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Somme

Submarine

Verdun

Wilfred Owen, "Gas"

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World War One Battles

Letters from the Front

The Eclipse Of The Democracies

Author: Wallbank Jewsbury
Date: 1992

Economic Disasters

Economic Crises And Political Retreat, 1918-1939

Introduction

World War I, the war that was to make the world "safe for democracy," left a legacy of physical damage, economic disruption, and doubt that endangered the hard-won liberal victories of the nineteenth century. The twenty years between the first and second global wars was a perilous time for democracy. The horrible costs of the war made the victory a hollow one for the European victors, and after the initial taste for revenge had been satisfied, revulsion for war became widespread. The economic dislocation caused by inflation and depression sapped the strength of the middle classes, the traditional supporters of democracy. The certainty and belief in progress that had helped fuel Europe's dominance in the nineteenth century was replaced by doubt and cynicism. ^1

[Footnote 1: E. H. Carr, The Twenty Years' Crisis (New York: Harper & Row, 1964), p. 224.]

Economic Disasters

One of the most serious problems facing the survivors of World War I was the confused and desperate situation of the European economy. Much of the direct and indirect cost of the war had been covered by borrowing, and now the bills had come due in a world unable to pay them. The lasting results of the war touched many areas. The conflict altered world trading patterns, reduced shipping, and weakened Europe's former economic dominance. The various peace treaties multiplied the number of European boundaries, which soon became obstacles to the flow of goods, especially in the successor states of the Habsburg monarchy and in Poland.

The Costs Of The War

It is impossible to give a true accounting of the costs of any war, because there is no way to calculate the contributions that might have been made by those killed in battle. From 2 to 3 million Russians died, and more perished in the civil war. Among the other major participants, almost 2 million Germans, over 1.5 million French, close to a million English, a half-million Italians, 1.2 million from Austria-Hungary, and 325,000 from Turkey died in battle. These figures do not count the wounded whose lives may have been shortened as a result of their injuries. Put another way, the young paid the highest price; it is estimated that Germany and France each lost over 15 percent of its young men.

Estimates of the financial drain of the war range between $250 billion and $300 billion, figuring the dollar at its early 1920s level. These figures do not bring home the depth of the war's impact on trade, shipping, and monetary stability. Belgium, for example, lost over 300,000 houses and thousands of factories, and 15,000 square miles of northeastern France were in ruins.

There is no balance sheet or set of figures to measure the psychological expense of the conflict. How does one calculate the cost of taking 75 million men who were mobilized away from their jobs and their homes? How can the mental carnage inflicted on the participants be measured?

Political institutions felt the effects of the war in different ways. The German, Habsburg, Russian, and Ottoman empires crumbled and disappeared from the historical stage. Replacing them were uncertain republics or dictatorships. Those colonial empires that remained were weakened and indigenous nationalist movements made substantial progress. Rail and communications lines had to be reconfigured to reflect the interests of newly created states.

The roots of the economic problems that plagued Europe after the war - agricultural overproduction, bureaucratic regulations, and protectionism - could be seen before 1914. Compounding these factors were the traditional challenges encountered in shifting from a wartime to a peacetime economy - especially that of demobilizing millions of soldiers and bringing them back into the labor market.

Edward Luckart

Albert Smith

A Special Christmas Story

Christmas 1914

Music from World War One

Over There

Long Way To Tipperary

Pack Up Your Troubles

The Debt Problem

A radical change had taken place during the war in Europe's economic relationship with the United States. In 1914 the United States had been a debtor nation, mostly to Europe, for the amount of $3.75 billion. The war totally reversed this situation. The United States lent billions of dollars and sold tons of supplies to the Allies. British blockades kept the United States from being able to deal with the Germans, blocking further profits, but by 1919 Europeans owed the United States more than $10 billion. This tremendous debt posed what economists call a transfer problem. The international obligations could be paid only by the actual transfer of gold or by the sale of goods.

