



## **Black Wednesday 30 Years On**

By David Ward<sup>1</sup>

It is an anniversary Tories prefer to forget. Thirty years ago, 16 September 1992, better known as ‘Black Wednesday’, the Pound was forced out of the European Exchange Rate Mechanism (ERM). The humiliation of John Major’s government fatally damaged the Conservative Party’s reputation for economic competence and ignited a Tory civil war over the Maastricht Treaty. With the benefit of hindsight we can see now that Black Wednesday launched the Tory’s transition into an anti-European Union (EU) party and sowed the seeds of Brexit.

Less widely understood is the impact of the ERM crisis on Labour. It almost certainly guaranteed the return of a Labour Government in 1997 but also had a significant influence on who would lead the party to victory; for this was the moment when, due to an avoidable mistake by Gordon Brown, Tony Blair took over pole position to succeed John Smith as leader. The ‘Black Wednesday’ effect on Labour was profound but has been largely ignored, especially by New Labour narratives of the period. This is surprising given that the biggest Labour beneficiary of the ERM debacle was Tony Blair.

As John Smith’s Head of Policy from 1988 to 1994 I was privileged to be involved in this important period in the political economy of the UK. In this paper I hope to shed some new light on the ERM crisis and its consequences for Labour. To set the scene I will briefly trace the twists and turns of the ERM policies of both Labour and the Conservatives, before exploring their powerful interaction and aftermath.<sup>2</sup>

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<sup>2</sup> For readers wanting an in depth understanding of the ERM crisis, highly recommended books are: Philip Stephens, *Politics and the Pound: The Conservatives’ Struggle with Sterling* (Macmillan, 1996) and William Keegan, David Marsh and Richard Roberts, *Six Days in September: Black Wednesday, Brexit and the Making of Europe* (OMFIF, 2017).

## The origins of the ERM

The origins of Black Wednesday go back to the efforts of the European Community (EC) to promote closer economic and monetary integration in the late 1970s. The European Monetary System (EMS) was established in 1979 to encourage currency stability through an exchange rate mechanism that was envisaged as a precursor to full monetary union. The ERM was created as a fixed but adjustable system in which its member states' currencies could make small adjustments in permitted bands around their entry rate. Wider realignments could also happen but would be rare. The German D-Mark soon became the ERM's benchmark against which other currencies would be measured.

The Labour Government (1974-1979) was involved in the EMS negotiations but decided against joining the ERM. Prime Minister Jim Callaghan was cautious about any scheme to peg the value of the Pound and adopted a 'wait and see' approach. As Leader of the Opposition Margaret Thatcher had criticised Callaghan's decision to stay out of the ERM "as a sad day for Europe" but after Labour's election defeat in 1979, Prime Minister Thatcher adopted a similar approach to join the ERM only 'when the time is right'.

With Labour advocating withdrawal from the EC in the early 1980s the ERM issue was off the party's policy agenda. This changed in 1983 under the leadership of Neil Kinnock who succeeded Michael Foot. Kinnock, with his deputy and Shadow Chancellor Roy Hattersley, began shifting Labour's approach to Europe and the ERM. In 1986 Kinnock raised the issue of joining the ERM in an article in the *New Statesman* exploring the potential for a European wide recovery strategy.<sup>3</sup> He outlined Labour's pre-conditions for membership including entry at a rate that would support the competitiveness of British industry.

After Labour's defeat in the 1987 general election Kinnock was determined to modernise the party's policy platform. He initiated a comprehensive review that aimed to jettison previous commitments to nationalisation, unilateral nuclear disarmament, and leave the EC. The ERM issue, therefore, returned as an important issue for Labour's 1987-89 policy review being

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<sup>3</sup> Neil Kinnock, 'Is there a European route to economic recovery?', *New Statesman*, 1 November 1986.

undertaken in a series of thematic groups led by members of Kinnock's reshuffled Shadow Cabinet.<sup>4</sup>

### **Labour's Policy Review**

A lead role in reviewing Labour's economic policy was given to Bryan Gould, the Shadow Secretary of State for Trade and Industry who chaired the group on the Productive and Competitive Economy. The new Shadow Chancellor, John Smith, although having overall responsibility for Labour's macroeconomic policy, was tasked with reviewing tax and welfare issues in the group on Economic Equality. Gould was a long-standing opponent of Britain's membership of the EC, a supporter of devaluation as a means to improve the competitiveness of British industry, and hence very sceptical about the ERM. Smith, in contrast - one of 69 Labour MPs that rebelled against the Labour whip to vote in favour of joining the EC in 1971 - was a strongly committed European.

