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PART I

THE PATHS OF ECONOMIC CHANGE

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CHAPTER I

THE CLIMATE OF ECONOMIC
EXPECTATIONS

In the 'sixties and early 'seventies of last century, the British economy was one of the fastest growing in the world.¹ Conditions were unusually favourable at that time in all of its great departments, in agriculture, industry, transport and foreign trade, for an exceptionally wide and rapid advance in output and incomes. Between 1875 and 1914 the increase of national product and of output per head continued, although at a rate which declined sharply in the early years of the present century. When the inhabitants of the British Isles went to war in August 1914 they were, although a third more numerous than they had been in 1871, on the average of their incomes more than one third richer. This is a statistician's average. It is not intended to deny that many people were little, if at all, better off than before or that deep poverty existed upon a most serious scale. But the increase of the national income as a whole over this period was important. Under late Victorian and Edwardian conditions, it had the most immediate social and political consequences.

The continued growth of incomes in a country where population was still rising—for the United Kingdom as a whole in 1871 it was 31,484,000 persons, in 1911 45,221,000—and, no less, the remarkable fall in the rate of that economic growth which took place at the beginning of this century, a slackening which lasted through the First World War down to the 1930's, raise economic questions which require an answer. How were incomes made and how were they increased? World conditions in 1914 were clearly very different from those of 1871. How did these affect the earning of a wage, a profit, a rent, or an interest payment? The expansion of British incomes obviously went on at all times under limitations and constraints, which seem to have increased their power in the early 1900's. What was the character of those constraints and limitations? Were they internal or external to the national economy?

To try to answer these and similar questions would be out of place in a selection of documents. No collection could cover the ground nor

¹ For an international comparison, see D. C. Paige, F. T. B. Blackaby and S. Freund, 'Economic Growth: the last hundred years', *Economic Review* (National Institute of Economic and Social Research), July 1961, p. 35.

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would it be complete without statistical evidence which is more conveniently to be sought elsewhere. Neither would documents and statistics go far towards solving such problems without analysis. What will be attempted in the following chapters, in relation to agriculture, industry, foreign trade and overseas investment, is to show how the business of earning a livelihood and an income looked to those persons who for one reason or another found themselves closely connected with the organization and direction of production. For the whole movement of the highly developed industrial economy which Great Britain was running at the end of the nineteenth century depended upon the views of such men. It was a capitalistic economy, in the sense that it relied, far more exclusively in those days than now, when public investment and control of the economy have become so important, upon the investment of private capital. The willingness of those who disposed of savings to put them into production or transport or distribution or banking turned in the long run upon their hope of a profit or their fear of a loss. The movement of the economy therefore depended at any given moment on the state of men's economic expectations.

Those expectations were strikingly mobile. Perhaps the most remarkable feature of them was the swiftness with which they could change. The business world of the early 1870's lived in a state of pleasurable excitement, induced by the most powerful international investment boom that had been known for many years. A few months of financial crisis on the Continent and in the United States in 1873 sufficed to bring that mood to an end, although production continued to rise for some time. The swings of the late nineteenth-century trade cycle, from the crest of activity in 1874 to the depths of unemployed resources in 1879, from the comparative cheerfulness of 1882-3 to the gloom of 1886, broke down an unthinking confidence in the future of British industry which had been built upon the experience of twenty years of unprecedented industrial expansion. Heavy fluctuations in prices and production set men talking about depression and decline through the 1880's and 1890's, until the vigorous investment revival of the late 1890's. For many years, members of the business and professional classes referred in a general way to the period after 1873 as depressed. The last quarter of the nineteenth century was in fact, as Marshall and other economists pointed out, a time of improvement and quiet prosperity for most of the nation. The period that followed 1905 saw, on the other hand, a marked return of hopefulness and investing confidence among the same investing classes. The mass of people were finding it more difficult to live in those years before the war, as prices and the cost of living rose, unless their trade union did an unusually effective job in securing a rise of wages for them. But the memory of the late Edwardian and the first Georgian

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years which men of the business and professional classes carried into the First World War, and, if they survived, looked back to with nostalgia, was that of a prolonged and cheerful investment boom. The dismal years of the early 1890's and of the period immediately after the Boer War had been forgotten.

How are we to account for these astonishing swings of opinion, which were often swift and transient, but sometimes deep and long lasting? Contemporaries would have said that they were to be explained by what happened to the general level of prices. Certainly prices in the markets varied widely from time to time, often over a wide range of commodities. The last quarter of the nineteenth century saw a world-wide tendency of prices to fall and the years after 1896 a tendency equally general for prices to rise. These events profoundly impressed opinion both in Britain and in many other countries. For economically about this time the Western world was becoming one.

