would have been as well to fix the currency at the then value, according to which most of the existing contracts had been made” (Keynes; 1923:154).

#### **4.9 Interest Rate Policy**

Interest rate policy is probably the most used tool of central banks. Aside from discussing higher interest rates at different times in the agricultural cycle, and some comments on the efficiencies of using the money market, rather than keeping reserves in gold, interest rate theory is not dominant in *ICF*, and is left to Keynes’ later work. Hirai (2007:44) looks at the comparisons between the *Tract* and the *Treatise*, noting that “the most conspicuous difference between the two texts lie in the position of the rate of interest. In the *Tract* it plays a marginal role, in the *Treatise* a central role”.

In the *Treatise*, Keynes establishes the cause of disequilibria as the difference between investment and savings, and having established investment as the volatile function and the banking system as the saviour to correct it, Keynes now develops the argument for the rate of interest being fundamental to establishing this equilibrium. “The attractiveness of investment depends on the prospective income which the entrepreneur anticipates from current investment relative to the rate of interest which he has to pay in order to be able to finance its production... That is to say the higher the rate of interest, the lower, ... will be the value of capital goods” (Keynes; 1930:154). Taking Wicksell’s lead, Keynes defines the natural rate of interest as “the

rate at which saving and the value of investment are exactly balanced... (with) every departure of the market rate from the natural rate tends ... to set up a disturbance of the price level” (Keynes; 1930:155).

Keynes shows the power which the rate of interest exercises over the capitalisation rate of new capital assets. “Upon what does the demand price of capital goods depend? It depends on two things – on the estimated net prospective yield from fixed capital..., and on the rate of interest at which this future yield is capitalized. It follows that the price of such goods can change for either of two reasons – because the prospective yield has changed or because the rate of interest has changed” (Keynes; 1930:202).

In the final chapter of the *Treatise*, dealing with international disequilibrium, Keynes notes the important role that the central bank has to play in correcting this disequilibrium and particularly in looking after its real economy in the process. He notes the same criterion which Eichengreen (1992) picked up with the value of hindsight, namely that “the central bank, whose policy is most independent of the policy of the other (central banks), and keeps its market rate nearest to its natural rate throughout the transition, will suffer least absolute change in its rate of earnings” (Keynes; 1930:337).

In dealing with the propensity to consume, Keynes is dismissive of the rate of interest having a powerful effect. “There are not many people who will alter their way of living because the rate of interest has fallen from 5 to 4 percent, if their aggregate income is the same as before” (Keynes; 1936:94). Its most powerful role is that of influencing investment.

However the investment market’s permanently very low interest rates may themselves create instability in the system. In the *General Theory*, it is recommended to drive down interest rates so as to improve the marginal efficiency of capital. Having learnt from the errors of the period 1919 – 1936, current central bankers have achieved laudable degrees of co-ordinated effort to drive down interest rates in an attempt to stimulate investment and alleviate the financial crisis which commenced with the collapse of Lehman Brothers in 2008. This concerted effort was preceded by a similarly determined effort to ignore the dual mandate of the Federal Reserve and follow the single mandate of price stability, as enshrined in the mandate to the South African

Reserve Bank and detailed in the 1996 South African constitution. This fixation with price stability, achieved by rigorous inflation targeting regimes throughout the world, preceded the current low interest rate regimes connected to the Lehman Brothers crisis, but achieved the same aim of low interest rates and related low capitalisation rates.

And yet, although Minsky (1975: 1986) fails to highlight it, we would suggest that the very low capitalisation rates on financial assets intimately connected to a low inflation and low interest rate environment is in itself a source of instability. If, as Keynes suggested, capitalisation rates on financial assets (including property) are closely connected with interest rates, then a modest move in the interest rate of, say, half a percent, has a much greater effect on a financial asset with a capitalisation rate of 2% than it would on the same financial asset with a capitalisation rate of 6%. If interest rates and capitalisation rates connected to them rise by, say, half a percent, the price of the financial asset in the first case would fall by 20%, whereas in the second instance, it would only fall by 9.31% percent. Also, a low interest rate environment is invariably easier to achieve and maintain with a low inflationary environment. In the first case, say the inflation rate is 1%, given that the financing of capital assets is denominated in nominal values, not real values, the devastating effect on the balance sheets of financial institutions of a 19% fall in the value of capital assets (20% real fall in asset prices minus 1% inflation), as detailed above, wreaks much worse havoc on the financial system than a 9.31% decrease in real values which, as a result of a moderate inflation rate, of, say 5%, means that nominal values of capital assets decrease by a modest 4.31% (9.31% real decrease in asset prices minus 5% inflation). In the second scenario, the balance sheets of the banks remain relatively healthy and the economy is spared the agony of a large debt deflation, which is mandatory in the first scenario. This is not to suggest that high inflation rates, those possibly above 10% and definitely above 20%, are not harmful to an economy. And yet, the evidence does not support the Washington consensus, inflation-targeting mantra that all inflation is evil. Given the above, Keynes' remedy of the euthanasia of the rentier, driving down interest rates to extremely low levels, which would only be really practical in an environment of extremely low inflation, seems less exciting an idea now as it may have done then. Indeed, Keynes' obsession with stabilising the economy through the stabilisation of the investment function, a laudable one both then and now, does not seem to flow naturally from driving down interest rates to as close to zero as possible. I would argue that a monetary environment of extremely low inflation and concomitant low interest rates creates a

situation, through the capitalisation of income process, whereby the much higher swings in the nominal value of capital assets create a destabilising influence on an economy with a debt financing system.

#### **4.10 Conclusion**

As this chapter makes clear, unlike the previous period from 1875 – 1914, when the orthodoxy went largely unchallenged, during the period in question, Keynes was an important part of developing an alternative to orthodox “sound money”, or Gold Standard theory. In the period before 1919-1936, the orthodoxy could allow itself to be lulled into confusing co-incidence with causation; given that economic prosperity and the Quantity Theory and Gold Standard subsisted side by side. As this dissertation seeks to show, particularly in chapters 2, 3, and 5, with minor exceptions, most of the participants in the monetary policy debates in South Africa in the period 1919 – 1936 took one or another theoretical position or variants thereof discussed in this chapter. Regardless of these vested interests, when the “sound money” edifice of the international Gold Standard began to crumble, all involved had to face the shortcomings of the prevailing orthodoxy: the Gold Standard and supposed specie-flow mechanism did not work. South Africa endured deflation in the period 1919 -1936, and hence the anti-inflationary virtues of the “sound money” Gold Standard was of little value, arguably even counter-productive.

Keynes’ (1923) warning about focusing on internal balance was ignored by the Pact government, and as a result, South African agriculture suffered in the period 1930- 1933. His ideas about a currency being competitive in order to serve the real economy and the need to support and regulate the banking sector (as the SARB did in 1931, see pages 153 - 154) runs like a golden thread through the narrative of monetary history of South Africa from 1919 – 1936. It is to this exercise – the interplay of ideas and power in the real world context – that I now turn in the main empirical chapter.

**CHAPTER FIVE**  
**A STORY OF THE EXPERTS AND THE INFLUENCE OF POWER – HENRY STRAKOSCH, EDWIN KEMMERER, GERHARD VISSERING AND THE SHADOW OF JOHN MAYNARD KEYNES**

Technical experts, including professional and academic economists, played a critical role in policy making in British colonies and territories as Timothy Mitchell brilliantly illustrates in the case of Egypt in his book *Rule of Experts: Egypt, techno-politics and modernity* (2002). That this was true also for South Africa in the early decades of the 20<sup>th</sup> century in so far as banking and monetary matters are concerned is clearly illustrated in the following extracts from the letters of the Chairman of Crown Mines, Samuel Evans, in 1921. The context is that the Secretary of Finance, Farrer, writes to Samuel Evans on the 29th of September 1921 "the government has decided to convene a conference to consider and report upon the following matters: 'whether the provisions of sub-section 3 of the Currency and Banking Act, 1920 (whereby the inconvertibility of gold certificates terminates on the 30th of June 1923) should be carried into effect or amended so as to extend the period of inconvertibility'".

Evans writes to Professor Edwin Cannan on the 5th of October 1921 enclosing Farrer's letter and the Memorandum attached to it and notes that, as far as the "experts" to be called by the government,

I'm afraid they mean Sir Henry Strakosch and perhaps Doctor Vissering, President of the Netherlands Bank. I understand from some of my Dutch friends that Doctor Vissering has been subject to a great deal of criticism in Holland. Doctor Van Dorp, in a letter which I have just received, writes that 'Doctor Vissering is not an economist at all... and like all practical men he abuses theory, but has quite a car load of theories himself. His writings on currency were from the beginning "combated by the real economists (Professor Van Gyn, former Minister of Finance, Professor Verriijn-Stewart, Professor Bordewyk, and Mr. Mees)'. I sent Doctor Vissering copies of my speech at the last annual meeting of the Crown Mines and of my paper on "The Gold Premium" and the reply to the discussion on that paper. He wrote to me an appreciative letter of thanks of some length, in which he

said that, whilst agreeing with much of what I had written, for a not unimportant part he still remained on the side of the practical man.... The Minister of Finance may possibly be thinking of Keynes as one of the expert advisors who is to be invited to come here. As far as I have seen neither Keynes nor Strakosch ever attempted to reply to your article on the South African currency in 'The Economic Journal' of December 1920.<sup>20</sup>

Who was in favour and who out of favour, was decided not so much by educational competencies, but rather by where the expert stood on key issues, and who he was connected to in power and authority.

When looking at the ideas that influenced monetary policy in South Africa in the period 1919-1936, two financial experts stand out for their enormous contribution – Sir Henry Strakosch, referred to in the above correspondence, and the American Professor Edwin Kemmerer. The Dutch economist Gerhard Vissering, while engaged with the South African debate, as a representative of a weaker and “neutral” country, did not find himself representing the powerful interests that Strakosch and Kemmerer did, and hence his role was less forceful. As a “neutral” he does however provide a fascinating insight into what transpired during and after the work of the commission.

What follows is an investigation into how these experts came to be the men that they were. In so doing we also undertake a comparison with the man responsible for our theoretical paradigm, John Maynard Keynes, the dominant academic and policy economist of this seminal era. In retrospect, all three experts operated in the shadow of Keynes, both when they agreed with his views and when they differed, making an examination of Keynes, the man, and Keynes the economist an essential component of our study. Later, we will be concerning ourselves with the central questions of ideas and power – how much of what our two highly influential men (Strakosch and Kemmerer) recommended as policy was in line with the theory which they held and how much of it was driven by the political imperatives of the power elites in London and New York/ Washington respectively. In conclusion we assess how the ideas, generated in these

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<sup>20</sup> Samuel Evans Papers, Barloworld archives - Box entitled “Politics 1899-1949, Reform Committee, 1895, Reform Committee, Relief Funds – mainly press cuttings and shorthand notes on gold”.

metropolises, made themselves felt on South African monetary policy and central banking developments.

The environment (the “world”) in which our protagonists were formed and that in which they operated as “experts”, paints a powerful picture of how they came to be the people that they were, and how they came to hold the views that they did. This is a role for good history to serve. In its absence the reader might wonder why they did not think or act differently. A good historical account shows why a much smaller number of paths were likely to be chosen from the many that were available.

## 5.1 Keynes and his World

John Maynard Keynes was born into a family of intellectual aristocracy, with his father being an academic at Cambridge and his mother becoming the first woman mayor of its municipality. While he was brought up in a Christian home, by the time he had settled into his group of friends at Cambridge University they

used to regard the Christians as the enemy, because they appeared as the representatives of tradition, convention and hocus-pocus. In truth it was the Benthamite calculus, based on an over-valuation of the economic criterion, which was destroying the quality of the popular ideal. Moreover it was this escape from Bentham, joined with the unsurpassable individualism of our philosophy, which had served to protect the whole lot of us from the final *reductio ad absurdum* of Benthamism known as Marxism (Keynes, 1949<sup>21</sup>: 96 - 97).

Unlike Kemmerer, whose background is dealt with later, Keynes’ predisposition to reject the marginal utility mechanism developed by classical economists, including Marshall and Pigou, can be traced to his rejection of the utilitarianism developed by the English philosopher, Jeremy

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<sup>21</sup> Although Keynes died in 1946, his friend, David “Bunny” Garnett, arranged for the publication of two memoirs (which were written by Keynes prior to his death and read to a small audience) in 1949, and hence three years after Keynes’ death. The first memoir is entitled “Doctor Melchior: A Defeated Enemy” and the second memoir is entitled “My Early Beliefs”.

Bentham. Bentham's hedonistic calculus can be seen as the building block on which the calculation of utility, using agency, is based.

As someone working comfortably within the class of the educated bourgeoisie into which he was born, Keynes eschewed ideals of "self-reliance", "the will and the way" and other mechanisms of self-advancement popular with Kemmerer and his peers. Keynes befriended the likes of the author of *In Praise of Idleness* (Bertrand Russell) and enjoyed the company of Bloomsbury artists, whose interpretation of their philosophical guru, G.E. Moore, involved relationships which were not utilitarian in the Benthamite or social Darwinist sense of the word. In describing the "new religion" of Keynes and his friends, based on the writings of G.E. Moore, Keynes says that "Broadly speaking, we all knew for certain what were good states of mind and that they consisted in communion with objects of love, beauty and truth. I have called this faith a religion, and some sort of relation of neo-Platonism it surely was" (Keynes; 1949: 86). Keynes describes his religion as "altogether unworldly – with wealth, power, popularity or success it had no concern whatsoever, they were thoroughly despised." (Keynes; 1949: 84). He says of his group that "Another compelling objective was 'important', provided it was quite clear that 'important' did not mean 'useful'" (Keynes; 1949: 88).

## **5.2 Keynes, Race and Sex**

To ignore major elements of Keynes's private life, however, as does his first major biographer, Roy Harrod -particularly Keynes's homosexuality, despite its featuring in nearly two decades of passionate and poignant personal correspondence from the early 1900s- is to underplay the importance of Keynes's associations outside official college and government circles, in particular with members of the Cambridge "Apostles" male secret society and the iconoclastic Bloomsbury group of London intellectuals and aesthetes. Keynes would famously write of the Apostles "We were....in the strict sense of the term, immoralists," by which he meant willing to break with conventions in pursuit of worthy public motives. Keynes's personal attachments had an undeniable impact on his ethical worldview and the sharp-edged rhetorical habits he practiced in official settings (Steil; 2013:63).

Chandavarkar (2009), Paulovicova (2007), Skidelsky (1992) and others have noted that Keynes enjoyed being provocative and shocking in his speech. “Words ought to be a little wild, for they are the assault of thought on the unthinking” (*The New Statesman* 15<sup>th</sup> July 1933). This shows up in Keynes’ mostly casual racial prejudices, which were typical of his class and time. Given the importance of race in South Africa in our period (1919-1936) we consider it useful to briefly address here Keynes’ controversial, though somewhat misunderstood, views on race.

Chandavarkar (2009: 144-159) and others deals at length with Keynes’ anti-Semitism, starting with his Etonian essay in 1900 in which he speaks disparagingly of the “characteristics of two oriental races... the Chinese and the Jews” (Keynes quoted in Chandavarkar; 2009: 146). Chandavarkar (2009) comes to the conclusion that, while there are plenty of examples of anti-Semitic comments in Keynes’ writings, on balance, and given his pro-Semitic writings and activities, it would not be fair to label Keynes as anti-Semitic.

Perhaps the final word on this subject should go to Keynes’ beautiful piece in the *New Statesman* on the 21<sup>st</sup> of October 1933, shortly after the publication of Albert Einstein’s *Special Theory of Relativity*. Its length might initially be off-putting, but it expresses in the most poetic way Keynes’ feeling for, and identification with, the outsider:

It is so indeed. The boys who cannot grow up to adult human nature are beating the prophets of the ancient race – Marx, Freud, Einstein – who have been tearing at our social, personal and intelligent roots... What traditional retort have the schoolboys but a kick in the pants?

Thus to our generation Einstein has been made to become a double symbol – a symbol of the mind traveling in the cold regions of space, and a symbol of the brave and generous outcast, pure in heart and cheerful in spirit. Himself a schoolboy, too, but the other kind – with ruffled hair, soft hands and a violin. See him as he squats on Cromer beach doing sums, Charlie Chaplin with the brow of Shakespeare...So it is not an accident that the

Nazi lads vent a particular fury against him. He does truly stand for what they most dislike, the opposite of the blond beast – intellectualist, individualist, super-nationalist, pacifist, inky, plump...How should they know the glory of the free-ranging intellect and soft objective sympathy and smiling innocence of heart, to which power and money and violence, drink and blood and pomp, mean absolutely nothing?

Yet Albert and the blond beast make up the world between them. If either cast the other out, life is diminished in its force. When the barbarians destroy the ancient race as witches, when they refuse to scale heaven on broomsticks, they may be dooming themselves to sink back into the clods which bore them (Keynes quoted in Skidelsky; 1996: 486).

Another marker of potential racism is Keynes' enthusiasm for eugenics. Keynes served as Director of the (British) Eugenics Society from 1937 until 1944. Keynes' only article in the *Eugenics Review* is one on population, which has nothing at all to say about racial purity, but is rather an analysis of the demand for capital in a country with a declining population and a look at interest rate policy to respond to this challenge. (*Eugenics Review*, 1937, Volume 30 (1), pages 13-17).

By his own admission, Malthus was one of, if not the, most important intellectual influences on Keynes, and Malthus' *Essay on The Principal of Population, As It Affects the Future Improvements of Society* (1798) had placed population growth as the foremost concern of many intellectuals, particularly economists, since it was published in 1798, including John Stuart Mill, Knut Wicksell and others. In an investigation on Keynes' writings on population, John Toye (2000) highlights Keynes' racism and points out that, regardless of Keynes' stature, the racist views that he expressed were not acceptable. As South Africans, we are acutely aware of the evils of racism and Toye (2000), while uncomfortable reading for an admirer of John Maynard Keynes, is an important work of scholarship in its exploration and condemnation of Keynes' racism. That said, a case could be made for Keynes' neo-Malthusian views being, not an end in itself, but a tool in support of his passionate advocacy for the legalisation of birth control, particularly in Britain.

Toye himself hints that this is the real motivator for Keynes' sometimes unpalatable views on population pointing out that Keynes believed that birth control safeguarded the economic standard of living, without which the social psychology of Moorean moral idealism could be undermined (Toye; 2000:40). Keynes asks "What is the use or purpose of all our strivings if they are to be neutralised or defeated by the mere growth of numbers? Malthus' devil... is a terrible devil because he undermines our faith in the real value of our social purpose" (The Collected Works of John Maynard Keynes; xix 122).

The motivations for fewer children would have fitted in well with the values and lifestyles of the Bloomsbury group of which Keynes was a member. Keynes discarded his neo-Malthusian advocacy after 1930, which Toye acknowledges was connected to "the approaching political victory for the advocates of birth control" (Toye; 2000 186). Keynes' obsession with birth control, connected to his view of some progressive notion of civilization, can be understood in the context of his rejection of superstition-based religious belief. If the church-based ban on birth control was abolished, it would have left the women he knew and cared about free to pursue art, literature, meaningful friendships and knowledge. We would argue that this notion of a progressive, humanist new world is central to Keynes' action in the political sphere, in support of women's rights, birth control, a secular society and a protection of "that degree of civilization which we have thus far attained" (Keynes, *Essays in Persuasion*; 1963: 323).

In this way, ironically, Keynes' racism, as seen in some of his writings on population, can be viewed as a tool in support of a progressive social agenda, which was his real motive. A similar line of thought, relating to an unacceptable view on race given in support of another cause, is contained in Loewen (1995) when he notes that the most often quoted passage in American history textbooks on Lincoln's views on slavery is contained in his letter to the *New York Tribune* dated the 22<sup>nd</sup> of August 1862: which included the statement "If I could save the Union without freeing any slave, I would do it" (Loewen; 1995: 181). Loewen goes on to show that, while this speech illustrates a political expediency which Lincoln clearly did possess, without the many other evidences of Lincoln's hatred of slavery, it paints a completely incorrect picture of

his personal motive. We would suggest that, judging Keynes as a whole, and taking all of his other influences into account, this is also true of John Maynard Keynes.

Keynes' sexual orientation provided a cause for identification with outsiders. He was homosexual for the first part of his life, with his lover, the painter Duncan Grant, set to inherit a large chunk of his substantial estate. He later married the ballerina, Lydia Lopokova and, by all accounts, had a successful heterosexual marriage during the second period (Skidelsky 1985; and 1992). Robert Skidelsky comments that "no one who has read Keynes' correspondence with Lytton Strachey or Duncan Grant can doubt that homosexuality for him was not just a sexual preference, but part of the good life as he then defined it" (Skidelsky; 1983: xvii).

We choose, in this dissertation, to raise questions about the homosexuality of Keynes and the probable homosexuality of Henry Strakosch, his friend and business associate, Brendan Bracken (the personal and political confidante of Winston Churchill), and Gerhard Vissering, not because it is ubiquitously important, but because it may sometimes be significant in understanding the way that Keynes attempted to influence ideas and policy in shaping the world of his time. Previous academics' failure to deal with the homosexuality of their subjects is often less because of a carefully thought through position that their sexual orientation was unimportant, and rather because of their discomfort with this subject, even although it is 43 years since the Stonewall Riots. A case in point is Anand Chandavarkar (1989: 171) who deals sensitively and intelligently with issues of racism and anti-Semitism, however is uncomfortable with Skidelsky's description of John Maynard Keynes' relationship with the Indian student Bimla Sarkar.

Chandavarkar, who sets out Keynes' affection for Indian students, including his speaking at the annual dinner of the Indian Majlis (the Society of Indian Students at Cambridge and Oxford University) in February 1911 and later (Chandavarkar; 1989: 150), and the affectionate assistance which he gave to various Indian students, seems to have difficulty with the possibility that some of this affection might have been rooted in a sexual attraction. He uses the word "grotesque" to criticize connections that Skidelsky (1983) has made. By contrast, in another context, Edward Said speaks approvingly of Jean Genet's homosexual sexual attraction towards Palestinians and other Arabs as part of Genet's reason for identification with the Arab nationalist

and Palestinian causes (Said; 2006: 80 – 90). As Fanon (1952) shows, sexual attraction for the “other” can be a form and extension of dominance and oppression; however Said argues that this was not the case in relation Jean Genet and the Palestinians, and clearly it was not the case with Keynes and Indians.

