

John Maynard Keynes and the  
'Scheme for the Rehabilitation of Europe'

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«Plano para a Reabilitação da Europa»

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This paper analyses the US rejection of the *Scheme for the Rehabilitation of Europe* proposed by John Maynard Keynes, one of the British delegates at the Paris Peace Conference in 1919.

The Great War finally ended in November of 1918, after fifty-two long months of war and more than seventeen million deaths. One outcome of the war was that "The international order had to be re-created on a new and different basis." The Peace Conference began with the aim of drawing up treaties between the dominant Allied powers and the then defeated Central Powers.

The *Scheme* proposed by Keynes is an event that allows us to better understand the various processes involved in the hegemonic rise of the US and the decline of Europe in the first place. It would have allowed stricken countries, whose credit had been temporarily shattered, to re-equip themselves and relaunch their economies based on loans guaranteed by the United States and the wealthiest countries. Furthermore, the idea of the *Scheme* carried with it a strong concept of European Union and solidarity, to be developed through economic links after the devastations of the war. These economic links, if developed, could possibly have been built into an early kind of union of European states.

**Palavras-chave:** Keynes; Europa; Conferência de Paz; solidariedade; EUA.

JOHN MAYNARD KEYNES E O  
«PLANO PARA A REABILITAÇÃO DA EUROPA»

O presente artigo analisa a rejeição pelos EUA do *Plano para a Reabilitação da Europa* proposto por John Maynard Keynes, um dos delegados britânicos na Conferência de Paz de Paris em 1919.

A Primeira Grande Guerra chegou ao fim em novembro de 1918, após cinquenta e dois longos meses de guerra e mais de dezasseis milhões de mortos. Um dos resultados da guerra foi que «foi necessário recriar a ordem internacional alicerçada numa nova e diferente base.» A Conferência de Paz teve por objetivo inicial elaborar tratados entre as Potências Aliadas dominantes e as potências centrais derrotadas.

O Plano proposto por Keynes permite-nos compreender melhor os diversos processos envolvidos na ascensão hegemónica dos EUA e no declínio europeu. O Plano teria permitido aos países afetados, cujo crédito foi temporariamente abalado, reequiparem-se e relançarem as suas economias com base em créditos garantidos pelos EUA e pelos países mais ricos.

Além disso, a abordagem do Plano baseava-se num forte conceito de União Europeia e de solidariedade, após a devastação da guerra, a desenvolver através de laços económicos, os quais, a serem desenvolvidos, poderiam eventualmente ter sido integrados numa união de estados europeus antecipada.

**Keywords:** Keynes; Europe; Peace Conference; solidarity; US.

JOHN MAYNARD KEYNES ET  
LE "SCHÉMA DE REHABILITATION DE L'EUROPE"

Cet article analyse le rejet par les États-Unis du *Plan de réhabilitation de l'Europe* proposé par John Maynard Keynes, l'un des délégués britanniques à la Conférence de la Paix de Paris en 1919.

La Grande Guerre s'est finalement achevée en novembre 1918 après cinquante-deux longs mois de guerre et plus de dix-sept millions de morts. L'un des résultats de la guerre a été que «l'ordre international a dû être recréé sur une base nouvelle et différente». La Conférence de la Paix a débuté en ayant pour objectif d'élaborer des traités entre les puissances alliées dominantes et les puissances centrales en perte de vitesse.

Le schéma proposé par Keynes est un événement qui permet de mieux comprendre les différents processus impliqués dans la montée hégémonique des États-Unis et le déclin de l'Europe au cours de la première décennie. Le Schéma aurait permis aux pays sinistrés, dont le crédit était temporairement détruit, de se rééquiper et de relancer leur économie sur la base de crédits garantis par les États-Unis et les pays les plus riches.

En outre, l'idée du programme était porteuse d'un concept fort d'Union européenne et de solidarité, après les devastations de la guerre, à développer par des liens économiques. Ces liens économiques, s'ils avaient été développés, auraient pu être intégrés dans une première forme d'union des États européens.

**Mots-clés :** Keynes ; Europe ; Conférence de la Paix ; solidarité ; États-Unis.

## Introduction

This paper analyses the US rejection of the *Scheme for the Rehabilitation of Europe* proposed by John Maynard Keynes, one of the British delegates at the Paris Peace Conference in 1919 and soon to become one of the most influential thinkers of the 20th century<sup>1</sup>.

This *Scheme* has not been studied intensively because most of the historiographical literature has focused on the Keynes's more substantial works, which achieved more obvious results, while the *Scheme* was rejected and therefore never implemented. Indeed, in her book *Peacemakers, The Paris Conference of 1919 and its Attempt to End War*, Margaret McMillan, one of the most important scholars of the Peace Conference, devoted no more than one page to the *Scheme*. In *The Versailles Settlement*, Alan Sharp wrote only a brief note: "[Keynes] as a member of Supreme Economic Council [...] prepared a plan for European reconstruction" (Sharp, 1991, p. 195).

The *Scheme* proposed by Keynes may seem to be an issue of minor historical and economic importance for the period after the Great War; however, it is an event that allows one to better understand the various processes involved in the hegemonic rise of the US, the decline of the European, especially British, hegemony, and how all efforts to rehabilitate the continent were weakened by two issues. Most biographies of British Prime Minister Lloyd George do not discuss the argument in depth, as in *David Lloyd George*, the official biography, where Malcolm Thomson touches on the Keynes's plan: "Keynes had furnished a Memorandum proposing a scale of payments rising from fifty to four hundred million pounds a year, and ultimately producing a total sum of eleven thousand million pounds" (Thomson, 1948, p. 310) Many biographies of President Woodrow Wilson also pay little attention to the Keynes Plan. The Walworth biography, for example, gives it a passing mention:

"Keynes's plan had been presented to Wilson in a letter from Lloyd George of April 23, 1919. Replying on May 5, Wilson had stated that Congress could not authorize a guarantee of bonds of European origin and that the Treasury wished to retire from the banking business and preferred that loans be made through private channels" (Walworth, 1969, p. 328).

