The Antecedents of the Austrian Financial Crash of 1931* **

By Eduard März and Fritz Weber

The subject matter of this essay is the crisis of the Austrian Crédit-Mobilier system during the 1920ies which culminated in the crash of the largest Austrian bank, the Creditanstalt für Handel und Gewerbe, held afloat only through the intervention of the Austrian state. The analysis focuses on the political and economic causes of the crisis and on the managerial decisions which contributed to the sharpening of the objective difficulties of the Austrian banking system. The spectacular financial breakdown initiated the Central-European banking crisis and led, in its later stage, to the crisis of the world currency system.

It is a truism that the development of the banking system reflects the development of the economy as a whole. This is especially so in the case of Central Europe where modern industry has been related to banking by powerful financial ties almost from its inception. World War I and its inflationary aftermath led to a further strengthening of these ties, for industry weakened by the enormous exertions of a *guerre á l'outrance* depended, for its recovery, on the generous supply of short as well as long term capital funds. As we shall see later on, the terms on which capital was provided, and the abrupt denial of the funds at the end of the 1920ies, explain to some extent the slow and stuttering pace of the Central European economy and its eventual downfall at the end of the decade.

The banking system itself was, of course, critically affected by the war and the political and economic disturbances following in its wake. There were two main causes for the precarious condition in which the great commercial banks found themselves in the early postwar period: as major shareholders in some of the key industries the steady deterioration of the capital endowment of all enterprises not directly involved in the production of war matériel had a palpable impact on their

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financial strength and solidity; a further source of weakness was caused by their sizeable war bond portfolio which depreciated *pari passu* with the inflation-bound fall in the value of the currency, although some banks succeeded in disburdening themselves of some of their war assets towards the end of the war. The decline in the value of their accounts receivable was by and large offset by a similar development of their accounts payable. This does not apply, however, to the sizeable foreign pre-war debt incurred by almost every major commercial bank.

So far we have focused attention on Central Europe as a whole. It is clear, however, that postwar Austria faced some special problems which arose out of the conditions attendant upon the break-up of the Danubian Monarchy. As is known, the territory of Austria-Hungary was divided among three new states, viz. Czechoslovakia, Hungary and the Republic of Austria. Four other countries, viz. Poland, Roumania, Yugoslavia and Italy received sizeable parts of the defunct Empire. As a result, the Austrian commercial banks suffered grievous capital losses: shipping lines and ship yards on the Adriatic littoral had to be handed over to Italian syndicates at prices more or less dictated by the new owners; proprietary interests in Czech steel, machinery and armanent enterprises had to be wholly or partially abandoned on terms grossly unfavourable to the reluctant Austrian sellers; the same fate was suffered by the banks with respect to some of their Polish oil holdings. Even more painful than these losses was the involuntary dissolution of the wide network of branch offices which the major Austrian banks had established in all parts of the Empire. For the sale of the branch offices to the native banks, in which the great Viennese houses acquired more or less substantial minority interests, implied the loss of the extremely profitable current banking business, especially in the Czech and Italian territories.[1] We shall see later on that Vienna devised some counter strategies to minimize these losses.

The Peace Treaty of St. Germain en Laye pledged the new rulers of Austria to maintain a status of strict political independence and, thereby quenched, even though temporarily, Pan German and Social-Democratic aspirations directed towards *Anschluß* with Germany. In opposition to these political currents Austrian finance capital nourished the vision of reestablishing, in the drastically altered Central-European scenery, the old economic and financial ties which had once secured Vienna a position of predominance in the Danubian basin. But it was clear to the main architects of financial and economic policy that Vienna could hardly hope to reacquire the preeminence of prewar times without radically overhauling its banking structure.[2]

[1] For details see: *März* (1981 a), 346 et sequ., 534 et sequ.
[2] *März* (1981 b).

The new philosophy propounded by the banking elite can be compressed in a single short sentence: Western capital plus Austrian know-how was to be combined to permit the Austrian banking system to carry on with its traditional task both inside and outside the present Austrian frontiers. It can safely be stated that the Viennese banking community adopted this policy stance with hardly a dissenting voice. As early as in spring 1920 Austria's leading commercial bank, the Creditanstalt, was able to inform the public that it had received a considerable infusion of equity capital from American and Dutch banking houses.

Soon other major banks followed suit: the Niederösterreichische Escompte-Gesellschaft established a close partnership with French, Belgian and British capital; the Boden-Creditanstalt strengthened its prewar links with American and British capital; the Wiener Bankverein found support among Belgian and Swiss banks, etc. As a result, the share held by foreigners in the equity capital of the big Viennese banks rose from 10 percent in 1913 to 30 percent at the end of 1923. Two other leading banks, the Länderbank and the Anglo-Österreichische Bank, were taken over lock, stock and barrel by their French and British creditors respectively. The Austrian government, which sanctioned the transaction, acted under the mistaken assumption that the financial status of these institutions precluded any other viable solution. British and French hopes that the banks would serve as jumping-off boards for the economic penetration of South-East Europe did not, however, materialize in subsequent years.

We have indicated above that the transfer of Austrian capital assets into foreign hands resulted from political as well as economic pressures. In the immediate postwar period political animosity towards Vienna prompted the successor states to take legislative and other action detrimental to Austrian financial interests.[3] When this first wave of hostility towards the new Austria subsided, other and more durable pressures caused a further hemorrhage of capital. Since the young Austrian republic was plagued for a number of years by an acute shortage of foodstuffs, raw materials and coal, and foreign credits were not readily available, vital imports had to be paid for by the sale of industrial shares and other securities. In this way, Austria's largest producer of coal, iron and steel, the economically pivotal Alpine Montan Gesellschaft, had to be transferred first into Italian and later into German ownership.

