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# CONTENTS

## PAPERS


Matthew Smith, *Technological Progress in the Theory of Accumulation of the Classical Economists and Marx* 9

Gabriele Guzzi, *Metaphysical or Anti-Metaphysical? A Critical Reconstruction of Vilfredo Pareto's Philosophical Assumptions* 37

Tristan Velardo, *Léon Walras'* Études d'Économie Politique Appliquée *Influence on Joseph Schumpeter's Theory of Bank and Crises* 65

Adrien Faudot, *Paul Einzig's Contribution to the Economics of International Clearing* 89

Alessandro Pavarin, *Francesco Vito and Corporatism* 113

Timothy Perri, *Gary Becker's Previously Neglected Early Research on Training on the Job* 163


## DEBATES


Steven Sawyer, *The Origins of Henry Sidgwick's Ideas on Waste: A Reexamination* 187

Ignacio Falgueras-Sorauren, *Towards a Clarification of the Concept of Scarcity: Some Comments on "There is no Such a Thing as a Free Lunch"* 199

Will C. Heath, *A Rejoinder to Professor Falgueras-Sorauren* 225


## BOOK REVIEWS


H. Spencer Banzhaf, *Pricing the Priceless: A History of Environmental Economics* (Antoine Missemer) 237

Ramesh Chandra, *Endogenous Growth in Historical Perspective: From Adam Smith to Paul Romer* (Paweł Kawalec) 240

Simona Pisanelli, *Slavery and Colonialism in the History of Economic Thought* (Cosimo Perrotta) 242

Hiroshi Yoshikawa, *Reconstruction of Macroeconomics: Methods of Statistical Physics, and Keynes' Principle of Effective Demand* (Massimo Di Matteo) 244

Benjamin Friedman, *Religious Influences on Economic Thinking: The Origins of Modern Economics* (Farhad Rassekh) 248

Cosimo Perrotta, Salvatore Rizzello, Claudia Sunna, *Human Capital. The Driving Force for Economic Development* (Silvia Leoni) 249

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# PAUL EINZIG'S CONTRIBUTION TO THE ECONOMICS OF INTERNATIONAL CLEARING

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Abstract · Paul Einzig (1897-1973) was a prolific financial journalist, best known as a commentator on economic life rather than a pure economist. Nonetheless, he remains an academic reference, above all for his study of foreign exchange markets. This paper introduces the reader to his writings on international clearing published in the 1930s and 1940s. The article shows the original approach adopted by Einzig, with one foot in academia and another in the world of financial practitioners and with a great freedom of speech. Einzig had an acute understanding of the international liquidity crisis that hit Europe in 1931 and the resulting exchange control and clearing agreement dynamics that spread throughout Europe. He saw clearing agreements as a new instrument for rebirth of Germany's economy. In 1935, he called for universalization and multilateralization of clearing. A few years later, he was a supporter of Keynes' proposals for an International Clearing Union. Einzig's interest in international clearing nurtured his later insights on foreign exchange markets and the post-war international monetary system.

Jel codes · B20, F31, F33.

Keywords · Paul Einzig, International Clearing, Bilateralism, Exchange Controls.

## 1. Introduction and Biographical Notes

Paul Einzig considered himself a commentator on economic life rather than a pure economist. He published an impressive number of books and articles. In his autobiography, published in 1960, he states that he published forty-six books (Einzig 1960, 124). Additional books would follow up to his death in 1973. His autobiography also reveals that he was a dedicated networker, meeting the most famous economists and political leaders from throughout the world, Keynes, Mussolini and Schacht among them. Born in 1897 in Brasov (a Hungarian city until 1920, becoming part of Romania following the Treaty of Trianon), he started his

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career as a junior journalist for a Hungarian financial journal in Budapest at the end of the First World War. At that time, he admired the British weekly newspaper *The Economist* and his dream was to be published in it. He emigrated to London with that objective in mind and was not long in achieving it (in 1919). His first two articles dealt with the monetary situation in Hungary and Romania. In 1920, after enrolling as a student at the London School of Economics, he published two four-page articles in *The Economic Journal*, an even greater achievement (Einzig 1920a; 1920b). He started on a long-term collaboration with the *Financial News*, a City-based journal that no longer exists, being absorbed by its rival, the *Financial Times*, in 1945. He moved to Paris in 1921 and became the *Financial News*' correspondent in Paris. He submitted his PhD thesis at Sorbonne University (Paris) in 1923 on price formation process. After his return to London, he became the same newspaper's foreign editor.

"Owing to the size of my output, I acquired a reputation of superficiality" (Einzig 1960, 125). Yet Einzig is still referenced by academics fifty years after his death. For example, in the recent *Handbook of the History of Money and Finance* (Battilossi *et al.* 2020), Einzig is quoted – sometimes extensively – in four different chapters by authors writing on a variety of topics. Maurer (2020) quotes him for his work on primitive money; Nogues-Marco (2020) for his work on the history of foreign exchange, including in the pre-industrial era; Accominotti (2020) on his 1930s work on foreign exchange issues and theory; and Battilossi (2020) for his late work on Eurodollar markets.

Admittedly, Einzig will not be remembered as a major contributor to economic theories of the 1930s and 1940s. However, his writings show that he was not simply observing the events of his time but also taking part in key discussions and influencing general opinion. He was ahead of his time in analysis of the clearing agreements that proliferated in the 1930s. As early as 1934, he perceived that these new practices were a financial innovation with significant potential, including for the United Kingdom, both for internal and international regulation of the economy. In this sense, he preceded and certainly influenced such prominent economists as John Maynard Keynes, with whom he corresponded. His expertise in international monetary affairs led him to take a stance on the attitude that official authorities should adopt vis-à-vis the collapse of the gold exchange standard and the rise of bilateral clearing agreements in Europe and beyond. A number of recent papers and articles have dealt with his work. Torre (2012) analysed his views on exchange rates, which influenced much of his lifework as a financial columnist and economist. Patalano (2023) devotes several pages of his article on international clearing to Paul Einzig, emphasizing that he proposed a multilateral clearing system in the mid-1930s. This paper's objective is to explain Einzig's views on international clearing, situate them in their historical context, and explore the connection between his vision of clearing and his other publications. It shows that Einzig assumed that clearing should be combined with planning and exchange controls. He went so far as to assume that exchange clearing was necessary for the smooth functioning of managed economies. He took the existing situation of bilateralism as a point of departure for considering multilateralization, which seemed desirable and more realistic at the time.

