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STABILIZING SOUTHEASTERN EUROPE, FINANCIAL LEGACIES AND EUROPEAN LESSONS FROM THE FIRST WORLD WAR**

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ABSTRACT: *This paper pays brief attention, although more than the recent flood of 1914 centenary books, to economic causes of the First World War before turning to its fateful economic consequences for Southeastern Europe. The Austrian lack of economic leverage over Serbia is cited as a reason for its resort to the military option. At the war's end, the option of the victorious powers to provide significant economic relief to the region where the conflict had begun was not taken. After tracking the brief, limited assistance provided, the paper reviews to the massive economic problems confronting four of the five of independent states, neglecting Albania as a special case, that could now be called Southeastern Europe. First Greece and then Bulgaria faced forced inflow of refugees. Romania and the Yugoslav Kingdom faced the economic integration of large new, formerly Austro-Hungarian lands. All of them were left not only with war deaths and destruction but also with large war debts, or in Bulgaria's case, reparations. The paper concentrates on the primary Western response to these four economies, an effort led by the Bank of England to replace immediate postwar inflation with the deflation needed to reestablish currencies with prewar convertibility to gold, now with Pound Sterling added to a gold reserve standard.*

Independent central banks, the major positive legacy of this initiative, were to lead the way. But the financial stability that all four economies did eventually achieve in the 1920s served only to reduce their war debts. Otherwise, maintaining the fixed and overvalued exchange rates restricted domestic credit, encouraged protective tariffs, and did not attract the foreign capital, especially new state loans, that this emphasis on a single, European financial framework had promised. A concluding section considers the lessons learned from a postwar period that promoted economic disintegration by the 1930s. Looking at the period since the end of the Cold War and then the wars of Yugoslavia's dissolution, we see EU leadership in the reduction of trade barriers, the promotion of common fiscal practice and the prospect of genuine European integration as Western lessons learned. Within the region, independent central banks have helped the process. But the stabilization of currencies around the overvalued Euro has posed a familiar post-1918 problem since the European downturn of 2008.

KEY WORDS: *financial stabilization, refugees, war debts, reparations, national currencies, gold reserve standard, central banks, Bank of England, foreign trade and foreign investment, capital markets*

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** On the occasion of the centenary of the First World War the Faculty of Economics – University of Belgrade has organised an international conference on the economic causes and consequences of this historical event in September 2014. The Editorial Board of *Economic Annals* is thankful to the author who offered an advanced version of his paper presented at the conference for publishing in our journal.

1. INTRODUCTION

The 1914 centenary has generated a flurry of Western publication on the war's short-term diplomatic and military origins, emphasizing contingent reactions and underlying political mentalities. But the longer-term causes and consequences have received little attention. This is particularly true for the framework of economic leverage and rivalry whose relevance to German war aims during the conflict itself were revived by Fritz Fischer in the 1960s. To be sure, the initial attraction of the Fischer thesis, extending those aims back before the war and making a case for German war guilt after all, has receded in subsequent Anglo-American and German scholarship. Declaring war primarily to stifle domestic opposition from Germany's rising Socialist Party has not stood up to widespread criticism. At the same time, however, this criticism has helped to turn attention away from any consideration of economic causes for the start of the war. Now the current attention to 1914 leaves the war's fateful economic consequences unattended. They are too often confined within critiques of the Paris Peace Conference. Its set of bad new borders and unjust treaties lead us right to the Second World War, according to this simplified scenario. The bloody dissolution of Yugoslavia in the 1990s has encouraged this retrospective narrative, making the creation of a Yugoslav state in the first place a prime example of the misdeeds of the victorious powers in 1919 (MacMillan, 2007).

The question of the war's economic causes deserves at least some brief attention before this paper turns to the clearly momentous economic consequences for Southeastern Europe. This seems justified because the three major Western studies in the flood of new 1914 studies that have appeared in 2014 pay no attention whatsoever to the economic background to the war. The contingencies of 1914 are seen as decisive. MacMillan (2013) concentrates on them with special attention to diplomatic disjunctures and political mentalities. Hastings (2014, p.20) draws on his background as a major military historian, to focus on competing plans for mobilization and warfare. At least in his Introduction, he credits a nuanced version of the Fischer thesis for being right about German military preparations from 1912 forward¹. Clark (2013, p.28) justifies the contingent diplomatic reactions of Germany and Austria-Hungary to the Sarajevo assassination of the Archduke, for which he finds the Serbian government directly responsible and unwilling to respond satisfactorily to the subsequent Austrian ultimatum. Clark's retrospective inclination may be seen in his Introduction's reference to

¹ For an insightful review of the mass of prior scholarship from Sidney B. Fay, see Martel (2014), pp. 401-431.

the Srebrenica massacre in 1995 as continuing a pattern of Serbian misbehavior, while his substantive argument on the war's origins has been criticized for what a Bibliographic Essay in *The Cambridge History of the First World War* has called "a bias against Serbia and towards Austria-Hungary and Germany, whose decision makers vanish from the narrative at decisive moments in 1914".²