Under these circumstances, the formerly mentioned objective of Austria's financial elite of maintaining Vienna as the financial centre

[3] *Teichova*, 195 et sequ.

of the Danubian area must appear as a rather dubious proposition. The attraction of Western equity capital was not of such magnitude as to compensate the Viennese commercial banks for what seemed at first truly staggering capital losses. Nevertheless, the banking community of Vienna devised a number of measures, designed to minimize as far as possible the continuous drain of capital and to bolster its position in the capital cities of the successor states. One of the favourite methods of securing a firm base in the new states consisted in the acquisition of substantial minority holdings in some of the well established Polish, Czech and Yugoslav commercial banks. Again, to protect some of their industrial enterprises against the bureaucratic chicanery of the new authorities, the Viennese banks established holding companies in Switzerland for the sole purpose of camouflaging the existing property relations.

In the early postwar period there were some isolated instances of capital export on the part of the Viennese banks. Undoubtedly, the most celebrated case was the founding in the summer of 1920 of the Amstelbank, Amsterdam, by the Creditanstalt and the Austrian house of Rothschild which were joined in this venture by two respectable Dutch banking firms. It is clear from contemporary press commentaries that the new western outpost of the Creditanstalt was meant to facilitate the task of mobilizing western capital for the resumption of expansionary investment policies in the Danubian region. It was another example of how the Viennese bankers proposed to combine Austrian know-how with western venture capital.

The Austrian commercial banks had traditionally confined their activities to their home territory. Foreign engagements had always played a minor role, and had frequently been dictated by political considerations. With the dissolution of the Habsburg Monarchy a new situation arose. A sizeable part of the investments of all major banks now lay outside the boundaries of the new Austrian state. As a result, Austrian banking business was no longer domestic in scope, but had acquired a multinational complexion. As we have seen, Viennese bankers proposed to cope with the new situation by soliciting venture capital from abroad. Their own capital base had become too small after four years of total war and after the spectacular capital losses of the immediate postwar period. Moreover, the new Austrian economy remained severely out of balance in its relations to the outside world even after the worst war damages had been repaired. Thus business on a multinational scale could only succed, if it was nurtured from abroad.

It is a matter of historical record that this "grand design" was wrecked beyond all hope of repair in the great financial crisis of 1931. To be sure, only two banks, the Creditanstalt and the Boden-Creditanstalt, made a determined and sustained effort to put it into operation and they had to resort to risky and ever more dubious methods before they went down under a mountain of irredeemable commitments. Let us hasten to add that the deeper causes of the failure of the policy should not be sought in human frailty, but in the poor performance of the Austrian economy even before the onset of the great depression. Consequently, Austrian finance capital — represented during the 1920ies essentially by four banks, the Creditanstalt, the Boden-Creditanstalt, the Wiener Bankverein and the Niederösterreichische Escompte-Gesellschaft — remained critically vulnerable to every vicissitude of the world economy.

In what follows we can give but a short outline of the poor record of the Austrian economy during the 1920ies. Its course of recovery after the First World War was uneven and tardy and soon reversed by the arrival of the Great Depression. The GNP per head amounted in the years 1918 and 1919 to hardly more than half of 1913, the last prewar year. Its rise during the following years was very slow. The prewar level was surpassed only slightly towards the end of the Twenties. In view of the precarious state of the Austrian economy the depression which now set in proved especially painful. In 1933, when the crisis showed some signs of easing up, the average income of an Austrian citizen was hardly more than during the early postwar years, when the Austrian economy had come to a partial standstill. The recovery phase which then followed was marked by slow improvement. In 1937, the last year before *Anschluß*, the GNP per head was 15 percent less than in 1929, the peak of the postwar recovery period.[4]

The extent of human suffering caused by this development is perhaps best illustrated by the unemployment statistics. Unemployment during the interwar period was subject to wide fluctuations. During 1920 - 1922, the First Republic experienced its only short period of full employment, inasmuch as Austrian products could be sold abroad at grossly depressed prices in consequence of the rapid decline of the exchange rate of the Austrian Crown. After the stabilization of the currency in 1923 the unemployment rate soon stood at 10 percent and remained at this level until the onset of the depression, when it rose to approx. one third of the labour force.[5]

The lack of dynamics characteristic of the Austrian economy during the interwar period is best illustrated by the slow and halting pace of

[4] Österr. Institut für Wirtschaftsforschung.
[5] *Rothschild*, 79 et sequ.

investment activity. In 1913 about 13 percent of GNP was devoted to gross public and private investment. Net investment in the last prewar year must have amounted to 7 percent. In contrast to this comparatively facourable record, the annual gross investment rate during 1924 - 1937 was no more than 7 percent, and thus investment activity during this period must have been barely enough to compensate for the wear and tear of capital stock. Naturally, the investment rate fluctuated during the various phases of the cycle. Gross investment grew during 1924 - 1929 by an annual rate of 13 percent. It fell during the depression by 20 percent per year, and thereafter grew by 12 percent annually until 1937. It is clear that the investment rate was subject to far wider fluctuations than GNP.

The weak and erratic investment activity of the Austrian economy during the interwar period gives us a clue to the economic and political malaise of this period. The Austrian republic had inherited from the time of the Monarchy a sizeable industrial endowment, but it was marred by considerable and not easily remediable disproportionalities. The energy base was small, several branches of the consumer goods industry were either underdeveloped or scarcely existed at all. Certain branches of the investment goods industry, on the other hand, had been proportioned in response to the needs of the big markets of the Monarchy and thus seemed grossly overextended under the new circumstances. As far as agriculture was concerned, its potential had never been fully developed because of the competition of the outlying rural regions of the Monarchy.

