Financial governance in historical perspective: lessons from the 1920s

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Abstract

This paper argues that the principal lesson to be drawn from an historical engagement with the evolution of financial governance during the 1920s is the crucial role played by states in reaching out and embedding financial markets within regulatory frameworks anchored by publicly sanctioned authority organized in part at the international level. In each phase of globalization from the early 19th century up to the present, public authorities have become progressively more involved in financial governance in order to make financial systems more effective, stable and efficient. The clear trend is towards more state involvement, and crucially more state involvement organized through international institutions. This is so because effective financial governance demands that public authorities exercise their responsibilities in a manner consonant with the arc of their financial institutions' transactions. Effectively organized governance requires the fusion of resources and authority at the international level. Today, like the 1920s, no single institution offers this precise combination of attributes; thus like the1920s, financial stability will continue to be frail and inadequately anchored by publicly sanctioned authority at the international level. The policy conclusion is clear: a sustained debate about how to anchor public authority in a globalized financial environment needs to be started before the next financial crisis unfolds, and this debate needs to be focused on how best to combine political authority, technical expertise and financial resources within and across the international institutions of governance.

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> "Out of the ruins of the Old World, cornerstones of the New can be seen to emerge: economic collaboration of governments *and* the liberty to organize national life at will" (Polanyi 1957: 254, italics in original).

Introduction: financial governance in history[i]

What are the central dynamics associated with financial governance today? How should we understand the historical development of financial governance, and what if any lessons do previous historical eras of financial governance hold for those preoccupied with today's issues? These are the questions which animate this paper, and they are explored within the framework of the contradictory pressures of national accountability and international capital mobility. That is, today as with the past, those who regulate financial institutions and their activities work within parameters that pull them in two often-conflicting directions. On one hand, they must strike a compromise between enforcing adequate prudential safeguards on institutions active within their jurisdictions without constraining such institutions unduly in their international activities. Here their lines of accountability are primarily national, albeit with significant international spill over effects. On the other hand, they must be wary of the trade-offs at play between maintaining satisfactory access to global financial resources for their economy without unduly amplifying its vulnerability to the external shocks that are the corollary of such openness. This trade-off has long existed, although its precise balance has shifted over time.

The principal benefit of looking at this trade-off historically is twofold: 1) to recognize and learn from the mistakes of the past; and 2) to consider parallels and discontinuities between past and present in order to better evaluate where we should be going. The inter-war period, and especially the 1920s, stands as a testament to the pitfalls of out-sourcing responsibility for the organization of the world's monetary and financial system to independent central banks. Governments digested this lesson over the 1930s and put into effect their responses in the early post-World War II years. The result was the relative subordination of central banks to governments (through ministries of finance), and of capital mobility to domestic economic considerations. John Ruggie (1982) astutely labelled this the 'compromise of embedded liberalism': after World War II, political authorities recast the power balance to privilege the stability of the national economy within the context of increased state authority, embedding international liberalism within a national welfare state.

Ruggie's famous term was itself built on the spirit of an earlier insight, developed by Karl Polanyi during the darkest days of World War II. Polanyi (1957) argued that the attempt to isolate and insulate the self-regulating market was a utopian enterprise that unsurprisingly prompted a societal countermovement – he called it a *double movement*. Fascism and socialism were political manifestations of this backlash, alongside democratic efforts to reform liberal capitalism. Polanyi's chief insight, picked up by

Ruggie, was that a new balance was being fashioned, one that refused to subordinate the national economy to international pressures. His historical narrative thus announced that the 1920s were an inherently conservative decade, while the 1930s proved to be revolutionary.

But if we examine the history of financial governance, this conclusion is suspect in at least two important ways. First, the history of the 1920s provides an example of governance innovations that confirm a powerful recurrent theme in financial governance: financial crises have always drawn public authorities further into regulatory initiatives as a significant part of the solution, and this deepened involvement hardens into a new baseline for future governance activities. Second, financial governance has increasingly acquired an international dimension that serves to anchor and support national-level financial regulation. Together, these two lessons turn part of Polanyi's insight on its head: in the world of financial governance, while it may be that markets require careful government oversight to operate on a sound and stable basis, this oversight needs to be solidly supported by an international infrastructure that bears a striking relationship to what many now call 'global governance'.