The economic case against the two Central Powers has long been neglected, in part because of Anglo-German trade relations, each being the other's best customer. Also, German trade with Serbia undermined the Austro-Hungarian tariff war with Serbia, 1906-11. So the old notion of a coordinated Austro-German trade offensive focusing on the Balkans is not persuasive, even after the several loans to a presumably anti-Serbian Bulgaria after the Balkans Wars. But two financial features offer support to the argument that the disposition to acting on military plans in both Berlin and Vienna from 1912 forward was too clear to call either of them "Sleepwalkers" in 1914. For Germany, calculations by my Maryland colleague Jon Sumida from the seminal work of Herrmann (1996, pp.234-237) on pre-1914 armaments reveal that military spending from the German budget doubled from 1911 to 1913 and the expenditure per soldier rose by 60 percent, far ahead of any other Great Power.³ Here was the advantage in heavy artillery, machine guns and training that made the Schlieffen plan seem realistic against the increased numbers of French troops. For Austria-Hungary, on the other hand, it was the lack of any financial leverage over its Serbian adversary that made the military option seem the only recourse despite its lagging arms expenditure. From Vienna's failure to obtain a controlling interest in the Serbian national Bank in 1883 forward through the ascendancy of French banks and state loans from 1906, the Austrian side had no way to exert financial pressure on Belgrade. After being forced to abandon as ineffective its Tariff War in 1911, Vienna's lack of economic leverage opened the way for the same "militarization of diplomacy" as in the other Great Powers and the long-standing argument of the Austrian General Conrad for a "preventative war" against Serbia (Djordjević, 1962; Lampe and Jackson, 1982).⁴

2 For a more detailed and dispassionate study of Serbian the July crisis of 1914, a downgrading of the strength and influence of the Apis organization of *Crna ruka* among Serbian arm officers that Clark emphasizes, see the chapter by Marc Cornwall, "Serbia" in Wilson, ed. (1995), pp. 55-96.

3 For a review of how the pace of German military spending supports the Fischer thesis, still minus a final decision for army chief Moltke's "preventative war" until Russian mobilization began in July 1914, see Strachan (2004), pp. 66-78.

4 On the general "militarization of diplomacy" by the July crisis, see Stevenson (1996), p. 360.

During course of the war itself, it has been argued that economic rather than military disadvantage provides the best explanation for the defeat of the Central Powers by 1918. That is the conclusion offered by Broadberry and Harrison (2005, pp.35-36 and 41-111) in their Introduction to the major set of Western studies of the war's economic costs and consequences, as supported by the chapters on Germany by Albrecht Ritschl and Austria-Hungary by Max-Stephan Schulze. Among the ten chapters in all, however, there is none dealing with Southeastern Europe or any part of it. The present paper seeks to repair some of that deficiency. We have already seen the role that German financial strength and Austrian weakness played in the outbreak of the war. A British plan to force German surrender in a few months by destroying its financial system was aborted as unworkable once the war was underway (Lambert, 2012). After the war, it was British policy led by the Bank of England that provided an overriding framework for economic recovery now including Southeastern Europe. It was based on a return to the prewar Gold Standard rather than the prewar competition for favor in the region by state loans, a competition in which Britain had taken no part and which the defeat of the Central Powers would now leave entirely to France.

The costs of the war across Southeastern Europe were heavy, and chances of recovery without external support were slim indeed. Beyond the damage to property, whose calculation remains controversial, the huge cost in human capital and trade relations can be measured. The death toll of combatants and civilians for Serbia/Montenegro led the rest of Europe at 5.7 percent of prewar population, and Romania fell just short of the 3.4 per cent lost by France. Voluntary migration on the prewar pattern was minimal, and the forced migrations that now disrupted the region's settlement resulted in a net gain only for Greece. Its failed Anatolian campaign brought in 1.5 million refugees to balance the million, mainly non-Greeks who left. The Greeks forced out of Bulgaria, the Hungarians out of Transylvania, and the Albanians out of Kosovo did not much advance the fortunes of the Bulgarians, Romanians or Serbs who took their place. Overall, postwar birthrates declined, but lower death rates and reduced migration kept rural population density rising and arable land per capita rising. Only Bulgaria and Greece had seen their manufacturing sectors expand during the war, and then continue to expand afterward. Romanian oil production and Yugoslav mining had also expanded during the war, partly under occupation, and continued afterwards, Bulgaria did experience a significant rise in industrial labor after 1918, but even there the rural share of the population remained at the regional norm of 80 percent. The destruction of rolling stock, rail lines and shipping links hit Romanian agriculture the hardest, as exports initially plummeted and crops returned to 1913 levels only in 1929. The continuing absence of east-west or

coastal rail connections across the new Kingdom of Serbs, Croats and Slovenes combined with the heavy war damage in Serbia to keep the potential of a large domestic market for economic integration from developing (Broadberry and Harrison, 2005, pp.22-37; Lampe and Jackson, 1982, pp.329-433).