We did not make use of all of Einzig's enormous output to prepare this paper, but only what seemed relevant to the study of international clearing. The main book analysed in this paper is *The Exchange Clearing System* (1935). In it, Einzig developed innovative thoughts on the need to reform the international monetary system, based on his acute knowledge of the financial practices of the time. We complemented these readings with other texts he published subsequently (1937; 1948; 1949), in which we see a common thread, along with Einzig's archives, which are held at Churchill College, Cambridge (UK). The next section focuses on the historical context of the early 1930s. Section 3 analyses Einzig's writings on international clearing, mainly based on his 1935 publication and other later texts. Section 4 explores some of the ideas developed by Einzig in publications on such related fields as forward exchange markets and the wartime debates on international monetary order.

## 2. The General Context of Einzig's Writings in the 1930s

This section aims to summarize the main historical facts relating to the 1931 crisis, which resulted in the development of clearing agreements and Einzig's interest in this evolution.

### 2.1. *The Crisis of 1931 and the First Clearing Agreements*

The First World War resulted in international treaties that imposed huge reparations on the defeated countries, Germany, Austria, Hungary, and Bulgaria in particular. These countries had to bear the burden of the Versailles Treaty and the related Trianon Treaty regarding Hungary. They imported large amounts of capital from the rest of the world, especially after 1923-1924, during which their currencies stabilized (Accominotti 2019, 263). In 1929, the flows of funds borrowed by Austria, Germany and Hungary began to stagnate and they decreased in 1931. This reversal triggered a currency crisis (Temin, 2008) sometimes referred to as a twin crisis – *i.e.* a banking and currency crisis – in the three countries (Schnabel 2004; Macher 2019), symbolized by the collapse of the Credit Anstalt Bank in Austria (Aguado 2001).

According to Einzig (1935, 35), the 1931 crisis was mainly due to institutional failure and «the result of unfettered activity in international finance and trade». The loans granted by creditor countries to debtor countries so as to enable the former to export goods to the latter were too large. In Einzig's opinion, there was excessive freedom of trade in the 1920s. Any shock would have led to rapid withdrawal of credits granted to such debtor countries as Austria, Hungary, and Germany.[1]

Those countries' governments gradually took measures to halt capital outflows and made various arrangements with their creditors through standstill agreements during the summer of 1931. However, confidence in their economies was destroyed. Maturing claims could no longer be renewed and new foreign loans were no longer granted (Child 1958, 8). In consequence, several countries were no longer able to reimburse their foreign loans. The "financially weak countries" (Einzig 1935, 53) were exhausting their gold and hard currency reserves and had to limit their imports. As a result, governments implemented exchange controls against a panic flight of capital, "the international equivalent of a run on the banking system" (Child 1958, 3). In return, the crisis hit the London financial market badly as it was exposed to trade finance activities (Accominotti 2019). In the beginning, policymakers and economists in creditor and debtor countries alike thought that the suspension of currency convertibility was only temporary. However, they initiated a trend that went on to include a growing number of countries.

Balkan and Latin American countries were very interested in this move to adopt new foreign exchange regulations initiated by Austria, Hungary, and Germany. Their interest arose from the fact that they were mainly agricultural countries, impoverished by the international fall in agricultural prices resulting from the 1929 crisis. Therefore, they applied foreign exchange regulations – some of them being already engaged in the implementation of such regulations at the time (*e.g.* Uruguay and Argentina). For their part, creditor countries were reluctant to adopt clearing agreements but nonetheless decided to do so in order to liquidate debts rather than suffer a mere default or a blockade of their claims. Most of the governments taking part in this movement concluded that it was in the national interest to balance their trade with each trade partner separately, on the model of multiple bilateral equilibriums.

### 2.2. *Einzig's Live Coverage of the Bilateral Clearing Policies Set up by Germany and Central and Eastern Europe*

The origin of exchange clearing can be traced back to Danubian and Balkan economies, although Germany soon followed suit (Einzig 1935,

[1] Einzig was also obsessed with the flows of short-term and «abnormal» capital movements, as was recognized by Kindleberger, who wrote that, among the economists who worked on the subject, "perhaps Einzig stands out" (Kindleberger 1937, 155).

chapter 6). The first clearing agreement was signed between Switzerland and Austria on November 12, 1931. Switzerland and Hungary's came two days later on November 14.[1] Thanks to the agreement, "there was no longer any need for Swiss and Hungarian importers and exporters to buy and sell exchanges in connection with their dealings between each other" (Einzig 1935, 55). The agreement's signatories failed to realize "the true significance of their innovation" (55-56) at the time. It may be argued (*e.g.*, Haines 1943) that the idea of international clearing was not new and had in fact been proposed at several international conferences in the 19th century, and at virtually all such conferences in the first three decades of the 20th century. However, proposals before 1931 were based on voluntary clearing between central banks, and "the idea of a universal and compulsory exchange clearing did not exist before 1931" (Einzig 1935, 57). In the 1930s, clearing became a subject of interest for researchers (see, *e.g.*, Ellis 1939), even though most of them still denigrated it.

The first generation of clearing agreements was concluded at the initiative of creditor countries, their purpose being to liquidate debts (Nyboe Andersen 1946). This explains why Switzerland – a country that was not financially on its knees – was involved in the first agreements from the beginning. Individual creditors in various countries (*e.g.*, Switzerland) formed associations that also supported the creation or renegotiation of clearing agreements in order to unblock their claims, as Milhaud reported (1936, 410-414). Einzig had a personal interest in studying bilateral clearing, as is revealed in his archives. As he was Hungarian and had worked as a financial journalist in Budapest before emigrating to London, Einzig had kept deposits and assets in Hungary amounting to 7,000 US dollars, a substantial sum at the time.[2] As the US dollar was a hard currency – subject to restrictions – it was impossible for Einzig to take his deposits out of the country. It seems that his first reaction after the agreement of November 14, 1931 was to try to recover his claims by pulling what strings he could, but he finally decided to give up the attempt and politely asked his correspondent in Hungary, Dr Racz, to "drop the matter". On June 3, 1932, he told Dr Racz that he accepted the fact that the Hungary's Standstill agreement did not plan "preferential treatment granted to specific creditors".[3] Despite this personal financial loss, he became increasingly interested in clearing agreements.