The incomes of important groups and institutions were sharply affected. In the price fall, when the market value of many farm products and of some metals was declining continuously and heavily, it was farmers and silver producers and merchants and governments with payments to make between countries which in those days used silver coins and those who used gold ones, who felt their interests to be hurt by this state of affairs. On the other hand, during the years of strongly rising prices before 1914 it was the social classes and groups whose incomes did not follow the cost of living up or did not follow it fast enough to maintain the value of their incomes who complained bitterly. General price movements gave rise therefore to a great deal of public discussion and led to much official and private inquiry. The documents in this first chapter will illustrate how strong this tendency to debate prices was in Britain, which stood at the centre of many of the most important world markets. Other documents in later chapters, for example, on farming, will show how influential at the time and, up to a point, how instructive such economic argument could be. They will also display what is perhaps difficult to understand today, the constant tendency in men's minds to connect price movements with the gold coins which were in general daily use before 1914 and to discuss general problems of the working of the economic system in terms of what was happening to the value of the precious metals. The events of a later economically far more disturbed age between the two world wars first forced British public opinion to penetrate beyond money and to think of economic processes in more consistently real terms.

Late Victorian and Edwardian business opinion was little troubled by questions about the volume of effective demand. Such questions shook the economic thinking of the 1930's, in the midst of a depression of incomes and demand more serious than anything which the nineteenth

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century knew. Perhaps the earlier age was not troubled enough, Victorian opinion was certainly prepared to tolerate an amazing waste of the national resources at regular intervals, under the impact of what it had learned to call the trade cycle. One might wonder too, with later experience in mind, whether the pressure of high prices upon the working class cost of living in the early 1900's and its effect upon the margins of expenditure of large masses of people may not have retarded the growth of those home markets as distinct from export outlets which it would have been useful for the country to possess later. But the opinion of fifty and sixty years ago was chiefly conscious, less of fluctuations and the constant changes in the economy, than of living in an age of amazing economic expansion. The rate of growth of the British economy—so far as it could be measured, and how fast it was growing was mostly a matter of popular impression—seemed only a little less impressive than that of, say, Germany and the United States, which were the two other highly industrialized countries of the day. Supporters of the reigning economic system agreed with its critics that the waste and unemployment brought by the trade cycle was lamentable. But this was generally regarded, except always by organized labour, as the price to be paid for an economic development which it was assumed must necessarily be uncertain. In any case, men were inclined to argue, was not the trade cycle much less of a curse than it had been, now that the Bank of England and the banks managed credit so much better than they used to do? There seemed little to worry about. The supreme concern of the investor was only where and how much to invest.

If we wish to understand today how the economy of 1914 grew out of that of 1870 and why it took the shape and direction that it did, we have to ask what happened to that relatively small part of the total national income which was neither consumed nor hoarded but was invested, either at home or abroad. Much of the movement of prices and much of the stir of opinion which meditated on market values was a consequence rather than a cause of the economic development which arose out of investment and the process of capital accumulation. The prime cause of growth, or of stagnation, where that occurred, lay in the decisions of the relatively few men who had savings to invest. It was they who, in building up their own capital and income, settled what the capital and the income of the nation as a whole were to be for years to come.

The major economic events of the age were therefore the product of great capital movements, the result of the consensus of investing minds. The true dimensions of these movements could only be guessed at the time, and they cannot be exactly known today. It is in these terms, of the rate of economic expansion due to capital investment and the

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relation between rates of investment in the industrial and the primary producing countries of the world, that historians would explain nowadays the late nineteenth-century price fall and the subsequent rise of world prices. It was the varying and uneven pressure upon real resources, as economic development proceeded in country after country, which was important, rather than the rate of gold output in the world's mines. The general movement of prices, however important it was to people socially and politically, was the consequence rather than the cause of these processes of fundamental economic change.

Great Britain, still in 1870 indisputably the leading manufacturing state, but yielding place by 1914 in the value of her industrial output to Germany and the U.S.A., stood very much at the centre of this world in course of transformation. Her capital history in these forty-four years was dominated by the remarkable fact that two strikingly different paths lay before her investing classes. They could invest at home or they could lend their capital overseas. Many Englishmen could not understand how other Englishmen could invest in any country but their own. Given Britain's position, however, throughout most of the nineteenth century as the centre of world trade and given the network of knowledge, personal connexions and credit established in London, the development of foreign investment was a natural step. Much investment of capital overseas was complementary to the industrial development of Britain herself. Other countries could produce the raw materials and the foodstuffs which she increasingly required. It became profitable to invest in such foreign production. Hence recurrent lending booms, when capital moved abroad, sometimes on a great scale, as in the periods 1871-4, 1886-90, and again 1905-13. These tended also to be the years of expanding commodity exports, as countries abroad increased their equipment with the aid of money raised in London. Between the capital export booms came long periods when it was home investment that was vigorous rather than foreign. Such were the years 1875-84 and 1895-1905. Home investment and foreign were to this extent both complementary and competitive with one another.