To complicate the picture, Allied powers in Europe had also lent each other funds, with the British acting as the chief banker, lending more than 1.7 billion. When their credit dried up, they turned to the United States for financial help. Even though Britain owed huge sums to U.S. financiers, it remained a net creditor of $4 billion because of its own European debtors. France, on the other hand, stood as a net debtor of $3.5 billion. In addition to war debts, the French government suffered greatly when the Bolsheviks renounced the tsarist debt of some 12 billion francs - one quarter of France's foreign holdings.

Some of the Allies argued that the inter-Allied debts were political, that all of them had, in effect, been poured into a common pool for victory. These people wondered how France's contribution in the lives of its young men could be figured into the equation in terms of francs, dollars, or pounds. They proposed that, with victory, all debts should be cancelled. The United States, which had gone to Paris with a conciliatory spirit toward Germany in the treaty negotiations, changed its tune when dollars and cents were involved. This attitude was best expressed in a remark attributed to Calvin Coolidge, who expected full repayment, when he said: "They hired the money, didn't they?" ^2 Beneath the extremes of these positions was understandable motives of getting out of paying a huge debt. The German side resorted to financial mismanagement. In the first three years after the war, the German government, in a policy of deliberate inflation, spent much more than its income. This policy was masked by "floating debts ... in other words, by the printing press." ^3

[Footnote 2: T. Harry Williams, Richard N. Current, and Frank Friedel, A History of the United States Since 1865 (New York: Alfred A. Knopf, 1960), p. 426.]

[Footnote 3: A. J. Ryder, Twentieth Century Germany: From Bismarck to Brandt (New York: Columbia Univ. Press, 1973), p. 216.]

The situation became so serious in the summer of 1922 that Great Britain proposed that it collect no more from its debtors - Allied and German alike - than the United States collected from Britain itself. Such statesmanship was prompted by the fact that London had gained what it wanted from the peace settlement: Germany's navy was destroyed; Germany's merchant ships were transferred as reparations; Germany's empire was gone. No more could be squeezed out. Britain saw that Germany would not be able to meet its reparations payments, and without them, the payments of the inter-Allied debts, especially debts owed to the United States, would be extremely difficult, if not impossible, to make.

Although the United States insisted that there was no connection between the inter-Allied debts and German reparations, negotiations were carried on, and debt payment plans were set up with thirteen nations. No reductions were made in principal, but in every case the interest rate was radically decreased. The total amount owed came to more than $22 billion.

Germany's debt problem was complicated by the additional problem of reparations. Although reparations constituted a drain of major proportions on the German economy, they were far more significant as a political factor.

The German government's calculated inflationary policies contributed far more to the economic disaster that occurred in 1923 than did reparations. Between May and September 1921 the value of the German mark fell some 80 percent. A year and a half later, after Germany defaulted on some payments, French troops, supported by Belgian and Italian contingents, marched into the rich industrial district of the Ruhr, undeterred by American and British objections. This shortsighted French move contributed nothing to the solution of Europe's problems and indeed played into the hands of radical German politicians.

Encouraged by the Berlin government, German workers defied the French army and went on strike, many ending up in jail. The French toyed for a while with the idea of establishing a separate state in the Rhineland to act as a buffer between Germany and France. Chaotic conditions in the Ruhr encouraged the catastrophic inflation of the German currency to make up for the loss of exports and to support the striking workers. The French, in return, gained very little benefit from the occupation.

Inflation And Stabilization

All European nations encountered a rocky path as they attempted to gain equilibrium after the war. Britain had minimal price increases and returned to prewar levels within two years after the signing of the Versailles treaty. On the continent, price and monetary stability came less easily. Only Czechoslovakia seemed to have its economic affairs well in hand.

France did not stabilize its currency until 1926, when the franc was worth fifty to the dollar (as contrasted to five to the dollar in 1914). In Austria prices rose to 14,000 times their prewar level until stability of sorts came in 1922. Hungary's prices went to 23,000 times prewar level, but this increase is dwarfed by Poland's (2.5 million times prewar level) and Russia's (4 billion times prewar level).