In what follows, I provide a narrative of financial governance that privileges this national/international dynamic. I then use this narrative to outline the important parallels and discontinuities between the contemporary period and the interwar era. This comparison allows me to distil three insights about the lessons we can learn from the 1920s. My principal argument is that financial governance works best when robust international institutions support strong national authorities. The trend of financial governance, in this sense, is increasingly global in scope even if it is national in execution. In terms of the future of financial governance, if it is to be adequate to the tasks set for it by the global financial system, it will need to adhere to this national/global formula. Like the world of the 1920s, states today require strong and active international institutions if they are to adequately govern internationally active financial institutions.

Financial governance and the interwar period

Defining finance, much less governance, is a complex affair. For reasons to do with the social nature of finance, I will assume for the purposes of this paper that by finance I mean financial networks, or more specifically networks of financial institutions, and that it is these which are the objects of governance. Furthermore, I will also assume that by governance I mean publicly sanctioned decision-making, whether by public or private authorities (or a combination of both). Financial governance thus refers primarily to publicly sanctioned decision-making directed towards establishing the framework of rules by which and through which financial institutions undertake and organize financial transactions within and across borders. This can be either national or international in formulation.[ii]

Historically, finance has been governed or regulated largely by national authorities. This is because the early modern roots of financial governance lie in the long drawn out struggles of competing national authorities to subject financial actors to their needs and demands (Braudel 1982; Ehrenberg 1963; de Roover 1963). But as nation-states became increasingly consolidated across Europe during the 17th to 19th centuries, and as their growing organizational capacities, self-confidence and imperial ambitions enabled them to stamp their authority on their economies and even their monies, financial institutions had ultimately to adapt to the exigencies of the new political world of modern sovereignty (Gilbert and Helleiner 1999). In short, financial systems developed in Europe under the parallel dominance of increasingly powerful *nation*-states and increasingly centralized *national* economies. The chief dynamics propelling financial governance, in other words, were national in scope (Kindleberger 1993; cf Börn 1983).

At the same time, although the modern era was dominated by the consolidation and then imperial expansion of national economies, a distinct and growing layer of economic activity could clearly be identified as global in scope by the middle of the 19th century. The most visible financial dimension of this layer of activity was associated with what Karl Polanyi (1957) identified as *hauté finance*, the internationally-oriented finance houses that comprised the pinnacle of the world's increasingly inter-linked financial systems. The activities of these finance houses – among whose number would be counted the Rothschilds of London, the Morgans of New York, Lazard Fréres of Paris and the Mendelssohns of Berlin – concentrated in a very few hands the bulk of international financial transactions, thereby centralizing the operational dynamics of the world's financial systems at the global level (Brown 1940; Börn 1983). As I have argued elsewhere, what emerged in the latter half of the 19th century was in effect a London-centered private global credit system (Germain 1997).

It was the high degree of centralization that enabled this credit system to be governed to the extent that it was. Governance worked at two levels. Most importantly, governance was exercised diffusely through the operation of a set of linked world markets mainly centered in London (Brown 1940; Williams 1963; Kindleberger 1993). London-based financial institutions organized development finance for the 19th century equivalent of 'emerging markets' on an unprecedented scale. Capital poured out of London destined for India, Australia, South America, South Africa, Canada and the US, financing the construction of railroads, ports, factories and fields (Thomas 1967). British capital also went to all manner of foreign governments to help finance their growing expenditures (Feis 1964). As a result of the dominance of London-based private financial institutions over global flows of capital, it was their practices and norms that provided the global financial system with 'governance', or what Paul Langley (2002: 27-29) calls 'world credit practices'. Global finance came to be associated with how these institutions operated, and what we would today call 'best practice' came to be symbolized by their 'gentlemanly' codes of conduct (Cassis 1987).

The second level through which governance was exercised during this time was central bank interaction. The 19th century was an era of nominally 'private' central banks, with governments conceding enormous latitude to central banks to manage the external value of national currencies relatively unconstrained by domestic political considerations. It thus fell to central banks – primarily those of the United Kingdom (UK), Germany and

France since the US did not establish its central bank until 1913 – to assist each other in their attempts to support their currencies and contain banking crises (Kindleberger 1993). This they could do precisely because of the high degree of centralization in the global financial system, with London at the apex and Paris, Berlin, Amsterdam and other Continental financial centers in a subordinate but supportive role. Central bank cooperation in this environment could work with markets because of the symbiotic relationship which these (private) banks had with other leading financial institutions (Eichengreen 1996).