These structural defects of the Austrian economy were aggravated by handicaps which Austrian policy makers could only marginally control. Foreign trade had played a minor role prior to the break-up of the Monarchy. The new Austria, by contrast, being one of the smaller states of Europe, was crucially dependent on favourable trade relations with its neighbours. The latter engaged, however, in a policy of economic nationalism which they sought to implement by administrative, tariff as well as monetary measures. Although the new Danubian states achieved remarkably little in the way of industrialization, there was a noticeable trend throughout the Twenties in building up excess capacities, if one looks at South East Europe as a whole.[6]

Economic nationalism in the Danubian region would have hardly mattered very much, if it had been pursued during a time of economic expansion. The growth record of the Twenties is, however, noticeably poor. According to the British economist Aldcroft, the period 1913 - 1929

[6] *Layton/Rist*, 12 - 13.

was marked by a much slower increase in income per head than the long period of expansion prior to the First World War. There were, of course, considerable differences between various regions. Japan advanced during this time to the rank of a major industrial power. Western and Central Europe, on the other hand, grew remarkably slowly, and most of its inferior performance must be ascribed to the poor showing of the United Kingdom, Germany and South-East Europe. Especially startling was the slow increase in European foreign trade whose growth rate was only a fraction of that of the prewar period.[7] Thus Austrian foreign trade which for traditional reasons tended towards the Danubian region encountered serious obstacles. A decisive reorientation towards the West and the overseas markets was to prove a long and drawn-out process whose consummation was achieved in the Second Republic.

Almost to its very end the First Republic was plagued by an enormous deficit in its balance of payments. The primary cause of the deficit was the trade balance which showed a persistent and alarmingly high excess of imports over exports. Only during the last recovery phase, which was cut short by the *Anschluß,* was it possible to reduce the trade deficit to manageable proportions. Thus Austria had, at long last, achieved stability in its economic relations with the outside world, but at the price of a low level of economic activity and a correspondingly high rate of unemployment.

In what follows we shall attempt to reconstruct the Austrian balance of payments during the first recovery phase of the Twenties. Since we do not have reliable information about two key items, i. e. short term capital movements and interest (as well as dividend) payments, the following table makes only clear that the huge trade deficit could only be met fractionally by Austria's international services (viz. freight, trade and tourist services) and that recourse had to be taken to short term borrowing from abroad. It must also be remembered that Austria's short term indebtedness arising from its passive balance of trade was further augmented by the heavy borrowing of the commercial banks for the purpose of channelling western funds into various and variegated investment outlets in the Danubian region. But no reliable estimate can be made of this additional debt burden which must have reached considerable proportions towards the end of the Twenties. Naturally, this debt vis-a-vis the West was offset by (corresponding though dubious) claims vis-a-vis the East.

It becomes clear from the above ennumerated credit and debit items that there remains an unspecified rest of AS 3905 million (AS 487.5 mill.

[7] *Aldcroft,* 324 et sequ.

Table 1

Austrian Balance of Payments 1923 - 1930
(Mill. AS)

			Annual average
1. Austrian trade deficit		— 8665.8	— 1083.2
2. International services			
Interest & dividends (balance)	— 812.4		— 101.5
Transit services	+ 622.8		+ 77.9
Transit trade	+ 900.0		+ 112.5
Tourist trade	+ 1646.0	+ 2356.4	+ 205.7
3. Long term capital movements			
Foreig loans (80 % of par value)		+ 1500.0	+ 187.5
4. Short term capital movements			
Austrian National Bank:			
Foreign exchange reserves			
1 January, 1923	+ 169.4		
31 December, 1930	— 1015.0		
		— 845.6	— 105.2
Foreign indebtedness 31 December, 1930		+ 1750.0	+ 218.8
Rest (errors and amissions)		— 3905.0	— 487.5

Sources: Österreichisches Statistisches Zentralamt, Der Außenhandel Österreichs in der Zeit zwischen den beiden Weltkriegen, Wien 1946, p. 20. Beiträge zur Zahlungsbilanz Österreichs in den Jahren 1926 - 1928, 1929, in: Statistische Nachrichten, Wien 1930 und 1931.

Wärmer, G. (1934), Die Auslandsverschuldung Österreichs, in: Mitteilungen des Verbandes österreichischer Banken und Bankiers. Wien, 282 f.

annually) which must be listed under "errors and omissions". The greater part of this amount should be regarded as part of Austria's short term capital debt. Moreover, some flight capital was repatriated during the Twenties.

How did the government propose to solve its two most harassing problems, viz. the high rate of unemployment and the persistent balance of payments deficit? Its only attitude seemed strict fiscal discipline, an attitude mightily encourage by various foreign advisers, among whom Mr. Zimmermann, Commissioner General, installed to supervise the execution of the Geneva reform programme, was the internationally best known figure. Non-interventionism thus became the battle-cry of a succession of Austrian governments. This policy, or rather lack of policy, reached an absurd height, when a high powered commission under the chairmanship of Ludwig v. Mises, the renowned advocate of laissez-faire economics, recommended in 1931, that the government abstain from any positive action: "The federal government, the states and the communities should act according to the principle that in economically depressed times the execution of all projects, no matter how useful and desirable they may be, must be deferred until there is an improvement in the situation."[8]

Under these circumstances, policy making devolved upon two institutions, the Central Bank and the commercial banking system. During the early postwar period, when Austria suffered from a runaway inflation, interest rates reached unprecedented heights. In later years they fell at an extremely slow pace and remained at a startlingly high level during the trough of the depression years. Only from 1933 onward was there a noticeable drop in the rates charged by the commercial banks. We may add that there was no attempt on the part of the Austrian National Bank to exercise a moderating influence on this policy. (See table 2 below.)