As the region's economies struggled within new borders and with transferred populations and disrupted transportation, the initial assistance from the victorious Western powers was modest indeed. It does not bear comparison to the UNRRA aid after the Second World War or the largely EU funding after the wars of Yugoslavia's dissolution. Food supplies from the US under the organization headed by Herbert Hoover provided \$100 million worth, almost evenly divided between Romania and the Yugoslav Kingdom by the end of 1919, but barely \$1 million to Greece. Bulgaria would subsequently receive \$4.8 million but, as a wartime ally of the Central powers, only in return \$2million in gold (Surface and Bland, 1931, pp.164-235). There followed in 1920 a proposal from the League of Nations to provide commercial credits for exports of needed primary and raw materials from individual Western firms, more specifically bonds to be secured by assets within the importing Central or East European country. A British banker was appointed to work out the details, but crucial American participation was absent. An effort to provide some lower-cost credit to Austria failed, and British officials treated the requests from Poland and the Yugoslav Kingdom skeptically. The international commission to facilitate what were called Ter Meulen credits, after its Dutch originator, was never formed. The project had vanished by 1922, leaving the Yugoslav Kingdom to obtain a loan for railway construction from the United States later that year, at a high 8 percent rate of interest with repayment tied to customs revenues (Orde, 1991, pp.121-123).

Meanwhile, to cope with postwar challenges posed to successor governments, the size of non-military state employment rose rapidly everywhere except Greece. In the course of the 1920s. the Yugoslav total tripled from prewar Serbia's already large numbers and Bulgaria's doubled, both of them falling short of the quarter million employed in Romania (Lampe and Jackson, 1982, pp. 501-505)⁵. These huge totals were a domestic burden in their own right, compounded by lack of training for lower level administrators. Low salaries fed corruption, especially in less attractive locations like Bessarabia or Kosovo. Its level may be judged from a crime rate for Bulgaria's state employees that was 400 percent of the 1910 level by 1926, versus 64 percent for the population as a whole (Lampe, 1986, pp. 64-

⁵ By a contemporary Western estimate, Beard and Radin (1929), pp. 180-86, the Yugoslav total could have been cut by one third at no loss in efficiency.

65). The attraction to state salaries and the inefficiency of overstuffed ministries would be a legacy to the post-1945 Communist regimes and, as we shall see, to recent Greek experience.

2. THE STRUGGLE FOR FINANCIAL STABILIZATION

Western financial policy, led by Britain and the League of Nations rather than the United States, shared a common postwar priority with the governments of Southeastern Europe, but for different reasons. The British lead, followed by the League's Financial Committee, sought to restore the Pound and other currencies to their prewar exchange rates under the Gold Standard, thereby subduing postwar inflation and the damage its persistence would do to capital markets. New York's challenge to London, including the huge US accumulation of gold reserves during the war, would be contained in the process. For Southeastern Europe, stabilizing their currencies at fixed rates of exchange backed by gold and reserve currency holdings offered the prospect of renewed access to Western capital markets, to loans repayable in currencies at attractive albeit overvalued rates of exchange. This new supply of badly needed capital and cheaper imports would make up for the smaller exports available for purchase at overvalued exchange rates. This was the bad bargain that famously cut into Britain's own exports and kept unemployment high through the 1920s. For our region, the lending that was supposed to follow from stable exchange rates enforced by independent central banks never came (Roselli, 2006, pp.33-42). Let us examine this common pattern before turning to distinctive features for Greece, Bulgaria, Romania and the Yugoslav Kingdom. Albania's fledgling economy, with its central bank founded in Rome and its financial support plus foreign trade under informal Italian control, could proceed with the inflationary note issue that the rest of the region and its potential creditors were determined to prevent.

The other four regional economies saw their foreign trade struggle through the 1920s with note issues of currency much reduced from prewar levels and the pressure of surplus imports addressed with protective tariffs. Per capita foreign trade in constant exchange rates did increase everywhere but Romania, whose exports were barely half of the 1906-10 level for 1921-25, but significant trade deficits appeared everywhere but Bulgaria. There the lower level of overall increase could be traced in part to the peace treaty's restriction into 1925 on signing a new commercial agreement with another country. The sharper and more consistent reductions from prewar levels appeared in currency note issue and state budget expenditures. All of their governments and banks of issue had faced an immediate

postwar inflation of their currencies, driving exchange rates down past 1,200 per prewar unit for Greece, past 1,400 for the Yugoslav Kingdom, and to 2,800 for Bulgaria and almost 4,000 for Romania by 1923. Under urging from the Bank of England in particular, as we shall see, they all reacted with concerted efforts to deflate and then stabilize their exchange rates, all at a cost to the domestic supply of investment capital. For 1926-30, only Greece's note issue exceeded 50 percent of the prewar level, and only its state budget could spend more in constant terms than it did in 1911. The other three showed greater reductions in note issue, particularly for 1926-30, and state budgets ranging from 47 percent of 1911 for Bulgaria up to 83 percent for the Yugoslav Kingdom (Lampe and Jackson, 1982, p.343 and pp.380-384).