But the key here was the high degree of centralization in the global financial system; without this degree of centralization central bank cooperation would have been rudderless and impotent, as was demonstrated during the turbulent interwar years. This critical point is supported by the research of Marc Flandreau (1997), who argues persuasively that central bank cooperation under the 19th century gold standard was fitful, sporadic and above all never institutionalized. Indeed, Flandreau points out that as often as not cooperation occurred in spite of the jealousies and animosities of leading central bankers, who acted on their own individual interests rather than out of a genuine sense of collective responsibility or belief on the so-called 'rules of the game'.

The highly centralized and finely calibrated pre-1914 financial system fell apart with the onset of hostilities in August 1914, with only a vestige of the old trans-Atlantic linkages surviving to fund the Allied war effort (Brown 1940). After the war, financial markets could not be seamlessly reconstructed along their pre-war lines, and the 1930s witnessed an almost total collapse of international financial transactions (Kindleberger 1973; Helleiner 1994; Germain 1997). Underlying the inability to reconstruct a global financial system was, as Kindleberger (1973) and others (eg., Block 1977; Walter 1993; Eichengreen 1996) argue, an international power vacuum in which no single state could take a leading political role to re-establish a properly functioning global economy (much less a monetary and financial system).

At the same time, as states were desperately searching for ways to reconstitute a vanished international political economy, they embarked on a number of startlingly innovative practices that were to bear fruit only after World War II. We will canvas these innovations at two levels. Nationally (or domestically), states asserted increased control over their economies as the inter-war period wore on: currency manipulation became evident, capital controls were experimented with, and trade became subject increasingly to governmental aims and objectives. Yet, it was in the international arena where the most interesting innovations occurred. International cooperation became more institutionalized, with new and untried institutions springing up to address issues associated with cooperation between states. Although these innovations had significant deficiencies, their revolutionary character should not be obscured.

national level innovations

Innovations in financial governance at the national level took three main forms: 1) in the practices associated with how governments managed their public debt; 2) in central bank operations; and 3) in jurisdictional developments. With respect to how governments managed their (growing) debt loads, innovation was largely concentrated in the types of government paper used to finance debt. In particular, in the UK and US treasury bills of various durations became very common, ushering in a period of increased government control over interest rates in the money markets. Prior to World War I, most government finances revolved around increasing revenue (until then mostly provided by customs duties and taxes levied on land, commerce and income) and issuing long-term debt. Issuing debt of widely different maturities was a startling innovation during wartime, as much for the additional revenue it raised as for the enhanced control over the money supply it promised. Both the UK Treasury and the Federal Reserve Board in the US, for example, began open market operations during the early 1920s, and this development revolutionized the way in which interest rates and liquidity within the financial system could be set and managed (Balderston 1989; Moggridge 1972; Wicker 1966). Monetary policy thus became much easier to fine tune during this period, allowing for a firmer grip to be established by state authorities on the activities of private sector financial institutions.

The second important national-level innovation concerned central bank operations. The 1920s mark the first great wave of central bank expansion in the 20th century. Many countries which had heretofore done without central banks created their own, whether due to the achievement of colonial self-government, due to the break-up of multi-national empires, or simply due to the exigencies of national development (Helleiner 2003; Flandreau, Holtfrerich and James 2003). Whatever the cause, central banks were established across much of central and eastern Europe, Latin America and Asia, and one of the chief tasks of these central banks was to establish modern standards of financial governance. For many of these countries this was an innovation of the first order.

The final national-level innovation comprised a new ‘sectoralization’ of financial governance, in which different parts of the financial system became subject to specific, often statutorily independent, regulatory agencies. This occurred most importantly in the US as a consequence of the collapse of the stock market. The speculative excesses of the 1920s in the US and the consequences of the 1929 crash led directly to the organization of government oversight over stock exchange regulation, which took the form of the Securities and Exchange Commission. The Glass-Steagall and McFadden Acts, which among other things separated investment from commercial banking, confined branch banking to state lines, and introduced deposit insurance, were also enacted during this period (Russell 2008; Garten 1997). Although these initiatives were not all replicated outside of the US, this marked the beginning of the trend towards ‘sectoralization’ within financial regulation.

