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Massachusetts Institute of Technology
Department of Economics
Working Paper Series

**MADE IN GERMANY:
THE GERMAN CURRENCY CRISIS OF JULY 1931**

Thomas Ferguson
Peter Temin

Working Paper 01-07
February 2001

Room E52-251
50 Memorial Drive
Cambridge, MA 02142

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The first part of the document discusses the importance of maintaining accurate records of all transactions. It emphasizes that every entry, no matter how small, should be recorded to ensure the integrity of the financial data. This includes not only sales and purchases but also expenses and income. The text suggests that a consistent and thorough record-keeping system is essential for identifying trends and making informed decisions.

Next, the document addresses the issue of budgeting. It states that a well-defined budget is crucial for controlling costs and maximizing resources. By setting clear financial goals and limits, individuals and organizations can avoid overspending and stay on track. The text provides practical advice on how to create a budget that is realistic and adaptable to changing circumstances.

The third section focuses on the importance of regular financial reviews. It explains that periodic assessments of the financial situation allow for the identification of areas where adjustments may be needed. This process involves comparing actual performance against the budget and analyzing the reasons for any variances. The document encourages a proactive approach to financial management, rather than reacting to problems only after they have become significant.

Finally, the document concludes by highlighting the long-term benefits of sound financial practices. It notes that consistent attention to detail and disciplined financial management can lead to sustained growth and stability. By following these principles, individuals and organizations can build a strong financial foundation for the future.

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Made in Germany:
The German Currency Crisis of July, 1931

Thomas Ferguson and Peter Temin*

February, 2001

Abstract

The Great Depression reached a turning point in the currency crises of 1931, and the German banking and currency crisis was a critical event whose causes are still debated. We demonstrate in this paper that the crisis was primarily domestic in origin; that it was a currency crisis rather than a banking crisis; and that the failure was more political than economic. We clarify the arguments involved as we present this view. German banks failed in 1931, but the problem was not primarily with them. Instead, the crisis was a failure of political will in a time of turmoil.

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Made in Germany:

The German Currency Crisis of July, 1931

The currency crises of 1931 have emerged as pivotal events in the propagation of the Great Depression. It was during these crises that central banks and governments had to choose between domestic economic stability and maintenance of the gold standard. With the prominent exception of Great Britain, most industrial countries opted for the latter, dooming the world to the horrors of depression. To understand the Great Depression, one needs to understand the currency crises of 1931.

The German crisis of July 1931 in particular has been a topic of study. Given Germany's location, size, and subsequent ill-fated history, historians have attempted to disentangle the many factors inducing the German crisis. It was both a domestic and an international crisis. It was both a currency and a banking crisis. And it was both an economic and political crisis, that is, there were malfunctions in both private and public institutions. Historians have differed widely on the emphasis given to these various dimensions.¹

There are two main strands to the literature on the first dimension. One, typified by Kindleberger and Eichengreen, emphasizes the international aspect of the German crisis.² The other, represented by James and Balderston, stresses the domestic nature of the crisis.³ This literature of course is not distinct from that on the other dimensions, and the combinations are myriad.

We assert in this paper that the German currency crisis was primarily domestic in

origin, that it was a currency rather than a banking crisis, and that the failure was more political than economic. We hope to clarify the arguments involved even as we present this view. The German government found itself in an impossible position as the recession of the late 1920s deepened. Like so many other countries, the German government's budget went into deficit as the recession progressed. The Weimar government lacked the political will to deal with the impending crisis, substituting rash statements about customs unions and Reparations for serious budgetary action. German banks failed in 1931, but the problem was not primarily with them. Instead, the crisis was a failure of political will in a time of turmoil.

We progress by first reviewing the literature on the German crisis of 1931. We then set the stage by describing economic conditions in Weimar Germany during the first two quarters of 1931. We examine banking data in that context to search for evidence of a banking crisis. We go on to describe the impending budgetary problem facing the German government in early 1931. We show how the government's inability to resolve this problem led to the crisis by a detailed review of the events preceding the crisis. A conclusion places the German crisis into the narrative of the Great Depression as a whole.

Existing Literature

The literature will be discussed in the three dimensional structure introduced above. We expand on that introduction here before placing the existing literature in this framework. The first choice is whether the crisis was primarily domestic or international. It was, of course, both. Trading in the mark was controlled in July 1931, a change in the external relations of Germany. Banks failed, a catastrophe for the internal functioning of the German economy. The question however is not the effects of the crisis, which were

widespread indeed, but its causes. Was the change that led to these failures a change inside or outside Germany? For example, an international crisis could have been triggered by the failure of the Austrian Creditanstalt in May 1931 and by a subsequent withdrawal from Germany of international deposits. Perhaps depositors could not distinguish between Germany and Austria; perhaps they had other reasons. But if the impulse to sell marks came from events outside Germany, then we can say the cause was international.

If by contrast we think that developments within Germany led to the crisis, then we would consider the crisis domestic in origin. An internal change might be bellicose rhetoric emanating from Weimar about Reparations that scared foreign depositors. This example shows how hard it is to disentangle the two causes, since both predict a fall in foreign deposits in Germany. It also indicates that a drop in foreign deposits is not by itself conclusive and that other evidence is needed to disentangle the source of the crisis.

Another possible domestic cause of the crisis is the budgetary problems of the Weimar government. As in all other industrial countries, the German government faced budget deficits in 1930 and 1931 as national income and tax revenues fell. The peculiar German response to this problem is a candidate for causing the July crisis. The historical issue in this case is not ambiguous evidence on the budget; it is the connection between a budgetary problem and a currency or banking crisis.

Many authors conflate the currency and banking crises. Since the mark was controlled and the banks failed, it is reasonable that problems existed in both areas. But while there may have been two quite separate causes or weaknesses, we must be aware also that what looks like two phenomena may be only one. Yes, banks failed, but they

may have failed because of problems that were not of their making. They could have been forced into an impossible position by macroeconomic events. Alternatively, banking problems by themselves might have been a catalyst for a run on the mark. This seems to have been the case in Austria, where the poor policies and consequent unsustainable asset position of the Creditanstalt led to a run on the schilling.

Finally, was the crisis the result of a political or economic failure? As in the other dimensions, the crisis clearly represented both aspects. There had to have been a political decision that would have avoided crisis if only it had been politically feasible. The crisis did not result from a presidential election or court decision that was divorced, even in the short run, from economics. We do not mean to say that either politics or economics was missing from the German crisis.

But we do seek to identify the changes that led to crisis. We seek to distinguish between, say, structural problems of German banks—an economic factor—and government budgetary actions—a political factor. Both may well have been present, but which was more important in causing a crisis? If the banks were so unstable that any slight perturbation of conditions would have pushed them into insolvency, then political factors were only one of many possible shocks that lit the flame. If the government's budgetary actions were making the banking problem worse rather than better, then perhaps any banks, however well-run, would have suffered and even failed. As before, we seek the events that led to the crisis even though the crisis itself had many aspects.

Historians have formulated narratives of 1931 that explicitly and implicitly take positions on these matters. For example, the initial German response to the crisis was to blame foreigners for withdrawing their deposits in Germany and selling marks.⁴ In this

story, the withdrawals were triggered by changes in financial fortunes on Wall Street or by contagion from Austria. They were not occasioned by events within Germany. This story was international because it placed the movements of international “hot money” at the center of attention. It was a story about currencies rather than about banks. And it involved the German government not at all. It consequently clearly located the July crisis at one corner of the three-dimensional box described above, as purely international, currency, and economic.

Kindleberger may be taken as the start of the modern English-language literature on the European depression. He stated, “At the end of May 1931, Austrian financial difficulties ramified widely and led to runs on the banks of Hungary, Czechoslovakia, Romania, Poland and Germany.”⁵ Kindleberger’s subsequent discussion focuses on the consequent problems of German banks and makes no reference to German budgetary problems. In this context of bank fragility, the Nordwolle failed in mid-June, setting off the final stages of the crisis.⁶ Kindleberger thus saw the German crisis as international in origin, mostly concentrated in banks, and determined by a mix of public and private acts.

Eichengreen extended this internationalist tradition. He also argued that the Austrian crisis affected Germany through its effect on confidence, even though German banks were not heavily invested in Austria. Confidence in Germany collapsed because foreigners could not distinguish between Germany and Austria and because Brüning took the occasion of the Austrian default to insist on a reduction in Reparations. Eichengreen did not mention the budgetary problems of the German government. Instead, he asserted that, “the failure of international cooperation was the key to Germany’s defection from the gold standard system.”⁷ Eichengreen agreed with Kindleberger that the German crisis

was international and carried the argument further. His account focused on currency problems and failures of omission by governments outside Germany.

James presented quite a different story with much more attention to internal German problems. He represented the crisis as a run on German banks that contained “structural weaknesses” and were “fundamentally unsound.” The main cause of instability, in other words, was internal to Germany. The small push that toppled this unsound structure, however, was the withdrawal of foreign deposits, primarily American. International aspects were important in this story, but secondary if the crisis was the result of unsound German banking. Any push would have toppled this weak edifice.⁸

In addition, James argued that the Americans were not to blame for pulling their funds, as the Americans claimed at the time. Instead, the Germans had brought the crisis on themselves by tolerating capital flight in 1930-31 and by mismanaging their debt. James agreed with this American view without detailing the nature of the purported debt mismanagement. He only introduced it into his narrative of the crisis at the last moment, arguing that the budget crisis surfaced on June 9 when revenue figures for April and May became available, that is, at a late stage of the crisis.⁹ In contrast to Kindleberger’s and Eichengreen’s story of international contagion, James’ story concerned German banks in a context of government financial problems. His domestic story tracked Kindleberger more than Eichengreen (who wrote after James) in its emphasis on banking problems, and he consequently ended up distributing blame to both private and public parties.

Balderston attempted to disentangle the banking and currency crisis even as he asserted both were present. He argued that the proximate cause of the crisis was a general run on bank deposits due to conflicts over Reparations and fiscal crises. The ultimate

cause of the banking collapse was the inability of the German banks to replenish their reserves either from foreign loans or the Reichsbank. Balderston argued that the inability of German banks to borrow abroad was the root cause of the crisis, for only in that case did they go to the Reichsbank. Like James, Balderston focused on the problems of German banks, but like Eichengreen, he attributed the crisis to a failure of the international economy.¹⁰

Balderston elsewhere presented a detailed account of the budgetary problems of the Weimar government in which he asserted that “the connection between the state’s cash crisis of June 1931 and the banking crisis which had been developing since May is too obvious to need elaboration.”¹¹ But he treated the budget question and the currency crisis quite separately in his book. He did not emphasize connections between them either there or in his subsequent paper. Balderston accordingly ends up with two rather disconnected stories of the crisis. His main story is about international aspects of German banking. But in the background runs a quite different story about the political problems of the German government. The two stories may be compatible, but they remain quite distinct.

Consumers of these histories have two choices. They simply can conclude that all the above factors were important and take away a story in which all these factors—domestic and foreign, banking and governmental, economic and political—figure as separate causes. Alternatively, and preferably, they can try to disentangle this complex knot of explanations and search for a unified story. This story would not ignore any of the factors noted above, but it would state clearly where the crisis originated and specify the channels by which it spread to become a national and

international tragedy. It is the purpose of this essay to provide such an account.

Economic Conditions In Early 1931

The banking crisis of June and July 1931 heralded a disastrous new phase of the world depression. But it was also integral to another, even greater, catastrophe – the collapse of the Weimar Republic and the Nazi seizure of power. The aura of impending doom that clings to all accounts of the period makes it difficult to assess how bad the situation in early 1931 was, since the final result almost beggars description. But a unified story about the banking crisis depends crucially on such comparisons.