An illustration of sexual attraction, and its effects on other elements of personality, which may in turn affect policy, is to compare John Maynard Keynes with Sebastian Sprott. In the period after the break-up of his very serious relationship with Duncan Grant in 1911, Keynes was content to keep his romantic life superficial, and Sebastian Sprott fitted the bill perfectly. “From October 1920, Keynes was considered by Bloomsbury to be ‘married’ to Sprott” (Skidelsky; 1992: 35). Sprott, notwithstanding his affair with John Maynard Keynes, was mainly attracted to working-class youths. “When he went to Nottingham University in 1925 as a lecturer in psychology, he dropped the Bloomsbury ‘Sebastian’ for the more proletarian ‘Jack’, and used discharged prisoners as domestic helpers in his grim Victorian terraced house” (Skidelsky; 1992: 36).

By contrast, “Keynes never shared his taste for the low life. He refused to idolize the working class, British or German. He worshipped artists, not toughs. His ideal universe never included working class ‘mates’ – something which distanced him from those who approached their socialism by this route” (Skidelsky; 1992: 36). It is therefore easy to see how John Maynard Keynes’ sexual attraction for artists rather than “toughs” supported his political affiliation with the Liberal Party, rather than him making the transition to the Labour Party.

We would argue that Keynes’ sexuality was to his outlook what Veblen’s immigrant background was to his. Thorstein Veblen was, after Karl Marx, one of the most important critics of mainstream economics, challenging basic assumptions of Marshall’s Laws of Demand, namely the downward sloping demand curve. Buchholz (1989: 177 – 178) notes that “commentators almost always link Veblen’s critical attitude to his family’s impoverished immigrant status. ...The pariah theory argues that Veblen’s outsider status gave him a unique and unbiased view of American economic life. He could see the cracks in the foundation of Capitalism because his eyes pierced through the façade. Veblen himself employed a similar hypothesis in his essay ‘The Intellectual Pre-Eminence of Jews in Modern Europe’”.

### 5.3 Strakosch's World

While the case for Keynes' "outsider thinking" is thick with evidence as detailed above, the background of Sir Henry Strakosch is not as well researched, archival material is limited, and hence inferences are more difficult. Certainly transferring himself into a British Imperialist world from the Teutonic, and possibly genealogically Jewish, world of his birth, would have required great powers of flexible thinking.

Henry Edouard Strakosch was born at Hohenau in Austria, close to the border with Moravia, on the 9<sup>th</sup> of May 1871, the second son of Edouard Strakosch, an Austrian sugar manufacturer and his wife, Mathilde Winterburg. After starting his education at the Wasa Gymnasium in Vienna he was educated "privately in England"<sup>22</sup>. Strakosch joined the Anglo -Austrian Bank in 1889. In 1891 he was transferred to the foreign exchange department of the bank's London branch. He went to South Africa in 1895 as a representative of the African Mining and Financial association, an organization formed by several prominent European financiers. In 1896, another European, Adolf Goerz, invited him to join A Goerz and Company, a mining and finance house in which his brother Fred W Strakosch also found employment. After the death of Adolf Goerz in 1900 Strakosch went to London as manager while Fred was sent to Paris. Henry Strakosch became managing director in 1902.

The Oxford Dictionary of National Biography notes that "despite his involvement with South Africa, Strakosch visited the country only twice after 1901"<sup>23</sup>, an extraordinary testimony to the importance of London in the economic affairs of South Africa at the time. Strakosch became a British citizen via naturalization in 1907 and survived the purging of the Board of Directors of Goerz and Co., (the Union Corporation as it became known after 1918), of the other Teutonic members after the outbreak of the First World War in 1914. This is all the more remarkable as Lionel Phillips notes with sadness, regarding Germanic Board members, how "Whether they

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<sup>22</sup> Oxford Dictionary of National Biography, 2004.

<sup>23</sup> Oxford Dictionary of National Biography, 2004.

were naturalized British subjects or not, the ban became general. They were all regarded as potential spies. Years of residence and good conduct made no difference. Popular clamour and the atmosphere of suspicion, coupled with the early victories of their countrymen, rendered life exceedingly unpleasant for them, and many businesses that were owned or administrated by them were wound up. Several members of the Board of Central Mining were of German origin, and it became my painful duty to secure their resignation to avert the danger of the enterprise being condemned or liquidated". (Phillips; 1924:161) Given the fate of these other Germanic directors, Strakosch's talent for finding himself on the right side of a shifting power elite is remarkable.

That he was trusted with advancing British interests goes some way in explaining his survival as a director of a German Investment company, despite his Austrian birth. Sayers (1976: 202) notes that "in the first year of Montagu Norman's Governorship (from 1920), Strakosch's name alone appears in Norman's diary forty six times, and he accompanied others more than twenty times."

Wanting to team up with Keynes, Strakosch wrote to Charles Seligman of Seligman and Brothers on the 3<sup>rd</sup> of July 1919, "I send you herewith a copy of my memorandum on gold and foreign exchange. I need not repeat how grateful I should be if you would arrange for me to meet Professor Keynes."<sup>24</sup> On the 14<sup>th</sup> of August 1919, Strakosch wrote to Keynes, indicating that they had already now discussed the proposed gold marketing organization, "our conversations of the other day has fortified me very considerably in the belief that it is right to pursue the matter further". John Maynard Keynes had agreed to meet him in London and so Strakosch wrote "May I further trespass upon your good nature by suggesting that you postpone your return to the country until the following day. I should be so glad to put you up here and would try to make you comfortable in my bachelor's establishment. It would give me an opportunity to arrange for Leon Ruef<sup>25</sup> to dine with us that night and to continue our conversation with him."<sup>26</sup>

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<sup>24</sup> Keynes Papers, Kings College Cambridge, L/St/1

<sup>25</sup> Strakosch misspells his name. Jacques Leon Rueff was, amongst other things, financial advisor to the French Embassy in London at the time (Chivvis 2006:703-704)

<sup>26</sup> Keynes Papers, Kings College Cambridge, L/St/24-25

On the 15<sup>th</sup> of August 1919, Strakosch wrote to Keynes regarding the mechanism of the organization and concluded that he was “looking forward to seeing you on Wednesday next”. In September 1919, Strakosch wrote

Will you please let me have your views. The most convenient way of settling things would be for you to come up to town if you can possibly manage it and apart from being able to arrange matters at great ease, it would give me an opportunity of arranging a dinner with the H.C. Hull [sic], an old friend of mine, who was the first Minister of Finance of the Union of South Africa, and who is on intimate terms with General Smuts, and whom you may be interested to meet. I should of course be very glad if you would again stay with me at 45 Chester Square<sup>27</sup>

an invitation repeated in many of Strakosch’s letters to Keynes.

Boyle (1967) notes how Montagu Norman relied on Henry Strakosch to provide intelligence about the Austrian banking system in the twenties (Boyle; 1967: 205). On the 24<sup>th</sup> of June 1931, Strakosch writes to Winston Churchill informing him “how greatly I enjoyed our talk last night, and I much hope that other opportunities may present themselves for further talks”.<sup>28</sup> On the 9<sup>th</sup> of September 1931, Strakosch writes to Churchill enclosing a “copy of the chart of which I spoke to you at lunch today” relating to gold movements.<sup>29</sup> On the 28<sup>th</sup> of December 1931 Winston Churchill requests advice from Strakosch on the state of the Gold Standard and related issues to which Strakosch responds with an eight page précis.<sup>30</sup> On the 1<sup>st</sup> of November 1935, in response to a request from Churchill, Strakosch prepares for Churchill an analysis of German government debt, the importation of materials necessary for the manufacturing of armaments, and related figures to prove that German rearmament is taking place on a much greater scale than Nazi Germany was admitting.<sup>31</sup> Churchill responds, thanking him for “such a weighty, lucid paper”.<sup>32</sup> He asks for permission to forward Strakosch’s paper to a third party and Strakosch gives consent,

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<sup>27</sup> Keynes Papers, Kings College Cambridge, L/St/58-67

<sup>28</sup> Winston Churchill papers CHAR2/ 178/ 8

<sup>29</sup> Winston Churchill papers CHAR2/ 178/ 11

<sup>30</sup> Winston Churchill papers CHAR1/ 400A/ 86 and CHAR2/ 186/ 1-8

<sup>31</sup> Winston Churchill papers CHAR2/ 244/ 53-59

<sup>32</sup> Winston Churchill papers CHAR2/ 244/ 48

stating in his letter of the 4<sup>th</sup> of November 1935 that “I have no objection to your sending the note on German armaments to Chatham House Information Department, but I should not like you to disclose the source”.<sup>33</sup>

Strakosch’s paper was sent to the Treasury for comment and the Treasury found his calculations to be too liberal, but agreed with Strakosch that substantially higher re-armament was taking place and that Germany’s public debt was substantially higher than admitted by the Third Reich government. On the 18<sup>th</sup> of January 1938, Brendan Bracken, Churchill’s closest confidante, writes to Churchill, informing him of Strakosch’s recovery from his serious illness and ending with “he is a lonely old bird and so I venture to suggest that you might ask him to lunch one day”.<sup>34</sup>

In 1937 Churchill, judging that the bear market on the New York Stock Exchange was over, invested heavily on Wall Street. Unluckily for him, Roosevelt decided to balance the budget after years of deficit spending. The market collapsed again early in 1938 leaving Churchill financially embarrassed. On the 7<sup>th</sup> of March 1938, Churchill writes to his bankers, asking them to “extend the overdraft until the middle of April by £500”.<sup>35</sup> In a calculation dated the 21<sup>st</sup> of March 1938, Churchill indicates a loss on New York Stock Exchange shares of £12 000.<sup>36</sup> Bracken approaches Strakosch to assist which he agrees to, suggesting that in a note dated the 29<sup>th</sup> of March 1938, that “it is suggested that the account should be taken over from Vickers Da Costa and be held for, say three years, with full discretion to sell or vary holdings at any time, but on the basis that no risk or liability to the present holder arises, thus removing altogether the speculative element. Interest will of course be paid”.<sup>37</sup> On the 19<sup>th</sup> of March 1938, Churchill writes to Brendan Bracken:

My dear Brendan, I was profoundly touched and relieved by what you told me last night of the kindness of our friend (Strakosch). If it were not for public affairs and my evident

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<sup>33</sup> Winston Churchill papers CHAR2/ 244/ 54

<sup>34</sup> Winston Churchill papers CHAR1/ 323/ 10

<sup>35</sup> Winston Churchill papers CHAR1/ 329/ 29

<sup>36</sup> Winston Churchill papers CHAR1/ 328/ 1-2

<sup>37</sup> Winston Churchill papers CHAR1/ 328/ 3

duty, I should be able to manage alright. I should indeed be grateful if I could be liberated during these next few critical years from this particular worry, which descended upon me so unexpectedly; to the chance of which I shall certainly never expose myself again. I cannot tell you what a relief it would be if I could put it out of my mind; and take the large decisions which perhaps may be required of me without this distraction and anxiety. I send you a short note which explains the position and perhaps you will show this to our friend (Strakosch)<sup>38</sup>.

The covering note says “My dear B, enclosed is a letter which you can show our friend (Strakosch). This is only to tell you that as Hitler said to Mussolini, on a recent and less worthy occasion ‘I shall never forget’ this inestimable service”.<sup>39</sup> On the 24<sup>th</sup> of March 1938, Strakosch writes to Churchill a hand-written letter “My dear Winston, I have today paid to Vickers Da Costa £18162.1.10, being the amount due to them by you and arrangements are being made for them to deliver to me the securities they are holding for you”, “as agreed between us, I shall carry this position for the three years, you giving me full discretion to sell or vary the holdings at any time, but on the understanding that you incur no further liability.”<sup>40</sup> A typed schedule of the securities dated the 10<sup>th</sup> of October 1938 shows that these shares had increased in value by £3 818.<sup>41</sup>

*The Age* newspaper of Melbourne, on the 7<sup>th</sup> of February 1944, reported on the will of Strakosch, who had died on the 30<sup>th</sup> of October 1943. It notes that “Mr. Churchill receives £20 000 under the will of Sir Henry Strakosch, one of Britain’s foremost financiers and an authority on currency and economics, who died last October, the estate is valued at £2 454 521, the largest since that of the tobacco magnate, Mr. W. M. Wills, who died in January 1941... Sir Henry Strakosch also left £10 000 to Marshall Smuts, £5 000 to Sir John Simon, Lord Chancellor, and £2 500 each to Mr. Brendan Bracken (British Minister of Information) and Sir Findlater Stewart, the Permanent Under-Secretary of State for India”. Even in death Strakosch was busying himself cementing the bonds between him and the power elite in Britain and their friends in South Africa.

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<sup>38</sup> Winston Churchill papers CHAR1/ 328/ 4

<sup>39</sup> Winston Churchill papers CHAR1/ 328/ 4

<sup>40</sup> Winston Churchill papers CHAR1/ 328/ 5

<sup>41</sup> Winston Churchill papers CHAR1/ 328/ 6

The Holocaust denialist and historian, David Irving, claims or insinuates that Strakosch popped up in Churchill's life in 1938 to rescue him from financial embarrassment and then wrote off the debt in his will and that this was some sort of inducement by the "Jewish" Strakosch to encourage Churchill to go to war with Nazi Germany. The anti-Semitism is so fantastical as to not merit a response, however, as shown above, Strakosch knew Churchill for many years prior to this loan. While Strakosch clearly did save Churchill from financial embarrassment in 1938, the research shows that the securities in question did in fact increase in value subsequent to them being taken over by Strakosch. What it does show is the extent to which Strakosch was prepared to go to make himself useful, including financially useful, to the British power elite.

Further indication of Strakosch's financial generosity to the power elite comes in the form of his letter to Jan Christiaan Smuts dated the 16<sup>th</sup> of April 1924, in which he writes "I gather that you have decided to go to a general election in June next. You will, I am sure, be needing party funds and I accordingly enclose a draft on the National Bank for £5 000 – which I trust may be of service in the great fight you are about to wage".<sup>42</sup> Smuts thanks Strakosch in his letter of the 7<sup>th</sup> of May 1924, "What a pleasant surprise it was this morning to receive your letter with the draft for £5 000 enclosed. It was like water in the dry desert. Thank you very much. You have been very good to me in all these recurrent crises, and I can only repay you in the pure, un-inflated coin of sincere gratitude".<sup>43</sup> Following financial assistance to fight yet another general election, Smuts writes to Strakosch on the 3<sup>rd</sup> of January 1938, "I wish to thank you most sincerely for the party cheque which Anderson handed me personally. It is most handsome and will be of material assistance in the coming elections. It is very good of you to continue these material tokens of your support and goodwill to us politically".

On the 21<sup>st</sup> of August 1941, Strakosch writes to Churchill thanking him for his congratulations on Strakosch's marriage (at the age of seventy), saying that "I appreciate more than I can say, that you should have found time to remember me, amidst all your preoccupations on your return from your meeting with Roosevelt, especially as I have already had a most charming letter from

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<sup>42</sup> Smuts private papers, Volume 30 (re-numbered Volume 214)/ 102

<sup>43</sup> Smuts private papers, Volume 30 (re-numbered Volume 214)/ 104

Mrs Churchill. As I told her, I am confident that our union will be a happy one. My wife's outlook on life and her tastes do not differ widely from my own and there is no great difference of age, all of which are factors making for understanding, contentment and happiness." There is a note from Mabel Strakosch dated the 3<sup>rd</sup> of March 1941 noting that "the nurse who is looking after Sir Henry Strakosch tells me that though he has been very ill indeed, he is a little better this morning, having had very much better night (sic)". A further note from "John", written from the House of Lords (probably cabinet minister John Simon who inherited £2 500 from Strakosch's estate) notes "My dear P.M. Kathleen and I gave your flowers to Henry Strakosch last night: he was much pleased and asked me to convey his thanks. We could only see him for a minute, for he is very ill". From this research, it is clear that Strakosch was very ill before his marriage to Mabel Elizabeth Vincent (the widow of Joseph Temperley, a ship owner) and before August 1942 when "Strakosch was diagnosed as suffering from cancer." "He died in his home, Heatherside, Walton-on-the-Hill, Banstead, Surrey on the 30<sup>th</sup> of October 1943." (Oxford Dictionary of National Biography, 2004). All of this reinforces the image of Henry Strakosch as a trusted servant of the British power elite.

#### **5.4 Strakosch and Keynes on forming a new gold selling organization**

Given this background, we are now ready to explore the influence that Strakosch and Keynes had over South African monetary matters. D.E. Moggridge (1992) records that Strakosch was a regular attendee of an intimate group of city monetary, banking and finance men known as the Tuesday Club. It met on the third Tuesday of every month at Café Royale to discuss economic and financial matters. "Amongst those elected in the first few years were Sir John Anderson, Basil Blackett, R.H. Brand, Sir Josiah Stamp, Walter Layton, Dennis Robinson and Sir Henry Strakosch, all of whom had or would play significant roles in Keynes' life." (Moggridge; 1992: 278). Given that two years were to pass before the formal letter which Strakosch wrote, on the 3<sup>rd</sup> of July 1919, asking to "meet Professor Keynes", one wonders whether they met each other in passing in the interim at the Tuesday Club.

At the time that Strakosch approached Keynes with his new scheme to sell all South African gold, all this gold passed through the Bank of England and was then sold by Rothschilds. This

was of great political significance, as Balachandran (1996), Ally (1994) and others have shown. It is a testimony to the boldness of both Strakosch and Keynes that Strakosch could conceive of a plan, and get Keynes' buy in, to attempt to wrestle control of the selling of gold from these bastions of British power. It is a testimony to the great standing of Strakosch and Keynes that they were not rendered *persona non grata* in attempting to bypass these two organizations and attempting to sell gold directly from South Africa to various destinations across the globe. Strakosch's bold scheme involved forming an organization which would in effect take over the then current arrangement to sell all South African gold, was contained in a letter to Keynes on the 25<sup>th</sup> of August 1919. It proposed that the two of them work on establishing a new "corporation, (which) by contract made in South Africa, contracts to buy all the gold produced by the contracting producers".

The gold which South African mining companies were forced to sell through London, fetched lower prices than it would if sold elsewhere. Strakosch's capitalized on the resentment caused by the previously lower sales price by suggesting that "the corporation in addition agrees to pay a premium corresponding to the premium on gold as expressed in the higher quotations for cable transfer on New York (as quoted in the "Times")... If the gold should be realized elsewhere to <sup>44</sup>be better advantage, the producers to be given the benefit of the better price so realised".<sup>45</sup> Strakosch goes on to suggest that the directors should be British subjects. "Two thirds to be appointed by the bank and its friends (of whom half to be persons not immediately connected with the bank) and one third by the gold mining interests".<sup>46</sup> He suggested that "It seems to me essential for it (the organisation) to accumulate strong reserves – both open and hidden. To do so it must be able to earn good profits. Hence my suggestion that the surplus profits should be divided in the ratio of one third to the gold producers and two thirds to the organisation".<sup>47</sup> Strakosch also proposed that the organisation end the then current practice of directing all of South African gold via London, and undertake that the organisation would take advantage of higher gold prices elsewhere in the world to sell and ship gold directly from South Africa to these other venues.

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<sup>44</sup> Keynes Papers, Kings College, Cambridge, File L/ST/ 26 and L/ST/28

<sup>45</sup> Keynes Papers, Kings College, Cambridge, File L/ST/ 26 and L/ST/28

<sup>46</sup> Keynes Papers, Kings College, Cambridge, File L/ST/30

<sup>47</sup> Keynes Papers, Kings College, Cambridge, File L/ST/26

Keynes' involvement in discussing the possible selling organization of South African gold with Strakosch so actively in this period is all the more remarkable considering that Keynes was hard at work in this period finishing his *Economic Consequences of the Peace*. "On 3 September he informed his mother that he had 'managed to keep up my average of 1000 words to fit for the printer every day, seven days a week; but there are still some very difficult bits to do. I hope to finish by the first week in October and have it actually published before the last day of the month". "By 23 September he had sent off the first five chapters to R and R Clark, MacMillan's Edinburgh printer, to be set up in galleys" (Skidelsky; 1983: 380 – 381). "By the 11<sup>th</sup> of October Keynes had sent off chapter 6 and the greater part of chapter 7" (Skidelsky; 1983: 382).

Regardless of the context of the regular meetings and correspondence between Henry Strakosch and John Maynard Keynes in the period June 1919 to December 1919, including Strakosch's numerous handwritten postscripts inviting Keynes to sleep over in order to discuss the plan, what is evident from our research is that both Henry Strakosch and John Maynard Keynes were treated seriously by authorities, the Bank of England, the British Treasury and the South African Government, and that they enjoyed the trust and confidence of the leadership of all three institutions.

Although John Maynard Keynes' economic theories later came to be viewed with suspicion by the Bank of England, Montagu Norman could not have been oblivious to the fact that Keynes enjoyed considerable standing amongst the power elite in the British Government. In the year that Montagu Norman became Deputy Governor of the Bank of England, 1917, the then Governor, Walter Cunliffe, was about to lose his job as a result of a run in with John Maynard Keynes and his colleague at the Treasury. "On the 3<sup>rd</sup> of July 1917, Cunliffe complained to Bonar Law (the Tory Chancellor of the Exchequer to whom Keynes reported during the war) that Chalmers (a colleague of Keynes) and Keynes were between them reducing his Exchange Committee to a 'cypher' by withholding from it information and assets. In retaliation he gave instructions to withhold the Bank's gold at Ottawa from Sir Hardman Lever in New York. He also demanded that Chalmers and Keynes be dismissed. Bonar Law retaliated by forcing the resignation of the megalomaniac Governor (Cunliffe)" (Skidelsky; 1983: 341).

At this point in our narrative, I would like to suggest a correction to the received wisdom on the role of John Maynard Keynes and Henry Strakosch in how monetary policy in the period 1919 – 1924 was decided. Much of this “conventional wisdom” comes from two outstanding sources, namely Parsons’ *Keynes and South Africa* (1983) and Harrod’s *The Life of John Maynard Keynes* (1951).

Parsons (1983: 421) states that

In early 1920, Smuts approached Keynes to visit South Africa for two months to assist in formulating our currency policy, but Keynes was unable to accept the invitation due to other commitments. Instead, he recommended Henry Strakosch for the task, who together with Arthur Gillett was involved in drafting legislation that year to set up a central bank in South Africa.

Harrod (1951: 288) states

This time he (Keynes) entered deeply into certain plans of Mr. Henry Strakosch for setting up a new company to sell South African gold. He and Strakosch were to be the managers. It was felt that the existing marketing arrangement could be improved. There was active discussion throughout the autumn, there was a meeting with the Rothschilds and consultation with the South African government. In the end it was decided it would be undesirable to start operations until the South African government had defined its currency policy more clearly. In early 1920, General Smuts wrote to Keynes asking him to come to South Africa for two months to define their currency policy for them, but the invitation was declined. He was all in the midst of laying the foundation of his career in the city of London, his book had just appeared and he sought to be ready to take part in any controversies arising out of it, and he did not wish to make a break in his college duties, so lately resumed.