Neil Kinnock, previously in favour of withdrawal, now shared Smith's pro-EC outlook. Both were interested in adopting a pro-ERM position. In an increasingly open economy subject to significant inflationary pressures Kinnock and Smith favoured a 'supply-side' strategy of investment in productive capacity. They believed this could be best supported through long term exchange rate stability promoted by ERM entry, albeit at a competitive rate.<sup>5</sup> Their economic advisers, respectively John Eatwell and Andrew Graham, were doubtful that a future Labour government could rely any longer on traditional Keynesian expansionary policies 'fine-tuned' with an accommodating exchange rate.<sup>6</sup>

Smith had also been impressed by the efforts of the Group of Seven leading industrial economies to curb currency fluctuation. In the Plaza and Louvre accords of 1985 and 1987 the

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<sup>4</sup> For more on 1988-89 Labour's Policy Review see Christopher Massey, *The Modernisation of the Labour Party 1979-97* (Manchester University Press, 2020).

<sup>5</sup> For more on the evolution of Labour's ERM policy see: Richard Hill, *The Labour Party and Economic Strategy 1979-1997, The Long Road Back* (Palgrave Macmillan, 2001), pp. 179-191.

<sup>6</sup> A very clear summary of these views is included in John Eatwell, 'The Development of Labour Policy, 1979-92', in Jonathan Michie (ed.), *The Economic Legacy 1979-1992* (Academic Press, 1992), 333-340.

US Treasury Secretary James Brady had successfully achieved a managed decline in the value of the dollar through coordinated central bank intervention.<sup>7</sup> Smith saw this as a welcome departure from reliance on unfettered market forces. In a major speech on global economic policy in April 1989 Smith welcomed such international policy coordination and praised the EMS as a means to achieve exchange rate stability. Presciently he also warned about imbalances between Germany and the rest of the EC, suggesting this might require “a substantial revaluation of the D-Mark against all the currencies in the rest of Europe”. In the *Financial Times* Philip Stephens reported that Smith’s speech “appeared to nudge the party a step closer to an eventual commitment to take Sterling into the EMS”.<sup>8</sup>

However, the Labour leadership’s increasingly positive attitude to the ERM was not reflected in the conclusions of the policy review, ‘Meet the Challenge, Make the Change,’ released in May 1989. The report’s economic chapter included ERM entry conditions similar to Kinnock’s proposals in 1986; but under Gould’s influence it adopted a distinctly anti-European tone. This made both Kinnock and Smith uncomfortable. They wanted to build on the vision of a ‘Social Europe’ offered by the President of the European Commission Jacques Delors in his influential speech to the Trades Union Congress in 1988 and capitalise on Labour’s victory in the 1989 European Parliament elections. For them a commitment to the ERM would be a powerful symbol of European engagement and a way to disarm accusations that Labour would be soft on inflation. They also expected that the launch of the European Single Market in 1992 would accelerate the scale of economic policy coordination required at a European level. This perspective was endorsed in an influential paper for the Institute for Public Policy Research by Gavin Davies - a leading Labour supporting economist - who argued that ERM entry was now “desirable and feasible”.<sup>9</sup>

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<sup>7</sup> See: Peter Baker and Susan Glasser, *The Man Who Ran Washington, The Life & Times of James A Baker III* (Doubleday, 2020), pp. 255-257.

<sup>8</sup> John Smith, Speech to the American Chamber of Commerce (UK), 22 March 1989, Ward Papers; Philip Stephens, ‘Smith nudges Opposition nearer pledge on EMS’, *Financial Times*, 23 March 1989.

<sup>9</sup> Gavin Davies, *Britain and the European Monetary Question* (IPPR, 1989).

Another huge attraction for Labour was that the ERM was starting to tear Mrs Thatcher's Government apart. The source of this division was the failure of the Tory's flagship experiment in free market monetarism of the early 1980s. Their Chancellor of the Exchequer Nigel Lawson, relying on monetary targets to control inflation, had cut taxes for the rich, kept interest rates low, privatised utilities and claimed an 'economic miracle'. In reality he had unleashed an unsustainable boom in house prices, followed by recession, rising unemployment, and soaring rates of inflation. Monetary targets had failed, so instead Lawson opted to shadow the D-Mark and tried to persuade Margaret Thatcher that joining the ERM would serve as a new anchor against inflation. However, as signalled by her speech to the College of Europe in Bruges in September 1988, Thatcher had become sceptical about Europe and hostile to the ERM, encouraged by her own economic adviser Sir Alan Walters. Open warfare was declared between Numbers 10 and 11, making both the Prime Minister and Chancellor easy targets for John Smith. In an Opposition Day debate on the Economy on 7<sup>th</sup> June Smith mocked them by singing the theme song to 'Neighbours'.<sup>10</sup> William Hague recently admitted that Smith was so funny he had "our own side cracking up when we weren't supposed to".<sup>11</sup>

With the Tories in disarray, it became more urgent that Labour clarify its own stance on the ERM. Kinnock and Smith were determined to move beyond the hostile tone adopted by Gould. This was achieved in a paper prepared by the Leader's office for the Economic Sub Committee of the Shadow Cabinet meeting on 27<sup>th</sup> June 1989. The paper argued that "It has been clear for some years that Britain could secure advantages in combatting inflation and maintaining currency stability if sterling entered the exchange rate mechanism of the EMS," and outlined four conditions which if achieved would make Labour "eager to negotiate entry".<sup>12</sup> The meeting minutes noted that these conditions were "reaffirmed" and also

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<sup>10</sup> HC Deb vol 154 (7 June 1989), c. 249.

