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**Margaret Thatcher's  
Case against Democratic  
Socialism and Keynesian  
Economics**

**Markets, Monetarism,  
and British Politics in the 1970s**

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# Introduction

Britain experienced two stunning developments in the 1970s. Postwar Keynesianism fell out of favor and, for the first time, British voters chose a female prime minister. From the day Margaret Thatcher entered Parliament, she was a partisan woman who fought Labour Party “socialism” with more commitment than almost all other Tories of her day. When she became leader of the Conservative Party in the 1970s, she was the first leader to oppose the consensus views of both the Labour Party and centrist Tories who, in varying degrees, accepted Keynesianism and state ownership of industry. She had great faith in a market economy of less government intervention. Thatcher’s economic stand against key Tory members was often cautious, but she paved the way for a significant realignment of the Conservative Party. In an argument with Tory centrist James Prior, she declared: “Standing in the middle of the road is very dangerous, you get knocked down by the traffic from both sides.”<sup>1</sup> Rather than a biography of Thatcher, this book is a history of her political rise within the context of the British economy and persisting Keynesian and socialist ideas. The focus is on conflicting economic views, both within Thatcher’s party and the Labour Party, and how economic stagnation and inflation resulted in the transformation of British politics and a greater expression of free-market ideas.

## I

For decades, Keynesianism ruled in academia, the Bank of England, and Whitehall.<sup>2</sup> John Maynard Keynes (1883–1946) was born in England to a distinguished family; his father was a Cambridge University professor and his mother had been mayor of Cambridge. He attended the best schools, and his

university education was at Cambridge. He wrote several important books, including *The General Theory of Employment, Interest and Money* (1936). The book is an unfortunate example of contorted and obscure writing, and it is difficult to find anyone who has read it cover to cover. However, it gave birth to a new branch of economics called “macroeconomics” that focused on national economies. Critical of the “misleading and disastrous” consequences of laissez-faire theory, Keynes rejected both the thinking that full employment was the normal state of the economy and that high unemployment was a temporary circumstance that eventually corrected itself.<sup>3</sup> He entrusted experts to manage the economy, thus giving credibility to the idea that government action could smooth the unpleasant side of boom-bust business cycles. When private investment waned, it was crucial for the government to borrow money, increase spending, and later, as the economy improved, run a budget deficit to repay past loans.<sup>4</sup>

Consistent with Thatcher’s rejection of excessive government action, she saw Keynesian deficit financing of public expenditure as problematic. For conservatives such as Thatcher, both Keynesianism and socialism had the serious flaw of promoting greater government management of the economy that did not allow the best allocation of scarce resources. High taxes, big government spending, and overregulation stifled wealth creation. How could the British people benefit from government waste and a stagnant economy? Thatcher apparently understood how best to undermine the Labour Party and Keynesian ideas. She effectively criticized Keynesian policies without using the word. In the Cold War years, the term socialism was a safer target. The “socialist” Labour Party that she took to task consisted of mostly those who embraced rigorous Keynesianism. The social democrats in the party far outnumbered the hardline socialists demanding comprehensive public ownership. When one considers pragmatism over idealism, the Labour Party’s preference for Keynesianism over hardline socialist control is not surprising. Some believed Keynesianism could be quite radical. There is the argument that Keynes wanted to see Britain adopt, in his own words, “liberal socialism.” In his revisionist work, economist James Crotty claims that genuine Keynesianism, as understood by Keynes himself, was more socialist than many recognized.<sup>5</sup> Perhaps Thatcher’s broad usage of the term socialism to fight Labour’s economic ideas was not too far off the mark.

Thatcher appreciated the ideas of Austrian economist F. A. Hayek (1899–1992), who was one of the few dissenters concerned that Keynesian economics and inflation eventually went hand in hand. When Hayek was a student at the University of Vienna after World War I, he witnessed how hyperinflation wrecked the German and Austrian economies. The University of Vienna barely functioned due to a shortage of coal, light, and food.<sup>6</sup> Hayek also saw an alarming problem with the central planning of socialist economics that

threatened liberty, the issue he discussed in *The Road to Serfdom*. Two years before the publication of Hayek's book in 1944, the British Labour Party declared in the pamphlet *The Old World and the New Society* that a "planned society must replace the old competitive system."<sup>7</sup>