Parsons' (1983) as quoted above creates the impression that the beginning of the process of taking advice on monetary policy was a letter from Smuts to Keynes, to which Keynes responds, both in early 1920. The importance of this incorrect impression is that it misrepresents the process by which experts are appointed and their ideas implemented. The letters between Smuts (dated the 27<sup>th</sup> September 1920)<sup>48</sup> and Keynes (dated 22<sup>nd</sup> October 1920)<sup>49</sup> are factual and are to be found in the Smuts Papers at the National Archives in Pretoria. And yet the importance of the fuller narrative set out in this dissertation is that it shows the thick web of correspondence and meetings between the power elite in the Bank of England, the Treasury and the mining houses which led to Strakosch's appointment and domination of the proceedings. An excellent summary of the sequence of events after Strakosch's arrival in South Africa is set out in his letter to Keynes dealt with on page 107<sup>50</sup>.

Parsons' analysis misses the reason for Strakosch's appointment. Both Keynes and Strakosch maintained contact with Smuts independently and Strakosch was responsible for trying to get Keynes to South Africa, when he was already here in 1920, not the other way around. I suspect that the error arose from Parsons (1983) not enjoying the privilege of examining the Keynes papers at Kings College, Cambridge, for the account given therein would have been different otherwise. Keynes' first, admittedly casual, invitation from the South African government to visit South Africa came in the form of a letter from Captain Lane, the Secretary, Office of the High Commissioner for the Union of South Africa, dated the 23<sup>rd</sup> of September 1919, replying to Keynes' letter to Smuts regarding the "Strakosch scheme". So by the time Smuts invited Keynes to South Africa, Smuts already had before him the "Strakosch scheme". Lane stated in this letter "I hope that you have now recovered from the very severe strain which you have undergone the last three or four years, but I am quite certain, in order to complete the cure, a quick visit to South Africa will be needed!"<sup>51</sup> Ally (1994:87-91) had the privilege of extensive research of primary sources in the Bank of England, and hence got this story right, although he did not fully explain Keynes's role in the process, perhaps because he did not manage to gain access to Keynes's papers in King's College, Cambridge.

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<sup>48</sup> Smuts Papers, National Archives, Pretoria Vol 23 (renumbered 207 in National Archives) Number 297.

<sup>49</sup> Smuts Papers, National Archives, Pretoria Vol 23 (renumbered 207 in National Archives) Number 298.

<sup>50</sup> Keynes papers L/ ST/ 130

<sup>51</sup> Keynes papers L/ ST/ 80-81

Harrod, who obviously thoroughly studied the Keynes papers, seems not to have had access to the private papers of Jan Christiaan Smuts (originally housed in what became the National Archives in Pretoria, and from which two microfilm copies were subsequently made, the one sent to Cambridge University, after Harrod's book was published, and the other now housed in the archives of the African Studies Department at the University of Cape Town). Harrod's account quoted above does not give sufficient emphasis to the power dynamics involved. It is all superficially true, and in fairness to Harrod, the part of the narrative which is central to this dissertation is only peripheral to that of Harrod's 1951 task. A closer re-examination of the source materials reveals, we believe, a picture which is much more concerned with obtaining the "buy in" of certain individuals representing powerful institutions and deflecting the criticisms of those in another camp.

Although, largely thanks to its failure, the details of the "organisation" which Strakosch proposed to set up is not of primary concern to this dissertation, the negotiations, and particularly the careful attempts by both Strakosch and Keynes to obtain the support of specific strategically powerful individuals is of great interest as it speaks to the role of power in the setting of monetary policy, which after all was closely related to the issue of this "organization". In response to the letter from Henry Strakosch suggesting that Midlands Bank should not be involved<sup>52</sup>, Keynes suggests pulling out of this arrangement, clearly uncomfortable with Strakosch's plan to exclude a trusted friend of Keynes, Reginald McKenna. Reginald McKenna was involved with the Midlands Bank, later Chairman from 1922 – 1943, and Chancellor of the Exchequer 1915-1916 "when JMK was his favourite official" (Skidelsky; 1992: 700). Although not specifically mentioning the proposed exclusion of McKenna by Strakosch as the reason, Keynes goes on to suggest that Strakosch goes ahead with this planned organisation without him "... it explains why I myself would have to think twice before agreeing to make myself prominently responsible for recommending or running it".<sup>53</sup>

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<sup>52</sup> Keynes papers L/ ST/ 43- 46 dated the 31<sup>st</sup> of August 1919.

<sup>53</sup> Keynes papers L/ ST/ 47-50, letter from John Maynard Keynes to Henry Strakosch.

Strakosch then backs down from his attempt to exclude Midlands Bank<sup>54</sup> and later reports good progress in his negotiations with Midlands Bank which seems to have kept Keynes sufficiently happy to continue with the negotiations for this proposed organisation. It is clear from previous research<sup>55</sup> into this particular drama where Strakosch and Keynes were attempting to boldly wrestle control of the selling of South African gold from the Bank of England and the Rothschilds, that Lionel Phillips, Managing Director of Central Mining, was a loyal servant of the Bank of England and Rothschilds as representatives of the British power elite. He had moved back to Britain in 1914 and remained there until 1924. Strakosch notes in his letter of the 9<sup>th</sup> of September 1919 that “my next step I think ought to be to meet my colleagues on the Gold Committee – Lord Harris and Sir Lionel Phillips – with a view to agreeing with them if possible a unanimous recommendation to be placed before the producers”. In Strakosch’s subsequent letter of the 16<sup>th</sup> of September 1919<sup>56</sup>, Strakosch notes “I fired my first shot today by talking to Lord Harris. I found him at first strongly disinclined to move in the gold matter. He thought that we should first wait the result of Rothschilds’ sales to see whether they have really obtained the best price for us.” In the same letter he confirms that he had been invited to see Mr. Anthony de Rothschild, whom he met on the 15<sup>th</sup> of September 1919. “The impression created on my mind is that the invitation to meet Rothschild was very largely prompted by Li Phi (Strakosch’s nickname for Lionel Phillips). He and Rothschild seem to feel that they are on weak ground and that it would be advantageous to get rid of my opposition or criticism by inviting me to become – so to say - a party to their dealings”.

The confidential notes of Strakosch’s meeting with Mr. Anthony de Rothschild on the 15<sup>th</sup> of September 1919 are attached to this letter<sup>57</sup>. Strakosch then obtains, no doubt as a representative of the gold producers, “a note giving details of the gold sales made by Rothschild up to September the 12<sup>th</sup>” on the 18<sup>th</sup> of September 1919<sup>58</sup>, which he shares with Keynes, noting that the total proceeds are “about half a mill better than the average of the highest ‘Times’ quotations”. The gold sales report from Rothschilds for the week ending the 19<sup>th</sup> of September

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<sup>54</sup> Keynes papers L/ ST/ 55 - letter from Henry Strakosch to John Maynard Keynes, dated the 5<sup>th</sup> of September 1919

<sup>55</sup> Gelb (1989: 52) records in footnote 47 how Lionel Phillips was “really disturbed at the way in which suggestion from this side (London) are turned down at your end (Johannesburg) without due consideration” (Lionel Phillips’ letter to Wallace, dated the 10<sup>th</sup> of November 1918).

<sup>56</sup> Keynes papers L/ ST/ 71

<sup>57</sup> And marked as L/ ST/ 68 – 70 in the Cambridge Papers

<sup>58</sup> Keynes papers L/ST/ 77

1919 is attached to a letter to Keynes<sup>59</sup> and Strakosch notes to Keynes “you will observe that the bulk of the gold was sold to India and the trade. In respect of these sales, no charges for shipment will be made by Rothschilds, but so far as the sales to New York are concerned, expenses amounting to about two-thirds of one percent will be deducted. You will observe that Rothschilds realizations at an average of \$4.163 are just about one percent (equal to about a quarter of a percent) less favourable than the average of the highest ‘Times’ quotations for the period covered by the sales”. Strakosch, needless to say, would have made good capital from this fact, but Rothschilds outmanoeuvres him because, in a letter to Keynes dated the 30<sup>th</sup> of September 1919, Strakosch notes that he “got Rothschilds’ gold sales for the week ending September 26<sup>th</sup> ... Their sales of September 26<sup>th</sup> were remarkably well executed considering the rise in the New York exchange. The sales to Switzerland deserve special notice because a price was secured far in excess of what is indicated by the position of exchange”.<sup>60</sup>

Strakosch then sent Keynes the notes from the group meeting of the gold producers of the 9<sup>th</sup> of October 1919 where the “organisation” was discussed.

At yesterday’s group meeting criticism was mainly directed to the possibility of opposition from:

- a) the Union Government,
- b) the banks and exchange dealers
- c) the general public.

As to a), General Smuts being in possession of my Memorandum and having been kept informed in regard to the latter development, I expect shortly to hear the views of the Union Government on the matter.<sup>61</sup>

Having come up against the formidable opposition of Lionel Phillips, supporting the interests of the Bank of England and the Rothschilds, and having received specific concerns about possible

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<sup>59</sup> Keynes papers L/ ST/ 82-84

<sup>60</sup> Keynes papers L/ ST/ 85

<sup>61</sup> Keynes papers L/ ST/ 102-103

criticisms by the Union Government, the explicit support of the “organisation” by General Jan Christiaan Smuts became all the more important.

Keynes then writes to Lane (Secretary, Office of the High Commissioner) on the 10<sup>th</sup> of October 1919:

A meeting of the small committee of the gold producers was held yesterday, as their report to the whole body of the mining groups was made this morning... Before passing a final judgment on the scheme... they wished to be assured that the scheme would not be objectionable to any of the powers that be, or likely to cause an outcry from the public or from big city interests. As regards (this) they attach special importance, the point raised in the first instance by Sir Lionel Phillips, to the attitude of the Union Government, and it was evident that some assurance that the Union Government felt no hostility, or indeed that it approved of this scheme, would weigh with the producers very heavily. I suppose that my earlier letter to you will be reaching South Africa shortly. Would it be possible, do you think, to ascertain General Smuts' attitude towards it by cable after the first letter has reached him?<sup>62</sup>

On the 24<sup>th</sup> of October 1919, Strakosch writes to Keynes reminding him that on Sunday “I was inclined to describe Li Phi's hesitating attitude to his having prior information in regard to the appointment of the committee to enquire into the South African exchange question”.<sup>63</sup>

Finally, Smuts responds in the most ambiguous and noncommittal of fashions, which is communicated in a letter from Strakosch to Keynes dated the 12<sup>th</sup> of November 1919 in which Strakosch relays to Keynes the contents of a telegram from Smuts via Lane “inform Keynes and Strakosch confidentially that I favour policy embodied in resolution of recent financial conference at Pretoria”. Strakosch concludes “P.S. would you care to dine with me tomorrow quietly at Chester Square and have a talk then? I need not say how glad I should be if you could

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<sup>62</sup> Keynes papers L/ ST/ 95

<sup>63</sup> Keynes papers L/ ST/ 111 - 112

arrange it”.<sup>64</sup> This conference certainly did not approve the “organisation” and so Smuts’ response was effectively meaningless as a tool to bed down this proposed “organisation”. Given the above, Harrod’s statement that “in the end it was decided it would be undesirable to start operations until the South African government had defined its currency policy more clearly” (1951: 288), a passage much quoted by many academics, while a good summary for the purpose of Harrod’s biography, needs the exposition detailed above to convey the power dynamic of what was involved.

Strakosch writes to Keynes on the 14<sup>th</sup> of November 1919 that

I have had a long talk with the Consolidated Gold Fields people this morning, but nothing of importance emerged from it. They continue to be sympathetic to our scheme, but they are at the moment much pre-occupied as to what the intentions of the Union Government are in regard to the recommendations of the financial conference. I very tentatively suggested that there was a faint possibility of my being able to induce you to go to South Africa to advise us in regard to the whole gold matter. The Gold Fields people are much taken by the idea, and thought if you were prepared to go out that you should do so on behalf of all the mining groups.<sup>65</sup>

On the 15<sup>th</sup> of November 1919, Strakosch writes to Keynes confirming that “I had an hour’s talk with Norman this morning”. He reports that he proposed to modify the current selling arrangement

so as to permit producers to either continue shipping their gold to the bank or, if they find it of benefit, to ship it directly from South Africa to its final destination.

Norman thought that the agitation in South Africa was political, and that it was bad policy to allow business matters to be too much influenced by politics. At a subsequent stage of our conversation he urged me to go out to South Africa to fight against any

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<sup>64</sup> Keynes papers L/ ST/ 121 - 122

<sup>65</sup> Keynes papers L/ ST/ 123 - 124

tinkering with currency matters and the present mode of disposal of our gold. He emphasized that he thought it best in everyone's interest that the gold should continue to come to London"<sup>66</sup> "I mentioned to Norman that there was a faint possibility that you might also go out to South Africa. He clearly welcomed the idea, for he thought that we should use every effort to enlighten South Africa and prevent them from rushing into currency measures (the effects of which he was sure they were not fully appreciating) which would be detrimental not only to the gold industry itself, but to the trade of the country and to the empire as a whole."<sup>67</sup>

On the 27<sup>th</sup> of November 1919, Keynes wrote to Smuts "I received through Lane your telegram (on the question of the proposed organisation for selling gold) to the effect that you were generally favourable to the policy of the conference held in Pretoria". Hinting at Smuts' unhelpful response Keynes says that "it would be unwise to proceed with any scheme for selling gold, until the currency position in South Africa has been cleared up... In the meantime, Sir Lionel Phillips is, I believe, proceeding to South Africa immediately, and Mr. Strakosch will follow him about the middle of December. I suppose that no final decisions are likely to be taken before the date when the latter should reach South Africa...".<sup>68</sup>

Strakosch writes to Keynes, shortly before leaving for South Africa by ship, on the 8<sup>th</sup> of December 1919, "I therefore gladly avail myself of your invitation to lunch with you at 1.30pm on Thursday at 46 Gordon Square (Keynes' London residence)". In a handwritten postscript he inserts

I am very glad that you propose to touch on the South African position from the Treasury point of view when you see Blackett on Thursday. The Treasury is vitally interested in the question and the sooner they appreciate what is in the wind, the better. You no doubt saw the two notes in this morning's *Times*. They were put in at my suggestion and will – I hope – be cabled to South Africa.<sup>69</sup>

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<sup>66</sup> Keynes papers L/ ST/ 125-128

<sup>67</sup> Keynes papers L/ ST/ 127

<sup>68</sup> Keynes papers L/ ST/ 136

<sup>69</sup> Keynes papers L/ ST/ 148 - 149

In the Keynes papers is a cable from Strakosch just prior to his departure by ship to South Africa:

Am strongly of opinion the only effective remedy is issue notes which, though inconvertible, are fully backed by gold in vaults of Treasury and the issue of which is confined to legitimate currency needs of South Africa. On this basis there is no danger of inflation nor of rise in commodity prices... Am sailing for South Africa on the 12<sup>th</sup> instant, Strakosch.<sup>70</sup>

### **5.5 Strakosch's role as an Expert Advisor to the South African Government**

As can be seen above, the research at the Bank of England and Kings College, Cambridge shows that, far from an invitation arriving from South Africa for Keynes to advise on policy, and Keynes recommending Strakosch, there existed a web of co-operation on monetary policy and on the appointment of the first Governor of the South African Reserve Bank, see section 5.7, in England between Keynes and Blackett at the Treasury, Keynes and Strakosch, Strakosch and Norman, Strakosch and Hull, Norman and Goodenough (Chairman of Barclays DCO), Strakosch and Goodenough (at Barclays DCO), Strakosch and Smuts and Keynes and Smuts. With the above-mentioned correspondence as background, the following two pieces of correspondence correct the errors of fact in Parsons' (1983) paper and errors of emphasis in Harrod (1951).

Strakosch's letter to Keynes dated the 17<sup>th</sup> of February 1920, posted from South Africa, is a brilliant summary of how an expert, who has the confidence of the ruling elite, can force his will on the process of decision-making

Two days after my arrival in Johannesburg, I went across to Pretoria and had a long talk with Smuts. He enquired after you and was disappointed that you did not come out... Towards the end of last month, I presented to Smuts my memorandum. A few days later we had a conference at which Mr. Orr, the Minister of Finance, and Mr. E.H. Farrer, the

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<sup>70</sup> Keynes papers L/ ST/ 130

Financial Secretary to the Treasury, were present. My views were adopted, subject to the advice of a committee consisting of representatives of the Associated Chamber of Commerce, Chamber of Mines, the Federated Chamber of Industries, the Agricultural Union and the banks. There are also to be three members nominated by the Government and the Financial Secretary to the Treasurer. I have been invited to act as one of the Government's nominees, which invitation I, of course, accepted.<sup>71</sup>

Strakosch then goes on to explain how he continued to sell to Smuts the idea of the "organisation" that the government should nominate a representative on the Board and that "I made the suggestion that you might be prepared to act in that capacity".<sup>72</sup>

The importance of this letter is to show a central finding of this dissertation, namely that in this case, and perhaps in many other cases, commissions of enquiry, and other mechanisms for arriving at government policy, are not open-minded processes where the Government's decision on policy is only decided after careful deliberation of all of the views canvassed through the process. In this case, Strakosch managed to win the confidence of the Prime Minister, let the Prime Minister know the basic thrust of his views on the currency question prior to sailing for South Africa, talked it through with him and probably gained his approval, wrote up these views in a "memorandum" which was then presented to Smuts, Orr and Farrer, which views were then "adopted, subject to..." Strakosch then boasts to Keynes in a hand-written letter from the Mount Nelson in Cape Town, written on the 20<sup>th</sup> of May 1920, "The committee desires me against all precedent – to be present during the examination of the other witnesses – present indications point to a substantial majority in favour of my proposals".<sup>73</sup>

Arndt (1928) and De Kock (1954) both frown upon Strakosch's enormous influence on the Select Committee of the Legislative Assembly on monetary policy in 1920, particularly we suspect, the decision to avoid a break with Pound Sterling, and related to that the decision not to return to the Gold Standard independent of Britain.

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<sup>71</sup> Keynes papers L/ ST/ 156 - 161

<sup>72</sup> Keynes papers L/ ST/ 161

<sup>73</sup> Keynes papers L/ ST/ 164

Mr. Strakosch was the only witness on the first nine days. At a start, he was permitted to read a pamphlet which he had in the meantime written on *The South African Currency and Exchange Problem* and ‘to amplify it in the light of more recent information and also in the light of comment and criticism made’. He was also a witness on the two other days and attended all the meetings of the committee at which evidence was taken... After hearing the evidence of the other witnesses, he was afforded a further opportunity to give evidence on matters where the views of such witnesses differed from his. Mr. Strakosch thus played a very important role not only in the original drafting of the currency and banking bills,... but also before the committee itself as the main witness who was, moreover, privileged to listen and reply to the evidence of others (De Kock; 1954: 16).

One would perhaps take Arndt (1928) and De Kock’s (1954) disapproval of Strakosch’s undue influence more seriously, if they were equally concerned by the undue haste in which Kemmerer’s advice was rammed through parliament early in 1925. But of course neither of them mustered much outrage in the second instant, because Kemmerer was doing the bidding of a (Pact) government whose aims they agreed with. Although Strakosch and Kemmerer were to be on opposite sides of a debate about whether South African monetary policy should align itself with that of Britain’s, or whether it should be independent of Britain, on the technical issues of central banking, there was in fact much common thinking. De Kock (1954: 34) notes that “According to Mr. Middleton, moreover, his draft had in turn been revised by Mr. Strakosch with Professor Kemmerer’s *A. B. C. of the Federal Reserve System* beside him”. It is ironic that Kemmerer, who was to undo much of Strakosch’s monetary policy work in South Africa, should have drafted one of the few texts on central banking, a text used by Strakosch.

Arndt quotes favourably from “Dr Evans” speaking at the Gold Conference held in Pretoria on October 22 and 23 1919 – “the practical men on the spot, the bankers, have been telling us that it was a wise policy to impose an embargo on the export of gold, to prohibit the melting of gold coins into bullion, and to make paper money inconvertible; that the enlargement of the paper circulation of South Africa from £2,150,000 to several times that amount was necessitated by the worldwide increase in prices, and could not have been avoided, and that it was for the good of South Africa that the banks should go on printing as much paper money as they considered was

required to carry on the business of the country”. “At the end of the conference, Mr. Jagger (a prominent importer and member of Parliament in the Union of South Africa) moved that it was highly desirable that the (gold) embargo be withdrawn as early as possible, ‘with a view to establishing natural exchange rates between the Union and the rest of the world and re-establishing the Union currency on a gold basis’. But this was rejected by seven votes to six.” (Arndt; 1928: 427).

Arndt then notes that “in early January 1920, there appeared on the scene a superior practical man in the person of Mr. (now Sir) Henry Strakosch. Sir Henry possesses persuasive powers of no mean order, and has a wide knowledge of the technicalities of the exchange market. He was consulted by the Union Government, and he confirmed that advice given by the banks, namely that the increase of paper money from £2,150,000 to over £8, 000,000 was not excessive; that additional currency was needed because of the increase of prices; that the increase of prices was attributable to under-production and over-consumption; and that it would be a grave mistake to remove the embargo on the export of gold or attempt to fix a date for its removal, and that, in order to protect the reserves of the banks against smugglers and hoarders, gold should be taken out of circulation and replaced by inconvertible paper” (Arndt; 1928: 428-429). Although Henry Strakosch, when he did his magnificent performance in South Africa between January and April 1920, was representing the “dominant orthodoxy” of the Bank of England, Britain was no longer strong enough to enforce a single orthodoxy throughout the world. In order to conserve gold and ensure its direction through the London gold market, Montagu Norman at the Bank of England required South Africa to tow the line and remain linked to sterling and not return to the Gold Standard prior to when the Bank of England was ready to do so itself.

“The committee met in February, 1920, with Dr Evans as Chairman and the amended bills constituted the report of the conference. Dr Evans rightly points out; ‘What occurred on this occasion convinced me that, for the time being, the practical man had definitely gained the ascendancy. The change in the attitude of the Government was unfortunate for South Africa’” (Arndt; 1928: 429). The use of the term “practical man” to describe Henry Strakosch is interesting. Firstly, because it identifies a clash which occurs again and again through monetary history between the representatives of industry, mining and other constituents of the real

economy on the one hand (“practical men”), and the purveyors of conventional economic wisdom being the dominant classical orthodoxy of the time, on the other. It was true in 19<sup>th</sup> century debates which we dealt with in chapter four and it is equally true today. It is somewhat rich for “Dr” Samuel Evans to describe Henry Strakosch as a “practical man”, discarding the virtues of economic orthodoxy which the true inner sanctum of orthodox academic believers espouses, when Samuel Evans’ doctorate was an honorary one (from Wits University)<sup>74</sup>. From Evans’ correspondence and his participation in monetary policy debates, it is clear that he was thoroughly conversant with monetary orthodoxies, and particularly well-schooled in arguments in favour of the Gold Standard.