<sup>11</sup> [The Rest Is Politics: William Hague on Boris Johnson, Blair, and Brexit, 8 August 2022.](#)

<sup>12</sup> The four conditions were: 1) Greater central bank collaboration to mitigate the effects of short term speculative flows as capital controls are removed; 2) Entry at a competitive rate; 3) A collaborative

recorded that it was unanimously agreed that “should the Tories enter the EMS before the next election Labour would stay in.”

In his autobiography Bryan Gould gives an account of the meeting claiming that he “carried the day” against an attempt to change ERM policy and boasted that, “No one dared really take me on in argument since, I assume, they realised they would not get the better of it”.<sup>13</sup> In fact, by indulging Gould’s habit of giving donnish lectures on the well-known problems of returning to the Gold Standard in 1925 and the Wilson Government’s devaluation in 1967, Kinnock and Smith secured a subtle but positive shift in favour of a negotiated ERM entry. Rather than an unchallenged demonstration of Gould’s power of persuasion, it marked the swansong of his influence over Labour’s macroeconomic policy. He was soon moved to the post of Shadow Environment Secretary with rising star Gordon Brown promoted to the role of Shadow Secretary for Trade and Industry.

With a more positive and united policy, Smith and Brown then undertook an Autumn tour of European capitals to test reactions to Labour’s four conditions for ERM entry. It included meetings with the French Prime Minister Michel Rocard, the Finance Minister Pierre Berezgouvoy, President of the European Commission Jacques Delors, the German Finance Minister Theo Waigel and the President of the Bundesbank Karl Otto Pohl. Unfortunately, Gordon Brown missed the German leg of the visit in order to take the lead for Labour’s front bench at Treasury questions. Brown’s absence from the meeting with Karl Otto Pohl subsequently proved to be as unfortunate as it was instructive for Smith.

Pohl and Smith got on well and the mercurial and self-assured Bundesbank President was remarkably open with his opinions. He supported the possibility of UK membership of the ERM, explained that rising inflationary pressures justified a realignment, that UK entry would be a good pretext for one, and that without it the system was vulnerable to collapse. Pohl

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growth strategy aimed at combatting unemployment; 4) A greatly expanded role for regional and structural funds to offset the depressive effects of the persistent German current account surplus.

<sup>13</sup> Bryan Gould, *Goodbye to All That* (Macmillan, 1995), p. 217

concluded with a warning “Don’t join at the wrong rate”. Smith then asked what would be the right rate and without hesitation - other than the a strong caveat not to be quoted - Pohl replied “no higher than 2.60 Deutschmarks”.<sup>14</sup> As we left the meeting Smith remarked that he was surprised that Pohl had answered the question and that his advice was the most important we had heard all week.

As well as obtaining crucial intelligence the Treasury team’s European tour also gained very positive media coverage. *The Guardian*’s Martin Kettle, under the headline a ‘Red carpet for the envoy with a red rose’ commented that Smith’s visit was “a pregnant symbol of a rapidly shifting political development in Europe and Britain”<sup>15</sup>. The *Sunday Times* Political Editor Michael Jones wrote that “the Shadow Chancellor was in all the right places last week” and noted that in a debate on the economy scheduled for the following week Nigel Lawson must “make a virtue of having nothing new to offer – except perhaps the head of Sir Alan Walters”.<sup>16</sup>

In fact, the only new thing offered by Nigel Lawson was his own head. On the day Labour’s Treasury team was in Brussels, the *Financial Times* reported that Walters that had described the ERM as “half-baked”.<sup>17</sup> This reignited the tensions between Lawson and Thatcher and made the increasingly forlorn Chancellor an easy target for Smith. In an ideally timed opposition day debate on the economy on October 24<sup>th</sup> Smith again relentlessly taunted the Chancellor advising him “to make an early decision on the important question of whether he will jump or be pushed”.<sup>18</sup> Two days later he jumped. In the *Financial Times* Michael Cassell highlighted Smith’s role in Lawson’s departure in an article headlined “Labour tastes real blood as the Tories lick their wounds”.<sup>19</sup> But the blood-letting over the ERM at the top of the Conservative government was only just beginning. Thatcher appointed John Major as

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<sup>14</sup> Mark Stuart, *John Smith: A Life*(Politico’s 2004), p. 182

<sup>15</sup> Martin Kettle, *The Guardian*, 20 October 1989.