At the beginning of 1931 the German economy was clearly in desperate shape. The Depression had begun in Germany in 1927 or 1928, before the collapse in the United States.¹² By the middle of 1931, production and employment had been declining for more than three years. The level of human misery had reached colossal proportions.

Some relevant data are presented in Table 1. Industrial production had fallen to three quarters of its 1928 level. Unemployment had risen to over 30 percent of the labor force by the end of 1930, and the prevalence of part-time work had risen from its “normal” level of under ten percent to about 20 percent.¹³ In many industrial towns essentially everyone was unemployed. The special fund that financed the Weimar regime’s proudest achievement – the 1927 law establishing a system of unemployment compensation – teetered on the edge of bankruptcy, as payouts ran far ahead of taxes paid into it. As the central government reacted by tightening eligibility and reducing payments, the armies of the unemployed -- including many war veterans but also young people and women -- grew increasingly desperate. Many were recruited into the swelling ranks of paramilitary groups run by parties and groups on the right; others joined groups run by

parties of the left, notably the German Communist Party (KPD). Those who exhausted their benefits or who could not qualify for any could sometimes obtain assistance from the patchwork of local welfare programs run mostly by cities or towns. But these rapidly were overwhelmed by the crush of applicants and financial exigency. With many cities and states (*Laender*) in desperate financial straits and clamoring for bailouts from the central government, community cohesion was severely strained. Paramilitary clashes between political groups were common, while individuals frequently resorted to all sorts of expedients to make do.¹⁴

The political situation looked equally bleak. In the Spring of 1930, only days after the Reichstag narrowly ratified the Young Plan revision of the Dawes Plan, President von Hindenberg and his adviser, General Kurt von Schleicher, put in motion a plan that they had been hatching for months.¹⁵ The President, a former general and hero of the battle of Tannenberg, who had personally helped mint the “Stab in the back” legend after World War I, dismissed the government headed by Chancellor Hermann Müller of the German Social Democratic Party (SPD). He offered the Chancellorship instead to Heinrich Brüning of the Catholic *Zentrum* party, promising to let Brüning do what the President had never permitted the Social Democrats: to make use of the President’s power to rule by decree under Article 48 of the Weimar Constitution.¹⁶

With industrialists, the army, *Junkers* (owners of large landed estates mostly in eastern Germany with hereditary ties to the highest rungs of the military, civil service and judiciary), and even the *Zentrum* already moving at different speeds to the political right, the President and his advisors judged the situation ripe for a broad “right turn” in both domestic and foreign policy. They wanted not only a far more authoritarian regime, built

on a political alliance with the Right, but a government that would rapidly shake off the Reparations accords and the restrictions the Treaty of Versailles placed on German power.¹⁷

Brüning, who, in Everard Kolb's words, "from start to finish regarded himself as holding office solely by virtue of the President's authority and in order to fulfill the mission assigned to him," immediately ran into heavy weather in the Reichstag, which could still overturn Hindenberg's emergency decrees (*Noteverordnungen*) by majority vote.¹⁸

The major stumbling block was the same issue that had given Hindenberg his pretext for dissolving the earlier SPD-led government: the budget. The problem was that tax receipts were falling while expenditures were rising. As production fell and expenditures for relief and unemployment compensation soared, government debt at all levels (federal, *Laender*, municipalities) ballooned. As shown in Table 2, Germany's total government debt rose from 15 million RM at the end of March 1928 to 24 million RM in 1931. It should be noted that these official figures underestimate the total debt, excluding for example another 6 million RM debt of public corporations.¹⁹ The federal government accounted for about half of the consolidated total, indicating that all levels of government were running deficits as the economy declined.²⁰

Comparatively little of this debt was raised abroad. Even though total foreign debt had risen, it did not comprise the bulk of government debt. In addition, relatively little of the official foreign debt was short-term. Most government debt was held domestically, and the volume of short-term debt rose with the total. (The sum of foreign and domestic debt falls short of the total by the amount of "old debt." As can be verified

by subtraction in Table 2, the volume of “old debt” did not change.)

Pressed to get this mountain of debt under control, Brüning tried a variety of ploys. They all failed. Eventually, a budget calling for savage spending cuts, lower taxes, cuts in the pay of government officials, and smaller transfers to the *Laender* and municipalities had to be enacted by *Noteverordnung*. But the move outraged deputies and key business figures on the right who wanted deeper cuts, while angering many on the left who considered the budget palpably unfair. As the big business oriented German People’s Party (DVP) committed binary fission, a majority of the Reichstag exercised its constitutional right to reject the decree. Hindenberg and Brüning reacted with a fateful step: They dissolved the Reichstag, called new elections, and reenacted the *Noteverordnung* with minor changes.²¹

A disaster for the government ensued. In the September elections, amidst the highest voting turnout in the Republic’s history, the Nazis dramatically emerged as the second largest single party in the Reichstag, while the Communists made substantial gains.²² Parties supporting the governing coalition now controlled only about a third of the Reichstag, with another third dominated by parties fundamentally opposed to the existing political system.²³ Not surprisingly, investors stampeded out of Mark assets. In a single month, 800,000,000 Reichsmarks worth of foreign capital left the country, while German securities fell sharply in foreign markets. The Reichsbank was forced to raise its rediscount rate by a full point.²⁴

In accounts of the banking crisis even by authoritative contemporary commentators, such as R.S. Harris of the Royal Institute for International Affairs, as well as many subsequent historians, the headlong flight from the Mark in the Fall of 1930

plays a pivotal role. Many accounts treat the summer 1931 crisis as a seamless projection of the earlier winter panic, that in a fundamental sense never really abated. A variant of this position holds that the 1930 crisis closed world capital markets to German enterprises and, especially, the German government, making it impossible for the government to service either its foreign or domestic debts.²⁵

None of these claims is true. What actually happened is that the government responded by redoubling its resolve to continue down the path of austerity so resoundingly repudiated by the electorate. Amid a flurry of sympathetic news stories in papers from Berlin to New York, Hindenberg immediately tapped Brüning to form a new government. Solemnly promising to make fiscal reform and deficit reduction his top priority, Brüning reappointed the entire cabinet. On the basis of more *Noteverordnungen* and additional measures mandating a sinking fund for debt retirement, steep rises in workers' contributions to the unemployment fund, higher taxes (including new levies on mineral water and individual citizens), and slashes in government spending, civil service pay, and inter-governmental transfers, the government floated a \$125 million loan through a syndicate headed by Lee, Higginson.²⁶

Financial markets perceived “every sign of returning calm” and hailed “the cessation of the withdrawals of money, especially foreign withdrawals.”²⁷ The spectacle of the government bowing to foreign creditors (whose connection to the austerity package was too obvious to escape acrid public comment at home) surely pushed down the government's popularity still more. But the shock of the election and fears about what might happen if Brüning failed forced the SPD and other democratic forces into an agonizing reappraisal. Staring into the abyss, the party came reluctantly to the conclusion

that while it could not openly support the Chancellor, it would have to “tolerate” his government as the lesser evil. When the Social Democrats flirted with the idea of voting down some of the budget measures, the Chancellor brought them into line by threatening a Zentrum pullout of the SPD-led government in Prussia. This was a powerful card to play: In the murderous climate of the times, the SPD simply could not afford to lose control of the police force that controlled the largest of the German *Laender*.²⁸

In speeches that made news even in New York, Brüning explained “like a patient and firm schoolmaster” that after cutting spending, the government would seek to consolidate its huge short term floating debt into longer term obligations.²⁹ Warning his countrymen and women that repudiating Reparations payments or other debts would be ruinous, he also solemnly committed Germany to paying all its international obligations even as he urged the creditors to consider a new settlement in their own long run interest.

International support for Brüning grew as his government moved to make good on its tough talk. In January, the International Institute of Finance, a think tank with strong ties to financiers interested in European debt, provided timely reassurance with a widely heralded survey concluding that foreign investors need not fear that Germany might be forced to repudiate private debts in the new year.³⁰

Bolstering this confidence were several other favorable developments. First and foremost among them was the fact that the balance of payments was firmly in the black. Germany had been importing capital steadily since the stabilization of the Reichsmark. It had in fact borrowed considerably more than its Reparations obligations leading to what Schucker called American Reparations to Germany.³¹ While the net capital inflow decreased in 1930, the decline in capital imports was offset by a fall in imports of goods

and services.

Relevant data are set out in Table 3. Exports reached their peak in 1929 and fell thereafter. But imports fell faster, leading to a rise in net exports. Capital imports also fell in 1929 and 1930. These two movements largely offset each other, as of course they must to make the balance of payments add up. (Other, smaller items in the balance of payments did not change as rapidly as these categories.) Net income, the resultant of all these forces, was remarkably stable.

The need to pay Reparations meant that Germany's balance of payments was not in equilibrium when net imports equaled the capital inflow, but rather that the balance of payments was in equilibrium when the capital inflow exceeded net imports by the amount of Reparations payments, which amounted to between one to two billion Rm. depending on the time period one reckoned over. This represented a shift of the location of equilibrium and a burden on Germany, but it did not change the dynamics of the balance of payments.³²

The balance of payments is national, while Reparations were an obligation of the Weimar government. This distinction between the national and government budgets is important. Even though Germany had sufficient foreign exchange earnings to pay Reparations, these earnings arose largely from the excess of exports over imports. The foreign exchange therefore was largely in the hands of exporters, that is, private firms within Germany. The problem for the government was to get hold of these assets. In early 1931, this did not seem all that difficult. The consensus view was that "there will be no difficulty in making transfer" of the payments due under the Young Plan.³³

But more than just the favorable trend in the balance of payments reassured

observers of Germany in early 1931. Other good news also trickled in. Widely reported indices of German industrial production rose slightly.(Table 1) Unemployment began to trend very slightly down. In an age that venerated gold movements as the ultimate test of economic sustainability, the Reichsbank's holdings of gold and foreign exchange rose slowly but steadily from January to April. Bankruptcies -- even now esteemed as one of the few clear external indicators of possible bank lending difficulties -- started falling in February, rose slightly in March, and then fell sharply in April and May (Table 1). Indeed, almost every indicator that subsequent analysts have suggested might herald a banking or currency crisis improved modestly in the early months of 1931. The German stock market also rose for four months, while the bond market -- including, notably, the internationally traded Young Plan bonds (Table 4) -- rallied sharply.³⁴

Inevitably, some optimistic commentators hailed these small upticks as evidence that the invisible hand was at last beckoning the German economy on. It is not necessary to share this touching faith -- or its corollary that only subsequent political disaster aborted recovery -- to acknowledge that in the early months of 1931 "authoritative banking opinion" held that "the Reich will be able to borrow sufficient funds to meet her domestic and international obligations" for the coming year.³⁵

The international bankers who have had occasion recently to investigate the conditions of Germany are optimistic regarding the future. Complex problems confront the German government, but in Dr. Heinrich Brüning they see a quiet, forceful leader, capable of guiding the nation through a difficult period. His desire to permit nothing of a domestic nature to influence the calm, reasoned course of Germany's foreign relations is accepted by the bankers as a fairly sure guarantee

of a new period of stability.³⁶

In February, the government made a successful return to international money markets, borrowing short term to cover the deficit Brüning was pledged to reduce.³⁷

As the Nazis walked out of the Reichstag in protest, giving Brüning a comfortable working majority, he momentarily acquired a stature almost larger than life. Leading international dailies waxed on eloquently about how the Chancellor was “stronger than ever,” while their business pages gushed about “the particularly welcome improvement in the Berlin money market due to the continuing inflow of foreign funds, largely in the form of three month months credits.”³⁸ “Bankers express the view that the ‘confidence crisis’ is ended” and that “further foreign credits will come in and correct the wide disparity between rates at home and international capital markets.”³⁹ Actual passage of the budget a few days later and the news that Brüning had persuaded the Reichstag to recess until October buttressed this confidence.