The competition between foreign and home borrowing ran, however, within strict limits, which were set not only by investment opportunities, but also by the structure of the British capital market. It would be misleading to think of the course of British economic history during this period as determined by a simple transfer of resources from home to foreign borrowers and back again¹ by the

¹ W. W. Rostow, *British Economy of the Nineteenth Century* (1948) seems to make this over-simple assumption. The importance of the distinction between the two types of investor was first pointed out, I think, by Dr C. H. Feinstein.

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decision of a single body of investors, calmly reckoning the line of maximum profit and pursuing the critical path between competing investment opportunities. The home and the foreign paths, if one may stick to that analogy, were traditional beaten tracks. They were habitually pursued by different men. Investors often moved most unwillingly outside the field of their best knowledge. The line of distinction was particularly important between those who put capital by custom and preference into home industry and agriculture on the basis of their personal knowledge, and those who did not. Home industrial and agricultural investment followed its own rules. It depended on the decisions of local men who often neither knew nor cared what foreign countries were doing or what merchant bankers in London might be offering. Foreign lending was an alternative to home investment largely as an alternative to house building, not to investment in industry. The years when foreign investment flourished at the expense of home were years when house construction in this country suffered. The early 1890's, for example, saw a house building boom, after the foreign lending of 1886-90 fell away. They were not particularly profitable years for home industry. Again, when overseas investment revived after 1905, the housing industry in some cities, such as Birmingham, felt a sharp setback. It was in this way that Great Britain took a housing shortage into the First World War which was in part the consequence of Edwardian capital export.

Industrial (including farm) investment, foreign loans and house construction formed the three dominant and interacting influences in the formation of new capital between 1870 and 1914. In the economic history of those years, there are few questions more important than this. Were the nation's savings used to best advantage? A proper answer would need to take into account all three forms of investment, for they formed the basis of the expansion of the economy. The record of their interaction, looked at cursorily, is interesting. Two phases of high total investment came at the beginning and the end of the period in the years 1870-2 and 1911-13. These were times of active capital export, fast rising prices, optimistic expectations and high employment. Something like 20 per cent of the gross national income was being invested, with home and foreign investment competing strongly for available savings. The twenty years of falling prices, 1875-96, which were also the time of recurrent complaints of depression, were a period when home and foreign investment together formed a smaller proportion of the gross national income than they did for the 1870-1914 years taken as a whole. Men became used in these twenty years to a rate of new capital formation rather lower than it could have been. Industrial investment stood up, it is true, fairly well in the decade 1873-83 when there were great developments in the steel industry.

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The gay 1890's were industrially not at all gay, at least not until after 1895. The early and middle 1890's showed the poorest investment record of all these forty-four years. The ten years 1895-1905 saw a remarkable recovery of investment. Based upon industrial expansion and city building at home, it was largely concentrated in a few years and did not last, for reasons which are still unclear.

The course of investment in farming and industry cannot be understood without going into much tiresome detail. It depended upon a multitude of conditions internal to each industry. Some of these special conditions are illustrated here, in the documents contained in chapters 2 and 3. They cover farming, mining and manufacturing industry. The outward facing side of the national economy represented by overseas trade and foreign investment and the incomes which they earned abroad come in for attention in chapter 4. Whether industrial capital was invested under monopolistic or competitive conditions bore directly on the expectations of investors. It receives some documentary treatment in chapter 5.

Capital was not all-important, even in a capitalistic age. Perhaps it never had been. In the Industrial Revolution of the eighteenth century, which laid the foundations of Britain's industrial power, the greatest productive advances had been made, not by mere accumulation of capital, but by the deliberate investment of savings in what were essentially new ideas. If technical innovation was important then, it was certainly no less so at the end of the nineteenth century. Great Britain was by this time no longer a solitary industrial state. She competed hotly for world trade with half a dozen other nations. The direction and quality of industrial investment was no less vital to her future development than its quantity. In her new and uncertain situation, an open mind to scientific ideas and a capacity to turn them to practical account were more urgent than the accumulation of capital along accepted lines. If technology had acquired a new significance, so too had management. The task of tying together the factors of production became more and more large scale and complex every year. Under the new conditions, could rule of thumb administration survive any more than the rule of thumb of the craftsman?