[1] Einzig made a mistake in his book, ignoring the agreement between Switzerland and Austria and considering that the Switzerland-Hungary agreement was the first.

[2] Dr Racz's letter to Einzig, June 6th, 1932; The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/2(33) – Correspondence 1930-1934.

[3] Einzig's letter to Dr Racz, June 3rd, 1932, The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/2(32) – Correspondence 1930-1934.

The first generation of clearing agreements produced satisfactory results insofar as trade was prevented from collapsing completely despite unfavourable international financial conditions. In the meantime, the economic problems (deflationary and beggar-thy-neighbour policies) that had led to the drop in international trade were not solved. 1934 marked Germany's "New Plan" and the second generation of clearing agreements (Roselli 2014, 127-129). Germany realized that it could use bilateral clearing strategically for rearmament purposes. Hjalmar Schacht, the Reichsminister of Economics and President of the Reichsbank, developed an ingenious network of bilateral clearings more in line with this objective and resulting in renegotiation of previous clearing agreements. In Europe, Schacht's New Plan "greatly reinforced the well-established philosophy of foreign trade and exchange controls" (Roselli 2014, 128) but, at the same time, caused even greater dislike of clearing agreements among the great majority of the elite in Britain and in the United States, which is why Einzig's books on exchange controls and exchange clearing, published in Britain in 1934 and 1935 respectively, were provocative.

## 3. Einzig's Opinions on Exchange Controls and Clearing Agreements

### 3.1. *Defining Exchange Clearing*

Einzig proposed a simple definition of clearing: "a process whereby two or more parties offset claims against each other with the object of eliminating or reducing cash transfers" (1935, 66).[1] Reduction of cash transfers has several advantages for all economic agents, who can satisfy real needs through consumption of goods and services without transferring cash, in as much as they can offer their trading partners an equivalent amount of goods and services as compensation. In this definition, Einzig recognized that clearing was a daily practice *lato sensu* even in the absence of formal international bilateral or multilateral agreements.

Einzig was interested in clearing as an organizational process of exchange. Later in his career, he developed this research further on monetary and barter exchanges in an article published in *Nature* (Einzig 1948) and a book on primitive money (Einzig 1949). The monetary practices of the 1930s and 1940s raised his interest in anthropological issues, especially the study of barter. He assumed that in the great majority of

[1] Clearing agreements must be distinguished from compensation agreements, the latter being more restrictive. Money did not have an active role in compensation agreements, which dealt with *definite quantities* of commodities exported by each partner. As Ellis (1939) wrote, compensation agreements are less "liberal" than clearing agreements.

instances, "the evolution of money was an unconscious and gradual process" (Einzig 1949, 353).

In a sense, international trade under clearing agreements was similar to barter due to the absence of monetary transfers and economists often conflated the two exchange arrangements (Staudinger 1940). Einzig wrote that bilateral clearing "was an advanced form of barter" (Einzig 1944, 27). Clearing is a system associated with credit (overdraft) without transfers of coins or cash. Readers familiar with studies of clearing may assume that Einzig's later exploration of anthropological studies was not incidental, as clearing agreements raise a good many questions relating to the process of exchange in merchant societies.

*Exchange clearing* is obviously interested in various forms of organisational processes of exchange. Most of the book is taken up with comparisons of different methods of clearing. Under a "regime of freedom" (1935, 203), (private) banks and foreign exchange markets carry out international clearing by themselves. In fact, any bank is itself an institution practicing clearing with its own network of customers – one of its tasks consists of marrying buying and selling orders. At national level, the domestic banking system is organized so as to offset its nationals' buying and selling orders against each other. In its relations with the rest of the world, it only has to find a foreign counterpart for the net balance in foreign exchanges.

To this end, foreign exchange markets act as agents of multilateral clearing of currencies. In his book, Einzig sometimes used the term "foreign exchange market" in the singular because markets located in the major financial centres were unified by telegraph and telephone facilities that facilitated marriage of transactions. Markets could clear different countries' balances in various currencies: "if on balance London is a buyer of dollars and a seller of French francs, and Paris on balance is a seller of dollars and a buyer of sterling, then the two markets offset their operations against each other." (1935, 67). This form of clearing "happens without any conscious effort to that end" (1935, 69).

Voluntary international clearing by public institutions existed alongside private clearing (Einzig 1935, 68), especially between post-offices and central banks – the latter dealing, for instance, with war debts through the newly created Bank for International Settlements.[1] All such initiatives remained marginal. Einzig (1935, 69) insisted that the main innovation, implemented in 1931, was *compulsory* clearing: "exchange clearing in the real sense of the term has to be compulsory". This meant

[1] The reference to clearing between post offices had already been made in 1922 by Albert Janssen, director of the National Bank of Belgium, in a report for the League of Nations on establishment of an international clearinghouse (Janssen 1922).

that the clearing office was the only legal channel for payments carried out by importers and exporters alike regarding international transactions. The distinction between private, voluntary, and compulsory clearing is of primary importance. With the 1931 crisis, private clearing broke down in the wake of the financial crisis and voluntary clearing was still only a marginal practice. As a result, whenever we use the terms "exchange clearing" or "international clearing" hereinafter, we mean compulsory clearing.

Einzig (1935, 69) highlights four types of exchange clearing:

1. Unilateral
2. Bilateral
3. Triangular or Multilateral
4. International

The first three types were existing forms of clearing agreements in the 1930s, while the fourth (international) was the project defended by Einzig, as an ideal solution (see the subsection below on Einzig's proposal). It is worth noting that this typology provided the rest of the book's structure.