[This] probably secures the country against an internal political crisis in the next few months. The attitude of the foreign banks has correspondingly improved and money has flowed into Germany from Holland, Switzerland, France, and Belgium. Berlin banks accepted the funds at reduced rates, but in general only to maturities of three months, while they paid one-month credits. This policy is due to the banks’ conviction that they will soon get foreign money cheaper.⁴⁰

The most dramatic development in regard to Germany’s potential creditworthiness during this period has been entirely forgotten. In February came sudden news that the French were reconsidering their previously hostile attitudes toward possible long term loans to Germany.

Save for the Young Plan loan, French banks had not participated in any major credit to Germany since 1929. Deeply alarmed by results of the September election, they had declined any part of the Lee, Higginson credit. Paris newspaper accounts also intimated that France, at the time the second largest creditor nation in the world thanks to the enormous inflow of gold that followed the Poincaré government's undervaluation of the Franc, possessed the financial clout to bring down the German economy by calling in loans.⁴¹

In December, however, the conservative, nationalist government headed by Andre Tardieu collapsed. A new government headed by Pierre Laval took over, with Aristide Briand, the long time champion of Franco-German cooperation, serving as Foreign Minister. Not for the last time in French history, a Laval-led government shifted policy toward Germany. Briand, who had his eye on the election for the Presidency of France scheduled for May, 1931, pushed the cabinet to restart the French economy and head off the rise of a still more nationalist government in Germany by easing tensions. In January news of the policy shift began leaking out. First came word that Lee, Higginson was once again considering a large loan to Germany. A few days later came the sensational announcement that at the request of the French government, the giant Banque de Paris et des Pays Bas would participate in the credit. This news "made a profound impression on the Paris bourse, where the move was widely interpreted as the initiation of a new foreign credit policy."⁴²

Additional details followed. "Participation in the present loan of several large French banks has inspired other French credit institutions to offer assistance to individual German banks, thus contributing to an unmistakable improvement in the Franco-German

atmosphere. It is also regarded as important that neither the French government nor the banks have made any attempt to attach political conditions to French participation....a big step for a nation hitherto wedded to the policy of making all foreign loans run parallel to its political desires.”⁴³

Despite attacks from the right, including, notably, deputies close to French steel interests, the cabinet voted formally to approve the loan.”The significance of French participation [was] far greater than the amount of money involved.”⁴⁴ Sitting on just over 20 percent of all the gold in the world, France was the only country in Europe that could realistically finance what Brüning’s government needed and professed to want -- a long term loan. “It has been recognized as frankly by financial Paris as by financial London, that an equilibrium can hardly be restored except through investment of French capital in long-term foreign securities.”⁴⁵ “Up to this time, France has given Germany no long-term credits except for the Young Reparations loan.....Berlin has now begun to hope that France will follow the recommendation of the League of Nation’s gold commission, advising better international distribution of capital and removal of restrictions on foreign lending.”⁴⁶

Economic conditions in the early months of 1931 therefore did not give much hint of the crisis to come. Conditions were not good in these harsh economic times, but there was little anticipation that they were about to get a lot worse. Expectations appeared to argue the opposite, that conditions were on the mend, as suggested by the slight improvement in the economic data shown in Table 1. Yet in the second quarter of 1931, something went wrong. The question is whether the change was in the stability of banks or of the Reichsmark, in Germany or without, in politics or economics.

The Banking Crisis

Once the crisis began, panic spread and everything fell apart. It therefore does not help us discriminate between various putative causes to describe the crisis itself. We must examine the process that led up to the crisis.

In this section we present banking data to distinguish the effects of the budgetary crisis from two other antecedents of the crisis whose effects also have been touted in the literature: the Austrian currency crisis in May and the weakness of German banks. The tests are rather different. To see if the Austrian crisis mattered, we examine the German reaction to the Austrian crisis. Did the Austrian crisis set off a sequence of events that led to the German crisis in July? To see if banks were unstable, we examine various indicators of bank performance in the months before the German crisis to see if there were signs of distress. The source material is almost the same for the two tests. The difference is that the first set looks specifically at timing, while the second examines banking indicators in a longer-run perspective.

There is an extensive literature about German banks, as noted above, but there is not a clear idea what to look for. At the risk of narrowing our focus excessively, we make explicit the implicit model of other scholars. When we talk about a banking panic, we refer to an American-style banking panic. In this kind of panic, depositors become fearful for the safety of their deposits. They withdraw their deposits, starting with the most liquid since they are in a hurry to get their funds into a more secure asset – cash as opposed to bank deposits. Banks operating with fractional reserves have to draw down their reserves in order to pay out deposits. Their reserve ratio falls. They call in loans to rebuild their reserves. Being short of reserves, they exert pressure on borrowers to pay up

as soon as possible.

In order to pay off these loans, borrowers need to withdraw their deposits from the banks where they keep money. The other bank withdrawals that may have started with a single bank or a small number of banks then spread to all banks as the ones affected initially call in loans that force other banks to pay out deposits. They draw down their reserves as they pay off their deposits, forcing them in turn to call in their loans. Soon all banks are calling in loans. Everyone is scrambling for liquidity, and there is not enough liquidity to go around.

There are two important steps in such a banking panic. First, scared depositors draw out their deposits. Since the spread of a banking panic is caused by the attempts of banks to rebuild reserves quickly, a marker of a panic is that people withdraw money from sight accounts. If they withdraw term deposits, they give the bank time to reconstruct its reserves without imposing as much pressure on other banks as when they need immediate help. Second, banks call in loans in order to rebuild their reserves. If they have some other way of getting reserves – say, from a central bank – they do not transmit pressure to other banks and initiate and intensify a general banking panic.

We examine German banking data to see if these two conditions were present. The following tables contain relevant banking data from 1931.⁴⁷ Table 5 reports deposits by bank class. The six Berlin Grossbanken are listed first. Kreditbanken are listed next. Finally, the Kreditbanken other than the Grossbanken are obtained by subtraction. Deposits are divided between those accessible within a week, labeled demand deposits (DD), and those accessible in eight days to three months, labeled time deposits (TD). Table 6 contains data on the largest assets of the Grossbanken. Table 7 reports time

deposits for individual Berlin great banks.⁴⁸

The first thing to note is that demand deposits did not fall at all in the crisis. If there had been a banking crisis, one might have expected these deposits to be withdrawn faster than all others. They were the easiest deposits to withdraw, and depositors should have converted them to cash or foreign exchange at once. Their stability suggests calm rather than panic. We do not mean to argue that conditions in Germany were at all calm in June 1931; rather we argue that fears of that time were not directed toward large banks.

The second thing to notice is the time deposits also stayed steady, although not so long. They were steady through the end of May. In fact, they were in the range that they had been in prior years. They ranged from 4,359 million Rm in May 1929 to 5,682 in August 1930. Demand deposits also were in the range of the immediate prior years: 3,434 in May 1929 and 4,289 in September 1931.⁴⁹ There is much discussion in the literature about the weakness of German banks before the crisis. Their ability to retain large deposits suggests that contemporaries were not aware of the putative weaknesses. The stability of deposits through May suggests also that the failure of the Creditanstalt did not lead to a panic of German banks.

The third conclusion is more complex. Time deposits fell sharply in June 1931. As shown in Table 7, all Grossbanken lost time deposits. But the fall appears to have been limited to these six banks; the data in Table 5 show that time deposits in other credit banks did not fall. If this fall is a sign of panic, it suggests a peculiar sort of panic. It extended to all the great banks, but not beyond. It affected time deposits, but not demand deposits. There is no sign of the contagion from bank to bank that is the hallmark of a general banking panic.

This movement does not suggest a loss of faith in banks; it suggests strongly that some depositors feared for the value of the mark. This conjecture is supported by the data on bank assets in Table 6, reporting the assets of the six Grossbanken. As shown in Table 5, deposits of these banks fell by 1,000 million Rm in June. Assets must have fallen by the same to balance their books. The table shows the largest categories of deposits; other categories were too small to account for the fall in June, and they did not fall in any case. Checks and bills of exchange (Wechsel) fell by 600 million Rm, accounting for almost two-thirds of the fall in deposits. Loans to business firms did not fall, although there was a small decline of loans against physical assets, that is, loans against the security of the firm as a whole. The rest of the decline in assets is unaccounted for.

The pattern on the asset side does not look more like a bank panic than the pattern on the debit side. Fewer bills of exchange must reflect changes in the international markets, whether of trade or of currency. Trade was declining as the Depression deepened, and traders began to hold their assets outside of Germany as they feared for the Mark. None of this suggests a banking panic. There is no contraction of loans by banks under attack which weaken other banks which in turn come under attack. There was no rush to withdraw the most liquid deposits and no inter-bank pressure to recoup reserves. Comparing these data to the pattern of banking crises shows that banks were not calling in loans that forced borrowers to withdraw deposits at other banks. The Grossbanken were not acting in a banking panic.

The Danat bank experienced more withdrawals in June than some other great banks, but it lost proportionately slightly less than the government-owned Reichskreditgesellschaft (RKG), as shown in Table 7. Depositors do not seem to have

singled it out as dangerous in June, despite its deep involvement with the Nordwolle failure. Depositors did draw more out of the Danat bank than from RKG in May and July, but it is hard to know what they were responding to. Nordwolle was not expected to fail in May, and deposits were controlled in July. For whatever reason, time deposits at the Danat bank had fallen the most of any great bank from the end of March to the end of July. Demand deposits at the Danat bank, however, had not fallen at all – more correctly, they fell slightly and recovered in July.

Due to the articulated structure of the German banking system, this test is not exact. American banks held deposits of both firms and individuals. If ordinary people feared for their bank balances, their actions would show up in the data on demand deposits. German banks were more specialized. The Grossbanken held deposits of business firms, while other types of banks held those of ordinary people. The data in Tables 5-7 therefore show that the business community was not frightened by bank behavior, but they do not indicate if people in the street were anxious. For that, we have to turn to data for other types of banks.