According to Hayek, central planners believed that modern capitalism, hampered by monopolistic tendencies and technological changes, did not allow true competition. Echoing the Marxist doctrine of the "concentration of industry," central planners saw government control of production as necessary to ensure the best economy.<sup>8</sup> But Hayek argued that central planning was a form of slavery because economic and social goals required authoritarian action. When speaking of freedom, socialists promised a new freedom, notably freedom from necessity. Ironically, if it took coercion to realize this freedom, so be it.<sup>9</sup> To no one's surprise, Labour Party politicians did not view *The Road to Serfdom* as a serious book.<sup>10</sup> In subsequent decades, the Labour Party consisted of a wide range of socialists who shared the idea that competition was an unsuitable method for realizing a just and productive economy. They believed that replacing "heartless" competition with planning was the proper thing to do. Thatcher disagreed and she used Hayek's writings for intellectual ballast. Although *The Road to Serfdom* offered no direct criticism of the Keynesianism that many Tories favored, the evidence suggests few Tory centrists read the book.

Hayek's writings were an important component of Thatcher's economic education, but the work of American economist Milton Friedman (1912–2006) did as much or more to shape her thinking. Friedman became the most influential free-market scholar in America. Both of his parents were Jewish immigrants from Europe. Having humble economic origins, Friedman was a mild-mannered intellectual who was friendly and respectful of opposing ideas. The label "heartless" capitalist, only concerned with defending the rich, did not fit him. His skill in presenting insightful economic analysis in layman's terms was obvious to the many readers who followed his *Newsweek* column begun in 1966. Friedman's monetary theory that focused on the role of money in causing both inflation and cyclical disturbances offered a serious critique of Keynesian thinking. The ideal system is when the "money supply increases at a steady or neutral rate (the monetarist rule)."<sup>11</sup>

More so than Hayek, Friedman demonstrated a keen interest in the British economy and sought to correct what he saw as misguided thinking about the cause of inflation: "In Britain, the explanation that everybody gives for inflation is that inflation is caused by trade unions, the greedy, grasping laborers who force up the wages that cause inflation." This was wrong. He presented data of recent British economic history showing the clear link between quantity of money and inflation. To make his point about trade unionism, Friedman noted the trend was almost identical in Japan where labor unions

were relatively small and insignificant. While visiting Britain, he took the unusual position of partly defending trade unionism: "Labor unions do a great deal of harm in many ways, but one thing of which they're innocent is producing inflation."<sup>12</sup>

Although his work on money supply set him apart from most British economists, Friedman's criticism of government intervention in the economy received wider support. Keynesian economists and policymakers were vulnerable. They relied on the Phillips curve, named after the Australian economist A. W. Phillips who noted the long-term inverse relationship between unemployment and inflation: when one increased, the other decreased. For example, when the unemployment rate increased (more people out of work), there was less upward pressure on wages and prices, thus less inflation. When the unemployment rate fell, the tighter labor market resulted in an increase in wages and prices. Following the logic of the Phillips curve, the Keynesian strategy of fighting inflation was to have the government decrease the amount of money to cool the economy and balance inflation and unemployment to an acceptable level.<sup>13</sup> However, the Phillips curve had no answer to the problem of both inflation and unemployment rising at the same time. Thatcher found the work of Hayek and Friedman helpful, but in her speeches she saw no need to get into specifics of their theories. Thatcher the politician voiced her opposition to state intervention, either Keynesianism or socialism, in simple terms: it was socialistic and wrong for Britain.

## II

After World War II the British economy was in a mess. Britain had large debts, low currency reserves, severe physical damage by aerial bombardment of major cities, and acute shortages of necessities. One of many examples of economic difficulty was housing. Enemy bombing destroyed almost 500,000 homes and temporarily disabled a far greater number.<sup>14</sup> On July 25, 1945, Prime Minister Winston Churchill was out. Voters chose the Labour Party to lead the nation. Years later, Thatcher viewed this shocking election as "the logical fulfilment of the collectivist spirit" that dominated wartime Britain.<sup>15</sup>

Led by Clement Atlee, the Labour Party favored planning, controls, and nationalization as the appropriate economic direction for the British people. The formation of the Central Economic Planning Staff was indicative of the government's greater role in addressing economic problems. However, there were obstacles to planning. In 1946, Edward Bridges, an important civil servant, wrote: "We are trying to work a planned economy without labour controls and in conditions of general inflationary pressure in which financial incentives alone cannot be strong enough to take their place." Many in the party viewed the nationalization of industries as a promising way to control

and plan the economy. They looked to the economic benefits of large-scale enterprises run by “experts”; nationalized industries could achieve economies of scale beyond the hopes of “fragmented, private entities.”<sup>16</sup> There was also a moral component. In 1949, Labour Cabinet minister Aneurin Bevan asked: “What is national planning but an insistence that human beings shall make ethical choices on a national scale?” Overall, the economic record of the Atlee government was weak; there were too many crises and shortages.<sup>17</sup> Economic growth in Britain was slower than in western European nations and Japan. Lacking innovation and entrepreneurship, the central planning of the Labour Party appeared less efficient than the market economies of competitors.