In addition to these important innovations, states themselves continued to refine their objectives and mechanisms for intervening in the operation of foreign exchange and capital markets. With the suspension of currency convertibility by all of the belligerent nations at the onset of war in 1914, governments became increasingly adept at intervening in foreign exchange markets to manage their currency’s exchange rate. The tools at their disposal were sharpened considerably as the inter-war period wore on.

Particularly noteworthy was the introduction during the early-1930s of exchange stabilization funds, which confirmed the recognition by governments of a long-term commitment to managing exchange rates.[iii] Where responsibility for currencies was the almost exclusive preserve of central banks prior to 1914, it now came to be recognized as an integral responsibility of governments.

A similar recognition occurred in the area of capital account openness, where the inter-war years witnessed an intensification of government involvement in controlling and directing capital movements (Helleiner 1994; Eichengreen 1996). Governments had of course long been part of the capital movement equation (cf. Feis 1964); yet, the difference after the end of World War I was that governments became formally and explicitly involved in mediating the impact of capital mobility on their economy's financial health.[iv] This concern was deepened in light of the jarring effects of the 1931 financial crisis and the Depression, when central banks proved incapable of maintaining the post-war monetary and financial system.

international level innovations

Despite the ultimate failure of economic reconstruction efforts during the 1920s, innovations in financial governance at the national level had their counterpart at the international level. Three developments are especially noteworthy during this period: the extension of the 19th century conference system to international economic issues; the deepening of public international financial networks to help steer the global economy; and the creation of a primitive international institutional capacity to assist in the coordination and facilitation of international transactions. Together, these developments constituted the beginnings of an early public infrastructure to support financial governance at the international level. We may therefore identify them as the first hesitant steps towards the emergence of a genuinely international system of financial governance.

The first development – the extension of the 19th century conference system into the economic realm – was initially the least successful. At one level, the conferences held during the 1920s (at Brussels in 1920, Genoa in 1922 and Geneva in 1927) to chart the reestablishment of the international gold standard and restore international trade must ultimately be judged as failures, simply because the gold standard itself so clearly failed. However, perhaps the lasting importance of these conferences can be discerned in their unstated but widely accepted premise: that governments had a crucial role to play in managing international exchange rates within agreed upon rules. The revolutionary nature of this premise should not be overlooked, since the role of government in the operation of the gold standard was considered to be minimal, implicit and informal prior to the outbreak of World War I. Additionally, it was considered by many bankers to be also undesirable, since it clashed directly with the imperatives and prerogatives of central banks as they had hitherto understood their role.[v] However, with the enhanced responsibility of governments more generally in the post-1919 environment increasingly recognized (albeit not always acted upon), monetary affairs could no longer be completely hived off to independent and private central banks; governments had to become involved, even if only to establish the wider framework within which central banks could operate. The Brussels, Genoa and Geneva conferences affirmed this premise, and for this reason can be considered an institutional innovation of some importance (Pauly 1997).

We might also consider the failed London Economic conference of 1933 to fall into this category. Convened to consider an international response to the Depression, it foundered on American President Franklin Roosevelt's affirmation just prior to its commencement that any actions taken to address the parlous economic circumstances must focus on the raising of domestic prices. By privileging national over international responses to the world-wide economic crisis, Roosevelt's actions provided more weight to the growing recognition that governments had to shoulder an increased set of responsibilities for the operation of financial and monetary affairs. It was, as Barry Eichengreen (1992) rightly argues, the first necessary step to combat the deflationary consequences of the gold standard.[vi]

What these conferences all acknowledged in different ways was the increasingly important role played by governments in guiding and otherwise regulating economic activity both within and beyond their borders. It introduced the element of negotiation and bargaining over economic issues on a multilateral basis into the international realm, and by doing so set the stage for the complex negotiations that took place at Bretton Woods in 1944. Far from being abject failures, the economic conferences of this period offered important learning markers for governments, and at least part of the achievement of Bretton Woods can be traced to the lessons learned at these conferences.