<sup>16</sup> Michael Jones, *The Sunday Times*, 22 October 1989.

<sup>17</sup> *Financial Times*, 18 October 1989.

<sup>18</sup> HC Deb vol. 158 (24 October 1989), c. 683

<sup>19</sup> *Financial Times*, 28 October 1989.

Chancellor, hoping that this would defuse the explosive ERM question. As it turned out Lawson's demise only intensified pressure on the Conservative Government to join the ERM.

### **UK Joins the ERM and Thatcher's Downfall**

In October 1990 Thatcher finally accepted ERM membership proving that the 'Iron Lady' was for turning after all. But in the process of joining, the Conservatives sowed the seeds of their own destruction. Thatcher's acceptance of the ERM came with a condition; an immediate interest rate cut from 15 to 14% with the announcement timed to take the headlines away from the last day of the Labour Party Conference then riding high in the opinion polls. But in her haste to gain favourable news coverage, the procedure by which ERM members were consulted in advance about the entry level wasn't followed. Members were curtly informed that the UK had unilaterally decided to join at a central rate of DM 2.95 far higher than preferred by the Bundesbank. These antics sent a signal both to the markets and to the UK's European partners that joining the ERM was driven, not by a considered commitment to multilateral currency coordination, but by opportunistic internal Tory politics...plus ca change!

Labour's response to the UK's entry into the ERM was tight lipped. Both Kinnock and Smith were dismayed at an entry rate which was clearly too high. Responding to Major's statement in the Commons Smith welcomed the decision but sidestepped criticism of the rate. He simply asked Major if "it his judgment that the rate at which we agreed to join is sustainable?". It was left to Labour back bencher Giles Radice to say what Smith was privately thinking; "Is not the trouble with the Government's decision of 5 October the fact that it was taken at the wrong time, for the wrong reasons and at the wrong rate?"<sup>20</sup>

The obvious dilemma facing Labour's leadership was that any overt criticism of the entry rate would expose them to the charge that it could lead to a run on the Pound. Ahead of what was expected to be a close fought election, any challenge by Kinnock or Smith over the rate would have encouraged speculators to bet against Sterling. This would have been both

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<sup>20</sup> HC Deb vol. 177 (15 October 1990), c. 937.



irresponsible and deeply damaging for Labour. Kinnock was determined to shut down any debate about devaluation; which is why in January 1992 he angrily stopped Michael Meacher from raising the issue in the Shadow Cabinet.<sup>21</sup> Ahead of the election there was simply no alternative but to maintain support for ERM membership at the Tory's chosen rate.

Meanwhile the Tory's internal battles over the ERM reached a new climax. Mrs Thatcher's reluctant capitulation over the ERM was followed by her defenestration as Tory leader. Sir Geoffrey Howe, an ally of Lawson over the ERM – demoted from Foreign Secretary to Leader of the House – was unable to stomach Thatcher's increasing Euroscepticism. He resigned and soon after, Thatcher was ousted by her own MPs in November 1990. Her successor, John Major, set about restoring Tory credibility. He ended the hated poll tax, looked statesman-like during the first Gulf war, and was seen to have skilfully negotiated the Maastricht Treaty establishing the EU by securing opt outs from the single currency and the Social Chapter. The new Chancellor Norman Lamont reduced interest rates in stages by 4.5% to try to pull the economy out of recession and stem further job losses. By the Autumn, Labour's previous strong lead in the opinion polls had narrowed. With the huge advantage of not being Mrs Thatcher, Major unexpectedly won the General Election on April 2<sup>nd</sup> 1992.

As a result, Labour was never tested on its commitment to the ERM. Ahead of the '92 election a form of words was agreed with the Treasury negotiated by Kinnock's office with Smith's approval. It confirmed Labour, "will do whatever is necessary to sustain the value the sterling in the ERM". However, this was never intended to be more than a temporary expedient. As Neil Kinnock's biography makes clear, had Labour won the election an early realignment would have been pursued. At the time I was not aware of any discussions with Smith about this, but that is hardly surprising given its acute sensitivity. I am sure, however, that he would have supported a negotiated realignment which Kinnock confirmed would have been "deliberate and controlled with co-operation from the other ERM states who were under serious strain. Contrast that with the shambles of Black Wednesday and everything that

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<sup>21</sup> Martin Westlake, *Kinnock: The Biography* (Little Brown And Company, 2001), p.592.

followed from it”.<sup>22</sup> As Kinnock ruefully observes, it was the Conservative’s commitment to the ERM that was to be tested to destruction.