All four faced the further burden of war debts, or in Bulgaria's case reparations. Although reduced from their daunting 1920 levels by 1930, their constant values still exceeded the already sizeable 1911 levels, by only 3 percent for Yugoslavia but 29 percent for Bulgaria and 35 percent for both Greece and Romania. These obligations deepened deficits on current account, and in the aforementioned absence of Western loans, capital accounts failed to make up the continuing deficits on balance of payments (Lampe and Jackson, 1982, pp. 428-429, 512-515). In general, the four governments responded with protective tariffs, and West European banks provided the same sort of short-term capital that the US market gave to the German economy until the Depression cut the supply line disastrously short. Only small fractions of Western loans actually obtained were use for productive purposes like railway construction. But the specific cases give us a better understanding of the postwar consequences of these prewar financial priorities. Let us consider them in turn before concluding with some disturbing comparisons but more promising contrasts with the region's postwar experience, following first the Cold War and the wars of Yugoslavia's dissolution.

Greece was the one regional economy to start the postwar period with its currency still stable at prewar par, thanks to Allied credits that covered a massive issue of bank notes and an increase in the public debt from 1.4 to 2.4 million drachmas by 1920. But then the Anatolian incursion, far beyond the original, British-encouraged coastal expedition, made military expenses two thirds of skyrocketing state budget expenditures. By the time that incursion collapsed in 1923, two thirds of total expenditures had to be covered by new foreign credits plus a forced domestic loan. The public debt had tripled. In the process, the drachma's exchange rate for British Pounds had fallen from the prewar rate of 26.6 to 140 by mid-1922 and then down to 387. In 1920, the League's Financial Committee had approved the move away from the prewar gold standard adopted

in 1910. In addition, remittances from the Greek diaspora which had helped to reduce the trade deficit had fallen to one third of their prewar level. These were the hard circumstances under which the new “Revolutionary Government” of the Republic declared in 1924 faced the accommodation of the 1.5 million refugees who had poured into northern Greece and Athens from Anatolia.

Mark Mazower’s seminal study (1991, pp.1-113) traces the accumulation of burdens and the failure of the post-incursion government to reign in the profits taken by domestic banks from the borrowing binge. Their regime’s initial effort abolished the Consortium of the five established banks, led by the National Bank of Greece. It had tried but failed to reign in black market currency speculation. Instead, the Liberal government imposed export duties and a 15 percent tax on bank exchanges of currency. The established banks continued to prosper, buoyed by a five-fold increase in net profits by 1922 after nearly as large an increase during the war years. Lacking the leverage of impose direct taxation, the Republic’s government fell back on further tariff increases. The private economy also took advantage of the badly fragmented set of labor unions to push down real wages, reversing their increase until 1922. The government’s search for new Western loans was frustrated by the accumulation of war debts. Only the recourse to League loans for refugee resettlement would prove successful before a London agreement on war debts in 1927.

Already in 1923, Anglo-American support for a proposal from the League’s Financial Committee overcame opposition from the Bank of England and began planning for a loan to finance a Refugee Settlement Commission (RSC). The new Greek government had asked for such assistance and renewed the consultations with the Financial Committee that the Venezelos regime had initiated in 1920. By 1924, a League of Nations loan of 12.3 million Pounds was in place, albeit at 8 percent interest, with an American advance allowing the staffing of the RSC and its construction of refugee housing to begin. By 1927, its Greek-American leadership and largely Greek staff had housed half of the homeless refugees from Asia Minor. After the dismissal of the brief military regime of General Pangalos in 1926 and the aforementioned agreement on Greece’s war debts to Britain, the restored Liberal government, again headed by Venezelos, could again turn to international capital markets. But the failure to agree even on the creation of a central bank or to restore the drachma to a fixed exchange rate under the gold reserve standard until 1928, both priorities for the Bank of England under Montagu Norman as we shall see, restricted access. The exception was a second refugee loan for the highly regarded RSC. The government’s new Committee of Experts, working with the American leadership of the RSC and British

representatives keen to reestablish their priority over US interest in Greece, pushed forward with a loan in 1928, as large as the first but at half the interest rate. Its arrival and new Greek borrowing for road construction allowed the RSC to announce in 1930 that the other half of the refugee influx had now been housed and connections between the largely northern settlements advanced. The ethnic Macedonian minority and also Greek peasants with claims to the settlement land suffered in the process, but otherwise the work of the RSC constituted the one significant Western contribution to postwar recovery in Southeastern Europe.⁶