Data for smaller savings banks, whose business was local and accounts were almost entirely in Reichsmarks, are revealing. All through the winter and spring of 1931, small savers were not fleeing their local banks. Indeed, at the end of May, three weeks after the announcement of the failure of the Creditanstalt that allegedly triggered the banking crisis, German savings banks actually held more deposits than they did at the beginning of the month. Only in June is there any sign of withdrawals, and the losses were not large. Roughly the same is true of the so-called “industrial cooperative” banks.⁵⁰

Finally we need to examine the deposit currency ratio to make sure that the

stability of bank deposits did not mask a shift of monetary holdings into cash caused by distrust of banks. Again, the parallel with the United States is not exact. Germans economized on cash through use of the Giro system, and the data for currency in Germany do not refer to the same part of the economy as the American system.⁵¹ While conventional accounts of the banking crisis do not focus on the types of banks that held deposits of ordinary people, the deposit-currency ratio may still be informative. It fell about five percent in April, but remained constant in every other month in the first half of 1931. There was no cumulative decline in the deposit-currency ratio as there was in the United States.⁵²

Could the “banking weakness” story be saved by abandoning all reference to the Creditanstalt, switching models, and pointing away from American style bank panics to Japanese style slow motion asset deflations? While accounts of the crisis by Balderston, James, and others all take some kind of banking panic for granted, their emphasis on long building banking weaknesses does not fundamentally involve – save perhaps in the final stages – appeals to chain bankruptcy at all. As the contemporary example of Japan reminds us, banks can also collapse and cripple an economy through the slow decay of their assets and corollary inability to lend.⁵³

Given that the Nordwolle did bring down the Danatbank and that other large German banks also failed, including the giant Dresdner; while still others, such as the Deutsche Bank, appear to have had narrow escapes, one cannot dismiss flippantly the notion that the German banking system was structurally fragile after three or four years of depression. Perhaps the large banks took excessive risks out of the conviction that they were too big for the Reichsbank to allow them to fail.⁵⁴

It is not easy to tell if this story about deteriorating assets is true in the absence of archival evidence about bank portfolios. But the available evidence is less than overwhelming. We have seen that savers were not running on the banks as the crisis approached. They evidently did not sense collapse coming. Neither do bank stocks, one of the few reliable external indicators of the onset of banking crises recommended by contemporary analysts of financial vulnerability, appear to provide support. While no comprehensive review of the stock market evidence is known to us, existing stock indices do not indicate unusual sell offs of bank stocks relative to other sectors. (Table 4) As discussed earlier, in early 1931 stocks, including bank stocks, were broadly rallying. Bank stocks did not rise proportionately quite as much as the broader market, but they also declined more gradually than the rest of the market after it peaked. As late as May 9, 1931, *The Economist* reassured readers that German banks' "gross profits have not declined very substantially; their decline has been counterbalanced by savings in expenses and taxation."⁵⁵ Another article in the same issue favorably compared the level of capital and reserves of the German banks to those of the British.⁵⁶ Bankruptcy statistics – the other obvious external indicator of asset unsoundness – were also headed in the wrong direction (Table 1).

By contrast the devastation wrought by the currency collapse is clear. Without the run on the large banks' foreign deposits induced by the currency collapse, the Danatbank would have been far better armored against the Nordwolle shock. And the Reichsbank would have had ample means to step in quickly, guarantee the deposits, and abort the final panic.

The Currency Crisis

Why, therefore, were depositors so worried in the late Spring of 1931, if they were not anxious about the soundness of German banks? Our answer is straightforward: They were alarmed by the latest manifestation of the Weimar Republic's long running fiscal crisis. This now threatened to go completely out of control and lead – for reasons of domestic politics – to a moratorium or repudiation of Germany's foreign currency debts and to default or postponement of payments even on domestic debt.

The first step down the fatal path came with the decision of Hindenberg and his advisers to have Brüning pursue a more aggressive and nationalistic foreign policy. Soon after taking the reins, the Chancellor ostentatiously snubbed a proposal advanced by French Foreign Minister Briand to broaden the "Locarno System" of European security arrangements that had helped to pave the way for Germany's return to 'normalcy' within the European order. The frosty response automatically carried the implication that German government would continue to seek border adjustments in the East, with all that potentially implied for the peace of Europe.⁵⁷ Even more ominously, Brüning, prodded by Hindenberg and the vast "National Bloc" of industrialists, *Junkers*, and right wing parties that helped power this whole "right turn," insisted on pushing ahead with the building of the notorious "Panzerkreuzer B," the second in a series of warships that were designed to evade the naval limitations of the Versailles Treaty. This step made no sense in terms of either the existing military balance or the Reich's budget situation. It also made it very difficult for even sympathetic SPD leaders to assist the Chancellor, tacitly or otherwise.⁵⁸

This more assertive foreign policy destroyed the basis for cooperative internationalist strategies over time. Because the point can easily be misunderstood, it is worth observing that Brüning and his cabinet were not exponents of autarchy, though

they were markedly more inclined to compromise on tariffs and trade treaties than earlier cabinets. They had, for example, simply refused to bring the Polish Trade Treaty to a vote, despite the years of negotiations that had gone into it. They also raised tariffs on a variety of goods, especially agricultural commodities, for straightforward interest group reasons and they were vividly aware that tariffs could be employed as a foreign policy weapon. But they did not believe Germany could survive without access to international capital markets. They meant what they said about cutting the budget, consolidating public finances, and retaining access to international credit markets.⁵⁹

Influential currents did exist within the German business community in favor of policies that assuredly would threaten Germany's access to international capital. Since the late twenties, some of the most powerful of those interests had become increasingly oriented toward expansion in eastern and central Europe, or as they (and Hindenberg and Ludendorff during the war) called it, "Mitteleuropa." In the beginning this gambit was not clearly perceived as an alternative to the free(r) trade strategy championed by the "liberal" business bloc that cooperated with the SPD, which included firms such as German General Electric, I.G. Farben, or Robert Bosch. Thus, the first stirrings of what developed into the famous proposal for a customs union between Germany and Austria drew support from across the spectrum of business opinion. Some German firms that championed the Stresemann policies of "fulfillment" of Reparations and lower tariffs, actually suggested that the region could be exploited by a Franco-German condominium, with the French contribution consisting mostly of capital. The prospect did intrigue some French firms and political leaders, though they imagined themselves in the leading role.⁶⁰

By 1931, however, international trade was shrinking and foreign exchange was

becoming scarce even for key currency countries. In both Britain and France interest group pressures to give pride of place in economic policymaking to overseas territories and the empire (“imperial preference”) were visibly growing. Such plans, if brought to fruition, would gravely threaten Germany and might effectively terminate its hopes of running export surpluses. In this context, a policy of *Drang nach Osten* looked like simple common sense to growing numbers of German firms, including several giants, such as I.G. Farben (which had close ties to the cabinet and political circles around the Chancellor), Siemens, and Krupp. In the eyes of many, this strategy increasingly emerged as an alternative, not a complement, to traditional internationalist economic policies, not least because some sort of exclusive tariff concession would be needed to ensure Germany’s primacy in these areas.⁶¹

The plans for what became the notorious proposal for a customs union between Germany and Austria did not originate with the Reichstag or other normal policy making channels. Instead, the scheme emerged from a secret planning committee convened by the aristocratic German Foreign Office, which had for years met regularly with leading German firms and enjoyed close ties to the military. While Brüning and the Foreign Minister (the project’s public champion, whose reappointment had been confirmed by President Hindenberg) knew of the proposal, the cabinet was not told until the last minute. Advised by Brüning that the timing was unfortunate but that Germany could not control this, the cabinet voted approval on March 18, making it public on March 21.⁶²

Ever since the end of World War I, the specter of *Anschluss* between Germany and Austria had alternately tantalized or repelled many Europeans. While the Treaty of Versailles barred Germany from incorporating Austria, the German government’s

interest in eventual amalgamation was patent, as was the impatience of much of the Right to see it brought about. Another postwar peace accord, the Treaty of St. Germain, blocked Austria from making any agreement that might threaten its sovereign existence.

While the Germans and Austrians were prepared to argue that a customs union did not infringe on these prohibitions, internal documents indicate that they knew very well they might be flying into the eye of a hurricane. They were right. When news of the plan leaked, a storm of protest immediately blew up. As France moved convulsively to counter the German thrust, its chilling implications dawned on the press and financial markets. As the *New York Times* headlined in late March, 1931: "Paris loan market shut by Reich move. Union held to kill prospects for intermediate or long-term credit aid by French. Outcry in press is fatal. Bankers fear customs plan will shatter regained faith of our investors in Europe's stability."⁶³

For a brief period, some held out hope that Briand might somehow once again bring off a grand bargain that reconciled all parties:

European bankers have recently been heartened by indications that American long term credits were once more about to flow to Europe, for without American participation large undertakings are held to be out of the question. London is unable to direct these without the assistance of New York, and the cooperation of Paris being so delicately attuned to political conditions, the burden falls largely upon American shoulders.

With this position in mind, financial centres are hoping, therefore, that Aristide Briand will again have recourse to one of those friendly compromises for which he is famous⁶⁴

But Briand, who only a couple of weeks previously in the French Chamber of Deputies had declared the notion of *Anschluss* dead, was seriously embarrassed. As he and the Socialists backpedaled furiously, the French right agitated, and the center of policy shifted decisively.

Closure of the international loan market put Brüning and his government into a box. The modest upturn in the economy had done nothing to help tax collections. For all the gargantuan budget cuts, the deficit kept swelling. At the beginning of March, Finance Minister Dietrich warned Brüning that the first quarter deficit amounted to some 430 million Reichsmarks and that the special fund for unemployment compensation required an immediate loan or infusion of another 83 million RM.⁶⁵ At the time, the shortfall did not seem to pose insuperable problems. The government inserted a special provision in the budget allowing it to make additional expenditure cuts if revenues continued to fall and persuaded the Reichstag to accept it. This won widespread applause from the financial community, and the government succeeded in rolling over some 53.5 million RM worth of Treasury bills and selling an additional 71.5 million RM of new T-bills.⁶⁶

But the government's efforts to place a longer term loan were unavailing. At least one banking house the government queried replied that additional loans would have to await a new Reparations settlement that eliminated the possibility that in a crisis recent creditors would have to stand in line behind holders of Reparations bonds.⁶⁷

In April, Dietrich told the Chancellor that still another cut of 440 million Reichsmarks would be necessary to keep the budget for 1931 in balance for the rest of the year.⁶⁸ By then, Brüning's situation was desperate. Ever since the September election shock, he had been exploring ways to strike a better deal on Reparations that would both

relieve his budget and give him a triumph to satisfy the Right and please Hindenberg. As several recent accounts have emphasized, his guiding idea was to continue paying on Germany's obligations while deflating the German economy until its foreign creditors perceived that their own interests lay in relenting, either because they feared social chaos and the drift to the right in Germany itself or because their own industries found it impossible to compete with a major competitor whose price level was falling.⁶⁹ Well aware that complete cancellation would almost certainly have to wait until after the U.S. elections in 1932, Brüning nevertheless appears to have at least sometimes harbored hopes for some intermediate relief, perhaps in the form of concessions or a temporary loan.⁷⁰

With all prospects dashed for a long term loan, Brüning focused sharply on convincing the creditors to grant relief from the burden of Reparations through a diplomatic offensive. Aware that Britain had the biggest direct commercial interests in Germany and central Europe, he prepared to make his first major move in the late Spring of 1931, when he expected to meet Prime Minister McDonald and other top British officials for a major round of bilateral conversations.⁷¹

This determined the timing of the banking crisis. To have any hope of convincing the British that Germany could no longer afford Reparations payments, Brüning had to consolidate German finances and make public a draconian budget before he met with them at Chequers. But the pace of German deflation soon made it clear that the task was sisyphian. Some cities were near default or actually in arrears, forcing the Reich to step in several prominent instances. Since municipal loans in particular comprised a major share of the portfolios of many smaller municipal savings banks, this stirred additional fears of

local defaults and put additional pressures on Reich finances.⁷²

Though some historians have maintained that the depths of the budgetary crisis only emerged on June 9, when it became clear that tax revenues for April and May had run far below projections, in fact the revenue problem was well understood and widely discussed in public long before then.⁷³ The desperate condition of some localities was well known or at least widely suspected.⁷⁴ Even more importantly, official publications of the republic's monthly tax revenues and a variety of budget numbers were regularly scheduled and closely watched. Readers of the *Frankfurter Zeitung*, probably the leading newspaper in Germany, for example, could read the virtually same figures that economic historians now use to illustrate the size of the tax shortfall almost as fast as they were compiled and published by the government.⁷⁵ In the unlikely event that readers failed to grasp the meaning of the numbers, the paper's increasingly alarmed articles on the growing budget shortfall could hardly have failed to alert them, or the financial community that worried constantly about the creditworthiness of German bonds. Not surprisingly, after hitting their respective year's highs in April (see Table 4), both the German stock and bond market began steadily selling off, long before news of the Creditanstalt debacle arrived on May 13.⁷⁶