Yet, with Lloyd George, one can see the inability of the European ruling class to look to the future: "Four years of war shook forever the supreme self-confidence that had

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<sup>1</sup> The sources for this paper are archival material, such as letter exchanges, memoranda, and official documents, on microfilm in the John Maynard Keynes Papers at Kings College Cambridge, a set of which is available at The Keynes Centre University College Cork. To supplement the study I drew on interdisciplinary sources ranging from economics, history and international relations to Keynes's main biographies (R. F. Harrod, 1952; D. E. Moggridge, 1992; R. Skidelsky, 1983), and Keynes's own writings such as *The Economic Consequences of the Peace*, *Essays in Biography* and his correspondence. Other history books, such as McMillan's books and Alan Sharp's *Versailles Settlement*, provided the economic and political context of the period. US hegemony is discussed, for example, in *The Wilsonian Century* by Ninkovic and Woodrow Wilson and *The American Diplomatic Tradition* by L. E. Ambrosius.

carried Europe to world dominance” (MacMillan, 2002: xxvi). With Wilson, the American behaviour towards its allies becomes painfully clear.

In addition, the idea of the Scheme was based on a strong concept of European Union and the solidarity that would grow through economic links after the devastation of the war. As the South African General and Defence Minister Jan Christian Smuts<sup>2</sup> put it to Lloyd George, after the *Scheme* was rejected and the Treaty signed: “This Treaty breathes a poisonous spirit of revenge, which may yet scorch the fair face – not of a corner of Europe, but of Europe” (Sharp, 1991, p. 192).

## 1. The Great War and the Peace Conference 1919

The Great War finally ended in November of 1918, after fifty-two long months of war and more than seventeen million deaths. One outcome of the war was that “The International order had to be re-created on a new and different basis.” (MacMillan, 2002: xxvi). The Peace Conference began the following year in Paris on 18 January, ironically the same day as the proclamation of the German Reich at Versailles forty-eight years earlier. Its aim was to draw up treaties between the dominant Allied powers and the defeated Central Powers.

The Council of Ten, or Supreme Council, was formed to discuss the most relevant issues and prepare resolutions to the problems facing the world as a result of the war. The group was composed of Thomas Woodrow Wilson, President of the United States; Georges Clemenceau, Prime Minister of France; David Lloyd George, Prime Minister of the United Kingdom; and Vittorio Emanuele Orlando, Prime Minister of Italy, with two representatives from Japan. They were assisted by Foreign Secretaries Robert Lansing, Stephen Pichon, Arthur James Balfour, and Sidney Sonnino. The smaller Allies and neutral countries were not invited to the Supreme Council.

In March, as the Peace Conference discussed new political and geographical arrangements, the Council of Ten replaced the Council of Four. This was made up of the four heads of state of the main dominant powers: France, Great Britain, Italy, and the United States.

One of the most important topics discussed was the amount of final reparations to be paid by the Central Powers, a contentious issue that raised the delicate question of inter-Allied debts incurred during the conflict. Unlike the other Allies, who were well aware of their catastrophic economic situation, the American delegation had arrived in Paris confidently and without a properly worked out economic plan (Keynes, 1920, pp. 146-150). In early 1919, for example, Italy was carrying an intolerable level of foreign debt and suggested that Washington might consider a general reapportionment of the cost of the war as a prelude to peace (Artaud, 1978, p. 116).

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<sup>2</sup> South African lawyer, politician, philosopher. South African Minister of Defence 1910-19. Member of the British War Cabinet 1917-19, and of the British Empire Delegation to the Paris Peace Conference.

The first remedy proposed by the then British delegate to the British Economic Council, John Maynard Keynes, was to reduce the demands on Germany. This solution could only be justified in the context of a much wider financial restructuring, to be followed by a general cancellation of all inter-Allied debt and a new loan of \$1 billion, which would enable reparations to be paid and world trade to resume (Keynes, 1920, p. 269). At the end of the war, the situation of the loans between the Allies was roughly as shown in Table 1.

Table 1: Inter-Allied Indebtedness. (Keynes, 1971, p. 420)

Loans to	By the United States (£ million)	By the United Kingdom (£ million)	By France (£ million)	Total (£ million)
United Kingdom	800	–	–	800
France	485	390	–	875
Italy	275	390	35	700
Russia	38	520	160	718
Belgium	56	90	90	236
Serbia	4	20	30	54
Roumania <sup>3</sup>	2	16	35	53
Greece	8	15	15	38
Portugal	–	10	–	10
Totals	1,668	1,451	365	3,484

As the table shows, Germany owed a large sum to France, France owed a large sum to Great Britain, and Great Britain owed a large sum to the United States, and so forth. Moreover, the total of these debts amounted to about £3.5 billion, making it difficult for the Allies to pay the principal and interest due from them on these debts. As a result, during the Peace Conference, the Allies discussed the possibility of imposing harsh reparations on the defeated nations in order to pay off their own debts.

“The economic mechanism of Europe is jammed” (Silverman, 1982, p. 145), Lloyd George told Wilson in April 1919, when he forwarded Keynes’s memorandum. “A proposal which unfolds future prospects and shows the peoples of Europe a road by which food and employment and orderly existence can once again come their way, will be a more powerful weapon than any other for the preservation from the danger of Bolshevism of that order of human society which we believe to be the best starting point for future improvement and greater well-being.”<sup>4</sup>

The British Empire and France were the largest debtors of the United States and at the same time would be the main recipients of reparations from Germany. This tied the

<sup>3</sup> Copy of the archival document, with the older version of Romania’s name.

<sup>4</sup> Stephen Alan Schuker, *The End of French predominance in Europe: the financial crisis of 1924 and the adoption of the Dawes plan* (Chapel Hill: University of North Carolina Press, 1976), 9.

question of German reparations to the question of inter-Allied war debts. These debts and credits could have been offset and Germany could then have settled directly with the US. (Schuker, 1976, p. 80)

In such situations, the conventional wisdom was that imports from European debtors and exports to American creditors should be encouraged in order to improve the trade balance between the indebted nations and the US. As early as 1916, Keynes advocated the idea of cancelling all inter-Allied European debts. Keynes knew that the existence of the Great War debt was a threat to financial stability everywhere and a serious obstacle to future trade relations between the Allies. However, the issue of inter-Allied indebtedness was closely linked to the intense popular feeling among the European Allies over the question of reparations and the growing conflict between nationalist aspirations and international obligations. With the rise of new states, such as those formed after the split of the Habsburg Empire, questions arose as to how Italy could be expected to pay such a large sum while Czechoslovakia paid nothing.