Refugees, primarily from northern Greece, also flooded into Bulgaria as a consequence of the First World War. Their numbers, 220,000, were far smaller than the Greek total but their armed VMRO militants politically more volatile. They soon seized control of the Pirin region in the southwest and disputed the border with the new Yugoslav Kingdom. There would be no League loan even partly available for their settlement until 1926. This was hardly surprising since Bulgaria's government had been the only one in the region allied with the losing side. From 1918 there were still some prewar debts to pay to French bondholders anxious not to allow the Bolshevik precedent of repudiation to be repeated. And by 1921 a far larger sum for reparations was due, half the state budget's annual revenues. This the Agrarian Party in power under Aleksandar Stamboliiski from 1919 refused to pay along with the prewar debts. Only some payments in kind to Yugoslavia and Greece were provided until the total due was cut by three quarters and the repayment period extended in 1923. The League's Financial Committee agreed to this concession only after a French proposal for military intervention had attracted no wider support and after Stamboliiski and his Agrarian government had been overthrown. Before then, only some desperately needed food supplies had been obtained from the US in 1919, worth \$4,8 million but as noted above requiring a payment of \$2 million in gold. The leva had already fallen to 75 percent of its 1911 value during the War and to 50 percent by 1918. German troop extraction of food supplies had mounted during the war, the resulting shortages threatening famine after the bad harvest of 1918. For the period of international isolation and antagonism from 1919 to 1922, the leva's exchange value declined seven-fold. Only in 1923 could Bulgarian reach accommodation with the League and the postwar financial framework that its Financial Committee was prescribing for all of the smaller Eastern states (Lampe, 1986, pp. 60-64).

⁶ The most recent refugee study, drawing on Greek as well as the long familiar Anglo-American sources, is Kontogeorgi (2006), pp. 73-110 on the RSC in particular.

The leading figure in shaping that framework was Montagu Norman, the powerful Governor of the Bank of England. Working with his close, originally Austrian colleague, Sir Henry Strakosch, they were determined to restore prewar financial stability by restoring the prewar Gold Standard. Under their influence, the League's reduction first in Hungarian and then in Bulgarian reparations were tied to the separation of the domestic central bank from commercial operations and its independence from the budgetary demands of the central government. This decoupling was to safeguard the money supply from the aforementioned inflation that had surged up as the war ended and decoupled their exchange rates from fixed prewar parities, with the French gold franc for our region. Even before Norman was able to restore the Pound Sterling precisely to its prewar rate of \$4.86 in 1925, he was advocating the widespread restoration of fixed rates backed by gold and Pound reserves. He and Strakosch envisaged the creation of an international consortium of central banks that would operate independently of their respective governments, inviting comparison with present EU efforts to create a Banking Union (Boycc, 1987, pp.39-47; Cottrell, 1997, pp.29-74). Because of its vulnerability over reparations, Bulgaria was the first state in Southeastern Europe to stabilize its currency well below the prewar rate of exchange but fixed under the new gold reserve standard. In 1924 the leva's value was thereby set at 3.8 percent of the prewar rate, less than half the 8.9 percent at which the Yugoslav Kingdom was stabilized the following year but still well above the leva's market rate of 2.7 percent in 1923. To maintain this overvalued exchange rate, the Bulgarian National Bank (BNB) restricted note issue and eliminated its state loans. The pressure on the state budget was only slightly relieved by the two League loans that were finally provided in 1926 and 1928.

As detailed by recent Bulgarian scholarship, the BNB restrictions and the pressure to reduce deficits in the state budget significantly reduced available funds. Avramov (2007, pp.260-293) has called the postwar economy "capitalism without capital". The newly limited lending from the BNB shrank to less than 10 percent of bank credit by 1928, versus one third before the war. Its ratio of reserve assets to note issue was the highest in the region and its discount rate among the highest. State budgets struggled to cut annual deficits under 20 percent by the late 1920s, pressing to keep import and export tariffs in place and raise indirect taxes. Stamboliiski's direct taxes on higher incomes and his Grain Consortium to raise export prices could be not maintained in the face of objections from the League's Financial Committee. Tariff revenues were still called upon as guarantees for the two League loans of 1926 and 1928. The first came through the London and New York capital markets and the second from London alone. They realized only 2.9 and 5 million Pounds respectively, far short of the two

12 million Pound loans to Greece. Large fractions of both loans simply went to settle prewar debts. Supposedly stepping in to fill the funding gap were the five West European banks that did indeed provide almost half of the credit available for 1924-29. But their initial disposition to invest in industry soon faded, despite its rapid growth from a small base. The postwar economy was left with abundant short-term commercial credit but not the long-term funding to which a fixed, overvalued exchange rate was supposed to draw European investors (Vachkov and Ivanov, 2009, pp.9-41 and 60-80).