But Samuel Evans was himself very much a “superior practical man”. Born in Wales, he worked as a journalist before getting his break in 1883 when he became private secretary to Sir Edgar Vincent, advisor to the Egyptian Government. Upon arriving in South Africa, he became a Director of the National Bank and later Managing Director of Crown Mines. His active involvement in the monetary policy debate at the time of the currency crisis of 1919 led him to consult widely on monetary policy<sup>75</sup>.

Besides, as Balachandran (1996:8-9) notes, “short-term macro-policy during the interwar years continued largely to be made by ‘practical’ men facing new and daunting challenges”. The “long-run” “liberal discourse”, as Balachandran (1996) calls it, didn’t provide adequate answers and so in was left to ‘practical men’ to find the short-run solutions.

Despite both Keynes and Strakosch attempting to “buck the system” of imperial interest in establishing an alternative selling “organisation” for South African gold, both retained the trust and confidence of the power elite in England in advancing imperial interests in the establishment of monetary policy in South Africa. Strakosch was, with the exception of his attempts to establish the “organisation”, a loyal servant of the Bank of England. His *modus operandi*, as

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<sup>74</sup> Samuel Evans Papers, Barloworld archives - Box entitled “Politics 1899-1949, Reform Committee, 1895, Reform Committee, Relief Funds – mainly press cuttings and shorthand notes on gold”.

<sup>75</sup> Samuel Evans Papers, Barloworld archives - Box entitled “Politics 1899-1949, Reform Committee, 1895, Reform Committee, Relief Funds – mainly press cuttings and shorthand notes on gold”.

evident throughout the correspondence sections from 1919, of the Montagu Norman Papers at the Bank of England, was to propose correspondence to third parties (particularly Clegg) and send such draft correspondence to Norman at the Bank of England for Norman's approval prior to the correspondence being sent to the third party. As dealt with above, Strakosch enjoyed friendships with the first Finance Minister of the Union Government and appears to have met Smuts previously.

Keynes of course established his relationship with Smuts during the Treaty of Versailles negotiations where they were in broad sympathy with the idea of not crushing Germany economically. Much has been said about Keynes' exile from government as a result of his bold criticism of the Treaty of Versailles. However a closer look reveals that "there is little evidence, for the period as a whole, that *The Economic Consequences of the Peace* had cut Keynes off from 'official circles'" (Skidelsky; 1992: xxvi). "In fact Keynes had more influence than he himself was willing to acknowledge" (Skidelsky; 1992: 18). "Keynes was certainly not cut off as a policy advisor from the moment his *The Economic Consequences of the Peace* appeared. Within a couple of months of its publication in December 1919, Austen Chamberlain, the first post-war Chancellor of the Exchequer, was consulting him on monetary policy, as though he had never left the Treasury. His Treasury friend and admirer, Basil Blackett, occupied the new key position of Comptroller of Finance at the Treasury. On reparations, as we shall see, he was 'uniquely' consulted by both the British and the German governments" (Skidelsky; 1992: 19).

Even his "falling out with the Bank of England, and particularly its Governor, Montagu Norman, in 1922" (Skidelsky; 1992: 20) had not yet manifested itself and, in the period of the discussions around the establishment of the South African Reserve Bank and the appointment of its first Governor, Keynes "as an ex-Treasury man... was consulted in February 1920 on what course monetary policy should take" (Skidelsky; 1992: 40). At a time when the political pressure from the Prime Minister and the Chancellor of the Exchequer was to reduce interest rates, Keynes supported Norman in pushing to raise them. Keynes made a "call for an eight percent interest rate (which) was echoed by the Governor of the Bank, Montagu Norman, who attended that meeting, but was vetoed by Chamberlain" (Skidelsky; 1992: 40). It is clear that, in 1919 and

1920, Keynes supported Montagu Norman in using high interest rates to kill inflation and that, at this point in time, and on this issue, Keynes was a supporter of Norman.

In summary, I would suggest that Strakosch sought to secure the acceptance of certain “big guns” for his proposal to replace the arrangement up to then controlled by the Bank of England and Rothschilds and failed because, while he did manage to obtain the buy-in of John Maynard Keynes, he was defeated by the efforts of Lionel Phillips and the Rothschilds and particularly defeated by his failure to obtain the unambiguous support of General Smuts.

What is of great interest to our narrative is the fact that Keynes and Strakosch were intensely involved in communicating with all of the important players who together decided on the establishment of the South African Reserve Bank and the appointment of its first Governor, albeit for the purposes of setting up an organization which failed. Although this organization failed to materialize, working on it meant that both Keynes and Strakosch engaged in intense communications with the British power elite and with Smuts. In the case of Keynes, this involved his close friendships at the Treasury, particularly with Basil Blackett, and his friendship with Smuts which was cemented by their commitment to a moral, but minority position at the Treaty of Versailles. In the case of Strakosch it involved his friendship with Montagu Norman, H C Hull (the first Finance Minister of the Union of South Africa) and his growing standing with Jan Christiaan Smuts. Smuts was no doubt fully aware of the standing of Strakosch and Keynes with the British ruling elite, and the fact that they enjoyed access and were taken seriously by the most important people in the City of London and in government, must surely have been a powerful factor influencing his invitation to both of them.

In 1937 Strakosch became the target of a tug of war between Hertzog and Smuts. Strakosch, a British subject not a South African citizen, had under the Smuts government represented South Africa at the Brussels Conference in 1920, the Imperial Conference in 1923 and was the South African Delegate at the League of Nations in 1923 and 1924. He continued to represent South Africa on the Raw Materials Committee of the League of Nations. But in early 1937 there was so question as to whether he would continue to do so. Smuts writes to Strakosch on the 22<sup>nd</sup> March 1937 and Strakosch, in his letter of the 8<sup>th</sup> April 1937 thanks Smuts for his letter noting “I

was very glad to gather from it that both you and General Hertzog see no objection to my continuing to serve on the Raw Materials Committee” but pointing out that he (Strakosch) had had a talk with Mr te Water (the South African High Commissioner) who said that the matter was not agreed and that Hertzog needs to decide it. Te Water placed a letter in the British Press effectively disowning Strakosch in public, stating that he had no right to represent South Africa on this committee<sup>76</sup>. Obviously this move was calculated to cause maximum embarrassment to Strakosch.

Although Smuts and Hertzog were by now in the same government, differences between them on the matter of assistance in South Africa’s affairs from British subjects based in London continued to be an issue. In this case Hertzog won and Strakosch was forced to resign his position. Eight months later, when Strakosch was handing yet another election campaign cheque to Smuts, via his confidant Mr Anderson, he complained again about his ill-treatment over the Raw Materials Committee matter. Smuts writes to Strakosch on the 3<sup>rd</sup> January 1938 disowning any South African government responsibility, on the part of him or Hertzog, and blaming Strakosch’s resignation on a misunderstanding between Strakosch and te Water. This is clearly nonsense as a High Commissioner would surely not disown a representative of the government at the League of Nations without expressed approval from his political superiors<sup>77</sup>. Notwithstanding Smuts’ attempted whitewash, we would argue that this incident shows the old “pro” and “anti” British battles that were still being fought, even within the 1937-1938 South African government. Having diverted briefly from our period, let us now return to it.

## **5.6 Strakosch’s ideas in the South African Monetary Policy Debates 1919-1924**

In October 1919 Strakosch and Norman met regularly at the Bank of England and were horrified that anti-Pound Sterling views were dominating the Gold Conference in South Africa. The Gold Conference was chaired by the Gold Standard and Quantity Theory fundamentalist, Samuel Evans and acted as a conduit for anti-British feeling, given the abuse of South African’s gold by the British during the First World War. Once he had the confidence of Smuts, Strakosch went to

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<sup>76</sup> Smuts personal papers, Volume 55 (re-numbered Volume 241 in the National Archives)/ 126 - 129

<sup>77</sup> Smuts personal papers, Volume 55 (re-numbered Volume 241 in the National Archives)/ 129

work in South Africa applying a “banking school approach” to countering the “currency school” line of argument of Samuel Evans and others. Strakosch took issue with the idea that inflation was due to the world’s currencies no longer being on a Gold Standard. The reason for the situation, he insisted, was not simply because of excess money supply, but because the war had destroyed the pre-1914 patterns of international trade. “The Strakosch doctrine on currency thus reduced itself to the following formula: if a country’s trade was in balance, its exchange would be at par; and conversely, if its trade was in deficit, its exchange would be below par” (Ally; 1994: 115). Strakosch warned that the sacrifices of a policy involving a strict return to the Gold Standard would include currency deflation, credit restriction and wage restraint.

Samuel Evans, Chair of the Select Committee appointed in March 1920 to consider the proposals set out in Strakosch’s memorandum, represented the opposing “currency school” argument: “The establishment of a sound currency is the first step on the road to prosperity, and in order to achieve greater economy and more production, we must begin by securing a stable monetary standard” (Ally; 1994: 119). Strakosch warned that: “The removal of the gold embargo would impede production, and it would foster importation, reduce our exports, and would lead to a withdrawal of capital from this country... If we have a rapid return to gold parity it will bring disaster; it will result in severe crisis; it will lead to a complete breakdown of credit and all our activities; our industries and trade will be enormously restricted; and thousands will be thrown out of employment”. (Strakosch, 1921, quoted in Ally; 1994: 120)

Aside from his influence in South Africa, Strakosch was also involved in British monetary policy debates. Strakosch’s monetary policy advice in the British monetary policy debate was firmly on the side of “sound money” and espousing the “Treasury view” which sought to restore the British pound to the Gold Standard at the pre-war parity as soon as possible. As an emissary of the British financial elite, Strakosch argued forcefully in South Africa for the exact opposite position, anxious to stop the South African authorities from returning to a Gold Standard independent of Britain. Despite his friendship with John Maynard Keynes, when it came to the Gold Standard debate in Britain, Strakosch came down firmly on the side of Norman.

Strakosch argued forcefully in favour of the Gold Standard in Britain in a “long letter... in *The Times* of London on the 31<sup>st</sup> of July 1925” (Skidelsky; 1992: 205). Keynes responded to Strakosch in the same paper, warning that returning to the Gold Standard in Britain “would leave price and wages to be the shock absorbers”, something that, in the British debate, Strakosch was prepared to sacrifice on the altar of the “sound money” of the Gold Standard.

In South Africa, Strakosch’s main brief from the London financial elite was to prevent the Union from returning to the Gold Standard independent of Britain, and rather maintaining its existing sterling standard. As occurred in India, a return to the Gold Standard in South Africa was viewed by local nationalists as a means of gaining financial independence from London. Given this sensitivity, the Select Committee, which Strakosch led and dominated, did not directly deal with the Gold Standard question in 1920. Kantor highlights this important issue, sometimes missed by other academics writing on this period, that: “The major issue, whether or not to link the South African Pound to Sterling, or the dollar, was largely ignored by the Select Committee” (1971: 67). We would suggest that this was not an innocent omission, given that Henry Strakosch, the driver of this particular Select Committee, had allegiances to London and hence was unlikely to train a spotlight on the possible severance of the South African Pound’s connection to Sterling. Having won the battle to maintain gold certificates instead of a fully fledged Gold Standard in 1920, the Smuts government decided to convene another currency conference in October of 1921 “to examine the implications of South African restoring its currency on a gold basis after the 1<sup>st</sup> of July 1923” (Ally; 1994: 124).

The prospect of having his work 1920 undone in 1921 motivated Strakosch to update his memorandum into a pamphlet *The South African Currency and Exchange Problem Re-Examined*. In it Strakosch stresses the importance of the stability of the currency exchange to its foreign trade. He boasts that, since the Currency and Banking Act of 1920 was enacted, for which he was largely responsible for drafting, “the South African exchange on London maintained almost complete stability, its fluctuations being confined to a range of only 1%.” (Strakosch; 1921: 6). He paraphrases that his opponents rely on the orthodox doctrine and that the value of the currency should be regulated by regulating its supply. He points out that, by this logic, “the respective purchasing power of the monies of two countries determines the ratio of

exchange between them” (Strakosch; 1921: 9). This, Strakosch points out, is the purchase power parity argument developed by Professor Gustav Cassel, which is notoriously unreliable. He points to the disconnect between money supply and prices, noting that “as far as South Africa is concerned, maximum prices were reached in July, 1920, while the maximum note circulation was attained at the 31<sup>st</sup> of December 1920” (Strakosch; 1921: 10). Strakosch quotes approvingly from Vissering’s address as president of the Committee on Finance and Exchange at the Brussels conference: “Gold has... retained its function of cover for a fiduciary circulation, but, practically speaking, at the present moment it no longer plays the part of international medium of exchange”. Vissering goes on to warn “If one were thus to issue gold as a means of payment to foreign countries... the stock of gold would be exhausted... Such export would give the country an appearance of strength, although this would not be more than an appearance... After a very few months the use of this medium of payment would be no longer possible, whereupon the great disillusion would follow” (Strakosch; 1921: 21-22). This could well be the source of Evans’ distrust of Vissering detailed in his letter on pages 81 -82.

In the spirit of Attwood, Thornton and Keynes, Strakosch concludes by warning that “a monetary policy which tends to impede production can, therefore, not be regarded as sound... To continue a drastic policy of deflation in the face of, for instance, seriously growing unemployment, and with it social unrest, would obviously not be sound” (Strakosch; 1921: 26). “The price of home produced goods, and sometimes even of imported goods, but especially wages, adapt themselves sluggishly to monetary changes.” “We may say then that the internal purchasing power adjusts itself only tardily to the changed monetary conditions” (Strakosch; 1922: 7).

So why would Strakosch argue in favour of a “sound money” Gold Standard in Britain, siding with Montagu Norman of the Bank of England and the British Treasury against John Maynard Keynes, and why would he “jump sides” and argue in favour of industry and labour in South Africa by supporting a sterling standard and opposing a Gold Standard?

Harris (1931) answers the question partly when he shows how restrictions imposed by London on the flow of gold affected the money supply of Britain positively and the dominions (including South Africa) negatively. In Britain “in 1917 and 1918, the authorities began to issue Bank of

England notes secured by gold received from South Africa ... The reduction of money and deposits resulting from the loss of gold undoubtedly explains in part the relatively moderate depreciation of South African currency” (Harris; 1931: 459). He points out that this milking of South Africa by London produced much resentment in South Africa (Harris; 1931: 460). Harris writes from America at a time when dismantling the British Imperial monetary and trade system was a central concern of the American power elite.

The rest of the answer is to be found in a brilliant article written about 70 years later by the Indian-born, Geneva-based economist Gopalan Balachandran (2008) as well as in clues to be found in the works of Ally (1994) (see section 2.2), Dalgaard (1981) (see section 2.3) and Dubow (2006). The question is: who provides the support for the global financial system based in London when the real economy underpinnings have eroded away? As shown in section 2.1, Balachandran (2008) provides key answers to this question. He shows how London used its position of political dominance to call for loyalty and, where it was not forthcoming, to coerce loyalty in propping up London’s faltering position as the centre of global finance. He shows the costs to the Dominion and Colonial economies, particularly in India and South Africa, of supporting a dying imperial system. Balachandran stresses the importance of studying the monetary policy and related issues in other British colonies in the period 1919 – 1936, and his comparisons of Australia and India with South Africa are rich, suggestive and evocative.

As we have shown on pages 149-150 below, once the international Gold Standard had broken down, London could no longer rely on preaching a single monetary policy gospel across its Empire. Now it needed to implement a pedagogic schizophrenia arguing different theories in different domains. Separate monetary policies needed to be encouraged into implementation in South Africa, India and elsewhere, dependent on what London needed out of that part of the Empire. In the case of South Africa, the London market needed to secure all, or as much of the gold of the Witwatersrand as possible. In the case of India, to discourage gold imports, and at the same time, to encourage British imports into India and discourage exports from it.

Having dealt with why Strakosch argued so differently in Britain and South Africa, let us look at why his views were so readily accepted. No doubt his powers of persuasion were great, his

confidence strengthened in the knowledge that he was doing the bidding of a powerful hegemon. But Dubow (2006) hints at why his ideas were so readily accepted, once they had been made. He deals with how the opinions of the metropolis manage to dominate those of the locals in dominions or colonies. His focus on the intellectual voices working through institutions in shaping identity is particularly important. He highlights the contrast between the eloquent arguments of ‘experts’ in support of imperial policy, experts who had the backing of prestigious intellectual institutions, with dissenting voices who did not enjoy a similar status. The “desire to emulate British norms was always present and deference to the metropole (London) was an ingrained reflex” (2006: 74). This quote, relating to the *Cape Monthly Magazine*’s relatively low prestige compared to British equivalents, would also apply to monetary policy ideas in 1920, with the oracle of the metropole being taken more seriously than the local Samuel Evans.

Strakosch’s role in South Africa as a representative of British power elite interests is further corroborated by his later experience in India. Cecil Kisch, at the India office, appointed Henry Strakosch as the main British representative on the Indian currency commission. Kisch was eager to ensure that “the external factors were given at least as much importance as local ones” (Balachandran; 1996: 141). Hilton-Young of the Bank of England “noted warmly from Bombay, [that] Strakosch was leading the party of orthodoxy and the economy of gold in the battle of standards” (Balachandran; 1996: 141). In this commission, Strakosch aggressively handled supporters of an Indian Gold Standard and was, in contrast, noticeably gentle on those who opposed it.

The British interest in Indian monetary policy in the 1920s was linked to London’s own attempt to close the gap between American prices and British prices which, by the middle of the 1920s, stood at a disparity of 10% higher than Britain.

Until 1923, Indian gold imports were sought to be restricted to stimulate monetary expansion in the U.S.A.” (Balachandran; 1996: 115). Also, Britain saw a dual opportunity in ensuring a strong rupee, both in stimulating Indian import of British goods and in dampening Indian exports, and hence lowering incomes. This policy “extracted a

price in the form of growing business and political opposition to the deflationary impact of the Indian government's monetary policy (Balachandran; 1996: 115).

By allowing the appreciation of the rupee at the time of good harvest, and actively fighting against its weakness at times of weakness in the real economy, the British managed to ensure that the Indian trade surplus actually halved between 1925-26 and the following two years. Indian gold imports fell from a peak of £52 million in 1924 to £27.8 million in 1925, and to an average of about £15 million per year over the next four years. Both the absolute amounts and the proportion to total world gold output of Indian inputs of the metal were, on average, lower during these four years than in the last decade before the First World War, and by January 1928, officials in New York were emboldened enough to predict that future Indian gold imports would be spasmodic and in small quantities. So, in addition to the ironies in the different approaches to monetary policy, arguing for 'sound money' in Britain and industry focused monetary policy in South Africa, there is a further irony in Strakosch's role in the Hilton-Young Commission in India in 1925. Balachandran has shown that the British policy was, not so much one of promoting 'sound money' in India, but rather actively suppressing Indian exports and stimulating Indian imports (particularly of British goods), so as to achieve the suppression of Indian demand for gold. While eloquent in promoting a monetary policy which would benefit South African industry, the monetary policy that Strakosch supported in India actively suppressed industry so as to satisfy London's gold policy.

Kisch was himself the co-author of the leading book on central banking, with a foreword by Montagu Norman, first published in 1928. In it he supports a Gold Standard, arguing "that in present conditions gold is still the least unsatisfactory standard of value and that the surest method of preserving stability in the purchase power of money is to base currencies on gold." (Kisch and Elkin; 1928: 3). This is again, of course, advice reserved for his home audience in Britain, contrary to the advice that he gave to the Indians. It is worthwhile noting that Strakosch's advice to the South Africans to set up a central bank was in keeping with the strategy of the Bank of England to set up central banks in all of the colonies and/ or dominions of Britain. This was in line with the Bank of England's plan to have very close relationships with the various central banks of its colonies and dominions in order for Britain to continue to exercise

control over the monetary policy of its empire, albeit a weaker control than when Britain could afford to maintain the Gold Standard centred on London.

Professor T. E. Gregory, biographer of Ernest Oppenheimer, seems to have developed an allegiance to his gold mining subject, as he was a supporter of an Indian Gold Standard and hence showed less theoretical schizophrenia than Strakosch. Strakosch's loyalty to the London power elite is evident by the fact that he argued against policies which would have resulted in the mining company, Union Corporation, of which he was the Chairman, earning more for its gold in the United States of America and India. Similarly, another representative of South African "gold producers", John Martin, argued in a forum of gold producers that it would not be prudent to take advantage of a "small" profit opportunity to sell their gold elsewhere rather than through the Bank of England and risk alienating London by "selling above the set price".<sup>78</sup>

In the correspondence between William Henry Clegg, the first Governor of the South African Reserve Bank, and Montagu Norman, it is clear that John Martin is treated as someone in whom the Bank of England has complete trust and faith. In a letter from Clegg to Norman dated the 21<sup>st</sup> of July 1930, Clegg is responding to a confidential and sensitive request from Norman on information relating to gold production "If John Martin was here, I would have talked to him, but in his absence, because the gold producers have not approached me, I cannot call them".<sup>79</sup> The loyalty of both Strakosch and Martin was rewarded by Norman, proposing both of them, at separate times, as Directors of the Bank of England (Sayers; 1976: 599). "It can be said with some confidence that in this procedure no one could be elected without the personal acquaintance of the Governor; it is equally certain that he was not always able to impose a candidate of his own. He failed in his efforts to get Strakosch onto the Board, and he wanted Clegg elected in the 1920s but had to wait until 1932 before his colleagues would agree" (Sayers; 1976: 600).

In the period in which Strakosch was an expert, this policy resulted in:

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<sup>78</sup> Bank of England Archives, "Sayers file" OV37/ 25, being a quote of a message sent by Martin to Central Mining, quoted in a letter from Harvey to Clegg, dated the 1<sup>st</sup> of August 1930.

<sup>79</sup> Bank of England Archives, "Sayers file" OV37/ 25

1. Gold's supply being channeled through the London market by active steps to discourage/ban exports to the United States of America and India, where it would have been more profitable for South African producers to export gold.
2. The flow of gold to London causing an expansion of British monetary supply, given that gold was the foundation of the monetary system at the time and given the extent and sophistication of fractional reserve banking in London. Similarly, forcing gold to flow through London at a price lower than its market price in the United States of America and India put a deflationary bias on Indian prices, stimulating imports and constricting exports and thus harming the real economy of India (Balachandran; 1996: 36-65). "For these reasons the international boomlets of the 1920s passed India by" (Balachandran; 1996: 41).