Unilateral clearing was a highly marginal emergency measure consisting of unilateral application of a barter transaction with a country, the latter having no choice but to accept settlement in goods instead of hard currency. In practice, such clearing was soon replaced by bilateral clearing, which formalized the new trade relationship. Einzig discussed bilateral clearings in detail. Such clearings were often limited in scope, which varied considerably depending on signatories. Einzig provided eight categories of bilateral clearings with graduated significance relating to the goods and services concerned by the agreements. The first only includes one specific commodity while the eighth comprises practically all commercial transactions, invisible trade, and payments of interest for financial indebtedness.

Bilateral clearings rested on bilateral trade and opposed the logic of multilateral trade, which economists have often referred to as triangular trade. Einzig acknowledged that, under a free regime, triangular trade was superior to bilateral trade. As triangular trade is hampered by bilateral clearings, triangular clearing restores it with even greater advantages than in a free convertibility regime. Einzig provided two rare examples of triangular clearing taking place in the early 1930s, the first being between Greece, Germany, and Czechoslovakia. Czechoslovakia had an agreement with Greece which resulted in a very large surplus in its favour. Greece had a surplus with Germany. With the German government's consent, the uncleared balance was settled by a transfer from the Reichsbank to the Czechoslovak National Bank. This was subject to governments' accepting that one country's claims could be transferred in order to settle a debt vis-à-vis another country – in this case, the German government. The second example was Greece's clearing agreement with Romania and Yugoslavia. As Greece had a favourable trade balance with the other two countries, it had the right to cede a percentage of its claims to another country. Triangular clearing could become multiangular clearing with increasing numbers of participants, not limited to three. It could then become the expected international exchange clearing: "the difference is that in the case of international clearing the number of participants would be larger, and that there would be an international organisation in charge of clearing" (Einzig 1935, 150).

Einzig upheld the contention that exchange clearing was not harmful to domestic banks' activities. Banks based in the UK and other capitalist countries were afraid they would lose a large part of their profitable activities due to implementation of clearing agreements. Einzig argued that they would be able to make profits from their role as intermediaries between national clearing offices and their customers. Furthermore, trade finance tools, such as trade acceptances, would still be necessary. Domestic credit policies to businesses and households would still exist. Banks' most severely affected employees would be foreign exchange dealers, who could well "be employed in other departments" (1935, 170). Exchange clearing would make foreign exchange markets pointless, at least as regards transactions taking place between residents of countries included in a clearing agreement.

### 3.2. *Criticizing the Professional Economists of his Time*

Einzig did not share the opinion commonly held by the economists of his day, who systematically condemned exchange controls and clearing agreements despite their widespread use. This general rejection was particularly prevalent in such free economic countries as the United Kingdom and the United States. As explained by Sayers (1956, 227-228), economists in Britain were generally opposed to exchange control because the German example was "distasteful": it involved suppression of foreign exchange market operators, employment of thousands of people for control enforcement and, last but not least, it would damage sterling's international status.

From the United Kingdom's point of view, implementation of exchange controls and clearing agreements would have several advantages. Einzig called for development of clearing agreement diplomacy initiated by the British government in order to liquidate the UK's outstanding credit. "I persisted in urging the government year after year to resort to exchange clearing to speed up the liquidation of the standstill credits" (Einzig 1960, 178). Furthermore, it could prevent the cross-border capital flows that endangered the pound sterling's exchange rate. Einzig claimed that he was responsible for convincing Keynes to denounce the loopholes in British foreign exchange policy in 1939-1940. If the Treasury postponed exchange controls in Britain until 1939, it was mainly because of the pound sterling's international status and London's significance for global financial markets. According to Einzig, sterling inconvertibility and loss of its international prestige would be the main disadvantages of exchange controls – but these problems might provide an opportunity as the government would have a free hand to implement new policies in a Keynesian spirit.

Einzig distinguished himself from the "orthodox school", which in 1935 still hoped to restore complete freedom of international flows of goods and capital. He accused it of overlooking «the fundamental changes in the world's economic and financial system brought about since 1914» (1935, vii). Orthodox economists still clung to the notion of an international economic system based on factors that had disappeared as early as 1914 and lost its *raison d'être* (1935, 23). He also criticized the "radical school of isolationists" (1935, vii), on the grounds that isolation was not desirable and increases in foreign trade and financing might improve the standard of living. Einzig mocked economists, who were in no way responsible for the invention of clearing: "When the first clearing agreement was concluded, it had no theoretical background. As is so often the case, practical statesmen and administrators stole a march on economists" (1935, 59). "Theoretical economists" simply ignored clearing until at least 1935. It should not have prevented them from believing in the further development of exchange clearing. "In the majority of cases the right thing is done for the wrong reasons; statesmen tumble on the right solution by mistake; changes of fundamental importance are adopted without anyone realising what is being done. This is how international exchange clearing will be adopted if and when it does become reality." (Einzig 1935, 200-201). It is worth noting that Keynes used almost the same metaphor in September 1941, in the letter introducing the first draft of his memoranda on *Post-war Currency Policy*, which corresponds to the first version of his proposals for an International Clearing Union: "[A]fter the above trials and errors Dr Schacht stumbled in desperation on something new which had in it the germs of a good technical idea" (Keynes 1980, 23).[1]

[1] Patalano (2023, 321) also shows the "spontaneous process" which "had brought to the fore the embryonic form of a new international order, based on clearing agreements". This process was reversed by the Bretton Woods agreements, which reinstated the liberal order based on free currency convertibility.

Practical economists' interest in clearing was evident, however, in a growing number of institutions, where there were no theoretical economists. The London Chamber of Commerce published a proposal for extension and multilateralization of clearing agreements in 1933. One prominent statesman who was interested in clearing, especially *international* clearing, was Lucien Lamoureux, the French Minister of Trade and Industry in 1934. Lamoureux was won over by the Milhaud Plan for an international clearing union (Milhaud 1933) and called for a League of Nations inquiry on clearing agreements in force in Europe and Latin America. As a consequence of this campaign, a report was commissioned by the Assembly of the League of Nations (LON 1935). The inquiry consisted of asking countries that participated in clearing agreements their opinions of clearing and analysing the answers. Einzig was in contact with members of the French delegation at the LON Assembly before they asked for an inquiry to be launched. He received a letter in September 1934 informing him that France would be initiating the LON inquiry; it was written in French and explained the merits of compensation and clearing.[1]

The League of Nations report published the following year was a disappointment for proponents of international clearing. Einzig adamantly rejected the objections made in the report, which took a negative view of clearing agreements. The inquiry's last question was "Does the extension of the clearing system to the sphere of multilateral agreements appear to you possible and desirable? If so, in what form?" (LON 1935, 142). The responses published were mostly negative, although some more encouraging and positive responses were also reproduced and commented on by Einzig in his book (1935, 138-140).