Romania's economy entered the postwar years with much better prospects to attract foreign investment in return for a currency fixed under the new gold reserve standard as advocated by the Bank of England in particular. But it was almost the last state in Southeastern Europe to adopt the new standard and did so only under sponsorship from the Bank of France in 1927, a year before Greece as noted above. By then, the resistance to paying war debts to the Western allies had combined with the aforementioned reaction to the region's largest postwar inflation exerted enough downward pressure on the leu to keep the constant per capita value of note emissions from the Bank of Romania at barely half their 1911 or 1920 levels. Here was the same sort of deflationary pressure that the gold reserve standard itself was supposed to provide.

Meanwhile, mining (oil and coal extraction) and attendant metallurgy doubled their production in the 1920s, after recovering from wartime losses to take advantage of the mineral resources in newly acquired Transylvania. But the attraction to direct foreign investment suffered not only from the uncertainty about debt repayment and currency rates but also the one major nationalization undertaken across the region in the wake of the First World War. The defeat of Germany and Austria-Hungary left their oil enterprise, equal in size and capital to the West European and US competitors that had flocked in since the 1890s, open to expropriation. Steua Română now became a state enterprise, although by the early 1920s it was already obliged to seek new investment funds in the Paris and London capital markets. Then in 1924, the National Liberal government used its predominant position, secured by the disappearance of its prewar Conservative rivals after their siding with the Central powers, to pass a new Mining Law. For oil and also coal extraction, it required 55 percent Romanian ownership and management of all foreign enterprises for mineral extraction from state land, plus two thirds of the Board of Directors. Royal Dutch Shell and the other large West European companies reluctantly complied. Only the American Rockefeller interests refused. But the US State Department then refused their request that Romania be given a significant concession on the repayment of war debts in

return for an exemption to the Mining Law. The Rockefeller access to operations in Romania were thereby reduced, and the attraction of new investment from the other Western oil companies also declined (Pearson, 1970, pp.10-50). The new National Peasant Party government elected in 1928 was determined to relax these restrictions on direct foreign investment, but its measures had little effect once the Great Depression descended from 1929 forward.

Attention should also be paid to the wartime and immediate postwar background to the Romanian failure to take greater economic advantage of its larger territory and resources. The momentum for the postwar inflation began during the last year of the First World War when the German occupation of Bucharest allowed a German-backed bank there to begin issuing lei at the same time that the long established National Bank was issuing notes from its location in Iași. The German authorities soon broke their promise to issue notes only for military purposes, so that the combined value of lei in circulation rose by one half in the course of 1918. Then came the postwar acquisition of Transylvania and the Banat, and with them the large amount of Austro-Hungarian crowns still left their in circulation and in bank deposits. Realizing the further inflationary potential of their conversion to lei, the leadership of the National Bank argued for a high rate of conversion, at 5/1 or more. But the several Liberal banks in Bucharest demanded a lower rate so as to facilitate their interest in attracting crown deposits. This tactic also favored the consolidation of Liberal political leverage in Transylvania over its large and reluctant Hungarian minority. It won the day, and the stamping of some Austro-Hungarian crowns begun in 1919 was followed in 1920 by their full conversion to lei at a rate of 2/1. The conversions accounted for a large part of the now doubled note issue and the accelerating inflation. Too slow to carry out their wartime promise for land reform, the now National Liberals were briefly forced from power in 1921. A non-party regime under General Averescu launched the land reform and its redistribution of land from large estates, also demobilizing some 200,000 army troops to aid in rebuilding damaged infrastructure. To cover some of the cost and also to replace inflation with deflation, his Finance Minister instituted a progressive income tax and a tax on war profits. But bank interests close to the National Liberals refused to provide the credits needed to proceed ahead until tax revenues accumulated (Durandin, 1985, pp.45-68). By 1922, the National Liberals had returned to power, finally going ahead with land reform but also maintaining the large army whose support strained the beleaguered state budgets. The National Bank continued to increase note issue, mainly to support expanded credit through its new branches in Transylvania and the Banat, in competition with a set of Liberal bank branches. It was left to the National Liberals to change course and introduce the most sharply deflationary measures

in the region. In late 1924, its Finance Minister, the powerful brother of the Prime Minister, Ionel Brătianu, placed statutory limit of note issue from the National Bank, tying its total to 25 percent of gold reserves. The two brothers wished to resist any supervision from the League's Financial Committee, let alone allow the British influence of Norman and Strakosch. Romania would thus proceed on its own (*prin noi înșine*) to pursue a convertible currency just as its industrial policy sought to rely on domestic management. Hence the huge reduction in note issue noted above and a sharp restriction in credit available only at 20 percent rates of interest. Still, only with sales of foreign exchange and further deflationary pressures could the leu be sufficiently stabilized in 1927 and proceed ahead under the gold reserve standard (Kirițescu, 1967, pp.145-190).