## **5.7 The Appointment of William Henry Clegg as First Governor of the SARB**

Gillett, Keynes, Goodenough and Strakosch were the four people that Smuts asked to form to committee with the purpose of finding the first governor of the South African Reserve Bank. In a letter from Smuts to Keynes dated the 27<sup>th</sup> September 1920, "Gillett and his wife have been staying with me in South Africa for some time. He now returns with the ship that carries this letter"<sup>80</sup>. Smuts asks Keynes to join Gillett, Goodenough and Strakosch in selecting the SARB's first governor<sup>81</sup>. At this stage, Gillett's bank had been taken over by Barclays and he effectively worked for Goodenough (Schwartz; 2011:312). In the much quoted letter from Keynes to Smuts, dated the 22<sup>nd</sup> October 1920 in which he notes "I have been very glad to serve on the committee to recommend a governor for your new State Bank ... we met yesterday and there are good prospects, I think, of a strong appointment"<sup>82</sup>. Keynes had Sir Ernest Harvey, the Chief Cashier of the Bank of England in mind in this letter, as is confirmed by the letter from Norman to Goodenough on the 1<sup>st</sup> November 1920 in which Norman states that Harvey would like to meet with Goodenough<sup>83</sup>. On the 9<sup>th</sup> November 1920 Strakosch and Goodenough jointly sign the letter

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<sup>80</sup> Smuts Papers, National Archive, Vol 98 (renumbered 289 in the National Archive), number 297

<sup>81</sup> Smuts Papers, National Archive, Vol 98 (renumbered 289 in the National Archive), number 297

<sup>82</sup> Smuts Papers, National Archives, Vol 23 (renumbered 207 in the National Archive), number 153

<sup>83</sup> Montagu Norman Papers, Bank of England Archives, File G1/432.

to Norman, on a Barclays Bank letterhead, in which, given their failure to convince their “first two” choices, they state that they what to offer the position to Clegg, the Chief Accountant at the Bank of England. They ask Norman to approach him, and if he is interested, to arrange to meet them at 11h30 the following day.

On the same day Norman writes back that Clegg is “favourably disposed” that he “assured Mr.. Clegg that I (Norman) shall spare no efforts to make it easy for him to change over to the new Bank”. Norman ends the letter noting the whole purpose of this new Central Bank in the Empire: “Finally let me say that I so fully realize the importance of this matter to the City of London and to the Empire that I am anxious to help in any manner you may desire”<sup>84</sup>. Following this selection process for the governor of a new central bank in a country within the British Empire, effectively run by F. C. Goodenough the CEO of a Bank (Barclays) based in London with the stated aim of expanding to cover the Empire (and become Barclays Dominion Colonial and Overseas), the Managing Director of a London-based Mining house (Strakosch) and an advisor to the British government (Keynes), and the Governor of the Bank of England (Norman); William Henry Clegg was appointed.

Ally’s summary of the position of the establishment of the South African Reserve Bank in the imperial capital/ national capital debate is much better than Gelb’s dealt with in sections 2.2 and 2.5 above. In fairness to Gelb, Ally benefitted from extensive primary resource research in Britain while undertaking the much larger task of completing a PhD, rather than Gelb’s more modest task of writing a journal article. Ally also benefitted from an additional seven years of scholarship (from 1987 to 1994). But whatever the reason, Ally’s summary is far better. He notes in sympathy with Gelb (1987) that the establishment of the South African Reserve Bank enabled the Bank of England to blunt “the more excessive features of economic nationalism that began to develop in South Africa in the immediate post-First World War years...” and goes on to emphasis what Gelb misses, namely that the Bank of England did “enjoy a fair measure of success in keeping South Africa within the imperial economic system” (Ally; 1994: 100), given the close working relationship between Norman and Clegg. He does concede a nod to Gelb by acknowledging that the South African Reserve Bank made it possible for South Africa to “pursue

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<sup>84</sup> Montagu Norman Papers, Bank of England Archives, File G1/432.

a more independent policy where monetary and banking matters were concerned” (Ally; 1994: 100).

## **5.8 Kemmerer and Vissering - Background**

It is also not surprising that the Pact government headed by Smuts’ rival, Barry Hertzog, appointed an American and a Dutchman to lead their commission of enquiry into monetary questions. The advice of Professor Edwin Kemmerer, the American ‘Currency Doctor’ and Professor of Economics at Princeton University, was sought throughout South America, Eastern Europe, Japan and South Africa, on issues such as the setting up of central banks and monetary policy. We would contend that though Kemmerer was an expert in his field, his selection also said something about America’s growing political and economic influence. A look at the regions in which he was active demonstrates this influence. South America, in line with the Monroe doctrine, had long been viewed by the United States of America as being in its ‘sphere of influence.’ So American economic interests, backed up by American imperialist power, may well have been a factor in appointing Kemmerer as their central banking and monetary policy advisor. Similarly, his role in Eastern Europe can be viewed in the context of Woodrow Wilson’s support for the independence of nationalist regimes in that region. American glee at eroding British influence in her colonies, with the appointment by the Pact government, of Edwin Kemmerer and Gerhard Vissering, is evident in the letter from John Parker Young, from the Commission of Gold and Silver Enquiry at the United States Senate dated the 22<sup>nd</sup> of October 1924 and addressed to Professor Kemmerer, “I am glad to know that you are going to South Africa. I can imagine how the British will enjoy having an American and a Dutchman install the Gold Standard in one of the leading colonies”.

Both Strakosch and Kemmerer dominated the proceedings of the two South African commissions to which they were appointed as leaders. The reports of these commissions essentially reflected the will and opinions of Strakosch and Kemmerer respectively, and in both cases the recommendations of these two commissions were accepted into law by the Smuts government and the Pact government respectively.

## 5.9 Kemmerer's World

Having dealt with the chameleon-like qualities of Henry Strakosch, arguably the most influential person determining monetary policy in South Africa in the 1920-1924 period, we now turn to Edwin Kemmerer.

Kemmerer is less kaleidoscopic, less complex and much more iconic as a representative of the prevailing economic orthodoxy. The Strakosch/ Keynes comparison detailed above, involves similarities and differences. Yet the comparison between Kemmerer and Keynes are far more archetypal and striking, running from background and predisposition through to policy advice and prescription.

Given this archetypal scenario, it is instructive to consider these two professors of economics as parallel lives. John Maynard Keynes' genteel and educated background has been described earlier.

By contrast, Kemmerer's father was "an official of the Lackawana railroad for 34 years".<sup>85</sup> Edwin Kemmerer grew up in a strict religious home, "with firm parental advice, occasional corporate punishment with a small but memorable ram hide whip".<sup>86</sup> Whereas Keynes did not have to self-finance his university education, Kemmerer did, holding down a job and buying eggs wholesale and selling them door to door.<sup>87</sup>

Given his experience of pulling himself up by his bootstraps, Kemmerer can be forgiven for falling under the spell of Herbert Spencer, the social Darwinist who twisted the Bible's message of God's concern for the weak and needy into one in which God helps those who help themselves. "The books I remember best are the writings of Herbert Spencer... which had great influence upon the youth of my generation."<sup>88</sup>

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<sup>85</sup> Kemmerer Papers, Box 277, Folder 5, page 4 of unpublished autobiography.

<sup>86</sup> Kemmerer Papers, Box 277, Folder 5, page 9 of unpublished autobiography.

<sup>87</sup> Kemmerer Papers, Box 277, Folder 5, page 11 of unpublished autobiography.

<sup>88</sup> Kemmerer Papers, Box 277, Folder 5, page 12A of unpublished biography.

This is, of course, in sharp contrast to the intellectual influences that Keynes describes in “My Early Beliefs” (Keynes; 1949) described above.

By contrast, Kemmerer’s favourite book had chapters entitled “Concentration, or Oneness of Aim, Self-Reliance, Attention to Detail, Self-Advertising, The Will and the Way, Reserve Power, and Economy of Time”<sup>89</sup>. Such titles would hardly be on the reading list of Keynes’ friends, Virginia Woolf and company. Rosenberg’s book on Kemmerer (1999: 31-39) shows how the virtue of “manliness” develops as a dominant theme concerning white Anglo-Saxon Protestant leadership in America. She traces the origins of these ideas in the works of George M. Beard (1881). Beard defined an idleness of “neurasthenia” as “nervousness – a lack of nerve force” caused by “the stress of over-civilization” which he believed was common “among white men who did brain work” (Rosenberg; 1999: 36 – 37).

George Simmel, author of the tome *The Philosophy of Money*, also talked of a “secret restlessness”, “an increase in nervous life”, “emerging from the speed and diversity of professional life” (Rosenberg; 1999: 36-37). Both Beard and Simmel believed that this was a particularly male problem, as women were “less evolved, less differentiated and complex” (Rosenberg; 1999: 37). These ideas of manliness connected with superiority and inferiority were extended on the political level and picked up by the US President, Teddy Roosevelt, who preached that “a (white) person who avoided having children was in effect a criminal against the race”. Roosevelt idealized the superiority of the white race defeating darker people in his *Winning of the West*, further building on these racist ideas of manliness.

Edwin Kemmerer’s fellow quantity theorist, Irvin Fisher, followed up his *Introduction to Economic Science* (1910) with *How to Live: Rules for Healthy Living Based on Modern Science* (1915) which includes a chapter on eugenics, encouraging the reader to choose a wife mindful of maintaining “race hygiene” which “aims to conserve the health of future generations through the actions of those now living” (Irvin Fisher and Eugene Lyman Fisk; 1925: 168 - 171). Kemmerer himself, following in Teddy Roosevelt’s shoes and identifying himself as a “progressive Republican” many times in his correspondence, said of the Philippines that “three centuries of

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<sup>89</sup> Kemmerer Papers, Box 277, Folder 5, page 13 of unpublished biography.

Spanish rule had ‘developed children, not independent self-reliant men’. Filipinos ‘have yet to learn the lessons of political honesty, of thrift and of self-reliance’.” (Rosenberg; 1999: 39) Edwin Kemmerer, the boy raised in the strict religious family with evangelical roots and imbibed with all of these white Protestant American notions of manliness would certainly not have placed Jews in the “manly” category. In advising on a choice of university, he told his friend to choose New York University over another university, as it was “more homogenous”, presumably a reference to the relative absence of Jews. More specifically, Kemmerer instigated dressing up as a Ku Klux Klan member for the masquerade ball on the ship to South Africa on the 4<sup>th</sup> of December 1924 and he boasted that it “made a good impression”. On board the ship for the return voyage, Kemmerer notes in a diary entry “January 21 to February 1”, that “most of the people on board are Jews and/ or bookmakers and everything is gambling. It is a pretty cheap crowd. At the masquerade ball I dressed as a Ku Klux Klan, but my three table companions who promised to do the same backed out for fear of criticism by Jews and Catholics on board. A Miss Aronson – Jewess – gave me hell in general for the Ku Klux Klan in US , as if I were responsible for it.”<sup>90</sup>

Vissering, in his diary entry of the 3<sup>rd</sup> of December 1924, goes into more detail of the costumes which they wore: “K. Jokes a lot and even dances every night. A very modern type of scholar” (see Annexure B for the original Dutch).<sup>91</sup> The delegation onboard the ship from Southampton to Cape Town included Professor Edwin Kemmerer, Dr Gerhard Vissering and Mr John James Innes Middleton, the Sub-Secretary of the Treasury of the Union of South Africa. All of these gentlemen were engaged by the South African government to advise on the currency problem at hand.

Of course, all human beings are complex and Kemmerer’s racism and anti-Semitism were, first of all, a product of their time and place and also not without counter-examples. Kemmerer made a donation of \$2.00 to the American Civil Liberties Union, which was acknowledged by them on

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<sup>90</sup> Kemmerer Papers, Box 293, Folder 3

<sup>91</sup> Gerhard Vissering Papers, De Nederlandsche Bank, Inventory Number 23600, transcriptions from G. Vissering’s diary, 1 August 1924 – 30 January 1925.

the 9<sup>th</sup> of November 1920.<sup>92</sup> According to his unpublished autobiography, he “taught the contribution to civilization made by Semitic peoples in religion, Greeks in art and Romans in law”.<sup>93</sup>

The point here is not to diabolise Kemmerer, but to show that, in addition to the “positive” aspects of this particular nature of manliness, we can add some weaknesses including: inflexible thinking, a lack of creativity and rigidity in applying principles and a lack of empathy for peoples who were not white and protestant, who bear the brunt of the economic discipline which Kemmerer and his other economic orthodox friends imposed.

With the benefit of hindsight, on monetary policy, Edwin Kemmerer was wrong and John Maynard Keynes was right. The “manly” (Rosenberg 1999:39) approach of controlling money supply, imposing on oneself the rigidity of the Gold Standard and enforcing balanced budgets became part of extending the misery of the Great Depression (Eichengreen, 1992). By contrast, if the world had listened to John Maynard Keynes in identifying the Gold Standard in the inter-war period as a “barbarous relic”, if they had followed his advice to pursue internal balance rather than external balance, as proposed in his *Tract in Monetary Reform* (1923), if they had taken his flexible, creative and empathetic approach, the misery of the Great Depression and its impact on the real economy and real people’s lives could have been so much shorter. In hindsight, the “dandy” approach was preferable to the “manly” one.

Before we go on to examine the workings of the Kemmerer-Vissering Commission, perhaps now is a good time to address perceptions of undue haste and lack of deliberation by monetary policy commissioners, from two classic academic texts. Arndt (1928: 427-429) uses the voice of Strakosch’s adversary, Samuel Evans, to describe the power that Strakosch wielded when drafting the Currency and Banking Act of 1920. In fairness to Arndt (1928), he curiously does not deal in any depth with the Kemmerer –Vissering Commission as far as its main function was concerned, namely the question of South Africa’s resumption of the Gold Standard, independently of Britain. Hence it is only possible to note that Arndt (1928) is critical of

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<sup>92</sup> Kemmerer Papers, Box 35, Folder 6

<sup>93</sup> Kemmerer Papers, Box 277, Folder 5

Strakosch's huge influence and silent in the face of the huge influence of Kemmerer. De Kock (1954) is much more blatant in his political bias. De Kock notes that "the government also decided to seek further advice and invited Mr. (later Sir) Henry Strakosch, a London expert on foreign exchange, to come to South Africa... Mr. Strakosch accepted the invitation and his appearance on the scene proved to be an event of considerable significance" (De Kock; 1954: 13). Strakosch's role is then told by De Kock through the voice of his major critic, Samuel Evans, giving considerable space to the counter-argument.<sup>94</sup> On the other hand, when dealing with the Kemmerer-Vissering Commission, De Kock (1954: 67-78) allows the commissioners to speak for themselves this time and even deals with the criticisms of the commission through the voices of the commission. De Kock notes the haste which had been shown in drawing up the Currency and Banking Act of 1920 that "there was more merit in the criticism that the Act had been drawn up in undue haste" (De Kock; 1954: 34). In dealing with the Kemmerer – Vissering report which was also rammed through with great haste, De Kock notes "this prompt adoption of the recommendations of Doctors Kemmerer and Vissering did not appear to have taken the country by surprise, as most people were agreed that South Africa should get back to gold at the earliest possible moment" (De Kock; 1954: 77).

If De Kock, writing from the benefit of hindsight in 1954, was an impartial historian, he may have ended his chapter on the Kemmerer – Vissering Commission by noting that its policy recommendation, adopted by the Pact Government, was a mistake and led to unnecessary economic hardship as the National Party stubbornly stuck to the policy which it recommended. De Kock fails to do this and instead ends the chapter noting that "the question of South Africa's ability to remain on the Gold Standard independently of Great Britain, about which there had been so much difference of opinion, was not settled by the test of actual experience at this stage, as Great Britain returned to the Gold Standard before the Union did" (De Kock; 1954: 78). Given the hardship which the productive forces, particularly in agriculture, suffered as a result of the stubborn adherence to this faulty policy, particularly in the period after Britain was forced off the Gold Standard in 1931 until the similar fate of South Africa in 1932/33, De Kock's inability to acknowledge the ultimate failure of the Gold Standard makes it difficult not to accuse him of

poor scholarship resulting from political bias. In fairness to De Kock (1954), his father, Dr. M.H. De Kock, was Deputy Governor of the Reserve Bank in 1932, at the time that the Gold Standard crisis came to a head, and a supporter of the Gold Standard at the time. Dr. M. H. De Kock was also Governor of the South African Reserve Bank in 1954, at the time that Dr. Gerhard De Kock (1954) was writing. Hence it is understandable that a son would want to refrain from criticizing his father's policy position in 1932, a father who was still in a position of monetary authority at the time of writing in 1954.

### **5.10 Kemmerer Relationship with the Fed and the Bank of England**

Kemmerer describes a European holiday which he undertook with his wife and children in 1914. After visiting Germany, a country which his children did not enjoy, the Kemmerer family visited Britain en route back home to the United States. Kemmerer used the opportunity to visit the Bank of England but was denied access because the First World War had by that stage broken out. The Bank of England felt that he might be a security risk "because of his German surname and the fact that he had just spent time in Germany."<sup>95</sup>

By his own admission, Kemmerer vowed not to visit the Bank of England again and, despite Montagu Norman offering him the use of the Bank of England's library as an office for the day, "I have never made a visit through the Bank of England."<sup>96</sup> On a subsequent visit to the Bank of England, he does not go "through" the building, but just to the cashier on the ground floor to demand redemption of a 5 pound note<sup>97</sup> in gold in the July 1925 – 1931 period, which can also be understood as part of this grudge. This adds personal reasons to the geo-political reasons for an American monetary expert to view the Bank of England in less than friendly terms.

Although Strakosch and Kemmerer were very different in terms of background, their relationships with their respective power elites were very similar. Just as Strakosch enjoyed the full trust of Montagu Norman at the Bank of England, so too did Kemmerer enjoy the trust and confidence of Benjamin Strong, the first Governor of the Federal Reserve. Writing about

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<sup>95</sup> Kemmerer Papers - unpublished biography, box 277, folder 5, p. 97

<sup>96</sup> Kemmerer Papers - unpublished biography, box 277, folder 5, p. 98

<sup>97</sup> Kemmerer Papers - unpublished biography, box 277, folder 5, p. 98

Benjamin Strong, Turnbull observes “Many of his friends recall Mr. Strong’s habit of inviting to his house groups of people ...One of his closest associates was Professor Edwin W. Kemmerer of Princeton University, the financial expert who was also advisor on currency and banking to so many foreign countries that he was popularly known as ‘The Money Doctor’. It was the friendship of these two men that crystallized Mr. Strong’s idea of a collection of original sources for the study of foreign public finance to be located in the library of Princeton University” (Turnbull; 1952: 7).

Evidence of the usefulness of Kemmerer to the US power elite appears as early as the 27<sup>th</sup> of July 1916, when Strong writes to Kemmerer about a newspaper which he felt was wrong in its understanding of government deposits, note issue and the operation of the gold settlement fund. Strong asks Kemmerer if he is “sufficiently interested to take a crack at then yourself?” offering to furnish him with all of the material necessary, “both as to the practical workings of the system and data and figures in support of our position”.<sup>98</sup>

Aside from Kemmerer’s close relationship with Strong at the Federal Reserve and with the State Department, he was also, at the time of the Kemmerer-Vissering commission, being paid a retainer by the financial institution Dillon, Read and Co. of New York. On the 19<sup>th</sup> of February 1925, Kemmerer wrote to Dillon Read: “I shall drop in and see you in the early future, and talk over certain matters in which we are mutually interested, particularly the situation as I found it in South Africa”.<sup>99</sup> On the 24<sup>th</sup> of February 1925, Dillon Read sent him a cheque for \$3 000.00 “in connection with the arrangement made whereby we are to have the benefit of your views in regard to foreign matters during the current year”.<sup>100</sup> Rosenberg notes that “Kemmerer, as usual, tried to interest Dillon Read in loans to South Africa after his return, but the bankers felt there would be little market for South African bonds in the United States.” (Rosenberg; 1999: 308).

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<sup>98</sup> Benjamin Strong papers, New York Federal Reserve Archives, file 1010.1

<sup>99</sup> Edwin W. Kemmerer Papers, Princeton University, Box 77.

<sup>100</sup> Edwin W. Kemmerer Papers, Princeton University, Collection MC146, Box 77.

## 5.11 Vissering's World

Gerard Vissering's background is closer to that of John Maynard Keynes and Henry Strakosch, than that of Edwin Kemmerer. He was born in Leiden on the 1<sup>st</sup> March 1865 the twelfth and last child, making him 18 years older than Keynes. Like Keynes he had an illustrious father a former Dutch Minister of Finance, Simon Vissering, (1818-1888). He completed a law degree at Leiden University from 1884 -1890 and after other positions, was made a director of Amsterdam Bank in 1900 before becoming President of the Java Bank in 1906 one of the oldest central banks in the world (Rossouw and Breytenbach; 2011), a position he held until his appointment as President of de Nederlandse Bank in 1912, a position he held until 1931. His biography at de Nederlandse Bank notes an interest in art and music as well as rowing and later sailing. Vissering never married, nor had any children. Like Keynes he was a leading figure in a declining power.

Vissering's position in the structure of the world in which he found himself is best summed up in his own words, set out in the foreword which he wrote for the Dutch version of John Maynard Keynes' *Economic Consequences of the Peace* (1919):

“The neutrals have always been in a very delicate position. It is not for them to ostentatiously take a part in any question, neither pro or against, but for them too it is of the greatest importance to be accurately informed about the great questions which after all influence all their existence”<sup>101</sup>.

Vissering did indeed make sure that he did not “ostentatiously take a part in any question, either pro or against” in his role as commissioner for the South African government 1924-1925. He was the President of the Central Bank of a relatively small “neutral” country, and left the advocacy to Kemmerer, a representative of a far from neutral emerging super-power. And yet he did in fact make sure that he was “accurately informed about the great questions” and the diary entries, letters, and memoranda of Vissering and his secretary, De Beaufort, are a very valuable record of the exercising of power by Kemmerer and the Pact government in the second half of 1924 and the beginning of 1925.

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<sup>101</sup> Gerard Vissering Papers, de Nederlandse Bank Archives, File 22629 and 22565

That said, when the Bank of England was financially embarrassed as Britain was forced off the Gold Standard in 1931, Dr. Vissering who had previously been sure that it was not for the Dutch to “ostentatiously take a part in any question, either pro or against” and had suffered from anxiety and was popping valerian when he was about to be a part of a commission which advised against the interest of the Bank of England in 1925 (see page 142), now found new courage. Vissering “felt so strongly that he descended in person upon the Bank of England with peremptory demand for full compensation” (Henry; 1963:237).