In early May, well *before* news of the Creditanstalt burst upon the world, the German government attempted to float a domestic bond issue for the Reichspost. It was an embarrassing failure. This debacle plainly owed nothing to international currency pressures and everything to fears by domestic investors of heavy losses.⁷⁷ By mid-month discussions between the political parties and the government over how to close the budget gap were becoming very tense. Paramilitary clashes, already running at high levels,

intensified, while the national SPD leadership, not coincidentally, voiced doubts about spending cuts of the size Brüning thought was necessary. Leaders of the Prussian SPD, however, who carried enormous weight both within the party and the government, faced elections in early 1932. They spoke out in favor of making big cuts now, rather than risk having to go through the whole process again later in the year. As Brüning and the cabinet -- who still lived in the shadows of 1918, the Kapp Putsch, and the myriad other disorders of early twenties German politics -- weighed their options, the crack of doom resounded: the Minister of the Interior warned that he could no longer guarantee the maintenance of order.⁷⁸

Not surprisingly the Chancellor concluded that if he were to ask Germans to tighten their belts yet again, he would also have to ask something from Germany's foreign creditors. Reichsbank President Luther and some other advisors warned that this risked destroying Germany's international credit. Worried about the domestic repercussions of the budget cuts, they and other pleaded for something less than "all or nothing." Some suggested trying a smaller package of cuts and an all out effort to line up international support for a loan. Their doubts about Brüning's strategy have been echoed by many later historians, who puzzle over why the Chancellor chose the high risk strategy of trying to convince the creditor countries that "the limits of the privations we have imposed on our people have been reached."⁷⁹

The answer is not difficult to find, but it lies entirely within the realm of German domestic politics. First, Brüning was aware, as many historians seem to have forgotten, that he would need votes from the right as well as the left to sustain his budget when it faced the inevitable challenge in the Reichstag. For the Right, including a major segment

of heavy industry, international creditors were not *a* bogeyman, but *the* bogeyman. A budget package that did not ask them to take a hit at the same time as it was demanding further sacrifices from Germans would be dead on arrival in the Reichstag. Perhaps even more importantly, not to act on Reparations would outrage parts of the Right whose strength, like that of the industrialists, could not be measured purely in electoral terms: General Groener, who along with his one-time protégé, General Schleicher, provided critical support for the government within the Reichswehr and Hindenberg's circle, advised Brüning not to wait on Reparations. This was advice that the Chancellor dared not ignore.⁸⁰

Second, and more subtly, Hindenberg, Brüning & Co. had already crossed the Rubicon, and they knew it. Once they had taken the plunge for the customs union with Austria, they were committed. Their plan was under withering public attack from the French and other European powers as Brüning deliberated on the budget. Indeed, many observers then and later connected disclosure of the Creditanstalt's condition to intrigues connected with the customs union proposal.⁸¹ In case anyone missed the connection, just days before the German budget crisis came to a head, Aristide Briand narrowly lost his bid for the French Presidency. While factors internal to French politics certainly figured in this outcome, the customs union proposal had certainly helped torpedo Briand's campaign. And the *Stahlhelm* were also staging gigantic rallies at which the French and their allies, the Poles, as well as, of course, "Marxists" within Germany, were roundly denounced; the last of these came just days before the government announced its fiscal program.⁸²

Soon afterward, Brüning was forced into negotiations with the Allies for an

international loan, a moratorium on Reparations, and a "Standstill" on existing lines of credit to Germany. His conduct of these negotiations, like his reparations for his bilateral talks with the British as he was actually deciding on the budget, make it clear that he fully appreciated that any help from France would come with conditions attached -- conditions that Hindenberg, on whom he depended completely, and the Right could never accept.⁸³

For essentially domestic political reasons, then, Brüning made the fatal decision to denounce Reparations and proclaim that Germany had paid all that it could.⁸⁴

The *Noteverordnung* of June 6 stunned not only Germany but the world, though municipal and *Laender* officials had been briefed on it three days earlier. Since at least May 25, German newspapers had been speculating that Brüning was likely to ask for some sort of relief in regard to Reparations. The French government and, doubtless, others, had drawn the inevitable conclusions: Rumors that Germany might postpone Reparations transfers had been circulating for some time, fanning the run on German gold reserves and major banks that appears to have begun about May 25. On June 3, at a meeting of the celebrated Langnamverein, a trade association of heavy industrialists, including many from the Ruhr, Albert Voegler, a leading figure in the steel industry, demanded the cession of all payments of foreign "tribute" and a shift in policy toward building up the home market.⁸⁵

The official announcement was read everywhere as heralding a broader German inability to make international payments, not least because it was accompanied by an official denial that Germany would soon be forced to suspend payments on both Reparations and private debts.⁸⁶ The run on foreign deposits (many of which were likely

held by German citizens) in the *Grossbanken* swelled into a torrent, while the Reichsbank's gold cover began to look dangerously thin.

Underneath it all, however, ran the wrenching fear that the government could not make its colossal budget cuts stick. In the early days of the run, with Brüning in England for the bilateral talks, this seemed likely. The SPD, the parties of the Right, the *Stahlhelm* (which had been afforded a share of the administration of youth programs in the budget), all vociferously denounced the budget cuts. Goering and other Nazis furiously attacked them. On June 11, Stresemann's old party, the DVP, split thunderously over the cuts. Since the party was somewhat inaccurately still labeled as uniquely a party of big business, the split was widely noted, even in foreign business centers. By June 13, the gold drain was so severe that the Reichsbank was forced to raise its discount rates two full points. Over the next few days, the financial situation worsened. Both SPD leaders and the General Groener, the Defense Minister, claimed to see revolution around the corner. Stories -- which appear to have a foundation in fact -- that the military was preparing to intervene swept Berlin and other major cities. Insiders were saying that the government was two weeks away from defaulting even on pensions.⁸⁷

All the tumult, along with frantic bargaining by Brüning (whose train, as he returned from Britain across Germany, was mobbed by Nazi thugs and other paramilitary groups) began to change the minds of the deputies. Pressure from various business groups and the Reichsbank intensified. Brüning and the cabinet made it clear that if the *Notverordnung* were overturned, they would all resign. Once again, Brüning threatened to overturn the SPD-led coalition that ruled Prussia. The chancellor also offered a few, minor compromises.⁸⁸

Economic historians who focus on the Creditanstalt and international factors in the banking crisis have noticed that something happened on June 16 that brought an abrupt halt to the foreign runs on German banks and the Mark. But they have typically identified that as the decision by Montague Norman, Governor of the Bank of England, to float a large loan to the Austrian National Bank. No doubt this decision helped stabilize Austria, but why should a British decision to bail out Austria have stopped internal drains from local German banks? Our answer is, of course, that it did not. Rather, something else that happened the same day that stabilized both domestic and international markets in which the Mark figured: The SPD and other parties decided not to try to overturn the budget. Brüning had won and the deputies dispersed.⁸⁹

This political success brought Brüning only a few days respite. On the heels of the dispersal of the Reichstag came the first, muffled reports of the Nordwolle's losses. The run on the Reichsbank swiftly resumed, as the shadow of death fell over the giant Danatbank, which was closely associated with the huge textile concern. In ordinary times, the bank could have turned to the Reichsbank for help. But the battles over the custom union, the budget, and Brüning's ill fated references to Reparations moratoria had left the Reichsbank in no condition to act as lender of last resort. As late as the end of May, the Reichsbank's cover of gold and foreign exchange exceeded 60% of the value of its own notes and 47% of the money supply as a whole. The gold cover fell dramatically in June, threatening the legal limit as word of the Nordwolle's condition began to leak out. The Reichsbank could no longer act as a central bank to its domestic constituents.⁹⁰

This, of course, is what happens in countries on a gold standard. The central bank focuses on maintaining the value of the currency. It needs to buy and sell gold in response

to international demands; it cannot divert its attention to care for commercial banks. The Reichsbank was a textbook example of this condition. It had maintained the value of the Reichsmark as its principal domestic constituencies and the Allies concerned about Reparations payments desired. But it could not at the same time take care of problems within Germany. When the force of the depression caused a few large firms to default on their loans, banks clearly needed some help. The Reichsbank was unable to help and the banks failed. But the problems did not originate in bank behavior; it came from the policy stance of the Reichsbank and from the political acts of the government that put its attention to that policy to the test.⁹¹ Grossman showed that no country that went off gold experienced a banking crisis.⁹² If Brüning had controlled trading in the Reichsmark earlier or announced the customs union later, German banks undoubtedly would not have failed either.

Conclusion

Keynes said during a discussion of the Young Plan in July 1929 that, “even if it were foreseen, the announcing of a moratorium would so damage Germany’s credit that a crisis would be precipitated by the announcement.”⁹³ He was right. Brüning’s announcement that Germany could pay no more Reparations generated a run on the mark in which banks failed and currency transactions were controlled. The ensuing run was on the mark, not banks, because the fear was that the German governments, not the *Grossbanken*, would not be able to pay their bills.

Could the banking crisis have been avoided? Yes. Brüning abrogated his international obligations in three ways during the spring and summer of 1931. He

promoted customs union, geared up to stop Reparations payments, and imposed currency controls. He did them in this order, placing great strain on banks. Had he done these three acts in any almost other order, German banks would not have failed. Had Brüning gone off gold by devaluing or imposing currency controls before one of the other announcements, German banks would have survived.

Could the currency crisis have been avoided? That is a harder question.

Adherence to the gold standard caused problems for countries far more stable than the Weimar Republic. It is unlikely that Brüning could have avoided going off gold in the end. Had he thought ahead, it could have been done more gracefully and with less damage to the German economy.

We therefore conclude that the German crisis of 1931 was a currency crisis caused by domestic political actions. True, banks failed, and the international economy constrained Germany. But the primary actions that led to the crisis of July 1931 were German, taken by Brüning in response to political pressures facing him and his supporters. The German crisis of 1931 was made in Germany.

And we draw another lesson as well from this analysis: The terms of the celebrated debate over the so-called "Borchardt thesis" need to be recast. Recent work showing that political forces in favor of reflation did exist inside the Weimar regime have made an important contribution.⁹⁴ But it is time to acknowledge that the truly significant political coalition that failed only by a hair's breadth was *transnational*. Put simply, there were powerful political forces in both France and Germany that perceived the advantages of an internationally cooperative strategy. This cross-national coalition always faced major obstacles, but as late as the Spring of 1931, its failure was not obvious. Indeed, the

cause of Franco-German cooperation, if not reconciliation, appeared to be making great strides forward. What destroyed it was, purely and simply, the German government's decision to pursue *Drang nach Osten*. It is all very well to say, as Duisberg and other apologists for the policy did, that this decision was a response to pressures for "imperial preference" among the allies. But only the reckless pursuit of "Mitteleuropa" destroyed the possibility of French financing for Germany. Stabilizing Germany by this means was clearly a goal of Briand's policy, and he came heartbreakingly close to bringing it off. What Borchardt and his followers now owe the rest of us is an answer to one simple question: Are they prepared to argue that German business groups and policymakers also had "no choice," no "Handlungspielraum" in this decision to swallow central Europe? That is what the denial of the possibility of an international version of reflation, if not full throated "Keynesianism" requires. As late as March, 1931, it seemed not a remote contingency, but a reasonable bet – one that even bankers were willing to take.