As is known today, certain initiatives to this effect were strongly opposed by the Bank of England. An interesting passage from the minutes of the Board of Directors (Generalrat) of the National Bank may suffice to illustrate the point. At the session of the Board of 23 March, 1925, Mr. Georg Stern urged the reduction of the discount rate which stood at the exorbitant level of 13 percent. Vicepresident Dr. Thaa, who had a distinguished record of service both as a civil servant and as a chief executive of the Central Bank, pointed out in his negative reply to Mr. Stern that "the Management of the Bank had the distinct impression that foreign interests do not believe that the time has yet come for a reduction of the bank rate. Surely, it would be wrong to ignore the opinion of these, from an Austrian point of view, so important interests, and thus it cannot be recommended to displease them by emphasizing our own opinion." In the minute it is further stated that Dr. Thaa observed that Austria was in the process of negotiating a foreign loan.[9]

In 1925, when Dr. Thaa insisted on the necessity of pleasing foreign interests, the bank rate could still be considered a signal which no commercial bank could afford to ignore. In the following years, when a

[8] Redaktionskomitee, 31.
[9] Generalratsprotokoll der Oesterreichischen Nationalbank, March 3, 1925. Archive of the Austrian National Bank.

Table 2

Interest Rates in Austria 1923 - 1937

Year	Interest rate for saving deposits (average p. year)	Prime rate*)	Bank rate (average p. year)
1923	7.0	20 - 30+)	9.0
1924	8.6	16.5 - 20.5	11.6
1925	8.2	20.5 - 16.5	10.9
1926	4.9	14.5 - 12.25	7.5
1927	4.2	12.25 - 12.0	6.3
1928	4.2	12.0	6.3
1929	4.8	12.0 - 13.5	7.4
1930	4.1	12.5 - 10.0	5.7
1931	4.3	10.0 - 15.0	7.2
1932	4.2	13 - 11	6.9
1933	3.4	8.5 - 11	5.2
1934	3.1	8.0	4.7
1935	2.8	7.5 - 8	3.8
1936	2.5	5 - 6	3.5
1937	2.5	n. a.	3.5

*) Kommission and other charges not included.
+) Estimates of Federn, W. (1925), 64.
Source: Monatsberichte des Österr. Instituts für Konjunkturforschung, 6/1938, 140.

steady flow of foreign short term credit was channelled into Austria, in consequence of the wide disparity of interest rates between Central Europe and the West, the banks became more and more independent of the discount services of the Central Bank, since the latter had no choice but to issue domestic currency in exchange for foreign reserves. Still the commercial banks showed no inclination to substantially lowering their lending rates.

It might of course be argued in defence of commercial banking policy that the banks were entitled to charging what the market could bear, since they had not been conceived as purveyors of charities. But the commercial bank rate, it must have been clear to the chief bank strategists, did not reflect the workings of an uninhibited market mechanism. The great majority of the industrial enterprises had no access to the international capital markets, and thus were compelled to submit to the dictates of a few financial obligopolists. During the latter part of the Twenties, it must be remembered, investment activity revived throughout Western and Central Europe. In Austria, too, the industrial investment rate which had, during the early years of the Republic, scarcely sufficed to ensure the renewal of used-up capital equipment, now rose perceptibly, though by no means dramatically.[10] In most branches of industry Austrian entrepreneurs realized ever more clearly that they had to modernize or to perish in view of the strong wave of rationalization, modernization and specialization sweeping over Europe. Since new equity capital was not to be obtained in impoverished Austria, especially after the disastrous losses at the Vienna stock exchange in 1924, investment could only be financed by bank credit, usually in the form of credit on current account.

The banks must have been aware of the risk which this kind of financial technique entailed, but since most of the enterprises which endeavoured to renew and expand their capital equipment were linked to the parent banks by age old financial and proprietary bonds, the latter could have hardly afforded to withhold the means urgently needed for modernization. Moreover, bank managers and industrial entrepreneurs tended, during the second half of the Twenties, to assess the prospects of Austrian industry optimistically, inasmuch as production and exports showed a rising trend.

Why, so it may be asked, did the banks insist on charging such exorbitant rates even to their own inner circle of industrial clients? They could have hardly had any illusions about the enormity of the burden thus placed on even the best reputed industrial firms. There is no easy answer to this question. Our own impression is that the major banks, which had suffered enormous losses during the early postwar period, were keenly interested in the earliest possible recovery of their former substance. Walther Federn, one of the best observers of the Austrian economic scene during the interwar period, commented as early as 1925 that the banks would perhaps have done more for the rebuilding of their erstwhile financial strength, if they had first concentrated on the task of rebuilding Austrian industry.[11]

Austrian City spokesmen rationalized the dear money policy by arguing that Austria, as an impoverished country, suffered from an acute capital shortage, and that the "selective" function of the interest rate assumed especial significance under these circumstances. They pointed, moreover, to the unusually high interest rates which sight and saving deposits commanded since the runaway inflation of the early postwar years, when the national saving rate had dropped to an

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[10] Österr. Institut für Wirtschaftsforschung, 17.
[11] *Federn*, 73 - 74.

abysmally low level. While this was true in the years 1919 - 1924, the margin between the rate for saving deposits and commercial loans noticeably widened during later years. (See table 2.)