Einzig explained that the report was drafted by a committee of seven orthodox economists – including an American (Oscar Ryder) and two British (Otto Niemeyer and Frederick Leith Ross) – who disliked any government interference in such matters and did not hide their preference for free trade and free currency convertibility. Another of the LON study's problems was that it was misled by Germany's behaviour in clearing agreement practices: Einzig was convinced that Germany used clearing agreements to exploit its trade partners. However, according to him, this was due to Germany's strong position in bilateral negotiations, and analysts should make a clear difference between such specific bilateral contexts and the clearing principle itself. Einzig repeatedly differentiated the innovative institution (clearing agreement) from the motivation of the government that negotiated it. He argued that Ger-

[1] Anonymous and undated letter to Paul Einzig, The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/2(53-60) – Correspondence 1930-1934.

many's advantage would disappear if clearing was multilateral and included other great powers. Germany was not even a genuine supporter of the exchange clearing system. Schacht was «an orthodox banker» who did not want a universal clearing system and only wanted to sign a clearing agreement when it was "in the interest of Germany to do so" (Einzig 1935, 184).

Despite the fact that his claims that economists had neglected the study of clearing seem largely justified, Einzig's ideas resonated with several high-profile economists who had a keen interest in exchange clearing. The best-known, of course, was Keynes (see below), who was clearly interested in the book and praised it for the burgeoning idea of multilateral clearing. Ragnar Frisch – who became the first recipient of the Nobel Prize in Economics in 1969 – was also interested in clearing and sent Einzig letter with his own scheme attached.[1] Dennis Robertson read the book and found it "very helpful and informative" but wrote to Einzig that he would not be "capable of a very high degree of sympathy with your standpoint, which I regard, in spite of your disclaimers, as extremist!".[2] After publication of *Exchange clearing*, Einzig received several letters from fellow economists who wanted to meet him, including Michael Heilperin, a Geneva-based academic who supported the Milhaud Plan, and Feliks Mlynarski's assistant, who contacted Einzig with a view to publishing a Polish translation of the book.[3] In short, *Exchange Clearing* reinforced Einzig's acceptance in academic circles.

### 3.3. *The Proposal for an International Exchange Clearing System*

In mid-1935, international clearing was still a recent idea: according to Einzig, the first proposal was published by the London Chamber of Commerce in 1933. One may challenge this assumption. After the First World War, a series of proposals emerged to facilitate the restoration of world trade and the solution to the reparation problem (*e.g.*, Janssen 1922). A few additional proposals had offered to create an international clearing house, for instance the Swiss-based "Society for Studying the Question of the Establishment of the International Clearinghouse Association and the International Currency Guarantee Corporation" in 1928.[4]

[1] Ragner Frisch's letter to Paul Einzig, March 7, 1936, The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/4(15) – Correspondence 1936.

[2] Dennis H. Robertson's letter to Paul Einzig, April 14, 1936, The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/4(19) – Correspondence 1936.

[3] Joseph Swidrowski's letter to Paul Einzig, September 16, 1937, The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/5(18) – Correspondence 1937.

[4] "War on War: The Cornerstone of Universal Peace" Society for Studying the Question of the Establishment of the International Clearinghouse Association and the International Currency Guarantee Corporation. BundesArchiv, Berlin Lichterfelde. BARCH R 57/7586.

Schacht had proposed in 1929 that a BIS emerge in relation with the inter-allied debts (Lüke 1985). However, all these proposals were largely ignored for lack of political support. The 1931 banking crisis in Austria and Germany and the implementation of exchange controls are the tipping point. Einzig had already written a chapter on the subject in his 1934 book on *Exchange Control*, but elaborated further on it in the 1935 book.

Einzig thought that evolution toward a multilateral clearing system would be a natural process due to the growing demand for harmonization and coordination of bilateral clearings and also because he observed that such planning, or at least a high degree of interventionism, was well established in many economies: a development that should make exchange clearing more appealing. According to Einzig (1935, 209), "under a managed economic system (…), exchange clearing is indispensable".

Einzig's proposal was recently rediscovered and presented by Patalano (2023). It made the case for the creation of an International Clearing Institute, which would be a permanent international institution: "to attain that end it is necessary to have some sort of central organisation which acts as a clearing-house between the national clearing offices. [It] would be the ideal permanent solution to the problems of international transfers" (Einzig 1935, 73). The institution to be created could be a section of the Bank for International Settlements or of the League of Nations Secretariat, or a newly-created institution; the third option might have been the best insofar as the BIS and the LON were both hostile to international clearing. The Institute would host an international clearing house with a universal purpose – *i.e.* it would cover all visible and invisible trade as well as financial flows.

The International Clearing Institute would be an informational hub. Its function would be "that of the broker who brings the parties together and provides technical facilities for them to come to terms with one another" (Einzig 1935, 150-151). It would have to collect information and data on the status of bilateral clearing accounts and communicate it to governments. Representatives of each of the organization's member nations could meet on a daily basis, making it unnecessary to arrange international conferences (156). This system could further evolve towards automatic clearing. Automatic clearing means that debit and credit balances are able to offset each other automatically without any specific negotiations. Paradoxically, this system "bears extreme resemblance, in substance if not in form, to the regime of freedom." (Einzig 1935, 162). There is less political interference in the clearinghouse's daily operations as automatic procedures prevail over discretion.

In its most ambitious form, international clearing would cover all cross-border operations. As Patalano argues (2023, 307), Einzig was one of the first economists to propose such a systematic institution for international clearing. Furthermore, Einzig tried to forestall all criticisms relating to any economic and technical problems that might result from implementation of his proposal.