Economic diplomacy, however, was only part of the process of deepening the involvement of public authorities in matters relating to financial governance. Another dimension of this process during the 1920s could be seen in the strengthening of links between European central banks and the newly established Federal Reserve Board in the US. During the early years of the Federal Reserve System, the New York Fed's first president – Benjamin Strong – worked especially hard to cement these ties. Strong had a clear grasp of the importance of the US financial system to the world's financial flows, and participated vigorously with his European counterparts – especially Montagu Norman of the Bank of England, but also Emile Moreau of the Banque de France, and eventually Hjalmar Schacht of the German Reichsbank – in facilitating cooperative monetary policies that would not undermine global financial stability (Chandler 1958; Clarke 1967; MacNeil 1986). The early successes that Strong is often credited with, however, were severely impaired by his premature death in 1928, and the onset of depression after the 1929 New York stock market crash.

Nevertheless, even the Depression, with all of its attendant contractions and inward orientations, could not sever completely the international connections and networks built up over the 1920s. Although private capital markets were for all practical purposes moribund after 1931, bankers in New York, London, Amsterdam and Paris continued to travel and meet regularly, as did government and League of Nations officials (Toniolo 2005). The search for suitable economic arrangements led both towards the development of regional solutions (such as the strengthening of the gold, dollar and sterling blocs) and towards inter-regional or perhaps better 'international' arrangements such as the Tri-Partite Agreement between France, Britain and the US in 1936, over managing the franc/sterling/dollar exchange rate (Drummond 1979). Despite the increased economic nationalism of the interwar period, financial and monetary affairs were never completely detached from an international trajectory, even if their cross-border connections struggled mightily during the 1930s.

The involvement of public authorities in the international organization of credit is also evident in the final dimension of international innovations during the interwar period: the creation of an incipient international institutional capacity to oversee or facilitate the operation of a rebuilt and refashioned postwar international economy. These included the creation of an Agent General for Reparations Payments in 1924 to oversee amended German reparations payments arising out of the Dawes Plan, the growth of an economic oversight capability within the League of Nations, and the creation of the Bank for International Settlements (BIS) in 1930. Each of these initiatives was a direct response to the vexed question of how to reconcile war debts and reparations with postwar economic and political realities, and each involved public authorities in the active management of the machinery of a growing international economic infrastructure.

The Agent General for Reparations Payments was created as an essential component of the Dawes Plan. This was the proposal by the Commission of the same name convened to find a way out of the fiasco of the French and Belgian occupation of the Ruhr consequent upon Germany's decision to discontinue reparations payments in 1922. The Dawes Plan promised to reestablish German reparations payments by floating a large international loan to be used by Germany to support its currency – which had been eviscerated by hyperinflation (Kindleberger 1993; Eichengreen 1992; McNeil 1986). The novelty of the Agent General's office lay precisely in institutionalizing a decision-making capacity to which others would have to submit, and which ideally would be insulated from the political machinations of both the French and Germans. It also required an American to serve as Agent General, and produced an intense search for an appropriate individual involving heated negotiations between governments, central bankers and especially New York financiers (Jones 1977).

The Agent General had the power to alter Germany's reparations payments in light of changing economic circumstances. This power was most pertinent to Germany, of course, but others too could and did have their expected payments changed unilaterally by Seymour Parker Gilbert, the young American who ultimately became the first Agent General. The granting of this power to the Agent General was most importantly an admission that the political decision to extract reparations needed to take into account a capacity to pay on the part of Germany, and that the victors were not entitled to make that decision unilaterally, at the expense of the vanquished. Of course, there were other important dynamics that made the creation of the Agent General's office attractive, such as the need somehow insulate the issue of reparations from the toxic effects of Franco-German rivalry, and of the pressing requirement that American private capital be made available to Europe but without American government guarantees (McNeill 1986). In terms of economic governance, however, the creation of the Agent General's office should be seen an important milestone not only in terms of assembling the required machinery to make international transactions workable, but also in terms of establishing the principal that the vulnerable or weak have an important stake in the construction of the apparatus of decision-making.

The Bank for International Settlements had a not dissimilar point of origin to the Agent General for Reparations Payments. It was part of the recommendation of the Young Plan, produced by an international commission with the mandate to break the reparations impasse that once again threatened to strangle international financial flows after 1928. The innovation of the BIS was precisely that it enabled payments to be made through a neutral third party in a manner designed to minimize upheavals in foreign exchange markets. It also had as an explicit part of its mandate the fostering of cooperative relations among the world's central banks (Simmons 1993; Toniolo 2005).