There was another reason why Austrian banks had no compunction to persevere in their high interest rate policy. As the Twenties progressed, they found little difficulty in placing western funds, lent to them on comparatively easy terms, in the markets of the successor states which were eager to build up their own industrial capacity.[12] The greater part of the money thus channelled, or rather rechannelled, abroad went, it must be emphasized, to foreign banks rather than to the industries destined to be the ultimate recipients.[13] There are no reliable data available that would make it possible to ascertain with some degree of accuracy how the capital obtained in the West was divided between Austrian debtors and foreign debtors in Eastern Europe. There can be little doubt, however, that the Austrian share was somewhat larger than that apportioned to the successor states. Thus the difficulties resulting from the dubious method of borrowing short and lending long were primarily caused by the slow pace of recovery of Austrian industry during the Twenties and by its catastrophic slump at the beginning of the Thirties.

In retrospect it must be said that there was surprisingly little public discussion concerning the appropriateness of such exorbitant interest rates. Instead, Austrian newspapers and professional journals focused attention on wages and social benefits which they considered inflated and damaging to Austrian competitiveness. While it was true that real wages during the greater part of the Twenties surpassed somewhat the markedly low prewar level, they lagged considerably behind the standards attained in Western Europe throughout the entire period. There was even a noteworthy differential between the Czechoslovak and Austrian wage level during the Twenties.[14]

The impressive banking establishment which Austria had inherited from the Monarchy went through a phase of expansion during the postwar inflation. In 1923, after the stabilization of the currency, a process of contraction set in which lasted for a full decade.

The story of the collapse of many of the small and middle sized banks which engaged in speculative currency and security transactions and failed to reach safe shores in the aftermath of stabilization, has been

[12] *Hertz*, 63 et sequ.
[13] This is the impression one obtains from the records of the great Viennese banks which are available in the archives of Creditanstalt-Bankverein.
[14] *Hertz*, 151 et sequ.

Table 3

Number of Banks in Austria 1913 - 1935

	1913	1919	1923	1925	1927	1930	1935
Joint stock banks	27	34	76	51	40	31	19
Private banks	150	146	282	230	152	n. a.	131

Sources: Federn, W. (1928), Die österreichischen Banken, in: 10 Jahre Nachfolgestaaten. Special issue of „Der österreichische Volkswirt". Wien, 56.

Compass. Finanzielles Jahrbuch 1931 and 1937.

told by the late Karl Ausch, the brilliant commentator on economic affairs of the First and Second Austrian Republic.[15] As we have pointed out above, only four major banks, which absorbed some of the moribund smaller establishments, survived into the late Twenties to carry on with commercial banking in the crédit-mobilier fashion.

We have already detailed the fateful policy decisions of the chief financial strategists after the war. They can be summed up in the trinitarian formula: the preservation, as far as possible, of the old empire relationships, the pursuance of a dear money policy and the borrowing of short term funds in the West for the purpose of rechannelling them into investment outlets both in Austria and some of the other Danubian states. It now remains to be shown that these erroneous policies were compounded by numerous day to day decisions which, in their totality, made all but certain the disastrous failure of the banking system in 1931.

Two of the four major banks, the Creditanstalt and the Boden-Creditanstalt, could boast in 1913 of a veritable industrial empire which extended throughout the realm of the Monarchy. In 1923, when the fog of the postwar inflation had lifted, their industrial and other financial assets were still impressive, but noticeable structural changes had occurred since the last prewar year. The Creditanstalt had been able to augment the number of its industrial holdings and of other assets both in Austria and the successor states, but the quality of its investments had undoubtedly deteriorated. From the following table it becomes clear that the number of foreign banks which it controlled or where it possessed considerable minority interests had noticeably increased; this was due, to some extent, as was pointed out above, to the dissolution of its network of subsidiaries and the transfer of these assets to Czech, Polish and Yugoslav banks. As for its industrial assets, the majority

[15] See: *Ausch.*

Table 4

Conglomerate of the Creditanstalt 1913 and 1923
(Number of firms)

Branche	1913	1923	CA property preserved since 1913	Newly aquired property after 1918
Banken	5	20	2	18
Versicherungen	4	3	2	1
Handel, Transport, andere Dienstleistungen	8	13	3	10
Erdölindustrie	3	10	2	8
Berg- und Hüttenwesen	5	6	2	4
Maschinenbau- und Metallwarenindustrie	20	19	12	7
Elektrotechnische Industrie und Elektrizitätswerke	5	5	3	2
Baustoff- und Bauindustrie	6	7	4	3
Textilindustrie	8	7	5	2
Diverse Konsumgüter	4	7	3	4
Nahrungsmittelindustrie	1	3	1	2
Zuckerindustrie	7	7	5	2
Spiritusindustrie	4	4	4	—
Brauereien	7	7	4	3
Chemische Industrie	6	5	2	3
Papierindustrie	4	5	2	3
Holz- und holzverarbeitende Industrie	6	8	2	6
Insgesamt	103	136	57	69

Source: März (1981 a), 537.

of firms to which it was closely linked, now lay within the confines of the new Austrian state. Valuable Czech as well as Italian properties were no longer part of the Creditanstalt-conglomerate.

The case of the Boden-Creditanstalt differed somewhat from that of its mighty rival. Although the majority of its industrial firms and other financial assets were located on the territory of new Austria, just as in the case of the Creditanstalt, its industrial empire in the successors states still looked quite formidable at the end of the inflationary period. Its sphere of influence abroad comprised such powerful industrial combines as the Mautner Textile Works, with affiliates in several of the Danubian countries, the Aussig Chemical Works in Czechoslovakia, the Fanto Oil Corporation with deposits in the Galician part of Poland etc. There could be no doubt that, in contrast to the Creditanstalt, the second major Austrian *crédit moblier* had retained formidable industrial interests in the successor states. Yet, the financial position of the Boden-Creditanstalt must have looked quite precarious to the few insiders who were able to assess the real value of the far-flung industrial empire, even as early as 1923. Some of its best known enterprises, the Danube Navigation Company, the Steyr Automobile Works, the above named textile combine Mautner, emerged from the inflation in a critically weakened condition. They, like a number of smaller firms, proved a continous drain on the resources of the parent bank.