As a way of eliminating all present- and future – problems, Keynes proposed the total write-off of all war debts owed to the Allies, which he “put forward as being likely to promote the well-being of this country and the world” (Keynes, 1971, p. 420). He also reasoned that the total amount of this tribute should not exceed the amount obtainable from the enemy: “I do not believe that any of these tributes will continue to be paid, at the best, for more than a very few years. They do not square with human nature or march with the spirit of the age”<sup>5</sup>.

As Keynes acknowledged, writing off the inter-Allied claims in full would cost the US £1.668 billion. Britain, as a large net creditor to the Entente, would also suffer a substantial loss of £651 million. The chief beneficiaries would be Italy, which would be relieved of £700 million of debt, and France, which would be granted £510 million in debt relief. Keynes tried to convince Washington of the disastrous consequences of maintaining the tangled web of inter-Allied war debts, emphasising the desperate situation of France. If Britain and America were to insist on full repayment, “victorious France must pay her friends and allies more than four times the indemnity which in the defeat of 1870 she paid Germany. The hand of Bismarck was light compared with that of an ally or of an associate.” (Keynes, 1971, p. 422)

But the Americans were determined not to allow intra-Allied debt relief. “I realize the efforts that are being made to tie us to the shaky financial structure of Europe,” wrote Wilson to the American financier Bernard Baruch<sup>6</sup>, who was one of his chief advisers, “and am counting upon your assistance to defeat the efforts.”<sup>7</sup>

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<sup>5</sup> John Maynard Keynes, letter to Austen Chamberlain, March 28, 1919.

<sup>6</sup> American financier, prominent Democrat, member of the American Commission to Negotiate Peace, and Supreme Economic Council, 1919. Famous for getting out of Wall Street just before the 1929 crash.

<sup>7</sup> PWW, vol. 54, pp. 196, 431, 494; House of Lords Record Office, Lloyd George Papers, F6/6/49, Cecil to Lloyd George, 31.5.19, and F89/2/35, Kerr to Lloyd George, 28.2.19; D. Lloyd George, *Truth About Reparations and War Debts*, chapter 9; House and Seymour, p. 484; Silverman, pp. 32-35; Kent, pp. 40-43.

The American delegates in Paris rejected Keynes's idea of debt cancellation, because the US Treasury ruled out any discussion of rescheduling foreign governments' obligations to the United States:

"The [American] Treasury [...] will not assent to any discussion at the Peace Conference, or elsewhere of any plan or arrangement for the release, consolidation, or re-apportionment of the obligations of foreign Governments held by the United States." (George, 1932, p. 105)

To further clarify the concept, Treasury Under-Secretary Carter Glass telegraphed Paris on 8 March 1919 that any further such proposal would be treated as a veiled threat of financial default. Washington insisted that Clemenceau should make a public commitment to refrain from any further demands for debt relief (Silverman, 1982, p. 32). In such circumstances, Washington could not be expected to consider any cancellation of intra-Allied debt. In response to their stonewalling, Keynes drew up a second plan within two weeks, the joint guarantee of reparation bonds. In the *Scheme for the Rehabilitation of Europe Credit and For Financing Relief and Reconstruction*, the Allies would accept German reparation bonds 'in final discharge of the debts incurred between ourselves'<sup>8</sup>.

## 2. The Scheme for the Rehabilitation of Europe

Keynes drew up this project after a conversation with Jan Christian Smuts, a member of the British Empire's Delegation to the Paris Peace Conference. As Keynes's main biographer noted: "They shared a high-minded approach to peace-making, against harsh French behaviour" (Skidelsky, 1983, p. 367). The *Scheme* took shape after the failure of Keynes's debt cancellation proposal and after Smuts's return from Hungary and Austria and his description to Keynes of the tragic condition of the inhabitants of Eastern Europe. This is recorded in a letter from Smuts to his friend Mrs Gillet on 9 April:

This afternoon [...] Keynes came to see me and I described to him the pitiful plight of Central Europe. And he (who is conversant with the finance of the matter) confessed to me his doubt whether anything could really be done. Those pitiful people have little credit left, and instead of getting indemnities from them, we may have to advance them money to live. (Skidelsky, 1983, p. 367)

Smuts also described the situation to Lloyd George. As Lloyd George wrote in his diary on 10 April:

"General Smuts came to breakfast, on his return from Vienna. He gave a most eloquently depressing account of the conditions there. It is a world that we cannot imagine, he said – a world completely gone to pieces. There is no authority – no business. [...] There is scarcely any food there & everyone is starving. Smut's batman & another soldier were walking in the streets of Vienna when a child came up & asked for food. One of the soldiers gave him a

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<sup>8</sup> John Maynard Keynes, letter to Austen Chamberlain, March 28, 1919.

biscuit. Instantly the two men were set upon by a swarm of children, who seemed to come from no-where, & they were almost torn to pieces as the children fought to get to their pockets to see if there were any more food anywhere.

It was a horrible description of a famine-stricken country & represents a terribly difficult problem to deal with. Nothing is moving. The only people from whom they seem to expect any help are the British. [...]" (Stevenson, 1971, pp. 178-179)

The *Scheme* would allow stricken countries, whose credit was temporarily destroyed, to re-equip themselves and relaunch their economies on the basis of loans guaranteed by the United States and the wealthiest countries.