The BIS of course failed spectacularly to alter the twin trajectories of economic depression and financial chaos unleashed over the 1929-1931 period. Perhaps, as Barry Eichengreen (1992: 263-4) argues, it was doomed by American abstention and fatally undermined by being charged with *both* facilitating reparations and forging a common monetary outlook. Or, alternatively, it (along with most governments) was simply overwhelmed by the scale of the unfolding disaster.[vii] The BIS was new, untried, light on resources, and working in an environment characterized by relatively ponderous personal communications. To expect more of this new institution in such a situation might be asking more than could legitimately be demanded.

At the same time, the creation of the BIS affirmed, alongside these other developments, the importance of the international dimension of public responsibility in the face of seemingly intractable economic tensions. It was an admission by experts that cooperation requires an international institutional infrastructure beyond what markets could themselves provide; some sort of publicly sanctioned support was needed for such machinery to come into effect. We can therefore see in the creation of the BIS another step in the long road to erecting a world financial system supported by adequate public authority organized at least in part internationally. It was a small and incomplete step to be sure, but it nonetheless pointed in the right direction.

The final innovation in financial governance at the international level concerns the economic activities of the League of Nations. These were spread over a number of committees (the Economic Committee, the Financial Committee, the Economic Intelligence Unit, the Economic, Financial and Transit Department, and the Economic and Financial Organization). While the record of these committees, departments and organizations is decidedly mixed (Clavin 1996; Eichengreen 1992; Pauly 1997), their work established important principles concerning the achievement of multilateral oversight, the creation and maintenance of a necessary international machinery, and the kinds of ideas that should or ought to inform sound economic policy. Ultimately such an institutional capacity could not lead where governments and private sector forces feared to tread; yet by establishing the general utility for cooperative activity of an international institutional capacity, the economic activities of the League offered another important learning marker for governments in later years.

As the above discussion indicates, the key dynamics driving innovation in financial governance during the 1920s were both national in origin and international in delivery. Governments laboured to regain control over their finances in the face of reconstruction burdens and the commitments entailed in working to re-establish a viable system through which international payments could be conducted. They also followed international practices in terms of establishing and/or strengthening their central banks. At the same time, governments were engaged in a desperate search for international arrangements that could resolve the conundrum of inter-allied wartime debts and reparations within the context of what almost everyone thought should be a return to some form of international gold standard.

The result was an impressive series of innovations in financial governance that witnessed the creation of a quasi-supranational reparations authority, a conference system and an incipient international institutional capacity centered on the League of Nations and the Bank for International Settlements. The pre-1914 web of central bank networks was for a time strengthened with the addition of the US Federal Reserve Board (via the international activities of the New York Fed under Benjamin Strong and his successor, George Harrison). And this network spread to envelop Ministries of the Treasury in the mid-1930s under the Tri-Partite Agreement between Britain, France and the United States. In this context, much of the groundwork for the Bretton Woods negotiations had already been prepared by the innovations enacted during the inter-war period (Pauly 1997; Toniolo 2005).

Looking back from the present: discontinuities and parallels

The point of any historical comparison is to probe for similarities and differences between the past and the present. With respect to the interwar period, while the discontinuities are important, the parallels are eerily familiar. Let us examine the discontinuities first. The most important difference between the 1920s and the contemporary period is illustrated by the overwhelmingly dominance of Europe and European powers in the world's political economy. In particular, Europe provided the principal cipher or prism for financial issues, despite the significant weight of the US in world economic and monetary affairs. Today in contrast, the world's political economy is globalized, perhaps to an unprecedented extent, and for the first time might be conceived to be genuinely transnational in scope (Robinson 2004). It is the US and Asia, together with their concerns, which act as the central cipher for financial and monetary affairs.

Beyond this, it is important to note that whereas the interwar period fell prey to the shadow of war, the contemporary period is mostly free of conflict on a global scale. This is not to argue that war between major powers is unthinkable – US/China relations, India/Pakistan relations and the entire gamut of potential conflicts unleashed by 9/11 and the Bush Doctrine of pre-emptive strikes must be of concern here – only that inter-state war on a global scale is currently beyond the realm of reasoned hypothesis. One reason for this of course is the difference in the inter-state balance of power between the two periods. During the inter-war period the inter-state balance of power moved from a position of post-1919 allied dominance to one of constrained equality in the 1930s, while today the inter-state balance of power is more heavily skewed towards the apparent military, political and economic dominance of one nation-state.