It is ironic that the Romanian adoption of yet another overvalued rate of exchange, albeit the lowest one in the region at 3.1 percent of the parity with the French gold franc, could find sponsorship, as noted above, only from a country whose own currency was significantly undervalued. France had struggled itself from 1919 forward with its war debts to the US and also Britain, hoping to cover them with German reparations. But when the ill-advised French occupation of the Ruhr in 1923 failed to yield the expected compensation, its government was forced to accept the Dawes Plan for reduced and much prolonged reparation payments from Germany and also Hungary and Bulgaria. A bookkeeping scandal in the Bank of France in 1925 over note issue beyond the statutory limit of 1919 accelerated the depreciation of the Franc and brought back Raymond Poincaré to form a new government in 1926. His new governor of the Bank of France, Émile Morneau, took advantage of political stability, rising exports and Pound reserves to stabilize the rising exchange rate for the franc under the gold reserve standard before it stopped rising. The franc would therefore remain undervalued for the rest of the 1920s before suffering in the 1930s for not leaving the gold reserve standard and what had become a relatively overvalued rate. Morneau was anxious to deny Norman further influence and assert French authority in Eastern Europe beyond the several banks who had rushed in to replace German and Austrian investors where they could. Advisors from the Bank of France were also more welcome in Bucharest than any from the Bank of England or the League's Financial Committee. But the French promise of a stabilization loan that would compensate for overvaluation could not be provided until 1929, when the Depression impended (Ahamed, 2009, pp.141-169).

The Kingdom of Serbs, Croats and Slovenes had already stabilized the dinar under a fixed if also overvalued rate in 1925. It did so under British encouragement but without formal adherence to the gold reserve standard or a stabilization loan

until accepting the standard in 1931, just as Britain left gold. This step was the famous initiative of Milan Stojadinovic, later a Prime Minister (1935-38) favoring state-led industrial policy but from 1923 a Finance Minister following Norman's financial orthodoxy. First trained in Germany, he had established postwar connections with economists in London. Stabilization at the region's highest fraction of prewar parity, 8.9 percent, reflected the earlier success by the central bank, now renamed the National Bank of Yugoslavia (NBY) , in restraining postwar inflation and falling exchange rates for the currency more rapidly than its counterparts around the region. But to push the Geneva exchange rate for the dinar up enough to fix its value, Stojadinovic forced a one third reduction in note issue on the NBY from 1924 to 1926. A new land tax was to help close the state's budget deficit while the stable dinar was to attract foreign loans and investment. The loans never came, and the bad harvest of 1926 reduced revenues from the new tax. Left with the deflation needed to maintain another of the region's overvalued exchange rates, the latest in the series of Serbian-led coalition governments passed protective tariffs in 1927 for agriculture as well as industry. Based in Belgrade and assuming its wider role for the prewar National Bank of Serbia, the bank's role in replacing inflation with deflation were seen as continuing a pattern perceived as conscious discrimination against non-Serb-areas. In Croatia in particular, this was a pattern believed to begin immediately after the war with the creation of the bank and its sole right of note issue.

The First World War had aggravated the financial problems of connecting Serbia with territories under Austrian, Hungarian, or Austro-Hungarian administrations before 1914 and before 1912 under Ottoman rule. The Austrian and Bulgarian occupation of Serbia, Macedonia and Kosovo from 1915 to 1918 had introduced their currencies but no capital investment. Meanwhile, the western Habsburg lands had remained disconnected from each other and under Austrian or Hungarian administrations that could not coordinate a united war effort. The major grain-growing areas in Slavonia and Vojvodina sent their produce to Budapest while starvation threatened Vienna by 1917-18 and continued to do so into 1919 in the absence of an agreed alternative to Hungarian crowns. The Austrian occupation in Belgrade made no effort to construct the railway to Hungarian controlled Zagreb that would have served the Yugoslav Kingdom so well after the war. By 1919, six different currencies were circulating, only the dinar having been issued within the new Kingdom's borders. And it took most of the year before agreement could be reached on a single new bank of issue.

The major problem facing the new National Bank of Yugoslavia (NBY) was the presence of Austrian or Hungarian crowns issued under their single state

that no longer existed. Here was the same postwar challenge that the National Bank of Romania had faced in Transylvania and the Banat. Its answer, as noted above, was a favorable 2/1 rate of exchange that would keep deposits in banks opened or taken over by interests of the ruling Liberal Party. There was no such option for the Serbian Radical Party dominating the new Belgrade ministries but not the parliament or the large surviving banks in Croatia or Slovenia. Their supporters pushed for crown conversion at 10/1, while 1/1 or at most 2/1 was the response from Zagreb or Ljubljana. The NBY choice of 5/1, later trimmed to 4/1 in 1920 thus represented the sort of compromise that would prove illusive in the subsequent economic history of the interwar Kingdom. Still, this rate of exchange was roughly the same as the open market rate being offered for crowns exchanged for francs in Vienna. This is a story long familiar from publication based on the author's initial research in the archives of the Bank of Yugoslavia (Djordjević, 1980, pp 139-156).⁷