After the stock exchange crash in the spring of 1924 the Boden-Creditanstalt, like most other commercial banks, felt compelled to purchase sizeable packets of shares of its client firms, to prevent them from falling to dangerous levels and thus to impair the financial substance of the parent bank. In 1925, after the Schilling currency was introduced, all Austrian enterprises had to reassess the value of their assets and to present to the public revised balance sheets which were supposed to be based on reliable data. It becomes evident from the so-called "Stern expertise" that the Boden-Creditanstalt, not unlike some other institutes, engaged on this occasion, i.e. when presenting the so-called "Goldbilanz", in a number of fraudulent manipulations of which the two most dubious aspects were the upward revision of the value of some of its most important assets and the transfer of certain securities from the security-portfolio to accounts receivable.[16] All of these measures were meant to deceive the public in regard to the true nature of the bank's position. Similar practices were indulged in by many of the enterprises belonging to the Boden-Creditanstalt-conglomerate with the explicit assent of the bank's management.

It becomes evident from the records of Austria's second largest banking house that from 1924 onward it found no other way to pay dividends than by dipping into hidden reserves.[17] The same was true of many of its client firms. An incident characteristic of this potentially dangerous situation occurred in 1925. Accordingly to the minutes of the Board of

[16] Hofrat Georg *Stern*, Gutachten, erstattet der besonderen Kommission bei der Österreichischen Creditanstalt für Handel und Gewerbe. Archiv of Creditanstalt-Bankverein.

[17] Vorstandskontrolle der Boden-Creditanstalt vol. 1924 - 1929. Archive of Creditanstalt-Bankverein.

Directors of the Boden-Creditanstalt, Mr. Herzfeld, Vice-President of the institute, informed his colleagues that the Mautner Textile Works had made known their intention of reducing the dividend rate on account of the worsening of the economic situation; this was thwarted, however, by the parent bank which insisted on the continuation of a 10 % dividend.[18] Another incident of this kind took place in June 1926: On the occasion of the above mentioned "Goldbilanz" the representative of the Boden-Creditanstalt urged the management of the Danube Navigation Company to raise the dividend rate by one third and to reassess various assets, so that the capital of the firm could be adjusted upward.[18]

As was intimated above, the main purpose of these manipulations was the desperate desire on the part of the banking establishment to stabilize the situation at the Vienna stock exchange where the continuous and pressing offer of securities caused a steady decline of the share index. The ultimate weapon with which the banks could hope to combat this fatal tendency — i.e. fatal, since it undermined their own foundation — was their readiness to intervene through purchase of tendered stock. Thus the security-portfolio of all commercial banks, and above all of the Boden-Creditanstalt, was steadily growing at a time, when the bank managers would have been well advised to follow an exactly opposite course. No doubt, like Mr. Micawber, they acted on the assumption that something would eventually turn up.

The ruinous policy of buying up stock so as to create the impression of stability was pursued with such consistency that the banks did not hesitate to intervene, when their own securities were offered for sale. Again, the Boden-Creditanstalt seemed to have been the most foolhardy of all sinners. In 1923, when an outsider, who had amassed a fortune during the war and postwar inflation, made a determined drive to obtain a voice in the affairs of the bank, the management had issued new shares which had to be placed with "business friends", as Mr. Sieghart, top executive during the Twenties, wrote in his memoirs.[19] From this time onward the portfolio of the bank seems to have been the refuge for a growing number of the bank's own securities. Shortly before the downfall of the bank in 1929, Mr. Sieghart made desperate efforts to disburden himself of some of these securities in western markets. Alas, he was not to find eager buyers. When the Boden-Creditanstalt closed its doors, it turned out that its portfolio contained more than one fourth of the total number of its own shares.[20]

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[18] Vorstandsprotokoll der Boden-Creditanstalt, June 1, 1926.
[19] *Sieghart*, 195.
[20] Hofrat Georg *Stern*, Gutachten.

In 1927 the Boden-Creditanstalt made a successful take-over bid for two other middle-sized Austrian banks, the Union-Bank and the Verkehrsbank, which had a wide network of branch offices all over Austria. The Boden-Creditanstalt which had not maintained subsidiaries up to that time, seemed now intent on developing the deposit business, inasmuch as it was plagued by increasing liquidity problems. But the acquisition of the two banks brought no visible relief. While the Boden-Creditanstalt succeeded in the same year to reduce its enormous foreign debt, its security portfolio kept on growing.[21] Before the end, the Boden-Creditanstalt made increasing use of the rediscount facilities of the National Bank until this last avenue of retreat was blocked in view of the lack of solid collateral.[22]

One last incident may be noted for it clearly demonstrates how detrimental the dear money policy had become to the bank's own enlightened interest. At the end of the critical year 1927 the Zivnostenska banka, one of the leading Czech commercial banks, which had a controlling interest in the Mautner combine, appealed to the Boden-Creditanstalt to lower the interest rate charged to this customer. In the minutes of the Boden-Creditanstalt, the Zivno is quoted as saying that "the Mautner Textil Works cannot longer submit to such a high rate, and that the Zivno itself has no other reason for charging the rate except that the Boden-Creditanstalt has fixed it at the present level."[23] One must conclude from the intervention of the Czech bank that the latter had a clearer perception of the havoc caused by this insistence on dear money than any of its Viennese sister institutes.