### **The build up to Black Wednesday**

To ease the domestic inflationary pressures arising from German reunification in 1990, the Bundesbank had raised its domestic interest rates. This forced other member countries to do likewise in order to remain within the ERM’s currency bands. The Pound was caught in this upward pressure on borrowing rates; the exact opposite of what was needed for the UK economy, then suffering a prolonged recession. The Bundesbank became ever more insistent on the need for an upward revaluation of the D-Mark, to reduce their reliance on higher interest rates and avoid exporting deflation across the rest of the Community. Despite holding the Presidency of the EC, which gave the British Government the opportunity to shape coordinated action, Major refused to recommend the realignment route. Instead, Major made the mistake, in Philip Stephens’ words, “of allowing an unsustainable Deutschmark parity of DM2.95 to define the difference between the failure and success of his administration”.<sup>23</sup> Major even boasted that he wanted the Pound to replace the D-Mark as the strongest currency in Europe. Such hubris would not last long.

The Pound was vulnerable to growing doubts that it could not hold its place in the ERM. Difficulties with the ratification process of the Maastricht Treaty also spooked the markets when a referendum in Denmark unexpectedly resulted in a ‘no’ vote. President Mitterrand then promised a referendum in France as opinion polls also pointed towards another possible ‘no’ vote. By early September markets sensed blood and currency speculation mounted, first against the Italian Lira. The Bundesbank again tried to promote an ERM realignment at a meeting of European Finance Ministers held in Bath on September 5<sup>th</sup>. However, Norman Lamont ruled out any official discussion of the option and instead unwisely

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<sup>22</sup> Westlake, op.cit., p.592

<sup>23</sup> Stephens, op. cit., p. xv.

tried to bully a furious Helmut Shlesinger, the newly appointed Bundesbank President, to cut German interest rates.

By September 13<sup>th</sup> the pressure on the Lira grew too strong and it was unilaterally devalued. In response the Bundesbank agreed to make a very modest reduction in its borrowing rates. The next day Shlesinger was reported in *Handelsblatt* saying that “the tensions in the EMS are not over. This will only happen when there is a comprehensive realignment. Further devaluations are not excluded”<sup>24</sup>. This emboldened currency traders who turned on the Pound, which fell to its permitted floor of DM 2.78. The markets opened on 16 September with the Pound facing a torrent of selling pressure. By mid-morning the Bank of England raised interest rates from 10 to 12% and then in the afternoon announced a further hike to 15%. But all to no avail. Despite spending billions in reserves, the Pound continued to haemorrhage support.<sup>25</sup> The clear winner in the trial of strength between the Bank of England and the speculators was George Soros, who made over \$1 billion betting against the Pound. Late that afternoon an ashen faced Norman Lamont stood on the steps of the Treasury and announced the UK’s withdrawal from the ERM.

In their definitive account of the ERM crisis, William Keegan, David Marsh and Richard Roberts pointed the finger of blame squarely at the Government’s refusal to support a realignment of the ERM. Fearful of associating the Pound with weaker currencies in the so-called ‘Club Med’ of Italy, Portugal, and Spain, Major had failed to push for a coordinated European response<sup>26</sup>.

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<sup>24</sup> Ibid., p. 243.

<sup>25</sup> By the end of the day the Bank of England’s reserves had been depleted by over £17 billion.

<sup>26</sup> Note: Both Major and Lamont have argued in their biographies that a realignment was not possible. They claim it would have been blocked by France due to its ‘Franc fort’ policy especially ahead of their referendum on the Maastricht Treaty. I think this is misleading. The Government could have used their EC Presidency to initiate a serious discussion about a realignment which was being actively advocated for by Italy and the Bundesbank. Instead they sat on their hands. In my view this was because they feared a realignment in which France might have opted to retain its DM parity but all the rest were reduced. This would have resulted in the Pound being aligned with the weaker so called ‘Club Med’ currencies. But such a general realignment could have allowed the Bundesbank to lower interest rates significantly, reduce pressure on the weaker currencies and, thereby, avoid Black Wednesday. Major couldn’t accept such an outcome because he was fantasising about the Pound replacing the DM as the strongest ERM currency. Their later claims that a realignment wasn’t an

Keegan et al persuasively argue that “France, Britain and Italy would have had a better chance of prevailing against the Bundesbank had they possessed the intelligence and strategic foresight to join forces in 1991, soon after reunification, in seeking a German revaluation”.<sup>27</sup> This failure in the long term proved to be catastrophic for the UK’s relationship with Europe. For Keegan et al Black Wednesday should be seen as “the first Brexit”: the catalyst to the Conservative’s slow-burn confrontation with the EU that culminated in the narrow vote to leave after the 2016 referendum.<sup>28</sup>