Thatcher’s initial attempts to enter Parliament failed. In the 1950 general election, she wanted to see the defeat of the government’s “socialism.” She campaigned hard, but she fell far short against her Labour opponent.<sup>18</sup> Although defeated again in the 1951 election, Thatcher was happy to see the Conservative Party return to power. For the next thirteen years, the prime ministers were Churchill (1951–1955), Anthony Eden (1955–1957), Harold Macmillan (1957–1963), and Alex Douglas-Home (1963–1964). The Tories, most of them supportive of Keynesianism, accepted much of the welfare state ushered in by the Labour Party. Any dismantling of progressive platforms was modest at best. Soon to be prime minister, Eden did not hide the role the Tory Party played in advancing and accepting bigger government. He declared in 1955:

We denounce the Labour Party’s desire to use the social services, which we all helped to create, as an instrument for levelling down. We regard social security not as a substitute for family thrift, but as a necessary basis or supplement to it. We think of the national health service as a means, not of preventing anyone from paying anything for a service, but of ensuring that proper attention and treatment are denied to no one.<sup>19</sup>

Tories were comfortable with an accommodationist approach that they believed most voters welcomed. Government expenditure as a percentage of GDP was similar for the Labour government ending in 1951 and the Tory governments of the 1950s. In the second half of the decade, Britain experienced low productivity, a declining demand for exports, and increased competition from other nations. Rather than turning to the free market for answers, the Tories turned to more state planning. Created in 1961, the National Economic Development Council represented a Conservative statism that Tories believed was capable of managing the economy.<sup>20</sup> Finally elected to Parliament in 1959, Thatcher later wrote that Conservatism “lacked fire” and its questionable “management of the economy” was in part responsible for the worsening economic conditions of the 1960s.<sup>21</sup> Others pointed to the economic incompetence of Tory leadership.

Throughout the 1960s, economists noted the slow rate of growth of the British economy compared to other nations. As early as 1961, Oxford economist Thomas Balogh, who later became an economic advisor for the Labour Party, wrote: “Unless we can increase our rate of growth . . . we shall have to stifle something.”<sup>22</sup> Led by Harold Wilson, the Labour Party took power in October 1964. In the following month, the new government faced a sterling crisis when the market lost confidence in the pound. To keep the pound at \$2.78, the intervention of late November almost depleted the cash resources of the Bank of England.<sup>23</sup> Britain continued to experience weak productivity, anaemic investment in private enterprise, and rising export prices. There was another sterling crisis in 1966 and in the following year the Labour government devalued the sterling by 14 percent from \$2.80 to \$2.40. Other economic problems included an increasing number of days lost to labour strikes and inadequate investment in new technologies.<sup>24</sup> The economy in the 1960s was troubling, but the next decade was far worse. Britain in the 1970s experienced appalling economic conditions and both the Tory Party and the Labour Party struggled to find a solution to the economic woes. As Thatcher saw it, there was a need for significant change.

### III

Scholarship on Thatcher is massive; no other British prime minister since Winston Churchill has received as much attention as this controversial woman. The publication of biographies and many other books on Thatcher as early as the 1970s is a testimony of her influence and importance in modern British history. Recent biographies by John Campbell, Robin Harris, Graham Goodlad, and Charles Moore cover much of her early life and political rise and her domestic and foreign policies. For good reasons, the bulk of the Thatcher literature is of her time as prime minister (1979–1991). Those who offer significant discussion of her economic policies focus mainly on the “Thatcherism” of the 1980s.<sup>25</sup>

This study focuses on the 1970s and seeks to better understand Thatcher’s interaction with the troubled British economy and her opposition to socialist thinking. Reading economic history can be a daunting task complicated by economic jargon and ideology. Avoiding confusing economic language, this introductory study offers a concise analysis of Thatcher’s criticism of Keynesian and socialist economics. There is no discussion of key domestic events such as Britain joining the Common Market, the devolution issue of Scotland and Wales, and the development of the North Sea oilfields. Considerable attention is on the divisions in each party and the key representatives of the various factions. Although political memoirs are typically self-serving and occasionally revisionist, they do capture the emotions of political

battle and the reality of strange and shifting alliances. The autobiographical accounts of both Tory and Labour politicians reveal interesting confrontations within each political party. The Labour Party consisted of mostly democratic socialists, and the Tory Party saw centrists dominating key positions within the party. However, there were others keen to challenge status-quo thinking.