The main argument in favour of an International Exchange Clearing system was that it would eliminate most of the disadvantages of bilateral clearings, such as diversion of trade at the expense of countries without clearing (Einzig 1935, 108-109). The diversion problems stemmed from the fact that countries with clearing tried to export to countries without clearing in order to get payments in cash (hard currencies), while they tried to import only from countries with clearing so as to avoid paying in cash.

Einzig was aware of the problems raised by negotiation of a multilateral clearing scheme, stemming from the political opposition or reluctance that had *de facto* prevented overcoming the primitive bilateral level. International exchange clearing should preferably be a permanent regime enabling interventionist policies and planning in line with the emerging Keynesian paradigm. However, Einzig (1935, 160) argued that even liberal economists, who fundamentally preferred the economic freedom regime for international payments, should aim at improving the clearing systems in force in 1935, as doing so could accelerate restoration of the international economy and make a return to the former regime of currency convertibility possible.

Einzig rejected the idea that multilateral and universal exchange clearing might be fundamentally opposed to the gold standard: "they are by no means incompatible" (1935, 215). Such opposition was highlighted by a number of proponents of international clearing but tended to antagonize economists. Under the exchange clearing regime, gold would cease to be shipped for arbitrage purpose but could continue to be used for settlement of balances that were not cleared through the netting process.[1] Einzig (1935, 217) also explained that gold could be combined with clearing for the purpose of capital transfers: Countries granting cash loans should agree to lose a corresponding amount of gold, which would require the consent of both countries involved and de facto capital controls.

Keynes read the book and was particularly interested in the multilateral clearing scheme. He seems to have been won over by the scheme proposed by Einzig. In a letter to him on December 10, 1935, he wrote:

> I have read [The Exchange Clearing System] with a good deal of sympathy. I agree with you in thinking that the various clearing systems may prove to have something rather important to contribute to the evolution of the International Exchange system of the future. (…)

[1] This idea seems to anticipate the clearing process chosen in the European Payments Union (1950-1958).

> On the other hand, I feel that you rather underestimate the advantages of triangular and multilateral clearing. (…) But, all the same, multilateral clearing is really essential. And, as there is no reason why it might not be feasible under clearing systems, there is no necessity to minimize its importance.[1]

Such encouragement certainly reinforced Einzig's opinion, which was further reaffirmed in his *Theory of Forward Exchange* published two years later and dedicated to Keynes.

## 4. The Influence of International Clearing on the Rest of his Lifetime Work

Einzig's stance on exchange clearing stimulated an important part of his subsequent research. This is what we assume and develop in the following sections.

### 4.1. *Einzig's Heterodox View on Money*

Einzig shared a Keynesian vision of money, banking, and international monetary relations. This was more especially evident in his writing on international monetary economics, *e.g.*, in his views on foreign exchange markets, but also in his criticism of the interwar Gold Exchange Standard. For Einzig, the interwar period was already one in which money was "managed" by the state. Central banks were engaged in operations designed to mitigate the effects of the Gold Exchange Standard – which Einzig (1936, 5) named "managed gold standard" – and these practices ran counter to its original precepts. The main problem was that this management was not assumed, and even less associated with rational planning.

His analysis of international monetary relations has implications for both understanding and mobilizing the national banking system. For him, the national monetary system had to be protected by exchange controls. In a sense, Einzig was, like Keynes (see Eich 2022, 141 and 162), proposing a solution that would maintain international economic integration while ensuring that states could intervene in the economy. This institutional context seemed necessary for him to fully assume a conception of money inspired by Knapp and Keynes, according to which money creation is not constrained ex-ante by a link to gold or a prior hard currency reserve. Einzig's interest in this endogenous conception of money led him to take an interest in other forms of exchange, such as those in primitive societies, or in exchange markets. The demystification of money is, in fact, a constant in his work. Whether studying the

[1] Keynes' letter to Einzig, December 10, 1935, The Papers of Paul Einzig, Churchill Archives Centre, GBR/0014/ENZG 1/3(25-26) – Correspondence 1935.

techniques of foreign exchange markets, Euro-dollars or clearing agreements, his interest in an analysis of money based on credit and overdraft and characterized by great adaptability is noteworthy. Money adapts to the needs of society. The same conclusion arises from his study of primitive currencies, which aims at continuing the insights of Keynes' *Treatise on Money* (Einzig 1966, xv).

However, like some post-Keynesians would later emphasize, he believes that it is a mistake to try to solve economic problems with monetary solutions only – such as cheap money or negative interest rates – without tackling production and distribution issues (Einzig 1933). According to him, "plentiful money does not in itself create markets" (Einzig 1936, 82). He asserted that monetary expansion was only desirable if carried out within the framework of economic planning. Regarding inflation, Einzig opposed the argument according to which inflation always results from an increase in money supply: "Such a rise [in prices] may take place for a great variety of reasons. Most monetary experts are inclined to assume that there can be no substantial and lasting rising trend unless there is some form of monetary expansion. They are inclined to underrate the non-monetary factors of the rise in prices" (Einzig 1940, 30). He argued instead that the increase in money supply may result from price increases.

### 4.2. *The Theory of Forward Exchange (1937)*

In *Exchange Clearing*, Einzig wrote that many people had "a semi sentimental attachment to the free foreign exchange market", although the system had "inherent deficiency" (Einzig 1935, 170). Two years later, Einzig (1937, 428) was still doing his best to debunk the myths relating to foreign exchange markets' self-regulation, arguing that if left to take care of itself, the forward exchange system "contains all the virtues and vices of economic liberalism".

Einzig's support for international clearing was still strong in 1937, when his most scholarly book came out. He advocated abolition of, or at least significant changes in the role played by foreign exchange markets – *i.e.*, the object of the entire book. "During the past three years or so I have advocated, in a number of books and articles, the adoption of international Exchange Clearing, which would, of course, mean the abolition of Forward Exchange in its present form. I am now more than ever convinced that Exchange Clearing is the rational system, and that it will be adopted sooner or later." (Einzig 1937, x).