The 'Keynes Plan', which in retrospect has been seen as a "*Marshall Plan*" on a smaller scale (Harrod, 1952, p. 288), recommended that the Central European states should issue bonds guaranteed by the Allies, which in turn would be guaranteed by reparations to pay for the investments supported by the loans. It is worthwhile reproducing the *Scheme* in its entirety at this point:

1. (i) German bonds to be issued to a *present* value of £1,000 million and to a *face* value of a 1,200 million, carrying interest at the rate of 4 per cent per annum and sinking fund at the rate of 1 per cent per annum as from 1 January 1925, these payments to have priority over all other German obligations whatever, including additional claims for reparation not covered out of the above, the difference between the face value and the present value representing the funding of interest from 1 January 1920, up to 1 January 1925.
- (ii) Austrian, Hungarian and Bulgarian bonds to be issued to the present value of £125 million, £170 million and £50 million respectively on similar conditions.
- (iii) Roumania, Polish, Czecho-Slovakian, Jugo-Slav and Baltic States bonds to be issued to the present value of £15 million, £40 million, £20 million, £15 million and £10 million respectively on similar conditions.
2. Interest on each of the issues of enemy bonds under I (i) and (ii) above to be guaranteed jointly and severally by the other enemy states, in the event of any one of them failing to provide the payments due.
3. In the event of the failure of the above guarantees, interest at 4 per cent on all the above bonds to the aggregate present value of £1,500 million (or £1,800 million as from 1 January 1925), to be guaranteed by the principal allied and associated governments, by the three Scandinavian governments and by governments of Holland and Switzerland.
4. In the event of the guarantee under (3) becoming operative, the guaranteeing governments to be responsible in proportions determined in advance, as set forth in the accompanying Schedule A.
5. In the event of any of guaranteeing governments failing to meet their guarantee, the remaining guaranteeing governments to make good this failure in the same proportions amongst themselves as under (4).
6. A failure of any government to meet its guarantee under the above clauses to be considered by the financial section of the League of Nations, and if judged by them to have been avoidable shall be punished by such penalty or forfeiture of a financial economic or commercial character as the League of Nations may determine.



7. The bonds to be free of all taxation in all the issuing or guaranteeing states.
8. Of the £1,000 million bonds to be issued by the German governments £724 million shall be paid over to the allied and associated governments on account of sums due for reparation; £76 million shall be utilised for the discharge of existing debts to the three Scandinavian countries, Holland and Switzerland, and the remaining one-fifth of the total, namely, £200 million, shall be left in the hands of the German government to be made available for the purchase of food and raw materials.
9. Of the bonds amounting to £345 million in all to be issued by the Austrian, Hungarian and Bulgarian governments, four-fifths in each case shall be paid over to the allied and associated governments on account of sums due for reparation, the remaining one-fifth being left in the hands of these governments for the purchase of food and raw materials.
10. The bonds amounting in all to a present value of £1,000 million to be received by the allied and associated governments on account of reparation to be divided between them in the proportions determined upon by them for the division of reparation receipts generally.
11. The bonds to be accepted at their par value plus accrued interest in payment of all indebtedness between any of the allied and associated governments.
12. The bonds to be acceptable as first-class collateral for loans at the central banks of all the issuing or guaranteeing states, subject to such terms and limitations as may be in force with these institutions from time to time.

#### Schedule A

British Empire	20%
United States	20%
France	20%
Italy	10%
Japan	10%
Belgium	5%
Norway	
Sweden	
Denmark	15%
Holland	
Switzerland	

In short, to get the repayment cycle going, Keynes's plan provided for a bond issue of £1445 million, to be issued proportionately by the German government and its defeated Allies, with £200 million to be used by the German government for the purchase of food and raw materials, £76 million to pay off German debts to European neutrals, and the remainder, £169 million, to be used to buy food and raw materials in Austria, Hungary and Bulgaria. Four-fifths of the issue, £1,000 million, would go to the recipients on reparations account, thus providing funds to finance recovery in countries such as France and Italy. The bonds would carry interest at 4 per cent and a sinking fund at 1 per cent. No interest would be payable on the bonds until 1 January 1925, and the

## EDITOR'S TABULATION OF KEYNES' FINANCIAL SCHEME

<i>By Countries</i>				
<i>Germany:</i>	repar.	} (4/5) {	£724,000,000 (M. 14.48 md.)	
	debts		76,000,000 (M. 1.52 md.)	
	food		200,000,000 (M. 4.00 md.)	£1,000,000,000 (M. 20.00 md.)
<i>Austria:</i>	repar.	(4/5)	£100,000,000 (M. 2.00 md.)	
	food	(1/5)	25,000,000 (M. .50 md.)	£ 125,000,000 (M. 2.50 md.)
<i>Hungary:</i>	repar.	(4/5)	£136,000,000 (M. 2.72 md.)	
	food	(1/5)	34,000,000 (M. .68 md.)	£ 170,000,000 (M. 3.40 md.)
<i>Bulgaria:</i>	repar.	(4/5)	£ 40,000,000 (M. .80 md.)	
	food	(1/5)	10,000,000 (M. .20 md.)	£ 50,000,000 (M. 1.00 md.)
ENEMY TOTAL.....				£1,345,000,000 (M. 26.90 md.)
<i>Rumania</i>			£ 15,000,000 (M. 0.3 md.)	
<i>Poland</i>			40,000,000 (M. 0.8 md.)	
<i>Czechoslovakia</i>			20,000,000 (M. 0.4 md.)	
<i>Yugoslavia</i>			15,000,000 (M. 0.3 md.)	
<i>Baltic states</i>			10,000,000 (M. 0.2 md.)	£ 100,000,000 (M. 2.00 md.)
GRAND TOTAL.....				£1,445,000,000 (M. 28.90 md.)
<i>By Categories</i>				
<i>Reparation:</i>	Aus.		£100,000,000 (M. 2.00 md.)	
	Hun.		136,000,000 (M. 2.72 md.)	
	Bul.		40,000,000 (M. .80 md.)	
	SUB-TOTAL		£276,000,000 (M. 5.52 md.)	
	Ger.		724,000,000 (M. 14.48 md.)	£1,000,000,000 (M. 20.00 md.)
<i>Foodstuffs:</i>	Aus.		£ 25,000,000 (M. 0.50 md.)	
	Hun.		34,000,000 (M. 0.68 md.)	
	Bul.		10,000,000 (M. 0.20 md.)	
	SUB-TOTAL		£ 69,000,000 (M. 1.38 md.)	
	Ger.		200,000,000 (M. 4.00 md.)	£ 269,000,000 (M. 5.38 md.)
<i>German debts</i> .....				£ 76,000,000 (M. 1.52 md.)
ENEMY TOTAL.....				£1,345,000,000 (M. 26.90 md.)
<i>Succession and Baltic states</i> .....				£ 100,000,000 (M. 2.00 md.)
GRAND TOTAL.....				£1,445,000,000 (M. 28.90 md.)