Thatcher's challenge of the postwar consensus of Labour and Tory leaders was both dramatic and subtle. The story of a shopkeeper's daughter upholding free-market capitalism against social democratic ideas defended by Labour politicians, often from privileged backgrounds, makes for captivating confrontations. But there are interesting twists to the story. Prime Minister James Callaghan (1976–1979) angered many in the labor movement with economic statements more in sync with free-market thinking, and Thatcher, stimulated by new economic thinking, nonetheless proceeded carefully so as not to antagonize Tory moderates distrustful of free-market ideas. In the end, the issue of inflation altered British economics and politics and Thatcher was there to take advantage of the moment and score a victory over “socialism.”

## NOTES

1. Jim Prior, *A Balance of Power* (London: Hamish Hamilton, 1986), 106.
2. William Keegan, *Mrs Thatcher's Economic Experiment* (London: Allen Lane, 1984), 45.
3. John Maynard Keynes, *The General Theory of Employment, Interest, and Money* (New York: Harcourt, 1963), 3.
4. Steven Pressman, *Fifty Major Economists*, Third Edition (London: Routledge, 2014), 145.
5. Crotty writes: “The consistency and clarity with which Keynes presented and defended his radical, pro-democratic socialist theory and policies in *The General Theory* once again raises a question I posed earlier. How is it possible that one of the most important and influential books in the history of economic thought, written by one of the most important and influential economists who ever lived, came to be so profoundly misunderstood by the economics profession?” See James Crotty, *Keynes Against Capitalism: His Economic Case for Liberal Socialism* (London: Routledge, 2019), 308–9.
6. Pressman, *Fifty Major Economists*, 165. Sylvia Nasar, *Grand Pursuit: The Story of Economic Genius* (New York: Simon & Schuster, 2011), 275.
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9. Caldwell, ed., *The Collected Works of F.A. Hayek Volume II*, 67, 76–78, 83.
10. Caldwell, ed., *The Collected Works of F.A. Hayek Volume II*, 21.
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16. J.D. Tomlinson, "The Iron Quadrilateral: Political Obstacles to Economic Reform under the Attlee Government," *Journal of British Studies* 34, no. 1 (1995), 96, 105.
17. Richard Toye, *The Labour Party and the Planned Economy, 1931-1951* (Woodbridge, Suffolk; Rochester, NY: Boydell & Brewer, 2003), 206, 208, 241.
18. Thatcher, *Margaret Thatcher*, 51–52.
19. Quoted in Robert M. Page, "The Conservative Party and the Welfare State since 1945," in *The Conservative Party and Social Policy*, ed. Hugh Bochel (Bristol, UK: Bristol University Press, 2011), 28.
20. Nick Ellison, "The Conservative Party and Public Expenditure," in *The Conservative Party and Social Policy*, ed. Hugh Bochel (Bristol, UK: Bristol University Press, 2011), 42, 46–47.
21. Thatcher, *Margaret Thatcher*, 76–77.
22. Glen O'Hara, "'This Is What Growth Does': British Views of the European Economies in the Prosperous 'Golden Age' of 1951-73," *Journal of Contemporary History* 44, no. 4 (2009), 697.
23. Michael J. Oliver, "The Two Sterling Crises of 1964: A Comment on Newton," *The Economic History Review* 65, no. 1 (2012), 319.
24. For a helpful discussion of some of the key literature, see Hugh Pemberton, "Relative Decline and British Economic Policy in the 1960s," *The Historical Journal* 47, no. 4 (2004), 989–1013.
25. John Campbell, *Margaret Thatcher: The Grocer's Daughter Volume One* (London: Jonathan Cape, 2000) and *Margaret Thatcher: The Iron Lady Volume Two* (London: Jonathan Cape, 2003); Robin Harris, *Not for Turning: The Life of Margaret Thatcher* (New York: St. Martin's Press, 2013); Graham Goodlad, *Thatcher* (London: Routledge, 2016); and Charles Moore, *Margaret Thatcher: The Authorized Biography: Volume One* (London: Penguin Books, 2014). Other biographies include Hugo Young, *One of Us* (London: Macmillan, 1989) and Jonathan Aiken, *Margaret Thatcher: Power and Personality* (London: Bloomsbury, 2013). Most of the literature on Thatcher as prime minister gives significant treatment of her break from the "socialist consensus" of the postwar period. For a concise biography with a section on Thatcher and the historians, see Goodlad, *Thatcher*. David Cannadine's brief biography, *Margaret Thatcher: A Life and Legacy* (Oxford: Oxford University Press, 2017), offers a guide for further reading.