### **5.12 The Kemmerer-Vissering Commission**

Although Vissering was approached directly by the South African government months before Kemmerer, and although the National Party was clearly hoping for some sort of racial solidarity based on a shared Dutch lineage, Gerhard Vissering was not a major influence on South African monetary policy in our period (1919-1936). The same cannot be said for Professor Kemmerer. Dalgaard says “Kemmerer... had been in communication with Mr. Samuel Evans, Chairman and Managing Director of Crown Mines Limited of South Africa, an intense practical economist, as early as October 1919. Occasional letters passed between the two as Evans sought out Kemmerer’s opinions on matters relating to the question of the Gold Standard. Kemmerer replied at length to Evans’ questions but prefaced his remarks by stating ‘My lack of familiarity with South African conditions prevents me from passing judgment’ on your views. In Kemmerer’s own words, ‘My knowledge of the current situation in South Africa is very limited since I have read very little on the subject’ (Dalgaard; 1981:72-73). He usually spoke in general terms or applied his knowledge from other countries such as Mexico, in answering Evans’ enquiries.

Kemmerer’s claims of ignorance about South Africa’s monetary issues are difficult to credit, as one of his students, Mr. J. Douglas Brown wrote a paper of South African currency problems. Brown’s 82 page article “The South African Currency Problem”, dated the 3<sup>rd</sup> of May 1921, is a thorough, well-researched and in depth look at South Africa’s currency questions, which shows that Kemmerer had knowledge of South Africa’s monetary issues as early as the period 1919 –

1921<sup>102</sup>. “This paper gave a good background on currency developments and discussed at length the war-time inflation and the legislation creating the South African Reserve Bank” (Dalgaard; 1981: 72 – 73). In Evans’ letter to Kemmerer on the 5<sup>th</sup> December 1921 he specifically discusses this excellent paper by Brown<sup>103</sup>. In addition to his correspondence in late 1919 with Edwin Kemmerer, Evans also corresponded with Mr. J. Douglas Brown<sup>104</sup>. Samuel Evans’ flurry of correspondence, successfully with Edwin Kemmerer and a single missive to John Maynard Keynes, seems to have started at the time of the Gold Conference held at the Union Buildings in October of 1919. Keynes reports in a letter to Strakosch dated the 25<sup>th</sup> of October 1919 that “I had, by the way, a letter from a gentleman signing himself Samuel Evans asking my opinion on certain points. Have you any idea who he is?”<sup>105</sup>

The fact that Evans failed to develop a long term correspondence with John Maynard Keynes, is not surprising given that Keynes did not shared Evans’ rigid orthodox approach to monetary economics or support for the Gold Standard. On the other hand Evans and Kemmerer were both wedded to monetary orthodoxy, as encapsulated by the Gold Standard, and so a mutually admiring correspondence flourished. Referring to a “very interesting and informative letter” of the 13<sup>th</sup> of November 1919 from Kemmerer, Evans writes to Kemmerer on the 20<sup>th</sup> of May 1920 that he has “all along urged the government to secure impartial expert advice before attempting to deal comprehensively with the banking and currency laws of South Africa”.<sup>106</sup>

Evans’ writes to the Secretary of Finance, Mr. Farrer, dated the 14<sup>th</sup> of February 1920, “I shall be very pleased to do my best as Chairman of the committee to advise on currency and banking reform”. He notes his positive impression of Kemmerer, who he credits with changing his mind on the Commonwealth banking system after “reading recent criticism by Professor Kemmerer, the President of the National City Bank of New York, and others, on the working of the Federal Reserve system in the USA”<sup>107</sup>.

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<sup>102</sup> Kemmerer papers, Princeton University Archives, Collection MC146, Box 38, Folder 5

<sup>103</sup> Kemmerer papers, Princeton University Archives, Collection MC146, Box 216, Folder 6

<sup>104</sup> Kemmerer papers, Princeton University Archives, Collection MC146, Box 35, Folder 6

<sup>105</sup> Keynes papers L/ ST/ 118

<sup>106</sup> Kemmerer papers, Princeton University Archives, Collection MC146, Box 216, Folder 6

<sup>107</sup> Barloworld Archives/ Samuel Evans papers/ Box entitled “Politics 1899 – 1949, Reform Committee 1895, Reform Committee, Relief Funds/ Mainly Press Cuttings and Short hand notes on gold”

As we have seen from the introduction, it seems that Gerhard Vissering was being considered as a potential monetary expert, at least in 1921, by the then Smuts government. If this is the case, it is likely to have been with the blessing of the London authorities, given Smuts' policy of co-operation with London.

The (National Party and Labour Party) Pact government wasted no time, after coming to power in June of 1924, in addressing the currency issues of the Union<sup>108</sup>. The Prime Minister (Hertzog) and his Finance Minister (Havenga) were anxious to achieve as much independence from Britain as possible. Gerhard Vissering was approached, through a meeting with the Sub-Secretary of the Treasury of the Union of South Africa, Mr. John James Innes Middleton, on the 1<sup>st</sup> of August 1924.<sup>109</sup> At roughly the same time the South African government approached the United States of America's State department, which recommended Edwin Kemmerer (Rosenberg 1999:307). Samuel Evans writes to a Mr. Karl Snyder Esq. of 15 Nassau Street, New York, USA on the 17<sup>th</sup> of September 1924: "Our government are about to appoint a commission to enquire into the advisability or otherwise of resuming specie payments on July 1<sup>st</sup> next year".<sup>110</sup>

Kemmerer's correspondence at the time of his official invitation on 9<sup>th</sup> of October 1924<sup>111</sup> suggests that this invitation came as a surprise. This does not square with the research of Rosenberg (1999:307) who shows that the South African government approached the State Department of the United States of America: "Turkey, South Africa, and Ireland also requested State Department assistance in arranging for a U.S. financial advisor in the early 1920s. In each case, the motive appears to have been to receive economic advice that was independent of British interests. To all three, the State Department recommended Edwin Kemmerer. Kemmerer declined Ireland's offer in 1925, ... Kemmerer also declined the offer from Turkey in 1924... Kemmerer did accept the offer from South Africa... His mission predictably recommended a hasty return to the Gold Standard, a plan that infuriated the British, who had not yet themselves gone back to gold.... (On South Africa, see various documents...)... NADS (National Archives, Records of the State Department), RG59, 848a.51/121-131" (Rosenberg; 1999: 307).

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<sup>108</sup> Edwin W. Kemmerer Papers, Princeton University, Box 215, Folder 2

<sup>109</sup> Edwin W. Kemmerer Papers, Princeton University, Box 215, Folder 2

<sup>110</sup> Edwin W. Kemmerer Papers, Princeton University, Box 215, Folder 2

<sup>111</sup> Edwin W. Kemmerer Papers, Princeton University, Collection MC146, Box 215, Folder 1

Rosenberg does not give reasons as to why Kemmerer declined the Irish and Turkish offers, but accepted the South African one, but we can guess that, with gold flooding into American coffers, and South Africa producing well over half of the world's supply, it was of a much greater strategic importance to his government that Kemmerer should come to South Africa, rather than to Turkey or Ireland. We would suggest that it was the American institutions of state power who licensed Kemmerer as the "money doctor", and it was these institutions who suggested where he might find his patients. Rosenberg's research findings in NADS tell us that it was not the great knowledge and personal charm of Kemmerer that the Pact government were after, but rather a recommendation from the United States of America State Department.

A telegram was simultaneously sent to Vissering on the same date, but Middleton picks up a politically important omission and writes a hand-written letter to Vissering, on the letterhead of "Imperial Hotel, Aberdeen" on the 11<sup>th</sup> of October 1924: "I have just received here a copy of the Union government's telegram of October 8<sup>th</sup> to the High Commissioner and of the latter's letter to you of October the 9<sup>th</sup>. I hope you will find it possible to visit South Africa. There is an important point in the Union government's message which the High Commissioner's office has missed in writing to you. The exact wording of the message is – 'Government has decided to invite Professor Kemmerer and Doctor Vissering to visit Union and investigate question of restoring of Gold Standard by Union independent of the United Kingdom... The significant portion of the message, omitted from the letter to you, I have underlined".<sup>112</sup> Vissering replies to Middleton on the 16<sup>th</sup> of October 1924: "I have to especially thank you for giving me in your letter the exact wording of the message of the Union government. I may add that I received in the meantime an additional telegram from the High Commissioner explaining that the question on which the advice is requested is: the restoration of the Gold Standard independent of the United Kingdom".<sup>113</sup>

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<sup>112</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 32.599, Sub-Folder entitled "Zuid-Afrika – Reis van President na Zuid-Afrika", 17 November 24 – 29 Jan 25.

<sup>113</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 32.599, Sub-Folder entitled "Zuid-Afrika – Reis van President na Zuid-Afrika", 17 November 24 – 29 Jan 25.

On the 17<sup>th</sup> of October 1924, Vissering sent a telegram to Norman: “Professor Kemmerer and I are requested by government Union South Africa to visit Union and give our advice on restoration of Gold Standard stop Am of opinion that I should not refuse my co-operation to such investigation and advice stop I should be very grateful to you if you could spend a few moments for a talk about this question stop would it be convenient to you to receive me Thursday next I will then cross Batavier line Wednesday night Vissering”.<sup>114</sup> Here Vissering starts his double game, very much in line with his statement that “the neutrals have always been in the very delicate position. It is not for them to ostentatiously take part in any question, neither pro or against”. He appears to be bringing Norman into his confidence, but crucially leaves out that part of the invitation which stressed and underlined that the question to be answered was the return to the Gold Standard independent of the United Kingdom.

In a letter from Norman to Vissering dated the 20<sup>th</sup> of October 1924 and marked “private”, Norman confirms that this is the first that he has heard of the proposed commission; “The information that you intend to proceed to South Africa is entirely new to me and, of course, most important. While you are here this week I shall be anxious to bring you in touch with Sir Henry Strakosch: perhaps you know him already. He seems to have been the backbone of the currency and financial policy of the Union and he is a most useful member of the Financial Committee of the League.”<sup>115</sup> Of course Norman knows the exact position of Strakosch. Montague Norman’s papers at the Bank of England are full of correspondence addressed to third parties, which Strakosch drafted and sent to Norman for his approval, after which this correspondence was sent by Strakosch on his letterhead to these third parties. Precious little correspondence from Strakosch on monetary matters did not first pass Norman’s desk.

On the 23<sup>rd</sup> of October 1924, Vissering meets Strakosch at the library of the Bank of England. In a memorandum recording this meeting Vissering notes that it was suggested that the South African government expects to get the advice that they must not go back to the Gold Standard without England. That the government cannot take this position directly but if two independent

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<sup>114</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 32.599, Sub-Folder entitled “Zuid-Afrika – Reis van President na Zuid-Afrika”, 17 November 24 – 29 Jan 25.

<sup>115</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 32.599, Korrespondente met Mnr Norman, Governor Bank of England.

experts advise the government, the government will take such advice.<sup>116</sup> Nowhere in Vissering's memoranda of the meeting does he inform Strakosch that the commission is specifically to advise on the Union's return to the Gold Standard independently of the United Kingdom. Indeed, Norman's recollection of the meeting, as he informs Clegg in his letter of the 27<sup>th</sup> of October 1924 is "Vissering, for his own part, is all in favour of a simultaneous return to free gold, by which I mean Holland, Switzerland, as well as South Africa and Great Britain".<sup>117</sup>

Norman continues, "He had better appear to the Reserve Bank as an independent Dutchman rather than as a Dutchman introduced from London". Norman notes that "Vissering has never met Edwin Kemmerer in his life" and that, while the South African government would be loathe to receive advice from Britain, "on the other hand, an eminent Dutchman and a cranky American might give precisely the same advice as was given to the last government".<sup>118</sup> After Norman had met with Vissering he made sure that Vissering had also spoken with Otto Niemeyer of the Treasury (who Vissering, in his diary, misunderstands to be Arthur Niemeyer), (Hawtrey and others). Strakosch when writes to Clegg at the South African Reserve Bank on the 29<sup>th</sup> of October 1924: "I think Doctor Vissering as good a choice as they could have made. (Doctor Kemmerer I do not know, except that he is a protagonist of the Federal Reserve System)".<sup>119</sup>

On the 27<sup>th</sup> of October 1924, Norman writes to Clegg, his trusted ex-Chief Accountant at the Bank of England whom he recommended to his current position, that of First Governor of the South African Reserve Bank, informing Clegg that Norman was "grateful to him (Vissering) for having come straight to London and put his cards on the table".<sup>120</sup> Clegg clearly also has no idea what is coming when he writes to Norman on the 22<sup>nd</sup> of November 1924 that Edwin Kemmerer and Gerhard Vissering are "friendly disposed towards the Reserve Bank and towards yourself".<sup>121</sup> The subterfuge continues as is evident from Clegg's letter to Norman dated the 31<sup>st</sup> of December 1924 where Clegg notes to Norman that Kemmerer and Vissering are "both

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<sup>116</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600.

<sup>117</sup> Montagu Norman Papers, Bank of England, File OV37-21.

<sup>118</sup> Montagu Norman Papers, Bank of England, File OV37-21.

<sup>119</sup> Montagu Norman Papers, Bank of England, File OV37-21.

<sup>120</sup> Montagu Norman Papers, Bank of England, File OV37-21.

<sup>121</sup> Montagu Norman Papers, Bank of England, File OV37-21.

extremely pleasant men... Vissering is more silent – partly because of the language”.<sup>122</sup> From his correspondence with Keynes and Norman<sup>123</sup> it is clearly that this is not true, Vissering was thoroughly conversant in English.

Middleton continues in his role as the loyal servant of the Pact government, and trusted confidante of Vissering, when he writes to Vissering on the 21<sup>st</sup> of October 1924 informing him that “Professor Kemmerer has asked \$15 000.00 and expenses and this has been agreed to. It would be desirable to have both fees the same”. He also notes, “I don’t think City people here (London) like the idea of any of the dominions going back to gold before Great Britain”.<sup>124</sup>

Dalgaard (1981: 75) notes. “In the evening of November the 18<sup>th</sup>, the day Kemmerer’s ship arrived; the commissioners were honoured by a dinner party at the residence of Sir Henry Strakosch. Those present in addition to the American professor and the President of the Dutch Central Bank and their secretaries included Montagu Norman, Sir Edgar Walton, Commissioner for South Africa, O.E. Niemeyer, Under-Secretary for the Treasury for Great Britain, and Mr. Miller, Financial Editor for *The Times of London*. Kemmerer noted that ‘It was a delightful dinner, but everyone, with the possible exception of Sir Edgar, was anti-gold and pro-sterling for S.A. and this was especially true of Mr. Strakosch and Mr. Norman’. When Kemmerer does arrive in England from the United States, there are further meetings with Norman and Vissering, and Vissering’s diary entry of the 19<sup>th</sup> of November 1924 notes that there was general agreement to promote a gold exchange standard in South Africa.

Hence it is easy to see how Montagu Norman and other authorities in England had come to the opinion that the “eminent Dutchman” and “cranky American” meant them no harm as they sailed for South Africa on the 21<sup>st</sup> of November 1924. Certainly, Kemmerer’s “memorandum of the conversation, held at the Bank of England, between the Commissioners and the governor of the Bank of England, the 20<sup>th</sup> of November 1924” makes no mention at all of the main purpose of the Kemmerer-Vissering Commission, and instead notes rather banal and unimportant details on

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<sup>122</sup> Montagu Norman Papers, Bank of England, File OV37-21.

<sup>123</sup> Montagu Norman Papers, Bank of England, File OV37-21 and Gerard Vissering Papers, de Nederlandse Bank Archives, File 22629

<sup>124</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 32.599, Sub-Folder entitled “Zuid-Afrika – Reis van President na Zuid-Afrika”, 17 November 24 – 29 Jan 25.

the South African Reserve Bank's needing to "take a more active part in the South African banking business" and usefulness of having an "agency in London".<sup>125</sup> As Ally (1994: 126) notes: "By the time Vissering was ready to leave for South Africa, Norman was confident ... that they could rely on him to advise Hertzog's government against taking any action that would be detrimental to British interests".

Contrary to this "general agreement to promote a gold exchange standard", In his diary entry of Thursday the 20<sup>th</sup> of November 1924, Vissering notes that at 11h30 he and Kemmerer met with: "Mister Postmus, General Manager of the Nederlandsche Bank voor Zuid-Afrika<sup>126</sup>, who was very keen to give us a witness statement. We took his statement down in shorthand. His evidence is excellent: in Prof. Kemmerer's opinion the best we have had."<sup>127</sup> Given that Postmus was "very keen" to give evidence and that Kemmerer thought that his evidence was "the best we have had", suggests that Postmus took a pro-Gold Standard and anti-sterling position on the question of which monetary standard South Africa should follow. The Dutch transcriptions of Vissering's diary entries quoted from here, and their translation into English by Siegfried Keil are attached as Annexure B hereto.

Contrary to the serious discussion with Postmus, in the time allotted, in which he in all likelihood indicated his support for Kemmerer's position, this was followed by lunch with Hawtrey of the Bank of England. In this lunch Vissering notes in his diary that it was "very agreeable, but no time for any serious discussion"<sup>128</sup>.

On-board ship, Kemmerer conducted a mock interview with a Mr. Van der Hum, which can be read as Kemmerer's practicing against "the arguments he expected to hear against South Africa's return to gold" (Dalgaard; 1981: 77). The interview is by no means an open-minded approach to the question, but rather that of an advocate sparring in anticipation of the coming monetary policy battle.

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<sup>125</sup> Edwin W. Kemmerer Papers, Princeton University, Collection number MC146, Box 216, Folder 2.

<sup>126</sup> Postmus was Deputy Governor of the South African Reserve Bank in 1931 when the decision was taken not to follow the United Kingdom in the abolition of the Gold Standard, and Governor during the difficult period of 1932.

<sup>127</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

<sup>128</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

The academic work, since Dalgaard (1981), including Ally (1994), mostly repeats the story of Doctor Vissering falling ill after arriving in the Transvaal. Dalgaard (1981: 79) notes “Kemmerer noted in his diary, ‘Doctor Vissering is taking little part in the proceedings. Work is practically all falling on me. Doctor Vissering says altitude is affecting him. Fears he cannot go to Johannesburg’”. According to Dalgaard’s (1981) account Vissering’s illness kept him from going to Johannesburg for much of the commission’s work.

And yet the diary entries, in Dutch and which were not researched by Dalgaard, tell a different story.<sup>129</sup> To recap, by the time Vissering gets on-board the ship to South Africa he is perfectly aware that his colleagues at the Bank of England expect him to do their bidding in the Kemmerer-Vissering Commission and recommend the gold exchange standard. Vissering left Britain with the British monetary authorities believing that Vissering was on their side and he did nothing to disabuse them of this notion. These officials, most important of which would have been Montagu Norman, would have been important colleagues with whom he would have co-operated with on European monetary matters. On the other hand Vissering would have been made aware by now that Kemmerer had fixed ideas which ran directly contrary to what suited the Bank of England. There is no evidence of Vissering giving any indication to Kemmerer that he would oppose him on the Commission and disappoint the government of the Union of South Africa, who was paying him, and clearly expected Vissering to advise South Africa to return to the Gold Standard independent of Britain. This catch 22 position would have made any normal human being very anxious. This anxiety is patently evident in his diary entries, particularly that of the 2<sup>nd</sup> of December 1924: ““Yet I’ve never before felt so hemmed in on board. I am longing for the voyage to end; I presume my heart plays a role in this, because I often feel anxious in my heart. I will therefore have to be very careful, also when I travel in South Africa. After all, Johannesburg is at an altitude of +/- 6000 feet, about the same as St, Moritz<sup>130</sup>.”

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<sup>129</sup> In the front of the main file (File 23.600) of the Gerhard Vissering Papers at De Nederlandsche Bank, there are only two requests for information from this file, the first being from a Mr. C. De Jong, Kantoort van die Ekonomiese Raadgewer van die Eerste Minister, Uniegebou, Zuid-Afrika, dated April 1960, and the second from Bruce Dalgaard, dated the 29<sup>th</sup> of May 1975. In it Dalgaard asks for a list of files in English, given the fact that he does not speak Dutch and would therefore only be able to research the English files.

<sup>130</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

In his diary on the ship he writes that he will be declining the invitation of the Dutch Consul in Cape Town, promising that “I will have to refuse such invitations as often as possible, both for the sake of my health and for political reasons”<sup>131</sup>. On arriving in Cape Town on the 8<sup>th</sup> of December 1924, Vissering notes in his diary that he consulted

Dr. Ploos de Lint, a former rowing mate, who has established himself in Cape Town as a heart specialist. The first thing they did was invite me to two parties. I quickly consulted Dr. Lint privately. He took my pulse and advised that I certainly shouldn't do that and that I should take it easy at the beginning. He had a supply of Kerridin, which reassured me greatly. He would therefore be able to treat me, if necessary.<sup>132</sup>

Professor (retired) Lynn Gillis, previously head of Psychiatry at the University of Cape Town, informed me that Kerridin was prescribed for anxiety. On arrival in Pretoria on the 11<sup>th</sup> of December 1924, Vissering again notes in his diary

3:30: Dr. Schols, who studied in Amsterdam, comes to visit. After an examination, Dr. Schols declares that he has not found any problems, but prescribes much rest to acclimatise, as well as 3 x 20 drops of valerian straight after meals and 3 x 1 pastille of Promonta, a patented remedy to calm the nerves. Dr Schols has no objections to the work I do, but to my travelling to Johannesburg.<sup>133</sup>

On the 27<sup>th</sup> of December 1924, as Vissering is now writing up what was to be a report which pleased the nationalists in South Africa and angered the Bank of England, Vissering notes in his diary

I felt very unwell last night; I was anxious all the time and couldn't get comfortable in any position. Pulse was very high. Dr. Scholtz came at 9 o' clock, summoned by Mrs. Lorentz, didn't diagnose anything serious, but gave me a new iron tonic and made me

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<sup>131</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

<sup>132</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

<sup>133</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

take up to 35 drops of valerian. That did me a lot of good in the course of the day and my calm returned. I kept very quiet that day and slept a lot.<sup>134</sup>

With most of the work on the controversial commission done (including the interviewing of most of the witnesses), Vissering notes in his diary on the 29<sup>th</sup> of December 1924 that his condition is improving and again records symptoms of anxiety. It should be noted that there is no evidence of Vissering continuing to suffer from “altitude sickness” beyond the 29<sup>th</sup> December 1924, despite the fact that he remained in Pretoria until leaving for Cape Town by train on the 14<sup>th</sup> of January 1925. Also, the excuse of an alleged “altitude difference” between Johannesburg and Pretoria is a particularly weak medical reason to explain why Vissering was unable to examine the witnesses of the commission, a task which fell to Kemmerer. On the 5<sup>th</sup> of January 1925, Dalgaard notes that Vissering and Kemmerer “met and worked out their position. ‘We agree apparently on most points, but differ on the advisability of gold exchange standard for S.A.’ Kemmerer noted in his diary<sup>135</sup>. Vissering yielded on this point two days later – evidence of Kemmerer’s ability to accomplish his ends” (Dalgaard; 1981: 83).