But Germany served as the laboratory of the horrible impact of inflation on society. Germany's prices went up a trillion times (a thousand billion) what they were in 1914. The German mark had been worth four to the dollar in prewar times. At its weakest point in November 1923, after the French occupation of the Ruhr, the German mark reached the exchange rate of 4.2 trillion to the dollar. During the worst part of the inflation, the Reichsbank had 150 firms using 2000 presses running day and night to print Reichnotes. To get out of their dilemma, the Germans made an effective transition to a more stable currency by simply forgetting the old one. ^4

[Footnote 4: David S. Landes, The Unbound Prometheus (Cambridge: Cambridge Univ. Press, 1969), pp. 361-362. Gustav Stolper, Karl Hauser, and Knut Borchardt, The German Economy: 1870 to the Present, trans. Toni Stolper (New York: Harcourt Brace Jovanovich, 1967), p. 83.]

The millions of middle-class Germans, small property owners who would be the hoped-for base of the new Weimar Republic, found themselves caught in the wage-price squeeze. Prices for the necessities of life rose far faster than did income or savings. As mothers wheeled baby carriages full of money to bakeries to buy bread, fathers watched a lifetime of savings dwindle to insignificance. Pensioners on fixed incomes suffered doubly under this crisis. The bourgeoisie, the historical basis for liberal politics throughout Europe, suffered blows more devastating than those of war, for inflation stole not only the value of their labor, but the worth of their savings and insurance.

Where the middle classes and liberal traditions were strong, democracy could weather the storm. But in central Europe, especially in Germany where the inflation was the worst, the cause of future totalitarianism received an immense boost. Alan Bullock, a biographer of Adolf Hitler, has written that "the result of inflation was to undermine the foundations of German society in a way which neither the war nor the revolution of 1918, nor the Treaty of Versailles had ever done." ^5

[Footnote 5: Alan Bullock, Hitler, A Study in Tyranny (New York: Torchbooks, 1964), p. 91.]

Temporary Improvements

After 1923 the liberal application of U.S. funds brought some calm to the economic storm. Business was more difficult to conduct because protectionism became more and more the dominant trait of international trade. Autarky, the goal of gaining total economic self-sufficiency and freedom from reliance on any other nation increasingly became the unstated policy of many governments.

Nonetheless, production soon reached 1913 levels, currencies began to stabilize by mid-decade, and the French finally recalled their troops from the Ruhr. Most significantly, in September 1924 a commission under the leadership of U.S. banker Charles Dawes formulated a more liberal reparations policy in order to get the entire repayment cycle back into motion. Dawes' plan, replaced in 1929 by the Young plan (named for its principal formulator, U.S. businessman Owen Young), reduced installments and extended them over a longer period. A loan of $200 million, mostly from the United States, was floated to aid German recovery. The Berlin government resumed payments to the Allies, and the Allies paid their debt installments to the United States - which in effect received its own money back again.

Prosperity of a sort returned to Europe. As long as the circular flow of cash from the United States to Germany to the Allies to the United States continued, the international monetary system functioned. The moment the cycle broke down, the world economy headed for the rocks of depression. One economic historian has written:

> In 1924-31 Germany drew some one thousand million pounds from abroad and the irony was that Germany, in fact, received far more in loans, including loans to enable her to pay interest on earlier loans than she paid out in reparations, thus gaining in the circular flow and re-equipping her industries and her public utilities with American funds in the processes in the 1920s before repudiating her debts in the 1930s. ^6

[Footnote 6: Sidney Pollard, European Economic Integration, 1815-1970 (New York: Harcourt Brace Jovanovich, 1974), p. 138.]

The system broke down in 1928 and 1929 when U.S. and British creditors needed their capital for investments in their own countries. Extensions on loans, readily granted a year earlier were refused. Even before the U.S. stock market crash on October 29, 1929, disaster was on the horizon.