Source: Editor's Tabulation of Keynes' Financial Scheme. (Burnett, 1965, p. 1014)

interest was to be jointly guaranteed by the enemy states, with priority over reparations payments, and underwritten in certain specified proportions by the Allied and Associated Governments, as well as by the Scandinavian governments, the Netherlands and Switzerland. Of the total, £1000 million in bonds would be paid to the European Allies, with the remainder retained by the Central Powers. The members of this consortium would in turn be accountable to the League of Nations. The bonds were to be accepted as prime collateral for loans by all central banks (Harrod, 1952, p. 288).

For Keynes, he had finally found the solution to the aforementioned problems: all inter-Ally debts arising from the war were to be reduced, and the balance paid by a German debt that could be transferred without putting immediate strain on Germany's balance of payments. European credit would be rehabilitated; the United States would be assured of a demand for its exports; the Central Powers would also obtain funds to feed their people and revive their industrial life; and, moreover, it would give hope to the defeated powers to put themselves in a position to meet their onerous obligations.

The Chancellor of the Exchequer, Austen Chamberlain (1919-1921), was a strong supporter of Keynes's plan. In a letter to Lloyd George, he wrote:

"I have no hesitation in recommending the scheme to you. It is marked by all Mr Keynes's characteristic ability and fertility of resource: it provides the stricken countries of Europe, whether allied or enemy, with the means of re-equipping themselves and restarting on a sound basis the trade and industry of the world; [...]"<sup>9</sup>

Chamberlain's letter was accompanied by a copy of the bond scheme and a cover note written by Keynes for presentation to the American, French and Italian leaders. In this note, he described the terrible problems that afflicted States after the Great War: the total economic standstill of the enemy country and the situations of new states, such as Serbia and Romania, whose economic and commercial fabric could not be created or re-created unless they were given the purchasing power with which to enter the world's markets. France, Italy and Belgium also needed outside help to rebuild their countries and resume normal peaceful activities. As he put it: "In short, the economic mechanism of Europe is jammed. [...] That capital has vanished; the complicated machinery of internal and external production is more or less smashed; production has to a great extent ceased."<sup>10</sup>

Without a solution to the problem (*i.e.*, his Scheme), Keynes believed in a scenario of a "morass of destruction", and, as a consequence, an economic disruption of Europe and a depopulation "by millions of person"<sup>11</sup>, Keynes observed that:

"The trade can only re-commence on the basis of credit of some kind, what better security can the lenders hope to secure than is herein proposed? [...] a scheme [...] can inspire that sentiment of hope which is the greatest need of Europe at this moment. A proposal which unfolds future prospects and shows the people Europe [...]"<sup>12</sup>

Keynes expected a negative reaction from the French delegation at the Peace Conference because of the French 'revanchism' towards Germany and lack of determination to support a German economic recovery. From his early drafts, Keynes tried to be

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<sup>9</sup> Austen Chamberlain, letter to Lloyd George, April 17, 1919.

<sup>10</sup> John Maynard Keynes, *Explanatory letter to be addressed by the Prime Minister to the President, M. Clemenceau, and Signor Orlando*, 1.

<sup>11</sup> John Maynard Keynes, letter to Austen Chamberlain, May 26, 1919.

<sup>12</sup> John Maynard Keynes, *Explanatory letter to be addressed by the Prime Minister to the President, M. Clemenceau, and Signor Orlando*, 4-5.

as favourable to France as possible in order to avoid a rejection. This can be seen in the figure below:

#### Schedule A.

Of the aggregate amount of Bonds issued under this scheme, £1,000,000,000 is to be received by the Allied and Associated Governments on account of Reparation, £75,000,000 by Neutral Countries on account of debts owing to them by Germany, and the balance of £425,000,000 is left as purchasing power in the hands of the countries originally issuing the Bonds.

*It is proposed (A.)*  
(The principle for distributing the proportionate responsibility of each of the guaranteeing Governments for the £1,500,000,000 worth of Bonds ~~should~~ ~~be~~ be based on this proportion being made up of two parts, - (i) a proportion of £1,075,000,000 corresponding to <sup>each</sup> ~~the~~ country's actual receipts out of the distribution of Bonds to this value, and (ii) a proportion of £425,000,000 corresponding to its general position in the world as a market for exports and otherwise.

It is suggested that the percentage responsibilities under (ii) should be as follows :-

British Empire	25	20
United States	25	20
France	15	20
Italy	10	
Japan	10	
Belgium	5	
Norway		
Sweden		
Denmark	10	15
Holland		
Switzerland		

That is to say, assuming for the sake of illustration that France received 50% of the £1,000,000,000 for Reparation and that the United States waived her share

Figure 1. Draft of Schedule A

Note that there are other percentages: British Empire and United States 25%, France 15%, and Norway, Sweden, Denmark, Holland and Switzerland 10%<sup>13</sup>. The French responsibility is 10% less than the United States' and British Empire's figures.

Even after increasing France's responsibility to 20%, bringing it in line with the US and UK percentages, Keynes noted in the accompanying cover letter to the *Scheme* addressed to the heads of state that: "France is probably the gainer from the scheme and is offered a way out from her almost overwhelming financial difficulties."<sup>14</sup> Keynes did not imagine that this would be the main reason why the United States rejected his scheme.