### **Labour’s Black Wednesday Bonanza**

The aftermath of Black Wednesday was a bonanza for Labour, now able to steal reputational advantage on the economy from the Tories. That is what Smith set out to do in the debate on the ERM which marked his first speech in the House of Commons as Leader of the Opposition. In a devastating onslaught on the Government he mocked Major’s ambition to have the Pound replace the DM “as having a certain detachment from reality of which Walter Mitty himself would have been proud” and labelled him the “devalued Prime Minister of a devalued Government.”<sup>29</sup> Smith’s performance was widely acclaimed; even John Major conceded that Smith gave a “brilliant debating performance” admiring his “brass neck” given his support for membership of the ERM.<sup>30</sup>

What Major overlooked was that Smith had made a significant switch in favour of an ERM realignment soon after the 1992 Election. Knowing that the Tories’ bungled entry in 1990 had left the Pound overvalued by as much as 20%, Smith doubted that the D-Mark 2.95 rate could be sustained. But rather than advocate unilateral devaluation he returned to the arguments

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option is disingenuous. It could have been done but Major/Lamont would have had to eat a lot of humble pie. Instead they flunked the opportunity and instead had to eat a much bigger and humiliating pie on Black Wednesday!

<sup>27</sup> Keegan et al., op. cit., p. 151.

<sup>28</sup> Ibid., p. 148.

<sup>29</sup> HC Deb vol. 212 (24 September 1992), c. 22.

<sup>30</sup> John Major, *The Autobiography* (Harper Collins, 1999), p. 339.

for a general ERM realignment that he had first recommended in early 1989. In June at a meeting with Labour Members of the European Parliament in Strasbourg Smith said this “was likely” and “could permit a reduction in German interest rates leading to similar reductions throughout the Community”.<sup>31</sup> This was followed in July by a speech in the House of Commons in which Smith again recommended the policy “as part of a concerted strategy to achieve lower interest rates”.<sup>32</sup> Later that month Smith was elected Labour Leader defeating Bryan Gould by a landslide vote of 91% in the electoral college.

In the Commons clashes with Major after Black Wednesday, Smith was able to exploit the realignment argument to great effect. Major was unable to answer Smith’s charge that the government had ignored the “only one feasible alternative: to have a general realignment so that the markets were not presented with an open invitation to speculate in circumstances in which our defences to their attack were weak.” “The Government,” Smith continued, “must tell us why this option--the multilateral option, the European option, the less inflationary option--was not taken when it was clearly in the national interest”.<sup>33</sup>

Black Wednesday proved that Smith’s swift adaptation of Labour’s ERM policy had been astute. But unfortunately, it also became a source of significant tension with Gordon Brown, the newly appointed Shadow Chancellor. Haunted by Labour’s past association with devaluation, Brown wanted to be sure that “if the Conservatives devalued they should get the blame for it”.<sup>34</sup> Smith certainly shared this ambition, but Brown went further. He rejected calls for an ERM realignment and refused to see that a multilateral agreement on an upward revaluation of the D-Mark was entirely different to a unilateral devaluation. On this Brown was awkwardly out of step with Smith but also with Neil Kinnock who on his last day as

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<sup>31</sup> John Smith, Speech to the European Parliamentary Labour Party, Strasbourg 9 June 1992.

<sup>32</sup> HC Deb vol. 210 (2 July 1992), c. 1050.

<sup>33</sup> HC Deb vol. 212 (24 September 1992), c. 18.

<sup>34</sup> Gordon Brown, *My Life Our Times* (Bodley Head, 2017), p. 91,

Labour Leader published a letter in the *Financial Times* urging “that the government takes a real lead among the ERM countries in pressing for an immediate revaluation the D-Mark.”<sup>35</sup>

To have a substantive difference between Labour’s Leader and Shadow Chancellor on such a key policy was risky to say the least. To avoid any confusion in late July a meeting was arranged to establish a common position in support of a general realignment but oppose unilateral devaluation. It was attended by Smith, Brown, Murray Elder (Head of the Smith’s Office), Andrew Graham and me. The discussion focused on how a D-Mark revaluation could break the interest rate log jam, allowing reductions throughout the EC. I recall that in the discussion Brown asked why we were so sure the Pound’s central rate of DM 2.95 was unsustainable. In reply I mentioned Karl Otto Pohl’s warning to us in 1989 that the entry level should be no higher than DM 2.60. Graham also circulated a note to Smith and Brown summarising the arguments in favour of a realignment.<sup>36</sup> We hoped that through these efforts a consensus on this key policy issue had been reached.