Few people in America could admit such a possibility during the decade, however. The United States had become the commercial center of the world, and its policies were central to the world's financial health. The United States still had an internal market in the 1920s with a seemingly inexhaustible appetite for new products such as radios, refrigerators, electrical appliances, and automobiles. This expansion, based on consumer goods and supported by a seemingly limitless supply of natural resources, gave the impression of solid and endless growth.

Tragically, the contradictions of the postwar economic structure were making themselves felt. The cornerstones of pre-1914 prosperity - multilateral trade, the gold standard, interchangeable currencies - were crumbling. The policies of autarky, with their high tariff barriers to protect home products against foreign competition, worked against international economic health. Ironically, the United States led the way toward higher tariffs, and other nations quickly retaliated. American foreign trade seriously declined, and the volume of world trade decreased.

There were other danger signals. Europe suffered a population decline. There were 22 million fewer people in the 1920s in the western part of the continent than had been expected. ^7 The decrease in internal markets affected trade, as did the higher external barriers. Around the globe, the agricultural sector suffered from declining prices during the 1920s. At the same time that farmers received less for their products, they had to pay more to live - a condition that afflicted peasants in Europe and Asia and farmers and ranchers in the United States.

[Footnote 7: Landes, The Unbound Prometheus, p. 365.]

In the hopes of reaching an expanding market, many food raisers around the world borrowed money to expand production at the beginning of the decade. Many farmers went bankrupt as they could not keep up with payments on their debts. The food surplus benefitted consumers, but across the world agricultural interests suffered. Tariff barriers prevented foodstuffs from circulating to the countries where hunger existed. By the end of the decade, people in the Orient were starving, while wheat farmers in Whitman County, Washington, dumped their grain into the Snake River and coffee growers in Brazil saw their product burned to fuel steam locomotives. The countryside preceded the cities into the economic tragedy. ^8

[Footnote 8: Pollard, European Economic Integration, 1815-1970, pp. 140-142.]

The Great Crash

Because of America's central position in the world economy, any development, positive or negative, on Wall Street reverberated across the globe. The United States, with roughly 3 percent of the world's population,

produced 46 percent of the globe's industrial output. The country was ill-equipped to use its new-found power. Its financial life in the 1920s was dominated by the activities of daring and sometimes unscrupulous speculators who made the arena of high finance a precarious and exciting world of its own.
This world, however, was not dominated by businessmen pursuing long-term stability. Their blind rush for profit led to America's crash, which in turn sparked a world disaster. ^9

[Footnote 9: William R. Keylor, The Twentieth Century World (Oxford: Oxford Univ. Press, 1984), p. 133.]

Even before the stock market crash, Wall Street had been showing signs of distress such as capital shortfalls, overly large inventories, and agricultural bankruptcies. But nothing prepared financiers for the disaster that struck on October 29, 1929 - Black Thursday. By noon, Wall Street was caught in a momentum of chaotic fear. The initial hemorrhage of stock values stopped by the end of the trading session, but the damage was done.

John Kenneth Galbraith has written: "On the whole, the great stock market crash can be much more readily explained than the depression that followed it." ^10 Overspeculation, loose controls, dishonest investors, and a loss of confidence in the "ever-upward" market trend can be identified as causes for the crash. Further causes can be traced to the inequitable distribution of wealth, with the farmers and workers left outwhile the top 3 percent grew incredibly rich and irresponsible. Industrial overexpansion was fueled by speculators buying stock on the margin, with insufficient cash backing for the investments. In addition, the government's hands-off policies permitted massive abuses to take place unchecked.

[Footnote 10: John Kenneth Galbraith, The Great Crash 1929 (Boston: Houghton Mifflin Co., 1961), p. 173.]

The international impact of the crash can be explained by the involvement of investors and bankers from a number of countries in the U.S. market, the interdependent world economic structure, the peculiar Allied debt and reparations structure, the growing agricultural crisis, and the inadequate banking systems of the world.