What was said of the Boden-Creditanstalt, can be applied with only a few modifications to Austria's largest commercial bank, the Creditanstalt für Handel und Gewerbe. Even after the collapse of the Monarchy and the tribulations of the postwar inflationary period the Creditanstalt still ranked among the leading banks of Central Europe. It was still endowed with a considerable capital which was partially held by eminent western financial establishments such as the British house of Rothschild, the Morgan Guaranty Trust Company, Kuhn, Loeb & Co, the Prudential Insurance Comp. and others. By its merger with the Viennese branch of the Anglo-Austrian Bank, which took place in 1926, its position seemed stronger than ever before. To the list of illustrious shareholders was added the name of the Anglo-International Bank which was known to be linked to the Bank of England.

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[21] Der österreichische Volkswirt. Die Bilanzen, March 17, 1928, 279 - 280.
[22] *Ausch,* 307 et sequ.
[23] Vorstandsprotokoll der Boden-Creditanstalt, December 2, 1927.

Despite its not inconsiderable losses of industrial assets in the early postwar period, the Creditanstalt succeeded in continually increasing its volume of business, a considerable part of which was done in foreign exchange. There can be little doubt that during the early Twenties the centre of attention was held by domestic business. But the focus of activity shifted with the progress of time. During the last years before the breakdown of the bank the channelling of credits to South-Eastern Europe, borrowed on short term from the West, assumed ever wider significance. The precarious position of the bank, primarily caused by the shaky state of the Austrian economy, was further undermined by the risky lending practices of later years.

The fatal mechanism, which we described above, was also at work in the case of the Creditanstalt. The latter, too, intervened at the stock exchange to bolster its own stock as well as that of its major client firms. Toward the end of the Twenties the security portfolio reached such enormous proportions that its value almost equaled the bank's total capital, i.e. share capital plus open reserves. The situation was further aggravated when, in 1929, the bank was forced, almost at gun-point, to merge with the totally bankrupt Boden-Creditanstalt. Reluctant as the Creditanstalt's management was to take over its prostrate rival, it may not have realized the full weight of the burden it was compelled to shoulder.

Intervening at the stock exchange had, as we have shown before, its own suicidal logic, for it necessitated the bank as well as its client firms to pay handsome dividends, even if no profit could be drawn upon. Thus hidden reserves had to be tapped, and if such were not available, assets had to be reassessed so as to create a semblance of hidden reserves. The afore mentioned "Goldbilanz" was of course a welcome opportunity to engage in such dubious manipulations on a large scale.

From the Stern expertise, which was based on the true figures of the bank, we get an impression of the extent of these reassessments. From 1925 onward the Creditanstalt took steady recourse to these practices. As can be seen from the data below, during 1926 and 1927 its publicly announced profits approximately equaled the amount of reassessments. In 1929 reassessments were almost twice as large as shown profits. Thus, during the last years before the collapse profits resulted largely from these dubious, if not fraudulent manipulations.

The true condition of the bank was of course much worse than is portrayed in the above figures. For, as one can say with the advantage of hindsight, the Creditanstalt systematically underestimated the extent of its dubious assets; as time went on, a goodly part of the short term

Table 5

Internal Reassessments of Creditanstalt assets 1926 - 1929

Year	1926	1927	1928	1929
Total extent of reassessments (mill. AS)	4.2	12.5	10.1	16.5
In % of annual shown profits	53.5	120.0	96.0	180.0

Source: Stern expertise (based on the internal figures of the Creditanstalt).

credits extended to domestic as well as foreign customers could not be redeemed, and had to be turned, nilly willy, into long term investments which, on the day of judgement, proved to be irreclaimable. It must be added that the Creditanstalt, as most other commercial banks, disguised the true nature of its foreign debt by identifying part of it as credit based on foreign commodity transactions *(Rembours-Kredit)*. The spurious *Rembours-Kredite* constituted, as Wilhelm Kalveram stated in his authoritative book on bank accounting, the greater part of the foreign short term debt of the Central European commercial banks. Their sudden withdrawal triggered off the financial crisis of 1931.[24]

Can the Creditanstalt and the Boden-Creditanstalt, which controlled among themselves the greater part of Austrian industry, plead extenuating circumstances for their ill considered policy of "giantism"? It must be said in their defense that after they had embarked on the disastrous course of maintaining their old "imperial" relationships, retreat became exceedingly difficult in later years, when an attempt to liquidate some of their foreign investments might have caused a mass withdrawal of western funds. Before the great crash they had virtually become prisoners of their ill considered policy to do business as if the Monarchy still existed.

During the Twenties questions were occasionally raised by qualified observers as to the soundness of the present course. If difficulties were admitted by the responsible quarters, as they occasionally were, they were usually excused on the ground that taxes and salaries had enormously risen since prewar times. What the spokesmen of Vienna's banking establishment forgot to add was the fact that despite the shrunken size of postwar Austria the major commercial banks employed a far greater number of employees than ever before. The figures relating to the Creditanstalt were as follows:

[24] *Kalveram,* 94 - 95.

Table 6

Employees of Creditanstalt 1913 - 1929

	1913	1922	1925	1927	1929
Territory of present day Austria	956	2365	1885	2076	2097
Territory of the Monarchy	1747	—	—	—	—

Source: Der österreichische Volkswirt, Die Bilanzen, 1927 - 1930.