Table 1
German Economic Data

Month	Industrial Production (1928 = 100)	Unemploye nt (% Trade Unionists – See Note 13)	Partially Unemploye d (% Trade Unionists – See Note 13)	Bankruptcie s (monthly rate)	Savings bank deposits (million RM)
October 1930	77.1	23.6	15.4	843	10191
November 1930	75.6	26.0	16.1	829	10272
December 1930	72.2	31.7	16.9	850	10400
January 1931	67.8	34.2	19.2	1085	10767
February 1931	69.2	34.5	19.5	1065	10946
March 1931	73.5	33.6	18.9	1240	11064
April 1931	76.3	21.8	18.1	972	11165
May 1931	73.9	29.0	17.4	956	11225
June 1931	74.4	29.7	17.7	1034	11074

Source: *Wirtschafts und Statistik*, 1930-31; See Note 13.

Table 2
 German Government Debt
 (million RM)

	3/31/28	3/31/29	3/31/30	3/31/31
All	14,599	18,159	21,319	24,022
governments				
Reich only	7,139	8,229	9,630	11,342
Foreign debt	2,157	2,294	2,595	4,799
Foreign ST		185	532	830
Domestic debt	5,547	9,263	12,415	13,181
Domestic ST		2,569	4,070	3,746

Source: Laenderrat 1949

Table 3

German Balance of Payments, 1928-31

(millions of Reichsmarks)

	1928	1929	1930	1931
exports	13,599	14,344	12,713	10,169
imports	13,912	13,676	10,617	6,955
net exports	-313	668	2,096	3,214
capital inflow	6,958	4,459	3,678	3,817
capital outflow	2,852	1,991	3,195	6,494
net inflow	4,106	2,468	483	-2,677
gold exports	0	510	192	1,653
gold imports	931	345	72	0
net gold exports	-931	165	120	1,653
net income	2,862	3,301	2,699	2,190
reparations	1,999	2,501	1,699	990

Source: *Statistisches Jahrbuch*, 1933, pp. 498-99. (As quoted in Carl Schmidt, *German Business Cycles, 1924-33*, 1934.)

Table 4
German Financial Data

Month	All Stocks, 1924-26 = 100	Bank Stocks (Kredit- banken) 1924- 26=100	Overnight Money (Tagesgel d) Percent	6% Gold Bonds (Gold- pfand briefe)	6% Public Bonds	Young Bonds
December 1930	87.3	---	5.66	85.58	---	70.50
January 1931	81.8	110.52	5.10	85.85	80.51	72.75
February 1931	85.6	111.10	5.78	85.78	80.61	78.75
March 1931	91.1	112.65	5.31	86.64	81.58	80.00
April 1931	92.4	112.61	5.88	87.46	82.47	80.63
May 1931	83.0	106.09	5.64	87.32	81.70	70.00
June 1931	75.9	100.58	7.07	86.28	78.44	75.00

Source: *Wirtschaftszahlen 1925 bis 1931* (Berlin: Verlag von Reimer Hobbing, 1932), p.

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---- Stocks, Overnight Money, Gold Bonds (Monthly Averages)

Statistisches Jahrbuch fuer das Deutsche Reich 1932 (Berlin: Verlag von Reimer

Hobbing, 1932), pp. 354-55 — Bank Stocks, Public Bonds (Monthly Averages)

Commercial and Financial Chronicle – Young Bonds (Value At End of Week
Nearest End of Month; See Note 34)

Table 5

Bank Deposits by Access (million Rm) - by bank class

	28/2/31	31/3/31	30/4/31	30/5/31	30/6/31	31/7/31
All Grossbanken						
DD	3,756	3,819	3,657	3,626	3,626	3,891
TD	4,627	4,666	4,801	4,632	3,519	2,370
All						
Kreditbanken						
DD	4,528	4,562	4,390	4,382	4,327	4,749
TD	5,578	5,668	5,850	5,611	4,432	3,152
Kredit. - Gross.						
DD	772	743	733	756	701	858
TD	951	1002	1049	979	913	782

Source: Various issues of *Wirtschaftsdienst*, 1931.

Table 6

Assets (million Rm) of the Grossbanken

	2/28/31	31/3/31	30/4/31	30/5/31	30/6/31	31/7/31
Schecks, Wechsel	2,497	2,530	2,528	2,547	1,914	1,280
Remboursekredite	2,006	1,894	1,828	1,781	1,748	1,599
Total Short-Term	5,896	5,890	5,834	5,734	5,668	5,484
Loans						
against securities	1,307	1,309	1,276	1,235	1,228	1,055
against physical assets	3,195	3,214	3,219	3,183	3,071	3,014

Source: Same as Table 5.

Table 7

Time Deposits (million Rm) - Individual Grossbanken

	2/28/31	31/3/31	30/4/31	30/5/31	30/6/31	31/7/31
De-Di	1,778	1,789	1,799	1,760	1,444	1,009
Dresdner	871	874	931	869	631	490
Danat	977	989	1,038	967	647	300
Compri	621	639	650	533	518	363
Reichskredit	181	176	187	215	133	160
Berliner	198	199	197	187	145	109

Source: Same as Table 5.

Notes

1. For a good inventory of the main works in both English and German, see Balderston, "Banks," pp. 43, n. 1.
2. Kindleberger, *World*; Eichengreen, *Golden Fetters*.
3. James, *German Slump*; Balderston, "Banks."
4. See e.g., the discussion of the German reaction in James, *German Slump* or Born, *Bankenkrise*; also Balderston, "Banks."
5. Kindleberger, *World*, pp. 148.
6. Kindleberger, *World*, pp. 148-49.
7. Eichengreen, *Golden Fetters*, pp. 276.
8. James, *German Slump*.
9. See James, *German Slump*, p. 306.
10. Balderston, "Banks."
11. Balderston, *Origins*, p. 312.
12. Ritschl, "Peter Temin."
13. Inter-war rates of unemployment have long interested both scholars and policymakers. But the statistics for various countries are very uneven and not easily compared. For a recent overviews, see the essays in Eichengreen, *Inter-war Unemployment* and Stachura, *Unemployment*. At the time, unemployment figures for Germany were published monthly in the Statistisches Reichsamt's widely read *Wirtschaft und Statistik*. The same figures also appeared in the *Monthly Bulletin of Statistics* published by the League of Nations, where it is explained that they are for the end of the month and cover trade unionists. These are the figures we use here. Regardless of how one might want to adjust them in the light of better information about coverage or the labor force, they are useful as an indicator of monthly trends that could be actually tracked by contemporaries.
14. The literature on the Depression's effects on Germany is immense; besides the sources we cite for our statistics and those cited in note 1, above; see, e.g., Winkler, *Weimar* or Feuchtwanger, *Weimar To Hitler*.
15. Accord on the Young Plan was a precondition for agreement at The Hague for the early withdrawal of French and other allied troops from the Rhineland. Hindenberg's

desire to replace the Social Democratic-led coalition has received extensive discussion in recent years. See, e.g., Winkler, *Weimar* and especially the third (German) edition of Kolb, *Weimarer Republik*, pp. 213ff.

16. On Hindenberg and the “stab in the back” legend, see, e.g., Feuchtwanger, *Weimar To Hitler*, pp. 70-71. For “rule by decree,” see, e.g., Feuchtwanger, *Weimar To Hitler*, pp. 219-20 and Winkler, *Weimar*. Note that Hindenberg considered granting this power to the Social Democratic-led coalition, but would not. See the commentary and references to recent literature in Kolb, *Weimarer Republik*, pp. 214. I. G. Farben and other large German concerns played direct rolls in the switch. See the account of Duisberg’s letter to Finance Minister Moldenhauer in Winkler, *Weimar*, pp. 369. Duisberg headed the famous Reichsverband der Deutschen Industrie, the leading (but not the only) big business association in Germany. He was also a top official of the giant chemical company, as Moldenhauer had been. The RDI had begun pressing for the fall of the government as soon as the Young Plan cleared the parliament.

Winkler, *Weimar*, pp. 371, also relates heavy industry’s roll in encouraging the Deutsche Volkspartei to break with the SPD.

17. The “right turn” receives extensive discussion in Winkler, *Weimar*, Feuchtwanger, *Weimar To Hitler*, and Kolb, *Weimar Republic*. It had deeper roots in industry, especially within the steel industry, than can be discussed here. See besides Winkler’s discussion, the analyses in Kolb, *Weimarer Republik*, pp. 228ff. and Abraham, *Collapse*. The long discussion the first edition of this latter book occasioned is largely irrelevant to this paper’s topic. For a review, see Abraham’s “Introduction To The Second Edition” and the literature cited there. An interesting collection of speeches and writings (admittedly excerpts) from various industrial and political leaders is Hoester-Philipps, *Grosskapital*. Some of these, e.g., those on pp. 79-80 or 140-41 by Duisberg, Silverberg, or the Vorstand of the Deutsche Bank, are quite striking. A variety of well financed organizations, such as the so-called “Luther Bund,” which gave a platform to Hans Luther, a former finance minister who eventually became head of the Reichsbank after Schacht departed, promoted major changes in the structure of government and the weakening of parliamentary control.

18. Cf. Kolb, *Weimar*, pp. 114.; his later German reedition is entirely consonant with this judgment. The discussion in Winkler, *Weimar* is also revealing.

19. Reichsamt, *Deutsche Wirtschaftskunde*, p. 345.

20. Estimates of total German indebtedness vary, though the differences do not add up to much for our discussion. In the twenties, various reports of the Agent-General for Reparations (who administered the Dawes Plan for the allies) presented a great deal of data, but were recognized even then as incomplete. As part of the Standstill negotiations, a commission chaired by Albert Wiggin of the Chase National Bank (one of the largest creditor banks) compiled estimates of various classes of German debts. Some of these, notably the figures for the public sector debt, were quickly recognized as too low. (See,

e.g., Harris, *Germany's Foreign Indebtedness*, pp. 8ff.) The Wiggin committee's report, sometimes referred to as the "Layton Report" after Sir Walter Layton, who played a major role in its drafting, appears to have been the source for much of the data published during this period in *The Economist* (which Layton edited). These two sources formed the basis for the estimates in Feinstein, "Private;" see especially p. 127.

Early German estimates of their indebtedness were sometimes suspect, since they were prepared as part of negotiations over war debts and Reparations. But the official German estimates made in the late twenties and after appear quite good and have hardly changed at all over the years. Compare the figures in Reichsamt, *Deutsche Wirtschaftskunde*, pp. 341-50 with those in Laenderrat, Vol II., p. 554 and Deutsche Bundesbank, *Waehrung*, pp. 313. See also the helpful discussion in Bachmann, *Reichskasse*, pp. 42ff.

Modern discussions of the size of the debt rarely take sufficient account of three points. First, as emphasized in Reichsamt, *Deutsche Wirtschaftskunde*, debts run up by public corporations were reckoned separately from the rest of the totals conventionally reported for official debts. Second, all through the Weimar period, a low intensity war raged in the courts and parliament over older public debts that had been inflated away. Some bondholders pressed for at least partial repayment. The state responded with various schemes for rationing its obligations, which made the total volume of debt recognized by the state a more amorphous entity than usually imagined. See the discussion in Southern, "Impact," Finally as emphasized by McNeil, *American Money*, truly remarkable efforts were often undertaken to hide borrowing or evade the (usually weak) German or American efforts to restrict borrowing.