Some economic historians believe that the cycle of highs and lows hit a particularly vicious low point in 1929. Crashes had occurred before, but never with such widespread repercussions over such a long period of time. In the United States, stock prices declined one-third overall within a few weeks, wiping out fortunes, shattering confidence in business, and destroying consumer demand. The disaster spread worldwide as American interests demanded payment on foreign loans and imports decreased. The Kredit-Anstalt of Vienna did not have enough money to fill demands for funds from French banks and failed in 1931. This set in motion a domino-like banking crisis throughout Europe. Forecasts by Washington politicians and New York financiers that the worst was over and that the world economy was fundamentally sound after a "technical readjustment" convinced nobody. There would be no easy recovery.

The World Depression

By 1932 the value of industrial shares had fallen close to 60 percent on the New York and Berlin markets. Unemployment doubled in Germany, and 25 percent of the labor force was out of work in the United States. In nation after nations, industry declined, prices fell, banks collapsed, and economies stagnated. In the western democracies the depression contributed even more to the feelings of uneasiness that had existed since 1918. In other countries, the tendency to seek authoritarian solutions became even more pronounced. Throughout the world people suffered from lowered standards of living, unemployment, hunger, and fear of the future.

The middle classes on the continent, which had suffered from inflation during the 1920s, became caught in a whiplash effect during the depression. Adherence to old liberal principles collapsed in the face of economic insecurity, and state control of the economies increased. Governments raised tariffs to restrict imports and used command economies, an expedient usually reserved for wartime. As conditions deteriorated, fear caused most governments to look no farther than their own boundaries. Under the competing systems of autarky, each nation tried to increase exports and decrease imports.

After almost a century of free trade, modified by a comparative few protective duties levied during and after World War I, Great Britain finally enacted a high tariff in 1932 with provisions to protect members of its empire. In the United States the Hawley-Smoot Act of 1930 increased the value added duty to 50 percent on a wide variety of agricultural and manufactured imports.

Another technique to increase exports at the expense of others was to depreciate a nation's currency - reduce the value of its money. When Japan depreciated the yen, for example, U.S. dollar or British pound could buy more Japanese goods. In effect, lowering the yen reduced the price of Japanese exports. In most cases, however, devaluation brought only a temporary trade advantage. Other nations could play the same game, as the United States did in 1934 when it reduced the amount of gold backing for the dollar by 40 percent, thus going off the gold standard.

The debt problem that grew out of the war worsened during the depression. In 1931, U.S. president Herbert Hoover gained a one-year moratorium on all intergovernmental debts. The next year at the Lausanne Conference, German reparations payments were practically canceled in the hope that the United States would make corresponding concessions in reducing war debts. The Americans, for a variety of domestic financial and political reasons, refused to concede that there was a logical connection between reparations and war debts. As the depression deepened, the debtors could not continue their payments. France refused outright in 1932; Germany after 1933 completely stopped paying reparations; Britain and four other nations made token payments for a time and then stopped entirely in 1934. Only Finland continued to meet its schedule of payments.

Individual families had as many, or more, problems in paying their bills as did the governments of the world. Factories closed down and laid off their workers. Harvests rotted in the fields as the price of wheat fell to its lowest figure in 300 years. The lives of the cacao grower in the African Gold Coast, the coffee grower in Brazil, and the plantation worker in the Dutch East Indies were as affected as those of the factory worker in Pittsburgh, Lille, or Frankfurt.

The 1929 crash occurred in an economic framework still suffering from the dislocations of World War I. It began a downturn in the world economy that would not end until the world armed for another global conflict. Whether the depression ended because of World War II or whether the world would have eventually come out of the low part of the cycle is a question that will always be debated. The weaknesses in American stock market operations were by and large addressed in a series of reforms.

From the major banks to the soup lines in villages, the depression had profound implications for politics. The combination of inflation and depression threatened representative government. Unemployed and starving masses were tempted to turn to dictators who promised jobs and bread. The hardships of economic stability, even in those countries where the democratic tradition was strongest, led to a massive increase in state participation in the daily life of the individual.