At the same time, however, there are several interesting parallels between the interwar period and today in terms of the structure of financial governance. Both periods are marked by significant and ongoing change in both the actual practices associated with finance – innovations in assets and activities alongside innovations in what and how governments involve themselves in financial matters – and the underlying structural organization of financial governance. What may be identified as the practices and processes of globalization are visible in both periods, as well as shifts in the form and geography of wealth creation. In the interwar period, electrification, the internal combustion engine and fordism or mass production transformed how wealth was created, while the invention and spread of mass consumption and consumer credit spread that wealth in new and significant ways. Today, the steady onslaught of the knowledge economy together with the evolving international division of labour are transforming how wealth is being created and where and to whom it is being distributed.

Politically, both periods have seen tremendous changes in the nature of the state's involvement in economy and society, together with significant movement in the international balance of power. At the close of World War I, three empires (Russia, Germany and Austro-Hungary) had disintegrated, one (Ottoman) was teetering and two (Britain and France) had been subjected to intense strains as a result of the war. Today, we have lived through the end of the Cold War, the disintegration of the Soviet Union, the peaceful dissolution and/or creation of several states, not too mention the continued pressure on highly centralized states of all political stripes. In both periods, in other words, international political leadership is under strain and contested. Financial governance as a result takes place in a fragmented and decentralized international political environment.

But the most significant parallel lies in the powerful nature of global pressures driving forward the logic and modalities of financial governance. The key pressure here is associated with capital mobility. The coterie of pressures associated with financial liberalization – privatization, deregulation and securitization – today frame nearly all debates about financial governance, along with the conduct and behaviour of financial institutions. Financial governance is about containing, leveraging and enabling liberalization and its attendant consequences. During the interwar period this was also the case, with one important caveat: efforts to organize financial governance beyond the nation-state during the 1920s were geared towards re-establishing the conditions that would make capital more rather than less mobile, while efforts during the 1930s were geared in the reverse direction. But in both cases it was the mobility of capital that was the wellspring and chief target of policy.

This common wellspring helps to account for the peculiar global origins of major policy innovations during the inter-war period. Institutional innovations such as the Agent General for Reparations, the League's Economic and Financial Organization and the BIS were global in scope, insofar as their membership was drawn from globally-important actors and the ideas underpinning them were global in origin. Central bank cooperation during the mid-1920s spanned the Atlantic, as did the negotiations leading up to the Tri-partite Agreement of 1936, even if that arrangement reinforced rather than undermined regional developments. In short, efforts to improve financial governance responded to and reflected globally oriented dynamics during the interwar period, including the turn towards regionalism during the 1930s.

In this context perhaps the most worrying parallel between the interwar period – and especially the 1920s – and the contemporary period is precisely the reluctance of governments to support and/or extend the international infrastructure which provides such a significant bulwark to domestic initiatives to govern financial networks and activities. In the 1920s governments were determined to return to central banks the control over monetary and financial policy which they had assumed during the war. This might have been a sustainable policy if at the same time governments had provided central banks with sufficient resources to support one another during moments of crisis such as in 1931. They did not however, and furthermore complicated the mix by engaging in a form of diplomacy that reflected the strangulated state of international relations after World War I. This refusal or inability both to bring central banks fully into *national* political structures and to build an appropriate *international* infrastructure doomed the interwar period to monetary and financial turmoil. The times called for clear public governmental leadership, but none was provided.

Our knowledge about economies and financial systems is today a good deal more advanced than during the early years of the 20th century. However, the political mistakes and miscues in evidence during the interwar period are again threatening to resurface. While the threat of global war may be slight, the degree and depth of international political change cannot be underestimated. The challenge posed to the prevailing financial power structure by the rise of emerging market economies such as China, India and Russia risks complicating (at the very least) the coordination of international relations necessary to extending the international infrastructure of governance in ways demanded by the increasingly integrated nature of global financial and monetary issues. Even worse, in those governments with the greatest stake in generating sound structures of international financial governance, a predisposition to cede authority to independent central banks and parcel up the regulatory patchwork with statutorily independent organizations and committees threatens to undercut the very political support which they will need to reassert a stronger public control over global financial networks and activities. The lessons of the interwar years, it seems, have been cast into the historical abyss.