21. The literature is immense; see, e.g., Winkler, *Weimar*, pp. 380ff., or Feuchtwanger, *Weimar To Hitler*. The political developments came in the context of sometimes rapidly changing strategies by major industrial and agricultural groups. See, for example, the literature discussed in Kolb, *Weimarer Republik* or Abraham, *Collapse*.

22. Winkler, *Weimar*, pp. 388.

23. The one-third estimate does not include the 41 deputies of Hugenberg's Deutschnationale Volkspartei, who really constituted an anti-system party of the far right. The Reichstag had 577 members. The practical effect was to increase still further Brüning's dependence on Hindenberg. Cf. Feuchtwanger, *Weimar To Hitler*, pp. 233.

24. See e.g., Ellis, *Exchange Control*, p. 162. Virtually all analyses of the period feature a discussion of the capital outflow.

25. See, for example, Harris, *Germany's Indebtedness*, pp. 15-16 or, less baldly, Ellis, *Exchange*; a variant is partly explicit and partly implicit in James, *German Slump*.

26. For Lee, Higginson, see, e.g., Ellis, *Exchange*, pp. 162., but especially Bachmann, *Reichskasse*, pp. 213, though we can not follow her judgments on several broader issues. For the post-election maneuvers on the budget, see, again, Winkler, *Weimar*, pp. 394-98 and Feuchtwanger, *Weimar To Hitler*, pp. 236-37.

27. The quotations come from *The Economist* of Jan. 3, 1931, pp. 17-18. The discussion there merits a longer look: "After the marked decline in deposits shown in the October bank balance sheets, in consequence of the credit crisis, the November balance sheets show every sign of returning calm...The cessation of the withdrawals of money, especially foreign withdrawals, has enabled the banks to reduce their rediscounts at the Reichsbank, which had risen during October...."

28. On Prussia, the *Noteverordnung*, and the Social Democrats, see the discussion in Winkler, *Weimar*, pp.392-402 and Feuchtwanger, *Weimar To Hitler*, pp.233-38.

29. *New York Times*, Feb. 6, 1931, p. 9.

30. *New York Times*, Jan. 20, 1931, p.35. The *Commercial and Financial Chronicle*, Jan. 31, pp. 763-64 outlines the study's conclusions and notes that the Institute was partially supported by the Investment Bankers Association of America.

31. Schucker, *American 'Reparations.'*

32. The Reparations payments had been deliberately scaled down and made to vary over time under the Young Plan. See, e.g., Moulton, *War Debts*, pp. 223ff.

33. *New York Times*, Feb. 9, 1931, p. 30.

34. On bankruptcies as an indicator of banking crises, see Goldstein, *et al.*, *Assessing Financial Vulnerability*, p. 20.; the monthly German data would more than meet the standards for frequency discussed there. For the improvement in the Young Plan bonds, see, e.g., *New York Times*, Feb. 9, 1931, p. 30: the "so-called Young Reparations loan had a sharp advance this week, ascribed to the improved German political outlook at home." Our Table 4 reports values for the Young bond for the end of the week closest to the end of each month; our source, the *Commercial and Financial Chronicle*, normally came out on Saturdays. The 1930 low for Young Plan bonds came on Dec. 29, when the bond traded at 67.88. On June 12, 1930, before the Brüning government's budgetary and electoral debacles, the bond had reached a year's high of 91.25. The entry for June, 1931 in the table, incidentally, reflects the impact of the President Hoover's proposal for a moratorium on Reparations. On June 13, the bond traded at 63. For perspective, by August 28, 1931, the bond was at 59.50.

The extent to which the rises in various indicators was seasonal was extensively discussed at the time. See, e.g., the discussion reported in the *Commercial and Financial Chronicle*, April 18, 1931, p. 2869.

35. *New York Times*, Feb. 8, 1931, p. 8.

36. *New York Times*, Feb. 8, 1931, p. 8.

37. See, e.g., Rosenstiel, "Kreditmaerkte," p. 18. Bachmann's determinedly pessimistic account notes the borrowing, without, in our view, absorbing its implications. Facts come

through that are inconsistent with her story line: Germany borrows, bankers are competing to bring out loans, one bank is striving to become the exclusive banker for the government, etc. Cf. Bachmann, *Reichskasse*, pp. 235ff.

38. *New York Times*, March 23, 1931, p. 33.

39. *New York Times*, March 23, 1931, p. 33.

40. *New York Times*, March 30, 1931, p. 30.

41. *New York Times*, Feb. 6, 1931, p. 11 relates details of French loan participation; on the French reluctance to loan, see, e.g., Bachmann, *Reichskasse*, pp. 216ff.; Bennett, *Diplomacy*, is an excellent general account, but overestimates the willingness of the French to consider a loan in the Fall. Knipping, *Deutschland*, pp. 198ff., by contrast, correctly links the later French shift to the change in the French government.

42. On the change of government, cf. Knipping, *Deutschland*, pp. 198-199. That the French interest was real is apparent from the French archives. See, e.g., the memos from the French Ambassador to Berlin to the French Finance Minister, Jan. 15 and Jan. 29, 1931. These are now in the Archives of the Ministry of Finance, Carton B31478. See also the brief note of Feb. 10, 1931 on the discussions between Governor Moret of the Banque of France and Reichsbank President Luther of the Reichsbank. in Carton B31469 in the same archive. For the reaction of financial markets to news of the French participation, see *New York Times*, Feb. 8, p. 11. No one doubted, by the way, that Briand was the moving force within the French government behind the French shift, though French banking opinion had also changed. See *New York Times*, Feb. 10, 1931. But the sentiment was widely shared among the French Socialists. Herriot, for example, strongly supported it. Cf. *New York Times*, Feb. 14, 1931, p. 9.

43. *New York Times*, Feb. 8, 1931, p.8.

44. *New York Times*, Feb. 8, 1931, p. 8.

45. *New York Times*, editorial, Feb. 5, 1931, p. 22. For the French share of the world's gold, see the table in *The Economist*, Jan. 3, 1931, p. 7.

46. *New York Times*, Feb. 9, 1931, p. 30.

47. The data come from "Zwischenbilanzen Deutscher Banken," *Wirtschaftsdienst*, 16, *passim*. For general account of German banking in this period, see Whale, *Joint Stock*.

48. It should be noted that the total time deposits on 30 May 1931 from the individual banks are 100 million Rm less than the total in Table 5.

49. Balderston, "Banks."

50. Reichsamt, *Die gewerbliche Genossenschaftsbanken in den Jahren 1931/1932*, pp. 101, Table, reports bimonthly on net flows in and out of the cooperative banks. In January-February, there were net inflows; March-April and May-June show very small outflows of sizes that rule out talk of a run. After July, the size of the outflows increases greatly. But that only makes our point.

51. See the discussion in Whale, *Joint Stock*, pp. 334-39.

52. The currency data are from Reichsamt, *Statistisches Handbuch*, pp. 326. The deposits are demand deposits for all credit banks, as discussed above.

53. Goldstein, *et al.*, *Vulnerability*, pp. 20.

54. Various versions of the “structural weakness” view exist; the account in James, *German Slump* certainly contains elements of such a view. Goedde, “The German Twin Crises of 1931”[Unpublished], 2000, presents a strong argument that German bankers over-lent in the conviction that they were “too big to fail.”

55. *The Economist*, May 9, 1931, p. 15; the article summarized “The German Banking Position.” On p. 8 of the same issue, the magazine wrote that “in the current year the marked upward movement in the share and loan market has been favorable to the banks and their investments are worth more than at the end of last year.” For data on bank stocks and stocks in general, see Reichsamt, *Statistisches Handbuch*, pp. 354-355.

56. *The Economist*, May 9, 1931, p. 8.

57. The celebrated Treaty of Locarno that had ushered in the famous Franco-German rapprochement of the mid-twenties only guaranteed borders in western Europe.

58. For Brüning’s response to the French, see, e.g., Winkler, *Weimar*, pp. 382ff. A particularly succinct summary is Feuchtwanger, *Weimar To Hitler*, pp. 239: “It had been an objective of Hindenberg and Schleicher in appointing Brüning that such a shift should occur. Their aims were fully shared by the Chancellor, though here, as in his move toward presidential government, caution was his watchword.” For “Panzerkreuzer B” and related issues, see Feuchtwanger, *Weimar To Hitler*, pp. 243, but especially Winkler, *Weimar*, pp. 400ff. Supporting the building of the Panzerkreuzer opened the SPD to KPD charges that they were abandoning their peaceful aims and wasting money on military spending. In the midst of the Depression, this resonated powerfully within German working class circles. But if the cruiser failed, the government fell – Hindenberg, Schleicher, the Reichswehr, and their supporters within industry would see to that.

It should be noted that upsetting the military balance had major effects not only on the French and other great powers, but in central Europe, where the smaller powers lived under a complicated set of restrictions formal and informal. Such moves, in other words, threatened to destabilize large parts of the world.

59. For the Polish Treaty, cf., Winkler, *Weimar*, pp. 383.

60. The literature on "Mitteleuropa" is huge. For a review that brings out its frequently neglected economic roots, see Berghahn, "Quest." For the period we are concerned with, however, the indispensable study is Stegmann, "Mitteleuropa." This contains a penetrating analysis of the splits within the business community and how France figured in the thinking of various groups. See his discussion of German General Electric, the chemical industry, etc., pp. 208ff. The famous German Mitteleuropaeischen Wirtschaftstag which agitated for German designs to the east had been subsidized for a while by the German Foreign Office and supported by Schacht while President of the Reichsbank. After a reorganization in 1931, Siemens, I.G. Farben, leading iron and steel firms, and a major mining association helped support it. The role this organization subsequently played in German politics after the banking crisis has recently become an object of discussion. See the "Introduction to the Second Edition" in Abraham, *Collapse*, pp. xxxi-xli., which also has a useful review of the literature on divisions within the business community during the Weimar period. Robert Bosch prominently championed French-German cooperation and helped defend the Young Plan in public along with the SPD. For the latter, see Abraham, *Collapse*, pp. 151, n. 127. For the French side, see, beside Stegmann, Knipping, *Deutschland*, pp. 168-75, though, like Winkler (whose own treatment contains additional evidence on blocs within business), we have some reservations about certain of his points.

61. See the discussion and references in Note 49, above. For I. G. Farben and the Brüning cabinet, see, e.g., Abraham, *Collapse*, pp. 157. In the French case, the vast buildup of gold reserves since the stabilization of the Franc also gave the French state new abilities to project its financial power into central Europe. There is no doubt this worried German policymakers and business groups, though the French strategy of "encircling" Germany to the east was not always pursued with single-minded resolution. It also disturbed British policymakers who were favorably inclined toward Germany. See, e.g., Montagu Norman's comments on French "encirclement" policy recorded in Henry Stimson's Diary for April 8, 1931. The original of the diary is at Yale University Library; our reference is to the microfilm version, Reel 3.

62. Once again, the literature is large, inconsistent, and contentious. But see Stegmann, ed. "Mitteleuropa," who brings out the institutionalized cooperation between big business and the government, as well as the secrecy which enveloped their deliberations. Bennett, *Diplomacy*, Stambrook, "German-Austrian," and Kaiser, *Economic Diplomacy* are also instructive. For Brüning on the timing and the (false) claim that Germany could not choose it, see Stambrook, "German-Austrian," pp. 38.

63. *New York Times*, March 26, 1931, p. 12. The remarkable speech of March 24, 1931 by Carl Duisberg of I.G. Farben defending the customs union proposal placed it firmly in the context of other countries' efforts to form tighter trade blocs and bluntly stated that reconciliation with France would come only after Germany moved east. Indeed, the speech spoke vaguely of an eventual bloc extending from Bordeaux to either Sofia or Odessa, depending on which version of the text one relies upon. See the text and notes reprinted in Michalka, *Deutsche Geschichte*, pp. 245-46.