## 2.1. UK Reactions to the Plan

The Chancellor of the Exchequer Austen Chamberlain wrote to Sir Robert Cecil, the British Government's representative on the Supreme Economic Council:

"[...] At least the Prime Minister now has two alternatives, either of which he can submit to the President, one, the mutual cancellation of debts and the other the scheme of mutual guarantee proposed by Keynes."<sup>15</sup>

In another letter, this time to the British Prime Minister Lloyd George, Chamberlain reiterated his support for the *Scheme* and his view that the mutual guarantee scheme needed more than Keynes's cover letter; he believed in the role that the public opinion could play in reaching an agreement:

"I believe that if this scheme be formally adopted by the British Government and formally and publicly presented to the Conference as their solution of a problem which confronts and embarrasses the whole world, the force of public opinion would drive all Governments to assent."<sup>16</sup>

Towards the end of the letter, Chamberlain reiterated his view that without strong ministerial support his case was lost. He would now look to another forum for his case, the informed public opinion:

"I am therefore most anxious that the scheme should not merely be privately discussed between yourself and the President though that may be right course to pursue in the first instance –

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<sup>13</sup> In the draft, he also wrote after the table: "That is to say, assuming for the sake of illustration that France received 50% of the £1,000,000,000 for reparation and that the United States waived her share of the receipts from this source. France would be a guarantor of the aggregate Bond issue of £1,500,000,000 to the extent of £m 500 + 15% of £m 425 = £m 563.75, i.e. to the extent of 37.6 per cent (approx.); and United States would be a guarantor to the extent of 0 + 25% of £m 425 = 106.25, i. e. to the extent of 7.1 per cent (approx.)."

<sup>14</sup> John Maynard Keynes, *Explanatory letter to be addressed by the Prime Minister to the President, M. Clemenceau, and Signor Orlando*, 2.

<sup>15</sup> Austen Chamberlain, letter to Robert Cecil, April 22, 1919.

<sup>16</sup> Austen Chamberlain, letter to Lloyd George, April 17, 1919.

but that it should be formally laid before the Conference as the policy of His Majesty's Government and that the general force of public opinion should be invoked in its support.”<sup>17</sup>

Lloyd George endorsed the scheme in a covering letter to President Wilson. As he reminds us in *Truth About Reparations and War-debts*, 1932, his cover letter to President Wilson, Lloyd George stated:

“Apart from private enterprise, His Majesty's Government see only two possible courses – direct assistance and various forms of guaranteed finance, on a very much larger scale than is at present contemplated, by the more prosperous of the Allied and Associated countries, which probably means to an extent of not less than 90 per cent, the United States; or an attempt to recreate the credit system of Europe and by some form of world-wide co-operation to enable the countries whose individual credit is temporarily destroyed to trade on their prospects of reparation from Enemy States or to capitalise their future prospects of production. Every consideration of policy and interest indicates the superiority of the second. [...] (George, 1932, p. 106)

There are many points in it which will require very careful discussions between our experts, and it is doubtless capable of much modification and improvement without detriment to the main ideas which underlie it. [...]

The good faith of the world as a whole is pledged for the carrying out of a scheme, the sole object of which is to set on its feet the new Europe. [...] only a scheme of large and broad dimensions, which can be announced to and understood by the whole world, can inspire that sentiment of hope which is the greatest need of Europe at this moment. (Burnett, 1965)

His position is a good example of the famous ditto: “I would if I could, but I can't, so I shan't do more”. However, in a letter Thomas Lamont wrote that Keynes, Smuts and Cecil, who might be called the main supporters of the *Scheme*, had limited influence with Lloyd George on this issue (Moggridge, 1992, p. 315).

## 2.2. U.S. Reactions to the Plan

American support was essential to give legitimacy and reassurance to Keynes's plan, though not necessarily because of its financial role, since the United States' percentage responsibility was only 20 per cent, the same as that of France and the British Empire.

On 3 May, Lloyd George finally received Wilson's reply. The American reaction to the plan was “disappointingly cool” (Skidelsky, 1983, p. 369) and fairly vague, as the reply to Lloyd George shows:

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<sup>17</sup> Austen Chamberlain, letter to Lloyd George, April 17, 1919.

“I am sorry to say, however, that Mr. Keynes’ plan does not seem feasible from the American point of view. Our Treasury and our financial delegates here in Paris are convinced that the plan as presented lacks many elements of economic and financial soundness. [...]”<sup>18</sup>

He goes on to explain why the plan is unworkable for the US:

“I am convinced, moreover, that it would not be possible for me to secure from the Congress of the United States authority to place a Federal guarantee upon bonds of European origin.”<sup>19</sup>

In fact, during this period, Congress was dominated by Republicans who were hostile to helping Europe, such as Senator Hiram W. Johnson of California, who stated: “It means the halting and betrayal of New World liberalism, the triumph of cynical Old-World diplomacy, the humiliation at end of American idealism” (Ambrosius, 1987, p. 140). Johnson had not wanted such a commitment on a global scale. Republicans had not wanted the American nation to preserve the British Empire or guarantee the possessions of France and Italy.

A day later, however, Keynes wrote to Sir John Bradbury (joint permanent secretary to the Treasury from 1913 to 1919 and chief British Delegate to the Reparations Commission in Paris from 1919 to 1925) to explain what he considered to be the ‘real’ reasons for the American rejection of the *Scheme* and why there “has been immediate and violent opposition on the part of Washington”.<sup>20</sup> According to Keynes, the US was against a general *Scheme* to restart Europe. They wanted to consider and play a different role for each of the separate problems of the new states and Eastern Allies, of the Enemy States, and of the Western Allies. In order of priority for the US:

- Financing new countries – the United States was only prepared to provide financial aid to newly created nations after the war. Given their vulnerability as a result of the war and their proximity to Russia, the US saw this as an assurance against the risks of influence from Russian Bolshevism:

“They are disposed to do something and it is on the head that we may expect counter proposals. They estimate the total amount of loans required for such countries at £100,000,000.”<sup>21</sup>

- The financing of enemy countries, particularly Germany – as regards to the aid to be given to Germany, the US found their first dilemma, as can be seen in Wilson’s letter to George:

“Germany requires working capital. Without that, she will be unable to start her industrial life again, and therefore unable to make any substantial progress in the way of reparation,

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<sup>18</sup> Woodrow Wilson, letter to Llyod George, May 3, 1919.

<sup>19</sup> Woodrow Wilson, letter to Llyod George, May 3, 1919.

<sup>20</sup> John Maynard Keynes, letter to Sir John Bradbury, May 4, 1919.