Conclusion: insights and lessons

To resuscitate the interwar years as a valuable learning marker for contemporary policy-makers, I would highlight three valuable insights we can glean from interrogating its history. The first insight must be that liberalism and all of the supposed benefits that flow from it demand a robust global public infrastructure that works to support national goals. In each phase of globalization from the early 19th century up to the present, public authorities have become progressively more involved in financial governance in order to make financial systems more effective, stable and efficient. Better financial governance has always involved more state involvement, first nationally, throughout the 19th century, and then internationally from the 1920s onwards. Effective financial governance thus demands that public authorities exercise their responsibilities in a manner consonant with the arc of their financial institutions' transactions. Since the early part of the 20th century, this has meant that financial governance has become increasingly global in scope. This insight is in line with Craig Murphy's (1994) observation that liberal internationalism requires global support for strong states, and that this support must itself draw on a clear set of linkages between the local and the global.

The second insight must be that finance, in terms of its organization and dynamics, is inherently global rather than national. Although a regional domain of finance may be identified, the dynamics that drive financial transactions and which inform financial institutions are predominantly global in scope and nature. This is in part due to the fungibility of money and credit, and in part to the array of possibilities opened up by technological innovation. But more fundamentally it arises out of the way in which credit networks have been organized historically, namely on a global rather than a national or local basis. Where these dynamics compel public authorities to respond, their response may sometimes take a regional form, but only when compatible with pre-existing global pressures. Thus the use of formal and informal imperial preferences in the 1930s as a way of insulating metropolitan economies from withering international competition, or the more recent development of EU-wide financial standards and a single currency to foster a European capital market: in both cases, however, these developments were shaped in significant ways by global pressures (Drummond 1979; Henning 1994).

The final insight is that an historical perspective on questions associated with financial governance can be part of an effective scholarly toolkit, especially where questions centering on institutions and their creation, consolidation and/or dissolution are involved. Part of the promise of pursuing an historical perspective in this regard resides in the contextualization of the problem that it provides; considering questions within an appropriate historical context provides the longitudinal frame of reference which helps to situate contemporary developments. In the case considered here, understanding the historical embeddedness of globalizing dynamics helps to account for the complementary relationship of enhanced state involvement in financial governance both nationally and internationally.

But an historical perspective can also go beyond simply providing historical context, or what has sometimes been labelled as the 'add history and stir' school (Amoore et al, 2000). It can provide a window onto unfolding and dramatic social transformations that touch the economic, political and ultimately social organization of the world. In Karl Polanyi's (1957: 4) arresting phrase, historical explanations do not provide a "convincing sequence of outstanding events, but an explanation of their trajectory in terms of human institutions". In the case of financial governance, an historical perspective provides the insight that strong national states buttressed by strong and well-embedded international institutions have historically been the most viable means of creating effective, stable and efficient governance mechanisms. The road to good financial governance, in other words, is more like a dual carriageway than a single-track road: it requires both strong and active states alongside strong and active international institutions.

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Endnotes

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[ii] The assumptions in this paragraph require a monograph to sustain. I have explored these assumptions elsewhere (Germain 2001; 2004; 2007), but it must be acknowledged that there is a lively debate about each assumption. For good overview volumes, see Andrews et al (2002), Cutler, Haufler and Porter (1999), Hall and Biersteker (2002), Hewson and Sinclair (1999) and Prakash and Hart (1999).
[iii] The UK Exchange Equalization Account was formed in 1932, while the US Exchange Stabilization Fund began operations in 1934. In the case of the UK, the EEA was used to help manage the sterling area in the 1930s (Drummond 1981). Important also, but in a different way, were the efforts made by fascist governments to control the international transactions of their citizens. In Germany's case, this resulted in the construction of an elaborate machinery to control all 'international' transactions with its central and eastern European neighbours (Neal 1979).

[iv] This concern is clearly voiced by Keynes and others about Britain's experience with the gold-exchange standard of the late 1920s (Skildesky 2003; Eichengreen 1992).
[v] Montagu Norman, Governor of the Bank of England from 1920 until 1944, was perhaps the chief exponent of this view of the relationship between central banks and governments on the question of the role and maintenance of the international gold standard (Clay 1957; see also Burn 1999).
[vi] There is a large literature on the London Conference. For decent portrayals, see Claven (1996), Eichengreen (1992) and Kindleberger (1994).
[vii] This is closer to Gianni Toniolo's (2005) argument, which is much more sympathetic than Eichengreen to the economic predicament into which the BIS was inserted in 1930.