Over that summer, however, William Keegan observed that Brown’s position on the ERM still appeared to be “inconsistent, even confused”.<sup>37</sup> Disquiet was also growing in the Shadow Cabinet and Parliamentary Labour Party. This was worrying and risked arguments at the Labour Party conference to which a pro-realignment motion had been tabled by the GMB trade union. We were also working on an NEC statement to conference on the economy which could not fudge the issue. On 5<sup>th</sup> September I sent a confidential note to Smith expressing concern about our ERM policy suggesting that “it was a mistake to have stopped making any reference to the possibility of a DM realignment. Restating this argument would enable us to differentiate ourselves more clearly from the Tories, point out more forcefully the weaknesses of the EC economy, and gain some favourable reporting of our new-found flexibility which

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<sup>35</sup> Westlake op. cit., p. 591.

<sup>36</sup> Andrew Graham, ‘Multilateral Realignment with the Emphasis on a DMark Revaluation’, 24 July 1992, Ward Papers.

<sup>37</sup> William Keegan, *The Prudence of Mr Gordon Brown* (Wiley, 2003), p. 101.

happened after your speeches in the leadership election but have been lost since”.<sup>38</sup> Smith agreed and in an interview with the BBC’s John Cole on 9<sup>th</sup> September at the TUC Congress in Blackpool, just days before Black Wednesday, he ruled out devaluation but repeated his call for a realignment.

Brown’s failure to unequivocally endorse this position ahead of Black Wednesday had become a source of argument in the Shadow Cabinet. Bryan Gould was scathing about Brown’s refusal to endorse a realignment. In his autobiography he claims that Brown had “maintained an even more intransigent line than the Tores throughout the ERM crisis”.<sup>39</sup> However, Gould soon resigned from the front bench and a few years later returned to New Zealand to pursue an academic career. More problematic for Brown was criticism from Robin Cook, David Blunkett, Michael Meacher, John Prescott, and Jack Straw who were reportedly ‘furious’ that Brown had ‘slammed the door’ on a policy option to realignment.<sup>40</sup>

In his autobiography Brown suggests that on devaluation he had “stood out against this for longer than I should have done”. But this isn’t an accurate description of what happened. As the July discussions had made clear, Smith shared Brown’s opposition to unilateral devaluation; the recommended action was to support a multilateral realignment. Brown’s memoir fails to mention this at all – a surprising omission, given he conceded in 1993 in an article for *Tribune* that “there was a far more comprehensive realignment possible... Faced with the choice between realignment within the ERM and leaving the ERM to devalue many of the difficulties could have been avoided with a realignment”.<sup>41</sup>

### **Selling Browns and buying Blairs**

The role of Shadow Chancellor is never easy, and Brown acted decisively to move Labour beyond the tax and spending policies of the 1989 Policy Review and Smith’s 1992 Shadow

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<sup>38</sup> Stuart, op. cit., p. 257.

<sup>39</sup> Gould, op.cit., p. 265.

<sup>40</sup> Paul Routledge, *Gordon Brown: The Biography* (Simon Shuster, 1998), p. 173.

<sup>41</sup> Gordon Brown, *Tribune*, 1 January 1993.

Budget. Whilst fiscal prudence wasn't likely to be a cause for celebration by Labour MPs, the necessity of avoiding early tax and spending pledges was widely understood and endorsed not least by Smith. What was much harder to understand was why Brown boxed himself into a policy position on the ERM that looked identical to Major and Lamont. According to Blair's biographer John Rentoul, this made Brown "the lightning conductor for discontent in the party" and he had "unwittingly sacrificed his prospects of becoming leader on the altar of monetary rectitude."<sup>42</sup> His failure to endorse the escape route of an ERM realignment was certainly ill-advised and happened before his subsequent close confidant Ed Balls (a critic of the ERM) was working for him.<sup>43</sup> Perhaps Balls could have prevented a mistake which devalued Brown's political currency? It was the moment when political speculators started to sell 'Browns' and buy 'Blairs'.

Appointed by Smith as Shadow Home Secretary, Tony Blair had no role at all in Labour's ERM policy up to and including Black Wednesday. But as Brown, in his own words, "walked into a storm" over the issue Blair gently breezed past to become the party's heir apparent.<sup>44</sup> Ironically, Blair's advance was accelerated early in 1993 when he began using a slogan given to him by Brown to position Labour as being "tough on crime and the causes of crime". Following Smith's untimely death on 12 May 1994, Blair became the clear front runner to take over as Labour leader.

In his autobiography Blair suggests that Brown was "only marginally tarnished" by his handling of the ERM crisis.<sup>45</sup> But this is typical of Blair's insouciance about the importance of these seismic events. His memoir mentions the ERM just three times, despite the fact that it proved to be a remarkable talisman for him. Black Wednesday was truly a triple whammy of political good fortune for Blair. First it winged his leadership rival Brown, second it wrecked

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<sup>42</sup> John Rentoul, *Tony Blair: Prime Minister* (Little Brown and Company, 2001), p. 189.