One may wonder why Einzig was set on studying forward exchange so thoroughly. First of all, he was well acquainted with financial practices and foreign exchange markets. He saw the evolution of the market, with a lack of literature on the subject that described modern practices. Einzig could not miss the opportunity to publish an additional book – he clearly seems to have been seeking academic recognition. Secondly, he thought that the advent of the international exchange clearing would take time. Meanwhile, academics and practical thinkers alike needed to stay fully updated on the latest evolutions in foreign exchange markets. In his book's conclusion (1937, 437), he wrote:

> Meanwhile, Foreign Exchange in general and Forward Exchange in particular will continue to exist for a long time. Were I not convinced that this will be the case, I should not have taken the trouble to write a book on Forward Exchange, even though it might be of some historical interest to future students after the universal and permanent adoption of Exchange Clearing.

He wrote repeatedly that the economists of his time were ill-informed on the mechanisms governing the developing forward exchange markets, a view supported by more recent studies on the subject (*e.g.*, Peel and Taylor 2002). Einzig added to Keynes' work on the anomalies observed on the foreign exchange market, which challenged the covered interest-rate parity theory. This would become the "Keynes-Einzig conjecture" (Peel and Taylor 2002).

### 4.3. *Denunciation of Nazi Germany Foreign Trade Methods*

Einzig's interest in political responses to the crisis of the 1930s led him to observe the variety of political regimes, and for a time he was interested, not to say seduced, by illiberal regimes such as Italian fascism. In *Economic Foundations of Fascism*, Einzig (1933, 13) wrote that "A great advantage of the Fascist economic system is that it facilitates and accelerates the process of readjustment, reducing to a minimum the "transition periods", and allaying to a great extent their inevitable disadvantages". He praised the corporate State, public works programmes against unemployment and the indirect government control over the banking system. Röpke (1935, 88) wrote that Einzig had a "remarkable lack of critical sense and analytical insight" with regard to the analysis of fascism.

Einzig had in contrast an aversion to Nazi Germany. In 1933, Einzig was already critical against National Socialism "merely manifesting itself in unpardonable excesses and short-sighted racial intolerance" (Einzig 1933, 121). From there on, he became one of the most uncompromising polemicists against any form of collaboration or appeasement with Germany. Einzig published numerous articles and books on German foreign economic policy during the 1930s. He came to the conclusion that Germany was penetrating the Danube area and plundering it economically. His analysis was contested by scholars stating that Germany was not exploiting the weaker countries in South-eastern Europe (Guillebaud 1940; Benham, 1940). It seems that Einzig was wrong or exaggerated German exploitation, at least during before the war. According to some empirically-based data, Germany had not favourable terms of trade for the 1930s with its Danubian partners – *i.e.*, it paid a high price to secure raw material imports and sold its export to low prices. Only with the war and the pressing needs of the Wehrmacht a brutal exploitation of the allied or occupied economies occurred (Ritschl 2001). During the controversy, the main problem was the availability of reliable data to establish indexes and measure the evolution of the terms of trade (Kindleberger 1954). While remaining cautious in his statements, Kindleberger (1954, 173) echoed Benham in writing that Germany paid a high price for its raw material imports from Danubian countries and its sales were at lower unit values. To some extent, Neal (1979) and Ritschl (2001) support this view.

With the outbreak of the war, Einzig's interest in the study of Nazi Germany only increased. He campaigned against appeasement views. Einzig's position was the consensus at the time (Kindleberger 1954, 173). He attacked Guillebaud (1940) and Benham (1940) in the *Economic Journal* (Einzig 1941). In his article, he argued that the multilateral scheme proposed by Dr Funk should be understood as an instrument of further Nazi exploitation of Europe. Einzig's 1941 book *Hitler's New Order in Europe* was reviewed by Hayek, who saw a pamphlet debunking Nazi propaganda on the alleged benefits of the New Order (Hayek 1997, 173-174). According to Einzig (1941, 12), although the multilateral clearing scheme remained an interesting theoretical proposal, in the case of countries conquered by the Nazis, their trade would be controlled by Germany for its own profit. Einzig assumed that "Germany abused the peculiar character of clearing system for exploiting the countries within her Lebensraum and for securing for herself an economic and political stranglehold over them" (Einzig 1944, 27).[1] Germany had, in the *Deutsche Verrechnungskasse* (the clearinghouse for dealing with German external payments with its headquarter in Berlin), in May 1945, a very significant debtor balance against its trade "partners" which would never be finally settled. France, Belgium and other occupied countries have therefore financed the war effort through the clearing scheme, which supports Einzig's thesis of Germany's exploitation through clearing (Einzig 1944, 61).[2]

[1] A legal action launched by Benham against Einzig and his publisher (Macmillan & Co) followed, which ended in a first clash with Keynes and led Einzig to stop contributing to the *Economic Journal* for years from 1942 onwards.

[2] The data of the *Deutsche Verrechnungskasse* are available in the German federal archives held in Berlin, Lichterfelde. BundesArchiv, Berlin Lichterfelde, BARCH R 184/186.

### 4.4. *Opinion on the Wartime British Clearing Plan and Rejection of the Anglo-American Agreement*

During the war, Einzig (1944) published an analysis that compared and discussed the American (Harry D. White) and British (Keynes) plans still being debated. He took a very positive view of Keynes' plan, considering it much more desirable than White's. The British proposals were similar in many points to the international exchange clearing scheme that Einzig had proposed several years earlier. Furthermore, Einzig was a true Keynesian. His admiration for Keynes is evident in the book. It was thanks to Keynes that proposals for international monetary reform, initially put forward in the 1930s by a few cranks (albeit correct according to Einzig), were given the stamp of respectability. Einzig wrote that the first intellectual battle over monetary theory and policy was fought and won "in the internal monetary sphere", arguing that "money must be made available for financing production to the limit of productive capacity" (Einzig 1944, 13). Wartime discussion on the post-war monetary system was the second battle, this time over the international monetary sphere. Hence the British Plan would enable domestic monetary expansionism and international monetary cooperation. The British Plan was "aiming at a change of the fundamental conception of money in its international aspects" (Einzig 1944, 112).