64. *New York Times*, March 26, 1931, p. 12.

65. German sources disagree slightly on the exact amount of the shortfall. Winkler, *Weimar*, pp. 403., discusses Dietrich's warning to Brüning. Bachmann, *Reichskasse*, pp. 249-50, cites internal documents indicating numbers close, but not identical, to those. Bachmann, in her study emphasizing "bad news" and the desperation of the period, does also record that the numbers did not then lead to a crisis and that with the budget adjustments later in the month and "einige guenstige Entwicklungen" the actual deficits briefly appeared likely to come lower than the estimates. This is in accord with our reading of the contemporary press reports and other documents of the period.

66. Again, various German sources disagree very slightly on the exact numbers, but – for all the pessimism that runs through them – not the key point of the success in borrowing. Compare Bachmann, *Reichskasse*, pp. 249 with James, *German Slump*, pp. 73. For the rejoicing that accompanied passage of the budget in international financial circles and foreign, see, e.g., *New York Times*, March 30, 1931, p. 30; the provision for further cuts in the event of budget shortfalls was noted earlier in the *New York Times*, March 26, 1931, p. 2.

67. For the banking advice, cf. James, *German Slump*, pp. 72; the banker in question, however, was strongly tied to particular groups in German politics and was not representative. The comment came right as Lee, Higginson was floating yet another large loan tied to preference shares in the Reichsbahn. (Compare James' date with that of Bachmann, *Reichskasse*, pp. 242; this latter deal, by the way, did have substantial French participation.) All through this period, Lee, Higginson was attempting to gain a monopoly on German government issues, while promoting Franco-German reconciliation. Other banking houses were also interested in bringing out loans, which is hard to square with claims that no one would extend credit to Germany. See the discussion in Bachmann, *Reichskasse*, pp. 235; work by one of us in French archives also supports this point.

Ritschl, "Reparations Transfers," argues that the Young Plan terminated capital flows into Germany by making private debts junior to Reparations. In our view this confuses the cart with the horse: Once capital inflows stopped, the question of debt priority indeed became pressing. But the best disproof of the hypothesis that Germany could not borrow after the Young Plan loans were floated is the simple fact that it did so, repeatedly. The French and other financiers, such as Lee, Higginson knew all about the Young Plan. Not the Young Plan, which helped Germany, but the customs union proposal destroyed Germany's international credit standing.

68. Winkler, *Weimar*, pp. 403.

69. See, e.g., Kolb, *Weimarer Republik*, pp. 218.; Bennett, *Diplomacy*, which draws out the need for a political success after the Fall 1930 debacle; and Feuchtwanger, *Weimar To Hitler*, pp. 249ff. Brüning saw his policy of cutting the pay of German government officials as part of this strategy of general deflation. Cf. James, *German Slump*, pp. 68. The wage cutting strategy was strongly supported by many industrial groups.

Note that Brüning's policy assumed everyone else would stay on gold; the British

devaluation eventually wreaked havoc, but this period lies outside this paper.

70. On Brüning's awareness that the American election would affect the timing of his plans, see Winkler, *Weimar*, pp. 404. See also *Commercial and Financial Chronicle*, May 16, 1931, p. 3636.

71. For the diplomatic issues, see especially Bennett, *Diplomacy*.

72. For the connection between the British talks and the domestic crisis, see Winkler, *Weimar*, pp. 404ff.

73. James, *German Slump*, pp. 306. makes this claim. But the April tax collection numbers had been published in May and were recognized at once as a serious problem. See the discussion and references below.

74. See, e.g., *The Economist*, May 9, 1931, p. 1001.

75. They were published regularly and quickly by several publications, including *Wirtschaft und Statistik* and often in daily papers, such as the *Frankfurter Zeitung*. Major foreign papers carried also discussed the dismal numbers. See, e.g., the *New York Times* report from Berlin on May 15 as excerpted in the *Commercial and Financial Chronicle*, May 23, 1931, p. 3810: "German Tax Revenue Below Estimate – Shortage of 500,000,000 Marks Now Indicated – Expenditure To Be Cut."

76. See, e.g., the following articles on the budget crisis in the *Frankfurter Zeitung*: "Wie Wird das Defizit des Reichsetats gedeckt werden," on p. 1 of the May 6th issue; "Bemerkungen, Das Defizit," on p. 1, May 21, 1931, along with more detailed material on p. 3. This contains a blunt assessment of the meaning of the April revenue shortfall.

In most recent literature by economic historians, the proposal for a customs union receives at most passing attention, as in James, *German Slump*. or Bachmann, *Reichskasse*. It is not integrated into a broader analysis, so that its pivotal significance emerges. It is worth noting, however, that some, but not all, contemporary accounts did realize the significance of the customs union proposal. Besides the *New York Times* story quoted above, see the discussion in Einzig, *World Finance*, p. 217, though he also touts the role of the Creditanstalt. Much sharper formulations can be found in Moulton, *War Debts*, p. 308 and especially Salter, *Recovery*. The latter, an influential figure in British financial and political circles, wrote that "...the sudden proposal of an Austro-German Customs Union caused alarm, as much by the procedure adopted as by its actual substance. It was felt that Germany, in her new mood, was perhaps about to embark on a policy of Treaty revision by successive acts of unilateral repudiation. In Europe the danger was now more truly appreciated; it was not the sudden outbreak of war, but of an increasing division of the Continent into two opposing groups which would ultimately make a conflict inevitable.....In June, as the conditions tending to a crisis developed, men were asking each other in New York, as they had been six months before in Paris, whether there was a danger of a new war in Europe. The addition of these fears to the existing doubts as to the solvency of debtors impoverished by the depression gave a fatal

shock to confidence.” (Pp. 225-26.) Primary sources such as the diary of American Secretary of State Stimson, now in the archives of Yale University, tend to confirm Salter’s claim.

We should note that our view does not absolutely rule out a minor role for the deterioration of the American market in triggering repatriation of funds by American banks, as some analysts have suggested. Federal Reserve behavior in this period did indeed suggest real anxieties and was markedly at variance with its actions during most of 1931. See the remarks on the Federal Reserve’s unusual behavior in the spring of 1931 in Epstein, “Loan Liquidation,” p. 965, n. 24.

By itself, however, the custom union project, particularly in the form Salter discusses it, quite suffices to wreck the situation along with the German budget crisis.

77. See *The Economist*, May 2, 1931, p. 944; for the failure, see *The Economist*, May 23, 1931, p. 1102. This is vague about the date, but not the flop. The issue came out on May 4, 1931; see the data in Rosenstiel, “Kreditmaerkte,” pp. 131, Table.

78. For the Prussian SPD, the street clashes, and the Minister of the Interior, see Winkler, *Weimar*, pp. 403-05.

79. For Luther and the debate about policy, see Winkler, *Weimar*, pp. 403-405.; Kim, *Industrie, Staat, und Wirtschaftspolitik*, pp. 73-81. We bypass here a large recent literature on the so-called “Borchardt thesis” for reasons of space. The quotation is from the Proclamation that accompanied the emergency decree, as translated in the *Commercial and Financial Chronicle*, June 13, 1931, p. 4294.

80. For Groener’s warning, and the urgency of heeding it, see Bennett, *Diplomacy*, pp. 120-21. Since the late twenties debate over Reparations and the beginnings of the effort to roll back the 1928 triumph of the Social Democrats, significant parts of industry had become very hostile to international financial obligations which they believed burdened Germany unfairly. See, e.g., Feuchtwanger, *Weimar To Hitler*; Winkler, *Weimar*; and Abraham, *Collapse*.

81. See the discussion in Bennett, *Diplomacy*, pp. 100-104. Kaiser, *Economic Diplomacy*, p. 36. dismisses this view because no clear reference has surfaced in French archives to support it. But internal French documents we have examined show very clearly that the French believed their trump card in battling the customs union was their financial strength. It is very likely that French capital and the government were asked to consider helping the Creditanstalt; such requests would probably have come through the Banque de France or one of the large private banks. One of us has spent much time in the archives of the Banque de France, but we would be the last to claim that all relevant documents have been produced even now.

82. For the rallies, see, e.g., Feuchtwanger, *Weimar To Hitler*, pp. 251; given the Versailles Treaty’s restrictions on the size of the German army, the Army believed it had to have the cooperation of the Stahlhelm in border regions (p.234) and, as shortly became apparent, it was also becoming far more interested in cooperation with the Nazi SA.

Some prominent industrialists were members of the Stahlhelm; Hindenberg was long its nominal head. For the French election, see Winkler, *Weimar*, pp. 406.

83. For the negotiations, see Bennett, *Diplomacy*, among many sources. Questions of naval agreements and disarmament raised major obstacles to agreement, but space makes it impossible to elaborate here.

84. The statement did not actually announce a moratorium. But it did signal unmistakably that it was coming.

85. For Voegler's speech and the meeting, see the account in the *London Times*, June 4, 1931, p. 13. Other prominent industrialists, including Thyssen and Reusch, who were present criticized Brüning for being weak and called for authoritarian methods and an anti-socialist drive. The article also discusses Hjalmar Schacht's promotion of a moratorium to a group of industrial leaders. Schacht had left the Reichsbank and famously opened close contacts with Nazi leaders, while continuing to appear before major industrial groups.

A "Note du Mouvement des Fonds" of the 26th of May, 1931, bearing the title "Reparations et Dettes Interalliees," now in the archives of the Banque de France (in a series of cartons numbered "59") shows that the French had taken the hints in the German press and expected that Brüning would raise the Reparations issue with the British.

86. The *London Times* account of the decree also reported the official denial. See the *Times*, June 6, 1931, p. 11. The *Commercial and Financial Chronicle*, June 13, 1931, p. 4293, quoted a story by the Associated Press forecasting an imminent move on Reparations by Germany, despite the denials. The *Chronicle*, p. 4293, noted that the Proclamation for the first time referred to Reparations as "tribute."

87. Winkler, *Weimar*, pp. 408-13, for the possibility of running out of money, the fears of Groener and others of a revolution, the possibility of military intervention, etc., and Feuchtwanger, *Weimar To Hitler*, pp. 246-48.

88. See, again, Winkler, *Weimar*, pp. 408-13. and Feuchtwanger, *Weimar to Hitler*, pp. 246-48.

89. Winkler, *Weimar*, pp. 413.

90. Temin, *Lessons*; see also Born, *Bankenkrise*, pp. 74ff. Our statistics on the gold and foreign exchange cover follow Reichsamt, *Statistisches Handbuch*, pp. 326. Born quotes slightly different figures that do not affect any issue under discussion; see his discussion on p. 74. The actual cover requirement was somewhat complex. Reichsbank notes in circulation required a minimum cover of 40% in gold or foreign exchange. Foreign exchange could not comprise more than 25% of the total cover; this is equivalent to a 30% gold cover rule. See Madden, *International Money Markets*, pp. 373ff., which also discusses the limited role played by the handful of banks that still had powers to issue notes.

91. Balderston argued similarly that the problem with the German banks was the Reichsbank's inability to supply reserves, but he did not connect the Reichsbank's position in June with Weimar's political act of March or to the German budgetary crisis. See Balderston, *Origins* and Balderston, "Banks."

92. Grossman, "Shoe."

93. Fleming, "Lectures of J. M. Keynes," p. 147.

94. See Borchardt, *Perspectives*; for the critics, see especially, Holtfrerich, "Economic," and Kim, "Industrie."

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