I would suggest that this is a naïve analysis of what was transpiring. Perhaps a better summing up of this final meeting of the two commissioners before their report was finalised was that, Doctor Gerhard Vissering, representative of the Central Bank of a neutral country which is always “in a very delicate position”, tried to recommend the gold exchange standard which Montagu Norman was under the impression had been agreed would be recommended by Kemmerer and Vissering to the South African government. Kemmerer, not because of some magical “ability to accomplish his ends”, but rather as a representative of the emerging economic super-power that was the United States of America, for whom the maintenance of the Gold Standard involved far less sacrifice than any other country, was in a much stronger position to enforce his will. As Innes (1984), in his treatment of Sir Ernest Oppenheimer has shown, as is often the case with history, heroic descriptions of agency in individuals representing powerful organizations or countries should be taken with a pinch of salt. Vissering, racked with anxiety caused by opposing expectations, and presented with a proposal which suited the most financial

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<sup>134</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

<sup>135</sup> Edwin Kemmerer Papers, Princeton University Archives, Collection MC146, Box 284, Folder 6.

powerful nation on earth (the USA), and government of South Africa, abandoned his attempt at doing the bidding of Norman at the Bank of England.

Just after Edwin Kemmerer started interviewing witnesses in Johannesburg, Norman, was finally convinced by Benjamin Strong (Chairman of the Federal Reserve) to come to New York for two weeks, in order to hear from the American financial elite their opinion and support for Britain's return to the Gold Standard. Norman had not been in New York for two years, but managed to "slip out of Britain undetected, like a shadow in the dead of night" (Ahamed; 2009: 225). He was met on the quay by Benjamin Strong on the 28<sup>th</sup> of December 1924 and taken to Strong's new apartment "in Maguery, an elegant apartment hotel located at 40-8<sup>th</sup> and Park Avenue, insisting that Norman stays with him. Over the next two weeks, during the day and in the evenings, Norman was subject to an intense campaign by the Americans, especially by Strong and the Morgan Bankers, to get the pound back on gold as soon as possible" (Ahamed; 2009: 226-227). The fruit of this meeting was that, in exchange for an undertaking that Britain would return to the Gold Standard, the New York Federal Reserve promised \$200 million of reserves and J.P. Morgan, the investors in Ernest Oppenheimer's Anglo-American, gave "a further tentative commitment of \$300 million" (Ahamed; 2009: 228). Montagu Norman's return from New York with loan guarantees to support Britain's return to the Gold Standard, with the only condition being his remaining governor of the Bank of England.

Strong wrote a letter to Norman on the 15<sup>th</sup> of January 1925, specifically to apologise for keeping Norman cooped up and bombarding him with Americans urging Britain to return to gold. "I fear that at times I was an inconsiderate host on the one hand, in keeping you too busy, and on the other hand, in giving you no opportunity for a little recreation while here".<sup>136</sup>

On the 8<sup>th</sup> of January 1925, the drafts of the Kemmerer-Vissering report were done and the following day the report was submitted by Kemmerer to the South African government. Two days later, Montagu Norman boarded SS France in New York and returned to London. "Addis (Charles Steward Addis was a Director of the Bank of England from 1919-1931) noted in his diary 8 January 1925, 'He (Norman) has evidently swung around to an early return to the Gold

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<sup>136</sup> Benjamin Strong Papers, New York Federal Reserve, File 1116.5

Standard.’ On the 21<sup>st</sup> of January, after Norman’s report to the committee of Treasury, Addis wrote, ‘He is now as much in favour of an immediate return to the Gold Standard as previously he was against it’” (Sayers; 1976, Volume 1: 141). Kemmerer and Vissering left Pretoria for Cape Town on the 12<sup>th</sup> of January 1925, and Montagu Norman would have arrived in London approximately a week later. Just as Vissering suffered from anxiety from being caught between a rock and a hard place, so too did Montagu Norman, being effectively bullied into returning Britain to the Gold Standard at a time when it was not convenient to do so, and when the British real economy was going to suffer from this decision. For approximately the first two weeks of March 1924, Montagu Norman took himself off for a holiday in the south of France to recover from this stress. (Ahamed; 2009: 233).

Churchill, then Chancellor of the Exchequer, was by no means decided on the question of Britain’s return to the Gold Standard. With the news of the Kemmerer-Vissering report fresh in people’s, and following Norman’s conversion to the cause of an urgent return to gold, Churchill invited leading protagonists and antagonists for supper at 11 Downing Street on the 17<sup>th</sup> of March 1924. “Norman, just back from the Riviera, was not invited.” (Ahamed; 2009: 233). The “Treasury view”, supported also by the Bank of England, was represented by Niemeyer and Bradbury, and the position against the Gold Standard was represented by Keynes, and McKenna, who was Keynes’ preferred banker for the proposed South African gold selling organisation which Strakosch and Keynes hoped to form. Keynes and Reginald McKenna stressed the point that the discrepancy between British and American prices was nearer 10% than the 2.5% indicated by the exchanges, and that domestic prices would therefore have to be deflated by 10%. This would mean unemployment and an attempt at a downward adjustment of wages which would cause major industrial unrest in the heavy industries. “It was much better, therefore, to try to keep the domestic prices and nominal wage rates stable and allow the exchanges to fluctuate for the time being”. Churchill then turned to McKenna, who had occupied the position of Chancellor of the Exchequer before and asked him which decision he would make. McKenna buckled: ‘There is no escape; you have to go back; but it will be hell.’.... On the 20<sup>th</sup> of March (1924) Churchill decided to lift the gold embargo in his budget statement” (Skidelsky; 1992: 199-200).

On the 28<sup>th</sup> of January 1925, and having received the news of the Kemmerer-Vissering report, Norman writes to Clegg “Close co-operation between Central Banks will become more than ever important”. Here he shows himself to be fully aware of the point that Kindleberger (1987) and Eichengreen (1992) make about the importance of the international co-operation of central bankers and monetary authorities in difficult economic times.<sup>137</sup>

On the 18<sup>th</sup> of February 1925, Clegg replies to Norman in the most prophetic of words: “It would be, of course, most interesting to see whether Edwin Kemmerer’s theories would actually stand the strain of practice, I should prefer not to be made the corpus vile of the experiment... I think our friend Vissering was rather hustled by Kemmerer. In fact his recommendation that South Africa should go back to the absolute Gold Standard was in such glaring contrast to his attitude in Holland, that I could not help pulling his leg when he came to say goodbye to me. I said, ‘I presume, Doctor Vissering, that when you go back to Holland, you will at once take steps to fix a date for Holland’s return to gold?’ He replied, ‘Ah! That depends on the Bank of England.’”<sup>138</sup>

Keynes himself was guilty of this practice of being unfairly hard on commission of enquiry witnesses who disagreed with his position and softer on those who did. “With Montagu de P. Webb... he was a severe questioner, relentlessly pressing him on the weaknesses and inconsistencies of the arguments he presented; with most other witnesses he was a critical, detached inquirer” (Moggridge; 1992: 226). And so the pattern of Select Committee of 1920, dominated by Strakosch, was repeated in late 1924 and early 1925, only this time it Kemmerer who was the favoured adviser, and Kemmerer’s vision which was adopted by the South African government.

### **5.13 The Kemmerer-Vissering Report**

The Kemmerer-Vissering report “On the Resumption of Gold Payments by the Union of South Africa”, submitted to the government and accepted in January 1925, noted that there were two courses open to South Africa: either to adopt the Gold Standard or the sterling standard

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<sup>137</sup> Montagu Norman Papers, Bank of England Archives, File OV37-21.

<sup>138</sup> Montagu Norman Papers, Bank of England Archives, File OV37-21

(Kemmerer-Vissering report; 1925: xi). It noted that the South African pound was close to gold parity (Kemmerer-Vissering report; 1925: xii). In summarising the advantages of adopting a Gold Standard, the report noted that the advantage of a Gold Standard was a “greater stability in the value of her monetary unit, namely its purchasing power, both internal and external” (Kemmerer-Vissering report; 1925: xvii). This of course erroneously assumed South Africa’s major trading partners would be able to maintain a similar standard. Once Britain, and a great deal of the world, was forced off the Gold Standard in 1931, this condition was not met, to South Africa’s detriment.

The report goes on to mention the “greater stability in interest rates and lower level of real interest rates” under a Gold Standard and the “stability of exchange with Gold Standard countries, which are continually increasing in number” (Kemmerer-Vissering report; 1925: xviii). Both of these arguments rely on the stability of the Gold Standard as an international currency regime in order to be valid. Keynes’ concerns about the sustainability of this regime proved to be well-founded and, when the system could no longer be maintained and fell apart in 1931, these virtues quickly evaporated. As Keynes predicted, and as Eichengreen (1992) was to show, maintaining the Gold Standard, when it was no longer economically viable to do so, caused serious damage to the real economy. The reason given in the report of “Greater Confidence of Labour” was valid at the time that the report was written. Cresswell, representing the Labour Party, supported the Gold Standard and Breckenridge (1995) has shown the support for payments in gold by black mine workers. This support for “sound money” policies by unionists is not ubiquitous over time as the union leader Ernest Bevin opposed the Gold Standard in Britain as he understood the economic pain that a rigid Gold Standard could bring. The final reason given in the report in favour of a return to a Gold Standard was “a benefit to the gold industry in South Africa through encouraging by example the return of other countries to the Gold Standard”. When considering the fortunes of the mining industry in our period 1919-1936, this reason given in the report was not only untrue, but the opposite of the truth, as showed on page 49 (Feinstein; 2005:105). Also many representatives of the South African gold miners opposed the restoration of the Gold Standard, given that it would eliminate the gold price premium which the producers enjoyed in the event of an under-valued South African pound.

In arguing against the relatively competitive currency that existed prior to the restoration of the Gold Standard in 1925, Kemmerer postulates that “there is no permanent advantage to the exporter or permanent disadvantage to the importer in a high rate of exchange; and likewise there is no permanent advantage to the importer or permanent disadvantage to the exporter in a low rate of exchange” (Kemmerer-Vissering report; 1925: xix). This was not the case in India, following the British-led policy of over-valuing the rupee (Balachandran; 1997:185-189), it was also not the case in South Africa in the period 1931-1932 where agricultural exports suffered greatly from the high rate of exchange as can be seen from the significant reduction in the contribution of agriculture to total exports (Fine and Rustomjee 1996:72).

Kemmerer, like other economists overly confident of the market’s ability to stabilise itself with financial instruments, notes that “the risks incident to a fluctuating exchange can be to a large extent avoided, and in most important countries are so avoided, by the simple expedient of making forward exchange contracts” (Kemmerer-Vissering report; 1925: xx). This method assumes the ready availability and reasonable price of such forward exchange contracts in an environment where such faith in market mechanisms may be misplaced. Kemmerer goes on to note that “a few witnesses have made much of the claim that South Africa is not in a position to maintain the Gold Standard independently of Great Britain. Your commissioners have no anxiety on this point, and they are confident that, unless this country has recourse to a policy of currency and credit inflation, she will have no difficulty in maintaining gold payments after they have once been resumed” (Kemmerer-Vissering report; 1925: xxiv). On this point Kemmerer turned out to be staggeringly wrong.

Following Britain’s abandoning of the Gold Standard in 1931, South Africa did indeed fail to maintain itself on the Gold Standard and, endured unnecessary hardship by stubbornly refusing to abandon it despite the evidence that the Pact government had made a grievous error. *Time* magazine, on the 9<sup>th</sup> of January 1933, summarised Hertzog’s position with the rhyme “My viewpoint is stuck that I really don’t care very much if the land goes to hell and the empire as well, provided that Hades is Dutch!”<sup>139</sup> Hertzog did indeed take South Africa through economic hell by his folly of sticking to the Gold Standard. Kemmerer went on to argue that “gold leaves a

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<sup>139</sup> Edwin Kemmerer Papers, Princeton University Archives, Collection MC146, Box 284, Folder 6.

country usually because it is pushed out by paper money and deposit currency inflation, not because there are demands from abroad” (Kemmerer-Vissering report; 1925: xxv). Again, Kemmerer’s excessive confidence in the quantity theory of money and what would later develop into a monetarist theory, turned out to be an incorrect prediction of what was to come when gold fled South Africa at the end of 1932 and the beginning of 1933. During his testimony before Kemmerer, Gibson of Standard Bank claimed that “South Africa was threatened with the loss of gold coin under any plan which had her returning to gold independent of England”. Dalgaard (1981: 101) quotes Kemmerer’s views on the function of the Gold Standard in response: “If there is a demand here for foreign payment, you have first your big balances abroad. You draw on them and you raise your exchange rate accordingly, making the rate more and more unfavourable for imports and more and more favourable for export; then if gold goes out, your reserve balances go down, your discount rates go up, your price level tends downwards and gold soon comes to be more valuable in South Africa than elsewhere, and the overflow stops”. Aside from the relative ease that Kemmerer ascribes to readjusting the exchange rate under a Gold Standard, the whole point of which is to peg the currency to a particular quantity of gold, Kemmerer’s excessive faith in the efficacy of the bank rate to equilibrate gold flows turned out to be misplaced.

#### 5.14 **Britain Leaves the Gold Standard in 1931**

One of the consequences of rigid thinking is that crises are ignored even when the catastrophe is right on top of you. So it was with the monetary crisis of 1931. We will deal with the correspondence between Clegg and the Bank of England in some depth as it goes to the heart of the central question of this dissertation relating to the relative effect of ideas and power on monetary policy. The background to the crisis is that, following Britain’s return to the Gold Standard in 1925 at the pre-war level which, by all calculations placed sterling in a position of being over-valued, the British real economy faced severe hardship. Orthodox economic theory postulated that prices would adjust downwards, including wages. Keynes pointed out in *The Tract* that wages would not adjust as fluidly as expected and in *The General Theory* that this adjustment would come in the form of lower total income. His was very much the minority view and the vast majority of those in power, including Norman and Harvey at the Bank of England,

believed the general equilibrium orthodox theory and in the stability of the Gold Standard. Initially the imbalance caused in the British real economy as a result of the over-valuation of sterling was dealt with by way of subsidies to industry, but when the money for these ran out the ruling elite expected the adjustment to take place through reduced wages. This dogmatic expectation resulted in the General Strike of 1926. Finally, with the collapse of the Credit-Anstalt Bank in Austria which started in May 1931 (Eichengreen; 1992: 265) questions arose in the financial markets about Britain's ability to maintain the Gold Standard. And with the May Committee report published on the 31<sup>st</sup> of July 1931 revealing a budget deficit and recommending cuts in government expenditure, as well as tax increases (Kenwood and Lougheed; 1983: 206) the drain on the London exchange escalated.

On the 1<sup>st</sup> of August, the Bank of England secured a credit of £50 million from French and American banks and, at the end of August, a further £80 million. Large flows of money continued to leave the London money market totalling approximately £200 million in the two months prior to the 31<sup>st</sup> of September 1931, when legislation was finally passed, suspending the Bank of England's obligation to sell gold (Kenwood and Lougheed; 1983: 207).

### **5.15 The Governors' correspondence during the crises**

The first correspondence considered is in the spirit of the close cooperation between Clegg and the Bank of England. In a letter from Norman to Clegg dated the 1<sup>st</sup> of July 1931, Norman confesses "you can really have little idea of the times through which we have been going here lately... Austria, Hungary and Germany... went over the dam".<sup>140</sup> Following the collapse of Credit-Anstalt Bank in Austria and its obvious implications for the international monetary system, Clegg telegrams Norman on the 6<sup>th</sup> of August 1931 "I notice slight tendency on the part of mining houses to avoid holding larger sterling balances than absolutely necessary. Can you give me any private reassuring message as to the position of sterling".<sup>141</sup> On the 7<sup>th</sup> of August 1931, Harvey telegrams Clegg assuring him that "there can be no doubt as to London's ability"

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<sup>140</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

<sup>141</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

to maintain its position.<sup>142</sup> In order to relieve Harvey of any worry about the correspondence reaching the public, Clegg sends him a handwritten letter dated the 12<sup>th</sup> of August 1931 informing him that South African mining houses have been placing sterling balances with the Reserve Bank and stipulating that they must be repaid in South African currency and emphasising that he did not want to “show any hesitation in taking sterling” and hence would appreciate their advice.<sup>143</sup> This is followed up again on the 25<sup>th</sup> of August with a telegram from Clegg to Norman stating that “in view of our large sterling balances... I shall be greatly obliged by some advice as to the current position”.<sup>144</sup>

Harvey responds with a telegram to Clegg on the 27<sup>th</sup> of August 1931 assuring him that the British government will defend sterling by cutting the dole by ten percent to balance the budget and informing him confidentially of the American and French loans to support sterling. This is followed up with a further telegram two days later informing Clegg of “large credits in New York and Paris which I trust will satisfy any *Doubting Thomas*”.<sup>145</sup>

On the 2<sup>nd</sup> of September 1931, Clegg writes Harvey a handwritten letter apologising for doubting the Bank of England’s ability to maintain the Gold Standard and again, in a typed letter, on the 16<sup>th</sup> of September 1931, asks Norman, “Kindly bear me in mind if any important development occurs in the position of sterling during the next month or two”. Despite the close and cooperative relationship between Clegg and the Bank of England, the Bank of England did not give Clegg any forewarning of leaving the Gold Standard and simply announced the suspension of gold sales in a telegram to Clegg on Sunday the 20<sup>th</sup> of September 1931. Clegg writes an angry letter to Norman on the 23<sup>rd</sup> of September 1931, “To say that I was thunderstruck is to use a mild metaphor... I had taken your assurances *as my gospel* in these latter days and I have not allowed myself to think of such a thing happening as anything more than a particularly odorous nightmare”. This is followed up by a letter to Harvey dated the 21<sup>st</sup> of October 1931 in which Clegg states, “I have certainly been disappointed that we have had no guidance from you during this crisis... I realise that it has probably been impossible for you to give any information... I

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<sup>142</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

<sup>143</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

<sup>144</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

<sup>145</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

must frankly say, however, that after my two cables to you in August asking you anxiously about the position of sterling and after your three assuring replies, I never thought it possible that I could have been left without any sort of warning to meet all the disastrous consequences of a departure by Great Britain from the Gold Standard.<sup>146</sup>

It is no co-incidence that Harvey uses the language of religion, “satisfying any Doubting Thomas” in trying to enforce a traditional conventional belief in the British Gold Standard, which has turned out to be hocus-pocus. And it is no co-incidence that Clegg responds in this idiom promising to take Harvey’s false assurances as his “gospel”. The near religious belief in the Gold Standard in the 1930s turned out to be like the religion of Keynes’ England that he criticised as “tradition, convention and hocus-pocus”. It was perhaps these kinds of rigid thinking which Keynes had in mind when he dismissed the power of vested interest “not, indeed, immediately, but after a certain interval” (Keynes; 1936:383). In 1931, regardless of the will of the most powerful people in Britain, the Gold Standard failed and, as Keynes had predicted, maintaining it had done enormous damage to the British real economy.

Henry also uses the religious metaphor to describe South Africa’s stubbornness about retaining the Gold Standard after Britain, and much of the world, was forced off it in 1931. Henry (1963:236) notes that “suddenly called upon to make a crucial decision of great difficulty and complexity, South Africa decided to be true to herself and her convictions, much as a grown-up son might decide to ignore the conversion of his father to another religion, Unhappily the question at issue was not a question of faith but of financial and economic health”.

Johannes Postmus, then the Deputy Governor of the SARB, who visited Vissering in de Nederlandse Bank before his return to South Africa in 1931, was the author of a SARB statement that “there is no reason apparent to the South African Reserve bank why South Africa should go off the Gold Standard” (Henry; 163:242). Perhaps a reason could be found in the fact that the reserves of the SARB fell by half by the end of 1931 (Henry; 1963:237).

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<sup>146</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

Eichengreen notes an interesting difference between those countries whose economies who relied on their real economies, and those who were home to international financial centers. The real economy group felt the economic pain quick enough to exit the Gold Standard sooner, and those countries with large financial centers, particularly the Netherlands and Switzerland, were the last to leave the Gold Standard.

### **5.16 The insolvency of the major South African Banks in September 1931**

Two telegrams of great interest to this dissertation have, we think, escaped the attention of other writers on the subject. Johannes Postmus, by a stroke of fate, happened to be visiting the Bank of England at the time of the August/September 1931 crisis and explained to Norman the position of the South African banks. Following the collapse of the British Gold Standard and the devaluation of sterling Norman telegrams Clegg at 7.45pm. Referring to Postmus' earlier telegram Norman says "I am persuaded that the three banks mentioned in paragraphs 3 are insolvent according to the figures disclosed by Postmus. So your whole banking and financial position is in jeopardy. In order to avoid a crisis I think assistance should be given by Union Government without delay. *Before considering method or details this fact needs to be recognized.* The following day Clegg instructs his deputy to meet with the London representatives of the "two banks", probably Standard and Barclays.<sup>147</sup> The probability that the South African banking system was insolvent in September 1931, and required considerable government assistance gives support to the idea of the banking system being inherently unstable as described by Keynes in *ICF* and later by Minsky (1975 and 1986) (see section 4.5).

Contrary to the predictions of Kemmerer and bewilderingly absent from the account of Dalgaard (1981), South Africa suffered economically when it stubbornly remained on the Gold Standard after Britain, and much of the world, was forced off in 1931. "The impact on South Africa of the world-wide decline in output, employment, and prices was aggravated during the 15 months when the Union remained on the Gold Standard after the depreciation of sterling and other currencies" (Feinstein; 2005: 121-122). Evans writes to Kemmerer on the 18<sup>th</sup> of January 1932,

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<sup>147</sup> Montagu Norman Papers, Bank of England Archives, file G1/135.

describing this disastrous state of affairs, but without the slightest bit of self-reflection on the fact that his fundamentalist faith in the Gold Standard turned out to be a horrible mistake; “The heavy fall in wholesale prices in the past two years, coupled with the suspension of the Gold Standard by Britain, Australia and other countries has created a disastrous state of affairs for all South African producers for export, excepting the gold mines, and even the gold mines are severely handicapped as compared with the gold mines in Australia and other countries. The net prices our farmers receive for what they export are about 20% below the pre-war level, while their cost of production and the prices of the things they have to buy are anything from 20-50% higher than in 1910-1914”.