<sup>21</sup> John Maynard Keynes, letter to Sir John Bradbury, May 4, 1919.

but the provisions of the reparation clauses of the proposed treaty demand that Germany shall deliver over at once all her working capital, that is, practically the whole of her liquid assets.”<sup>22</sup>

This was the financial dilemma: how would it be possible to help “put Germany on her feet”<sup>23</sup>, if the Allies deliberately start out by taking away all Germany’s current capital?

- The financing of France and Italy – this was Wilson’s political dilemma. The US was not sympathetic to further loans to France and Italy; the Americans were trying to solve the dilemma of assisting Germany and new states without helping old allies.

“As regards they are determined to do anything. Their annoyance both with France and Italy is at the present time intense and there is nothing less likely than that at the present juncture the President will give any financial assistance to either of them.”<sup>24</sup>

These three points represent, respectively, the unwillingness of the Americans to aid the new states, the economic dilemma in relation to Germany which the Americans found in Keynes’s *Scheme*, and the political dilemma of not helping France and Italy.

In his letter above, Keynes did not seem to be too disappointed by the American’s sharp rejection of his plan. This may have been related to the dinner he had in Paris on 3 May with General Smuts and the US delegates to the American Commission, Norman Hezekiah Davis<sup>25</sup> and the treasury representative Thomas Lamont<sup>26</sup>, to discuss the American reactions. What exactly did they discuss? A letter from Lamont, the representative of the US Treasury, to Robert Henry Brand, the English banker, member of the British delegation and financial adviser to Lord Robert Cecil, provides perhaps the greatest clarification. In this letter, he expressed his willingness to extend American credit through ‘normal commercial and banking channels’ rather than through the government apparatus. He proposed setting up a private finance corporation in the United States to channel American savings to Europe in cooperation with British banking groups:

America has ample credit resources, Great Britain has wonderful credit machinery all over the world. Why not make a combination of the two? You people have splendid banks established in the Far East and all through South America. Now, we in America are right on the verge of duplicating every bit of that banking machinery. [...] The result will be, you will make smaller profits, and so shall we, and we shall be very keen rivals. Why don’t we avoid all that by our buying a half interest, no more, in a lot of your banks, and thus make a combination of your machinery and our credit resources? I suppose the very idea sounds fantastic to you. It did to

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<sup>22</sup> Woodrow Wilson, letter to Lloyd George, May 3, 1919.

<sup>23</sup> Woodrow Wilson, letter to Lloyd George, May 3, 1919.

<sup>24</sup> John Maynard Keynes, letter to Sir John Bradbury, May 4, 1919.

<sup>25</sup> American banker. Former assistant Secretary of State US Treasury (1917), member of the American Commission to Negotiate Peace and Supreme Economic Council 1918-19.

<sup>26</sup> American banker, partner in J. P. Morgan & Co. (1911-1940). US Treasury representative on American Commission to Negotiate Peace 1918-19.



Keynes when I sprang it on him the other night at dinner. His ready answer was, that your banks wanted to run their business and didn't want any interference from the outside. It was a very complete answer, because it showed the spirit of the whole thing. When a man goes into partnership, of course, he is no longer free to manage his affairs by himself. The same is the case when he takes a wife; but the state of the married man is supposed to be more blessed than that of the single.

Now, I think that if the British and Americans were to start out towards a goal of partnership, they would both make a lot more money than they ever will by staying apart and competing against each other; and what is of infinitely greater importance, they would establish such a rapprochement that the world could never shake us out of peace and into war.<sup>27</sup>

The Lamont Scheme can therefore be seen as proof of the real motivation behind the rejection of the Keynes Plan. Two key passages from this text which illustrate this point are when Lamont goes on to say that: "[...] if British and Americans would make a lot more money than they ever will by staying apart and competing against each other [...]" and "It did to Keynes when I sprang it on him the other night at dinner."

One could try to imagine the effect this had on Keynes, who had been working on a plan to rehabilitate *Europe*, and not *just* the British Empire, in particular after hearing harrowing reports from Hungary. Keynes's reaction was recorded in a letter from Smuts:

Poor Keynes often sits with me at night after a good dinner and we rail against the world and the coming flood. And I tell him that it is time for the Griqua prayer (The Lord to come himself and not to send his Son, as this is not a time for children). And then we laugh, and behind the laughter is Hoover's terrible picture of 30 million people who must die unless there is some great intervention. But then again we think things are never as bad as that; and that something will turn up, and the worst will never be. And somehow all these phases of feeling are true and right in some sense. (Moggridge, 1992, p. 310)

It is not surprising therefore that Keynes wrote to Sir John Bradbury, as mentioned above, that "The whole position is disappointing and depressing". Hence, Keynes' straight answer to Lamont's proposal was that British banks wanted to run their business without any outside interference.<sup>28</sup>

Now the context behind the rejection of Keynes's *Scheme* becomes clearer. On the same day that Lloyd George received Wilson's reply expressing the American concerns about the *Scheme*, American envoys were dining and plotting a bilateral plan with Great Britain and excluding the rest of Europe – the opposite of what Keynes's Scheme proposed. This may be why, in a letter the day after the dinner, Keynes wrote that:

The Americans do not really intend to do anything; and even apart from that no concrete proposal capable of being put into force can come into existence in the unreal atmosphere of Paris. (John Maynard Keynes, letter to Sir John Bradbury, May 22, 1919)

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<sup>27</sup> Thomas Lamont, letter to Robert Henry Brand, June 10, 1919.

<sup>28</sup> Thomas Lamont, letter to Robert Henry Brand, June 10, 1919.

Wilson wrote to the American financier Bernard Baruch<sup>29</sup>, who was one of his chief advisers: “I realize the efforts that are being made to tie us to the shaky financial structure of Europe, and am counting upon your assistance to defeat the efforts” (MacMillan, 2002, p. 184). The meaning is clear: The US did not want to help Europe, but to formulate a financial and therefore political link with Great Britain, ignoring and overlooking all ideas and possibilities of strong links between European states. Baruch supported Wilson’s view of the need for new forms of cooperation and the creation of the League of Nations.

Therefore, it is clear that the problem the United States had with Keynes’s Scheme was in its very title: *Scheme for the Rehabilitation of Europe* (emphasis added).