These aspects of the economic life of pre-1914 Britain have received much attention of late years from economists and historians. They have pointed out that, towards the end of the nineteenth century, the range of industrial techniques with which the prosperity of Victorian Britain had been identified, steam and iron and the railway, were beginning to exhaust their possibilities. The industrial future lay with new forms of power and transport and raw materials. Whether and how quickly British industry could adapt itself to a fast-changing situation was a question debated at the time, as an examination of

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some of the documents printed here will show. The pressing importance of industrial innovation was connected with another trend of the times. This was the change in Great Britain's international position. For many years she had occupied an exceptional position in the trade of the world, based in the long run on her industrial advantages. As these comparative advantages over other nations declined towards the end of the century so too did her easy dominance in commerce. The change was marked from the 'seventies onwards. New problems then began to come into sight. Where was the incentive to industrial change to come from which in the recent past had arrived so regularly in the form of overseas demand? Could the home market take its place? If so, where were the production and the new industries to come from to serve and to provoke demand from within the economy?

These questions are easier to put now than they were at the time. The basic issues were at that date obscure. Much of the interest of the history of this period lies in seeing how men approached them, by what stages, and how clarification arrived, if it came at all. In the chapters which follow, an attempt has been made to set down side by side some of the evidence concerning the state of economic expectations from time to time; some of the evidence as to what men thought was happening, at the time it happened; and some of the evidence of what appeared to have been the outcome, looking back. It is only by entering into these shifting points of view that we can, however imperfectly, appreciate the rational and the irrational elements which entered into men's expectations and understand the decisions which determined the use of the nation's resources.

Economic questions which are posed fifty, sixty and seventy years after the events to which they relate may appear to be of little human interest. To think so would be a mistake. Questions of the best use of resources take their rise and, strictly speaking, they only possess a meaning in terms of the ends which are to be served. The problem of economic welfare, i.e. what the British economy in late Victorian and Edwardian days produced in the way of incomes for the individual and the State and how far personal and communal purposes were satisfied, is the other side of the allocation of resources. It will be approached through a different range of documents in the second half of this volume. The failures and wastes of the economy—the recurrent standstill of a proportion of all resources in the trade cycle, the decline in the rate of growth of industrial investment after 1870, the depression of the 1890's—require to be considered against this general background of individual and social need. For the price of any resources which may have been wasted, the real cost of idle men and idle machines, was not transmitted to posterity. It was paid at the time, day by day and hour by hour, in the conditions of those who lived through these

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years, not least by that great number of people, the majority of the nation, who had no income to save and no savings to invest, and who never made an economic decision in that sense in the whole course of their lives.

FURTHER READING

The place of capital in British economic history and of the conditions surrounding its formation during these years have been much discussed. Many of the basic economic statistics are in B. R. Mitchell and P. Deane, *Abstract of British Historical Statistics* (1962) and P. Deane and W. A. Cole, *British Economic Growth 1688–1959* (1962). There are estimates of income and investment for the period in C. H. Feinstein, 'Income and Investment in the United Kingdom 1856–1914', *Economic Journal* (June 1961).

W. W. Rostow, *British Economy of the Nineteenth Century* (1948) began the modern discussion of the problem but also seriously oversimplified it. Compare J. Saville, 'A Comment on Professor Rostow's British Economy of the 19th Century', *Past and Present* (1954), pp. 66–81.

A. K. Cairncross, *Home and Foreign Investment 1870–1913* (1953) is indispensable for an understanding of the relation between capital accumulation and economic expansion. See also the useful sketch by J. H. Lenfant, 'Great Britain's Capital Formation 1865–1914', *Economica*, New Series, XVIII (1951), 151–68.

For the highly important influence of technical change on both capital growth and economic expansion, E. H. Phelps Brown and S. J. Handfield Jones, 'The Climacteric of the 1890's', *Oxford Economic Papers*, New Series, IV (1952), 266–307. See also, however, D. J. Coppock, 'The Climacteric of the 1890's: A Critical Note', *The Manchester School*, XXIV (1956), 1–31. The observations in the earlier chapters of A. K. Cairncross, *Factors in Economic Development* (1962) are relevant.

The other great influence on economic expansion and capital growth, the change in markets, was discussed by W. A. Lewis, *Economic Survey 1919–1939* (1949), ch. 5. See also D. J. Coppock, *ibid.*

For the problem of adaptation as a whole in the British economy in the generation before the First World War, J. Saville, 'Some Retarding Factors in the British Economy before 1914', *Yorkshire Bulletin of Economic and Social Research*, XIII (1961), 51–60.

The relation between economic expansion and price-levels came in for a good deal of attention, both at the time and later. See, for example, A. Sauerbeck, *Prices of Commodities and the Precious Metals* (1886) now available in E. M. Carus-Wilson (ed.), *Essays in Economic History*, vol. 3 (1962) and W. T. Layton, *Introduction to the Study of Prices* (1912). For a modern view, G. Maynard, *Economic Development and the Price Level* (1962).