### **5.17 In hindsight**

Evans continues without the slightest hint of contrition, “You will probably have seen from the report of the meeting of the Transvaal Chamber of Mines, held in November last, that I have come to the conclusion that the devaluation of our currency is unavoidable... Devaluation is the only way in which the serious disparity between the cost of production and wholesale prices can be successfully remedied... I fully relies that the suspension of the Gold Standard with the intention of restoring it after the disequilibrium between prices and the cost of production has been eliminated, involves grave risks, but it appears to me that we have no choice in the matter. As things are, deflation cannot possibly be made a success”.<sup>148</sup> In a subsequent letter to Kemmerer on the 16<sup>th</sup> of January 1933, Evans now notes with approval that “the general belief is that we can come to parity with sterling within the next few days, but there is no certainty, largely because our bankers do not know exactly what to do. As far as I can judge, the views of all of them on the exchange problem are based on the balance of trade fallacy. It is true that sterling is not stabilised on the gold basis, but parity with sterling means monetary parity with nearly all the countries that buy South African products other than gold”.<sup>149</sup>

So not only does Evans set out plainly that South Africa was forced off the Gold Standard, causing tremendous damage to its real economy, just as Strakosch said it would, but in his letter

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<sup>148</sup> Edwin W. Kemmerer Papers, Princeton University, Collection number MC146, Box 217, Folder 5.

<sup>149</sup> Edwin W. Kemmerer Papers, Princeton University, Collection number MC146, Box 217, Folder 5.

of the 16<sup>th</sup> of January 1933 he now seeks to establish a de facto sterling standard, just as Strakosch suggested. It seems that Evans now admits to Kemmerer the disastrous consequences, of which Strakosch warned (see 133), of a monetary policy which he and Kemmerer so rigidly advocated.

Histories of South Africa's experience debating monetary policy in the inter-war period often fail to mention what with hindsight is now obvious:

1. That a relatively competitive currency, stabilised by official efforts to devalue it rather than to strengthen it, was demonstratively better for the real economy.
2. That South Africa's return to the Gold Standard independent of Britain, the country with which she conducted 70% of her foreign trade, was unsustainable and a monetary policy aimed at maintaining a competitive South African currency stabilised against sterling would have been preferable.
3. That, as Eichengreen (1992) has shown, those countries which stubbornly maintained the Gold Standard after Britain and much of the world was forced off it in 1931 suffered unnecessary economic hardship which was only relieved once South Africa was forced off the Gold Standard at the end of 1932 and the beginning of 1933.

Kemmerer's faith in the Gold Standard prescription for South Africa, while benefiting the United States of America, was a failure for the Union of South Africa.

## CHAPTER SIX

### CONCLUSION

In the context of the narrative of this dissertation, what can we say about Keynes' thoughts on ideas and power: "sooner or later, it is ideas, not vested interests, which are dangerous for good or evil" (Keynes; 1936:385)

What is clear from the research is that monetary policy in South Africa in the period 1919 -1936 was about finding ideas that matched the interests of the powerful. This is the dominant process of causality in the short-term – vested interest employs the ideas which suit them. But this is not the full story over the long-term. As Fine and Rustomjee so brilliantly show, "class agencies", what we might call the will of "vested interests", do not automatically translate into economic welfare for the favoured group. We need to pay attention to "actual and potential economic linkages" (Fine and Rustomjee; 1996:144-145), or in other words, the structure of the world in which we live. Just because the powerful will it, does not mean that it springs into being.

In 1931, regardless of the will of the most powerful people in Britain, the Gold Standard failed and, as Keynes had predicted, maintaining it caused enormous damage to the British real economy. At the end of 1932, the Union was forced off the Gold Standard, and agriculture suffered much more as a result of this folly.

Despite the sermons from his pulpit, all recommending the same policy package, and regardless of the context, Kemmerer was wrong, the Gold Standard did not bring lasting stability and prosperity to the countries in which he implemented it, or his home country, the United States of America. The USA was forced off the Gold Standard in 1933.

The human desire to find models which work in the world, and in our case in the economic world, is not just about tracing the exercise of power. Bertrand Russell warned of the dangers of this tendency:

Man, formerly too humble, begins to think of himself as almost a God. ... In all this I feel a grave danger, the danger of what might be called cosmic impiety. The concept of 'truth' as something dependent upon facts largely outside human control has been one of the ways in which philosophy hitherto has inculcated the necessary element of humility. When this check upon pride is removed, a further step is taken on the road towards a certain kind of madness –the intoxication of *power* which invaded philosophy with Fichte, and to which modern men, whether philosophers or not, are prone (Russell; 1946:782) italics mine.

Economics is of course not an abstract discipline. It relies heavily on induction, on evidence from the material world. But ideals derived from induction have their own set of challenges. In Economics and Economic History, we as humans try to find in the presenting data, ideas (models) which explain our complex reality.

Whether by induction or deduction, when the ideas which the powerful hold do not align with the reality of the world in which they live, they will eventually be forced to face the fallibility of their thinking. Holding onto ideas which have been shown to be outdated is something of which rigid religion has been guilty. This “tradition, convention and hocus-pocus” is something which the atheist Keynes resisted all his life, both in personal and social matters and in Economics.

The final three sentences of the *General Theory* read as follows:

I am sure that the power of vested interests is vastly exaggerated compared with the gradual encroachment of ideas. Not, indeed, immediately, but after a certain interval; for in the field of economic and political philosophy there are not many who are influenced by new theories after they are twenty-five or thirty years of age, so that the ideas which civil servants and politicians and even agitators apply to current events are not likely to be the newest. But, soon or late, it is ideas, not vested interests, which are dangerous for good or evil (Keynes; 1936:384).

As Fetter has shown, the period 1870 – 1900 in Britain was one in which little debate on monetary policy occurred. It was a period in which British domination of the economic world was at its height, and serious challenges to Quantity Theory and the Gold Standard were almost non-existent. Given that experts and decision-makers would have been in universities studying the world of 1870-1900, it is no wonder that they were so ill-equipped to consider alternatives, when their economic world was falling apart in our period (1919-1936).<sup>150</sup>

Today we have an equally ill-prepared group in power, in finance, government and other corporations. Let us take 2008 as our year of focus. Those in power in 2008, at least in their mid-forties and probably older, would have been in “leading” universities by no later than the early 1980s. The economic world that they would have looked at to build their models would have been that of 1950 until 1980. Thus, they would have taken for granted the herculean effort of the previous generation, led by Keynes in ideas and Franklin D. Roosevelt in policy, to stabilise the chaos of the previous era of unregulated capitalism. Taking the stabilising force of the state for granted, they would have focused on the problems of stagflation and the desire to deregulate. By the mid-1980s, they would not have been taught Keynes, let alone Marx.

So when the entire financial system of the United States collapsed in 2008, those in power were left without a model to explain what had happened. As Skidelsky argues, the fundamental cause of the crisis was the models taught and not taught in the Economics departments of “leading” universities (Skidelsky; 2009:28-51). These departments trained the power elite of 2008 and were as bereft of understanding as their illustrious ex-students. After all, Minsky had died in obscurity, his books unread until the crisis of 2008.

Part of the fascination of the subject and period of this dissertation are the many similarities with our current era. Both periods involved great monetary disturbances. In both periods, currency and banking systems were either threatened with collapse, or did collapse. Both were periods in which a declining world power worked hard to maintain the dominance of its financial sector, after it had long since lost dominance of the real economy; Britain in our period and America in

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<sup>150</sup> This was not the case in the United States of America, where William Jennings Bryan was the Democratic Party candidate for the presidency of the United States in 1896, 1900 and 1908, losing each time, and making opposition to the Gold Standard and the Wall Street banks a central plank of his election manifesto.

the current era. In the period 1919-1936, Britain's primary economic interest in South Africa involved securing Witwatersrand gold for the London market.

Kemmerer, as an advocate of an international fixed Gold Standard and *laissez-faire* in international lending did not bring stability and prosperity to the (mostly Latin American) countries that he advised. After the collapse of the American loan market from 1929, these countries struggled to service their debt, and further debt was not forthcoming (Rosenberg; 1999). In the modern era, it is the Washington Consensus which claims a global Pareto efficient model. Yet, Rodrik (2003) points to the failure of the current orthodoxy favoured by international capital, just as Keynes had done in the period 1919 -1936. Rodrik shows that Asia, which by and large ignored the Washington Consensus has enjoyed much higher growth rates (Rodrik; 2003:4-8). It could be argued that the failure of Washington Consensus policies in Latin America have been a significant contributing factor to the election of Leftist governments in the region over the last decade.

It is a sad testimony to the state of economics that Sraffa and Minsky's thinking on Keynes are not the dominant ones. Decades of writing on banking, and the importance and instability of the investment function are brushed aside for a simplistic read of the *General Theory* focusing on consumption spending as the message of Keynes' writings. In our period, the divide was clearly between the real economy and finance. The imperial banks prospered when parity was maintained between the nominal values of the South African Pound and the British Pound. When the South African pound devalued, the mining and agricultural sector prospered and the banks suffered.

From 1919 to 1936, the voices of "sound money" were more numerous and vocal than those concerned for the economic health of the real (productive) economy. Thanks to Strakosch, the real economy benefited from monetary policy in the period 1920-1924. Thanks to Kemmerer, the South African real economy suffered in 1931-1932, but recovered once this "sound money" fanaticism could no longer be maintained.

In this period, rigid monetary orthodoxy was finally destroyed because it no longer worked, and South Africa was driven from the Gold Standard and forced to repair its real economy. It was a time of turmoil, and one in which Keynes, when challenged on his fluid thoughts, was to retort: “When the facts change, I change my mind. What Sir do you do?” It turned out to be THE operative question.

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## Annexure "A" - Primary source archival research conducted by major writers on the subject

	This dissertation	Russel Ally <i>Gold and Empire</i>	EHD Arndt <i>Banking and Currency Development in South Africa 1652 - 1927</i>	G. Balachandaran <i>John Bullion's Empire</i>	Bruce Dalgaard <i>South Africa's Impact On Britain's Return to Gold 1925</i>	Emily S Rosenberg <i>Financial Missionaries to the World</i>	Stephen Gelb <sup>1</sup> <i>The Origins of the South African Reserve Bank 1914-1920</i>
Bank of England Archives London	√	√		√			
Public Record Office Q		√	√	√		√	
Rothschild Archives London		√					
Central Archive Depot (now the National Archives)	√	√	√				√
Princeton University Archives	√				√	√	
New York Federal Reserve Archives	√			√	√	√	
John Maynard Keynes Papers	√						
Kings College Archives Cambridge University							
Churchill Archive Churchill College Cambridge University	√			√			
Barloworld Archives	√						
Bloemfontein Archives			√				
Cape Town Archives			√				
Indian Office Library and Records London				√			
National Archives and Records Administration Washington DC				√			
National Archives of India New Delhi				√			
Neru Memorial Museum and Archives New Delhi							
School of Oriental and African Studies London				√			
South Asia Centre Cambridge				√			
University Library Cambridge				√			
William Cullian Library Wits University	√						
Nederlandse Bank	√				√		
Library of Congress						√	
Dillon Reed Archives New York						√	
Standard Bank Archives							√
Lionel Phillips Correspondence							√
Secretary for Finance Files							

Barry Eichengreen *Gold Fetters* - not stated  
 Liaquat Ahamed *Lords of Finance* - not stated  
 Brian Kantor *The Evolution of Monetary Policy in South Africa* - not stated  
 Andrew Boyle *Norman Montagu* - not stated  
 M.H. De Kock *The Economic History of South Africa* - not stated  
 Charles Kindleberger *The World in Depression 1929 - 1939* - not stated  
 J.A. Henry *The First Hundred Years of the Standard Bank* - not stated  
 Sir Julian Crossley and John Blandford *The DCO Story* - not stated  
*A Banking Century- Barclay's Bank (Dominion, Colonial and Overseas) 1836-1936* (Author undeclared) - not stated  
 S.E. Harris *Monetary Problems of the British Empire* - not stated  
 R.S. Sayers *The Bank of England 1891 - 1944* - not stated  
 R.F. Harrod *The Life of John Maynard Keynes* - not stated  
 Robert Skidelsky *John Maynard Keynes-Hopes Betrayed 1883 - 1920* - not stated  
 John Maynard Keynes *The Economist as Saviour 1920-1937* - not stated

<sup>1</sup> Gelb does not separately state his bibliography in the copy of his article which I have, however it does seem probable that he did not have access to primary source material in Britain.

**Annexure B – Dutch/ English Translation of the diary of Gerard Vissering undertaken by Siegfried Keil.**

In his diary entry of Thursday the 20<sup>th</sup> of November 1924, Vissering notes:

<p>“11.30 uur de heer Postmus, General Manager van de Nederlandsche Bank voor Zuid-Afrika, die er zeer op gesteld was zijn getuigen voor ons to brengen. Wij nemen zijne verklaringen stenografisc op. Zijn evidence is uitmuntend; volgens professor Kemmerer’s meening de beste die wij gehad hebben.</p> <p>Wij lunchen bij Mr. en Mrs. Hirst, alwaar ook Mr. Hawtrey van de Treasury is. Zeer genoeglijk, maar voor een ernstige discussie geen tijd.”</p>	<p>“11.30: Mister Postmus, General Manager of the Nederlandsche Bank voor Zuid-Afrika, who was very keen to give us a witness statement. We took his statement down in shorthand. His evidence is excellent: in Prof. Kemmerer’s opinion the best we have had.</p> <p>We have lunch at Mr. and Mrs. Hirst’s, and Mr. Hawtrey from the Treasury is also there. Very agreeable, but no time for any serious discussion.”</p>
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Vissering notes in his diary entries 27 November – 2 December:

<p>“Het gezelschap, met Professor Kemmerer en den heer Middleton, blijft zeer aangenaam. K. is vol grappen en danst zelfs iederen avond. Wel een modern geleerde. In zijne zakelijke opmerkingen is hij zeer goed, duidelijk, niet opdringerig; hij is vatbaar voor argumentatie tegen zijne meening in.”<sup>1</sup></p>	<p>“Prof. Kemmerer and Mr. Middleton remain very enjoyable company. K. Jokes a lot and even dances every night. A very modern type of scholar. His professional comments are very good, clear, not aggressive; he is open to arguments against his own opinion.”<sup>2</sup></p>
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Vissering notes in his diary entry of the 2<sup>nd</sup> of December 1924:

<p>“Toch heb ik mij nog nimmer zoo beklemd gevoeld aan boord. Ik verlang naar het einde van de zeereis; vermoedelijk speelt daarbij</p>	<p>“Yet I’ve never before felt so hemmed in on board. I am longing for the voyage to end; I presume my heart plays a role in this,</p>
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<sup>1</sup> Gerard Vissering papers, de Nederlandse Bank Archives, file 22058

<sup>2</sup> Gerard Vissering papers, de Nederlandse Bank Archives, file 22058

<p>het hart een rol, daar ik mij op mijn hart dikwijls beklemd gevoel. Ik zal daarom heel voorzichtig moeten zijn, ook met het reizen in Zuid-Afrika. Johannesburg toch ligt op +/- 6000 voet hoogte, dat is ongeveer St. Moritz.</p>	<p>because I often feel anxious in my heart. I will therefore have to be very careful, also when I travel in South Africa. After all, Johannesburg is at an altitude of +/- 6000 feet, about the same as St, Moritz.</p>
<p>Ik ontving een telegram van den heer Groenman, Nederlandsch Consul te Kaapstad, om bij hem to logeeren en van 8-10 December de Hollandsche bijeenkomst bij te wonen. Daar wij onmiddellijk moesten doorgaan naar Pretoria, had ik goede aanleiding om te bedanken. Ik zal dergelijke invitaties zoo veel mogelijk afwijzen, èn om de gezondheid èn om politieke redenen. Ik kom niet als Hollander in Afrika maar als technicus, en zal mij alleen daarnaar gedragen”.<sup>3</sup></p>	<p>I received a telegram from Mr. Groenman, the Dutch Consul in Cape Town, inviting me to stay with him and to attend the Dutch gathering from 8-10 December. Since we had to travel on to Pretoria immediately, I had a good reason to decline. I will have to refuse such invitations as often as possible, both for the sake of my health and for political reasons. I haven't come to Africa as a Dutch national, but as a specialist, and my behaviour will be guided only by that.”<sup>4</sup></p>

On arriving in Cape Town on the 8<sup>th</sup> of December 1924, Vissering notes in his diary,

<p>“...Vertegenwoordiger van de Nederlandsche Bank voor Zuid-Afrika, en dr. Ploos de Lint, een vroegere roeimakker, die zich te Kaapstad als specialist in hartziekten heeft gevestigd. Zij begonnen mij dadelijk voor twee feestelijke bijeenkomsten uit te noodigen. Ik consulteerde even dr. Lint afzonderlijk, en die verklaarde na polsopneming dat ik dat zeker niet moest doen en heel kalm moest beginnen. Hij had Kerridin in voorraad. Dat geeft eene groote</p>	<p>“... Representative of the Nederlandsche Bank voor Zuid-Afrika, and Dr. Ploos de Lint, a former rowing mate, who has established himself in Cape Town as a heart specialist. The first thing they did was invite me to two parties. I quickly consulted dr. Lint privately. He took my pulse and advised that I certainly shouldn't do that and that I should take it easy at the beginning. He had a supply of Kerridin, which reassured me greatly. He would therefore be able to treat me, if</p>
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<sup>3</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

<sup>4</sup> Gerhard Vissering Papers, De Nederlandsche Bank, File 23.600

geruststelling. Hij kon mij dus, indien noodig, behandelen”.	necessary.”
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On arrival in Pretoria on the 11<sup>th</sup> of December 1924, Vissering again notes in his diary

“3:30 bezoek bij mij van Dr. Schols, gestudeerd hebbende in Amsterdam. Na onderzoek verklaart Dr. Schols geen bezwaren te hebben gevonden, doch schrijft veel rust voor acclimatisatie voor, en valeriaan 3 x 20 dr. direct na de maaltijd en 3 x 1 pastille Promonta, patentgeneesmiddel voor kalmeering zenuwen. Dr Schols heeft geen bezwaar tegen mijn werk, maar wèl tegen mijn gaan naar Johannesburg.”	“3:30: Dr. Schols, who studied in Amsterdam, comes to visit. After an examination, Dr. Schols declares that he has not found any problems, but prescribes much rest to acclimatise, as well as 3 x 20 drops of valerian straight after meals and 3 x 1 pastille of Promonta, a patented remedy to calm the nerves. Dr Schols has no objections to the work I do, but to my travelling to Johannesburg.”
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On the 18<sup>th</sup> of December 1924, Vissering notes in his diary

“Des middags Dr. Schols gehad die zeer tevreden was en mij veel beter bevond dan een week geleden. Hij had niet het minste bezwaar dat ik mijn werk voortzet. Hij verklaarde dat ik geen hartkwaal had, maar dat mijn hart door veel werk en vermoeienis wat zwak was. Door hieraan wat toe te geven, door rusten en veel in de open lucht zijn, kan ik aan dat kleine inconvenient zeer goed tegemoet komen. Hij had geen bezwaar dat ik naar Indië zou gaan”.	“Dr. Schols came to visit in the afternoon and was very satisfied, finding me much better than a week earlier. He had no objection at all to my continuing to work. He declared that I was not suffering from heart disease, but that my heart was a little weak as a result of working a lot and exhaustion. By being mindful of this condition, by resting and spending a lot of time in the fresh air, I could easily do something about this small inconvenience. He had no objections to my going to India.”
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On the 27<sup>th</sup> of December 1924, as Vissering is now writing up what was to be a report which pleased the nationalists in South Africa and angered the Bank of England, Vissering notes in his diary

<p>“Ik gevoelde mij dezen dag niet lekker. Had ‘s morgens een pols van meer dan 100 slagen. Na medicijnen genomen te hebben (Valeriaan) teruggang tot 86 slagen. Dat gaf verademing. Ik gevoel toch dat ik op de grens van mijn kunnen ben ik zal wat moeten inbinden.”</p>	<p>“I didn’t feel well today. Had a pulse of over 100 in the morning. After taking medication (valerian) it went down to 86 beats. That provided some relief. I feel I have reached the limit of my capabilities and have to restrain myself a little.”</p>
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and on the 28<sup>th</sup> of December 1924 he notes:

<p>“Ik ben dezen nacht erg onlekker geweest; was voortdurend benauwd en kon op geen zijde liggen blijven. Puls was weer frequent. Dr. Scholtz op 9 uur, door Mevrouw Lorentz geroepen, constateerde niets ernstigs, maar geeft mij een nieuw ijzertonicum en laat mij tot 35 dr. valeriaan nemen. In den loop van den dag doet dat veel goed en de rust keert weer. Ik heb mij dien dag heel rustig gehouden en veel geslapen.”</p>	<p>“I felt very unwell last night; I was anxious all the time and couldn’t get comfortable in any position. Pulse was very high. Dr. Scholtz came at 9 o’ clock, summoned by Mrs. Lorentz, didn’t diagnose anything serious, but gave me a new iron tonic and made me take up to 35 drops of valerian. That did me a lot of good in the course of the day and my calm returned. I kept very quiet that day and slept a lot.”</p>
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With most of the work on the controversial commission done (including the interviewing of most of the witnesses), Vissering notes in his diary on the 29<sup>th</sup> of December 1924:

<p>“Om 5 uur kom Dokter Scholtz. Constateert dat mijn toestand veel beter is. Op mijn verzoek expliciteert hij aldus mijn toestand: door doorlopende oververmoeienis heb ik een telkens opkomende anemie in de hersenen. Mijn hart is goed, mankeert niets, maar is feitelijk niet groot en sterk genoeg voor mijn grootte lichaam, en is nu momenteel niet in staat voldoende tegen die anemie in te pompen. Vandaar die gevoelens van onmacht en van pols-frequentie, die zoo</p>	<p>“Dr. Scholtz comes at 5 o’ clock. Finds my condition much improved. At my request, he explains my condition as follows: as a result of constantly being overtired, I have recurring anaemia in the brain. My heart is well, nothing wrong with it, but is actually not large or strong enough for my body size, so it is currently unable to pump enough to compensate for the anaemia. Hence the feelings of fainting and the high pulse rate, which make me feel uncomfortable and thus</p>
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<p>onaangenaam aandoen en zulk eene onzekerheid, beklemming en bijna vrees tevoorschijn reopen. Door rust en minder werken kan dat overwonnen worden, en tijdelijk door tonica. Overigens bevindt Dr. Scholtz niets ernstigs, geen afwijkingen aan het hart. Hij heeft dan ook geen bezwaar dat ik naar Indië ga, maar dringt aan op veel rust en minder inspanning van werk. Ook geregeld beweging. Ik gevoel mij hierdoor reeds veel beter”.</p>	<p>cause insecurity, anxiety and almost fear. This can be resolved by resting and by working less, and temporarily by taking a tonic. Other than that, Dr. Scholtz has not diagnosed anything serious, nothing abnormal about the heart. He has no objections to my going to India either, but insists that I must rest a lot and reduce the pressure of work. Also regular exercise. This is already making me feel a lot better.”</p>
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