<sup>43</sup> Ed Balls became Brown's economic adviser in 1994. In 1992, he had published a Fabian Society Discussion Paper No. 14 (*Euromonetarism*) that was critical of the straitjacket' ERM membership had imposed on the UK economy.

<sup>44</sup> Keegan et al., op. cit., p. 100.

<sup>45</sup> Tony Blair, *A Journey* (Hutchinson, 2010), p. 59.



the credibility of John Major, and thirdly it was followed by a UK economic recovery for which the Tories could claim no credit.

Freed from the ERM and the deflationary impact of German unification, the UK was able to cut interest rates and allow the Pound to depreciate by about 15%. These measures coincided with a drop in the rate of inflation and a recovery in annual Gross Domestic Product from 0.40% in 1992 to 2.49% in 1993. This marked the beginning of a 16-year period of uninterrupted growth which helped rather than hindered Labour's progress towards victory in 1997. As Professor David Sanders argued, this was because the ERM debacle had produced "a sea change in voters' perceptions of the Conservatives as competent economic managers" with the result that "the recovery in economic expectations of 1996-97 failed to translate into a Conservative political recovery".<sup>46</sup>

The humiliation of Black Wednesday was correctly seen as policy failure wholly owned by the Conservatives. John Smith's charge that Major and his government had been devalued was immediately reflected in polling data. Labour gained the lead as the Party best able to handle the economy and quickly established a huge 22 point poll advantage over the Conservatives. MORI's net satisfaction with Major plummeted down to levels below Thatcher's just before she was ousted and stayed low. The ERM crisis was then followed by ratification of the Maastricht Treaty in which Major was ambushed by rebel Tory MPs, forced to concede a vote of no confidence to the Opposition, and undermined by 'bastards' in his own Cabinet.<sup>47</sup> The Conservatives' woes were summed up by Norman Lamont who was fired as Chancellor in May 1993. In his resignation statement he warned that the government "gives the impression of being in office but not in power".<sup>48</sup>

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<sup>46</sup> David Sanders, 'The New Electoral Battleground', in Anthony King et al., *New Labour Triumphs: Britain at the Polls* (Chatham House Publishers, 1998), pp. 209-249, at p. 224.

<sup>47</sup> Major, *op. cit.*, p.343.

<sup>48</sup> HC Deb, vol. 226 (9 June 1993), c. 281.1

After Black Wednesday Labour began an unstoppable electoral winning streak. Notably in June 1994 they achieved a landslide in the elections to the European Parliament held less than a month after Smith's death<sup>49</sup>. According to Sir Bob Worcester, the founder MORI, after "the Tories self-destructed in 1992, Labour would probably have won under Neil Kinnock"<sup>50</sup>. And recently Professor Sir John Curtice answering the question why Labour won in 1997 offered the reply, "Was it Blair? No. It was Black Wednesday"<sup>51</sup>. So perhaps the *Sun's* headline on 2<sup>nd</sup> May 1997 should have been 'It was the ERM wot won it'?

New Labour's standard narrative of the 1997 election, by contrast, barely acknowledges Black Wednesday at all. Their preferred explanation of Labour's landslide gives credit exclusively to their modernisation project. Targeting the 'centre ground' of British politics and symbolic internal party reforms such as scrapping Clause 4 are presented as a 'sine qua non' of electoral success. This is the central theme of Philip Gould's insider account of New Labour that only mentions the ERM twice.<sup>52</sup> Like Blair, Gould ignores the electorally fatal damage that was inflicted on the Conservatives by the ERM crisis which was largely nothing to do with Labour at all, whether 'modernized' or not.<sup>53</sup>

This is not to suggest that Black Wednesday validates the old saying that "Oppositions don't win elections, Governments lose them"; rather that Blair exemplifies the wisdom of the Roman philosopher Seneca who said the "Luck is what happens when preparation meets opportunity". Thirty years on it's time to recognize that, whilst New Labour's preparation undoubtedly delivered a landslide in 1997, it was built on the huge opportunity of Black

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<sup>49</sup> David Butler and Martin Westlake, *British Politics and the European Elections 1994* (St Martin's Press, 1995), p. 23.

<sup>50</sup> Robert Worcester and Roger Mortimore, *Explaining Labour's Landslide* (Politico's, 1999), p. 88.

<sup>51</sup> [Q & A with Sir John Curtice - In From the Cold \(substack.com\)](#), 6 February 2022.

<sup>52</sup> Philip Gould: *The Unfinished Revolution: How the Modernisers Saved the Labour Party* (Little Brown & Co., 1998), pp. 285-286.

<sup>53</sup> It could be argued that Labour's support for ERM entry in 1989 increased pressure ahead of the Tory's decision to join in 1990 later but probably only marginally.

Wednesday. That is why 16 September 1992, the springboard for the Blair ascendancy, is a day Tories still look back on in horror.