Einzig was so much in favour of the Keynes plan that he tried to thwart negotiations by publishing the American plan – which was still supposed to be confidential –in the *Financial News* on April 5, 1943. According to Einzig, this briefly interrupted negotiations. However, Einzig was dissatisfied with the hesitation of the Keynes plan to call for the continuation of exchange controls. He clearly maintained that multilateral clearing could not work without exchange controls and economic planning. Regarding the former, Einzig (1944, 128) made it clear that exchange controls had to be a feature of the post-war system: "If the choice lies between the Keynes Pan without exchange control and exchange control without the Keynes Plan, the latter should be chosen without hesitation, apart from other reasons, because the Keynes Plan without exchange control is doomed to break down within a very short time." As in 1935, he insisted on the compulsory aspect of exchange controls and clearing agreements.

The Keynes plan failed to be adopted, with the White plan winning the battle and reinstating the liberal international monetary order (Patalano 2023). The newly created International Monetary Fund would ask its members to restore their currency convertibility and the Anglo-

American Financial Agreement of December 1945 made it clear that sterling convertibility had to be restored within one year after the effective date of the agreement (Naef 2022, 12).

On his return from the US, where he eventually signed a compromise very much in line with the American plan, Keynes invited several financial editors (including from the *Financial News*) to disclose the final agreement and tried to get their support. Einzig was disappointed by the Anglo-American agreement, which gave birth to the Bretton Woods system. He stood against the compromise resulting from the Bretton Woods negotiation, arguing that it was against the Keynesian spirit, and lost no time in attacking Keynes. As regards the Bretton Woods agreement, his criticisms were similar to those put forward by Thomas Balogh and Ernst F. Schumacher (Faudot 2021), and he lent his support to a system with exchange controls and without the interwar Gold Exchange Standard's failed principles. He supported the Labour Party members who opposed the Final Agreement in the British parliament, so annoying Keynes.

Einzig reported his 1944 clash with Keynes in his autobiography, writing that he "hit hard at Keynes for having lent his authority to a system so obviously at variance with his own fundamental ideas" (1960, 174). This opposition was noticed, including by Heilperin.[1] Later, Einzig expressed some regrets that his relationship with Keynes had deteriorated and had not been re-established before Keynes' death. Later, Einzig (1970, 12) nuanced his views. He wrote nonetheless that Keynes was, in 1944, "willing to abandon the 'Keynes Plan'".

Einzig anticipated the failure of the restoration of sterling convertibility in summer 1947, as provided for by the Anglo-American agreement (Einzig 1947a). He ascribed the failure to Britain's trade deficit and dollar-greedy governments willing to drop sterling for dollars (Einzig 1947b). As a result, the UK would need to become part of a regional fortress such as the European Payments Union, which was a regional multilateral clearing union protected by exchange controls, renouncing currency convertibility until 1958. In the meantime, Einzig suggested that the UK adopt a policy of preferential and bilateral agreements in order to circumvent the dollar area and relieve it of the threat of dollar shortage. From there on, he became increasingly interested in the development of the Eurodollar system and published books and articles on it. Einzig's interest in the new developments of the international

[1] In his opposition to the Bretton Woods Agreements, Einzig goes so far as to call them a "suicidal measure" for England. Such opposition was based mainly on a "complete refusal to accept any sort of international commitments, any international "discipline" whatsoever, any connection with gold" (Heilperin 1945, 76). Heilperin probably exaggerated Einzig's isolationist position.

monetary system with the expansion of the Eurodollar system marked the continuous focus on new monetary practices challenging economists' beliefs.

## 5. Conclusion

Einzig's writings are an invaluable source of information on international monetary affairs and especially on clearing. Any researchers interested in international financial issues during the 1930s and 1940s will admit that Einzig was an essential reading. Analysis of clearing was the focus of many of his writings in the 1930s. He was not only an observer but was also at the origin of a proposition discussed by fellow economists. His publications contributed to "preparing British opinion" on the new system of exchange clearing (Einzig 1960, 162). Arguably, Einzig was not the only thinker to propose a reform of the international monetary system in the 1930s (Patalano 2023). Dozens of other proposals were published at the time. However, Einzig's work on international clearing is outstanding insofar as it is echoed in subsequent published works on other related monetary issues, on Eurodollars, exchange rates, primitive money and the Bretton Woods system crisis. In line with Einzig, we think that international clearing and, more generally, the study of clearing practices are understudied gateways to studying the nature of money, including in contemporary monetary systems. The fact that Einzig adhered to a particularly heterodox view of money helped him to elaborate innovative proposals of exchange clearing.

Furthermore, Einzig was committed to promoting an international clearing order based on the principle of *multilateral* clearing, with a view to overcoming the shortcomings of bilateralism while rejecting the failed liberal international monetary order at the same time. In this sense, he was a precursor of Keynes and then of post-Keynesians who relentlessly supported reform of the international monetary system, including in recent years. He thought that the international clearing union to be created would be able to provide both a truly multilateral monetary system and a means to retain some State's intervention at the national level. At the same time, his increasingly critical approach of Nazi Germany foreign trade methods shows that he was aware that clearing could be manipulated and its functioning should remain under scrutiny to avoid the exploitation of weaker countries. Despite his undisputable anti-Nazi stance, he was consistently supporting the creation of an international clearing union, making, like Keynes did, a clear distinction between the Nazi experience with clearing and the potential benefits of an international clearing system. All these insights have anticipated several key debates on the prospect for a reform of the international monetary system that remain topical.

The context of the 2020s is without any doubt different from that of the 1930s and 1940s. International trade is no longer threatened by deflationary forces due to currency shortages. In recent years, some countries have been nevertheless considering clearing as a solution to carry on trade transactions without resorting to a universally accepted convertible currency. To maintain trade with Iran without using the US dollar, some European countries had created such a scheme in 2019 with INSTEX (McDowell 2023, 132). Russia has also thought about clearing to circumvent the US dollar payments systems after 2022 (Pilipenko 2022). Einzig's object of study is therefore still living today. The serious and increasing risk of international open military and economic conflicts and the absence of meaningful role for the international institutions are strong arguments in favour of a new Bretton Woods aiming at financial disarmament and the creation of new multilateral institutions. Organizing international trade through a truly multilateral clearing is part of the most desirable solution.

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