The charge of giantism cannot be raised against all commercial banks that survived into the late Twenties. The Niederösterreichische Escompte-Gesellschaft, the Mercurbank and the French-controlled Länderbank followed a more moderate course and consequently could be navigated quite successfully through the stormy waves of the depression. The story of the Wiener Bankverein demonstrates rather clearly that Austrian commercial banking as a whole could have fared far better, if it had shown more restraint and wisdom under the drastically altered conditions after the collapse of the Monarchy. In 1913 the Bankverein ranked among the four leading banks of Austria. In some respects, e.g. in the field of deposit banking, it even surpassed its renowned rival, the Creditanstalt. After the war the Bankverein attempted, as far as possible, to preserve its far-flung industrial empire, but did not resume the policy of rapid expansion it had practiced prior to 1913. During the latter part of the Twenties the Bankverein, by contrast to its two big rivals, did not embark on an ambitious investment policy neither at home nor abroad. Before the outbreak of the 1931 crisis the total foreign short term debt of the Bankverein amounted to appr. 120 mill. as against 700 mill. in the case of the Creditanstalt.[25] Thus during the crisis of 1931 and the succeeding years its losses were far less serious than those of the other banks.

The changing fortunes of Vienna's banking system during the Twenties and early Thirties are reflected by the composition of the Central Bank's annual balance sheets.

The note circulation rose consistently during the Twenties, indicating the slowly rising volume of business activities; it peaked in 1929 and declined during the years of depression. Its gold and foreign exchange

[25] *Clarke*, 187. Direktionsrats-Protokoll des Wiener Bankverein, April 10, 1931. Archiv of Creditanstalt-Bankverein.

Table 7

Austrian Note Circulation and Coverage 1923 - 1932
(in mill. AS)

31 Dec.	Note circu- lation	Sight deposits	Total circu- lation	Gold and ex- change res. as % of circu- lation	Dis- counts	Dis- counts as % of circu- lation	Govern- ment Secu- rities
1923	712.6	64.9	777.5	51.0	132.5	17.0	253.4
1924	838.8	55.3	894.1	62.2	188.1	21.0	217.8
1925	890.0	55.0	945.0	68.1	180.6	19.1	187.9
1926	947.3	37.4	984.7	76.0	133.9	12.6	177.3
1927	1005.3	39.6	1044.9	79.4	132.1	12.6	173.2
1928	1067.3	56.5	1123.8	79.4	208.5	18.5	116.2
1929	1094.4	63.9	1158.3	71.5	306.6	26.5	108.7
1930	1090.1	92.7	1182.8	85.5	149.0	12.6	101.2
1931	1183.3	128.1	1311.4	25.1	933.8	71.2	95.6
1932	913.8	218.6	1132.4	18.0	404.9	35.8	663.0

Source: Wärmer, G. (1936), Das österreichische Kreditwesen. Wien, 21 f.

coverage rose from 50 percent in 1923 to 85.8 percent in 1930. From this record height it then shrunk to 25.1 percent in 1931 and a mere 18 percent in 1932. Up to 1931 bills had constituted only a small part of bank coverage; only in 1924, when certain Viennese banks encountered difficulties, the discount facilities of the Bank were resorted to on a larger scale. The same was true in 1928 and 1929, when the Boden-Credit-anstalt made a desperate effort to avoid bankruptcy. The composition of the Bank's assets changed drastically in 1931, when the Creditanstalt was faced with enormous withdrawals and the government decided to meet the commitments of Austria's biggest commercial bank. One year later, there was a partial swap of government bonds for bills of exchange, after the government decided to turn the short term liabilities of the Creditanstalt into part of the national debt.

The Creditanstalt crash, apart from its international repercussions, deepened the severe crisis in Austria, since many of the straggling client firms could no longer be kept afloat by financial injections. Moreover, the momentous decision of the Austrian government to assume full responsibility for the bank's liabilities, which was taken at the prompting of the Creditanstalt's foreign creditors, resulted in an acute imbalance of Austria's public finance, which could be resolved in no other way than by the floating of an international loan granted to Austria on similar terms as the ill-reputed Geneva reform loan.

Summary

On the eve of World War I the Austrian Crédit Mobilier system stood at the zenith of its development. The collapse of the Habsburg Monarchy and the economic disintegration of Central Europe led to a drastic change of the environment within which the banks had to conduct their business. The large Viennese commercial banks, although weakened by war and inflation, decided to continue their traditional business policy which embraced the Danubian area as a whole. They were aided in this by two factors: the influx of short-term capital and the acquisition of equity capital by the west. The chronic industrial stagnation undermined the capital base especially of those banks which persisted in an expansionary business policy. A a result, the Boden-Credianstalt had to be merged with the Creditanstalt in 1929, and the latter foundered after the inception of the world depression and initiated the Central-European financial crisis.

Zusammenfassung

Am Vorabend des Ersten Weltkrieges befanden sich die österreichischen Crédit-Mobilier-Banken am Höhepunkt ihrer Entwicklung. Der Zerfall des Habsburgerreiches und die ökonomische Desintegration Zentraleuropas veränderten in drastischer Weise die Rahmenbedingungen für die Betätigung der Banken. Die Wiener Großbanken entschieden sich — obwohl durch Krieg und Inflation geschwächt — für die Fortführung ihrer traditionellen, auf den gesamten Donauraum gerichteten Geschäftspolitik. Dies wurde ermöglicht durch den Zustrom kurzfristiger Auslandskredite und durch die Beteiligung westlicher Banken an den Wiener Kreditinstituten. Die chronische Industriekrise untergrub die Kapitalbasis insbesondere jener Institute, die an einer expansiven Geschäftspolitik festhielten. Im Jahr 1929 mußte daher die Boden-Creditanstalt mit der Creditanstalt fusioniert werden und nach Ausbruch der Weltwirtschaftskrise geriet auch die letztere ins Wanken und löste damit die mitteleuropäische Finanzkrise aus.

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