The news of the rejection of Keynes’s Scheme was also reported by French newspapers. *Le Temps* wrote on its front page on 4 May:

“Le gouvernement des États-Unis n’accepte pas le projet que la Trésorerie Britannique avait élaboré, pour donner une valeur immédiatement négociable à une partie des indemnités dues par les puissances ennemies. [...] [Le gouvernement américain] préfère se réserver le choix de moyens et les avantages d’une complète liberté d’action.”<sup>30</sup>

Seeing the potential for saving Europe squandered by the rejection of his plan, Keynes wrote to his mother:

“One most bitter disappointment was the collapse of my Grand Scheme for putting everyone on their legs. After getting it successfully through the Chancellor of the Exchequer and the Prime Minister and seeing it formally handed to Wilson and Clemenceau, the American Treasury (of whom no more was asked than ours) turned it firmly down as a most immoral proposal which might cost them something and which Senators from Illinois wouldn’t look at. They had a chance of taking a large, or at least human, view of the world and unhesitatingly refused it. Wilson, of whom I’ve seen good deal more lately, is the greatest fraud on earth.”<sup>31</sup>

## Conclusion: A Threat to the US Hegemony Plan?

The problem with the Keynes Plan was the creation of financial duties and trade obligations between all European countries tied to a credit system. This economic link, if it were to be developed, could possibly have been built into an early kind of union of

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<sup>29</sup> “In 1916, Baruch left Wall Street to advise President Woodrow Wilson on national defense and terms of peace. He served on the Advisory Commission to the Council of National Defense and, in January 1918, became the chairman of the new War Industries Board. With his leadership, this body successfully managed the US’s economic mobilization during World War I”. (Leab, 2010, p. 11).

<sup>30</sup> *Le Temps*, May 4, 1919.

<sup>31</sup> John Maynard Keynes, letter to Mrs Keynes, May 14, 1919.

European states. We do not know, of course, but it was not in the US interest as it was perceived in Washington at the time.

If political cooperation was ruled out, economists like Lamont and Herbert Hoover<sup>32</sup> recognised early on that European prosperity was indispensable to America's economic well-being. But this did not hold for all European states.

For example, because of their high level of indebtedness, the French really liked the idea that the United States should use its financial resources to get Europe going again after the war. Etienne Clémentel, the Minister of Trade and Industry, drew up an elaborate plan for a "new economic order" in which organisation and coordination would replace wasteful competition, resources would be pooled and shared out as needed, and the whole would be run by technocrats. If Germany was politically stabilised, it too could be part of the new order, safely enmeshed in a stable and prosperous organisation. The project was finally turned down by the Anglo-American allies in April 1919. The effort bore unexpected fruit after the Second World War when Jean Monnet, who had been Clémentel's assistant in 1919, founded the economic organisation that became the European Union<sup>33</sup>.

In short, Wilson recognised the merits of Keynes's Scheme, but asked: why should the United States finance Germany in order to settle German reparations with other European countries? At that moment, the American policy preferred to sabotage a unique plan in which it would be the financier of a European economic recovery, in favour of a strong relationship only with Great Britain.

The peacemakers appalled Keynes. They fretted about revenge while European civilisation tottered on the brink of collapse. "What did they achieve in their gilded rooms?", MacMillan asked. According to Keynes, a peace that completed the economic destruction wrought on Europe by the war. They were drawing new lines on the map when they should have been setting up a free trade area; they were haggling over the debts they owed to each other when they should have cancelled them all (MacMillan, 2002, p. 182). Keynes wrote in a letter to Norman Davis on 5 June 1919, two days before he resigned from the Paris Conference:

"I am slipping away on Saturday from this scene of nightmare. I can do no more good here. You Americans are broken reeds, and I have no anticipation of any real improvement in the state of affairs." (John Maynard Keynes, letter to Norman Davis, June 5, 1919)

Keynes's proposals, like those of the French and the Italians, were immediately vetoed by Washington. The Americans wanted no link. To maximise its leverage, the Wilson

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<sup>32</sup> In charge of US relief to Europe during WW1 and Armistice. Member of the Supreme Economic Council 1919. Future President of the United States 1929-33.

<sup>33</sup> Marc Trachtenberg, *Reparation in world politics: France and European economic diplomacy, 1916-1923* (New York: Columbia University Press, 1980), 1-10.

administration wanted to deal bilaterally with each Allied debtor. Wilson had accurately predicted that after the war the United States could “force [the Europeans] to our way of thinking, because by that time they will, among other things, be financially in our hands.” (Ninkovich, 1999, p. 90)

Indeed, the United States, long a debtor nation, was by the end of Great War a leading creditor nation, the world’s banker. Thanks to the historic wartime turnaround in its balance of payments, New York had replaced London as the world’s leading exporter of capital. As Benjamin Strong of the Federal Reserve Bank of New York put it: “Our influence in central bank circles is almost predominant.” (Ninkovich, 1999, p. 91)

Economically, at least, the challenge of internationalism is to undo much of the peace settlement rather than to get America to abide by it. The restoration of prosperity in Europe was not likely to be achieved while the generation of the 1920s was saddled with the huge burden of debt incurred by their political forebears (Ninkovich, 1999, p. 91).

By then the American establishment had woken to the fact that Europe had burned up too many resources (financial and human) in the Great War to recover in the short term. After 1919, every state in need of financial aid had to turn to the US, the only Western power that had not been severely devastated. The US was aware of its potential new role; that it would grow in a context of European decline.

Wilson’s problematic policy and agenda at the Conference, regarding his Fourteen Points and the question of reparations and colonies, was confirmed by the failure of the American Senate to ratify the Treaty of Versailles. In the long run, however, the US would become the true and only victor of the Great War, reversing the American pre-war isolationism with a new foreign political power in order to lay the foundations for global hegemony.

“Anglo-American officials [...] dreamed that world history could, and should, begin, would begin if the war were properly perceived as an opportunity to turn Europe into Americans or Englishmen. What was missing in central and eastern Europe were the institutions and the traditions of democratic government.” (Boemeke, Feldman & Glaser, 2006, p. 621)

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