New research from Serbia has now added to our understanding of the trials during the initial postwar period, trials in which the presumed Serbian hegemony faced a set of disconnected territories in which Belgrade's authority was either challenged or ignored. The familiar struggles of the new NBY to assemble capital from more than Serbian sources is only one example. Three sales of bank shares into 1921 were needed to raise the desired capital of 40 million dinars. The increasingly favorable terms for delayed payment, finally in bank notes, attracted only one quarter of its final total from outside of Serbia. The large Zagreb banks were conspicuously absent, understandably so given interest rates for credit of 13-21 percent, versus the modest 8 percent available from the NBY. From this small non-Serbian share in the NBY's founding capital would follow, not surprisingly, followed discount credits in Serbia that were twice those in Croatia and four times those in Slovenia. This imbalance posed no difficulties for the western lands in the 1920s. Their banks built on the attraction of deposits and capital from the disconnected financial sectors of Vienna and Budapest in the immediate postwar period and then prospered with support for enterprises with easier access than Serbia's to export markets, in distance and available transport. While the new central bank in Belgrade was failing to ground itself more broadly, the new central government also found that its fiscal reach fell far short of the hegemonic control for which it would later be blamed, especially in the 1930s. Ivan Besić begins his survey of postwar financial policy by reviewing the first state budgets, none of which the Finance Ministry was unable to pass as presented to the

⁷ Useful detail may be found in the bank's own published history, *Narodna Banka* (1934), pp. 92-118.

Serbian-dominated parliament until 1923. Temporary decrees were needed for 1919-22. Enough lower level financial and trade officials from the prewar period remained in place in the western lands to keep the Serbian-controlled Belgrade ministries from collecting uniform taxes or preventing trade blockades between Croatia and Slovenia for instance. Meanwhile in Belgrade, the Finance Ministry was unable to prevent a combination of royal and army influence from arranging unsecured foreign loans, primarily to support new military spending (Besić, 2003, pp. 39-107). Its use to consolidate central control in Kosovo and Macedonia contrasts with the weak state framework and the limited economic coordination that connected rest of the new Kingdom of Serbs, Croats and Slovenes by 1923.

These disconnecting postwar consequences formed the background for the hard deflationary measures undertaken by Stojadinović's Finance Ministry from 1923 to 1925. Externally, they were successful. By 1925, the restriction of note issue had advanced the dinar's exchange rate by 50 percent and reduced its destabilizing fluctuations in the process. A legal statute of 1926 then set a fixed rate based on the Geneva exchange for gold reserve currencies. The recent review of interwar currency and foreign exchange policy by Nikolić (2001, pp.219-221) emphasizes the positive side of this belated centralization. The dinar remained stable through rest of the 1920s and its high exchange rate did attract more foreign capital if not foreign loans. But the resulting restriction of credit and upward pressure on interest rates and export prices did more than push the Belgrade government toward the aforementioned protective tariffs of 1927. It opened the country's financial center that had grown up in Zagreb around its private banks to the danger of an overvalued exchange rate if a downturn in the international economy reduced trade and capital flows. As detailed in a recent Croatian study, this is exactly what happened in the Great Depression, although without the political bias in Belgrade assumed by earlier scholarship from Croatia (Bićanić and Ivanović, 2004, pp.64-83). Already in 1928, pressure especially from Croatian industry proposed a reduction in the dinar's exchange rate, but it was unsuccessful. The full impact of Depression in the 1930s left Zagreb banks at the mercy of runs on deposits and the inability of borrowers to repay. The leverage of the NBY, neglected outside of Serbia in the 1920s, now shifted the financial center of Yugoslavia from Zagreb to Belgrade. But the shift was largely the result of the unbroken emphasis on monetary stability that had been the principal economic consequence of the First World War for all of Southeastern Europe.

3. CONCLUSIONS

What lessons may then be drawn from the limited economic causes and widespread economic consequences of the First World War for this region known as Southeastern Europe only from the war's end? Of course the first lesson from both 1914 and 1918 is to avoid the temptation to draw historical parallels too easily tied to current events and then read backward. A French philosopher once called such temptations "the illusions of retrospective determinism". Setting aside the political and 9/11 terrorist parallels tempting some recent scholarship on the Sarajevo assassination in 1914, the economic causes of the First World War still seem limited. Worth noting however are the prewar German buildup of the army ordinance needed to invade France and the Austrian turn to military action against Serbia in the absence of financial or commercial leverage. The comparable economic lessons for the wars of Yugoslavia's dissolution would be the large arms production for a large army that created the capacity for full-scale war combined with a failing national economy whose disconnections invited regional rivalry. Otherwise appropriate plans for economic reconnection, under the financial leadership of the NBY, foundered when left to the mixture of Communist and Serbian nationalist imperatives of the Milošević regime. The Communist leadership of Croatia and Slovenia led the rejection, and the League of Yugoslav Communists soon ceased to exist.

While the economic consequences of the First World War suggest only contrasts to the end of the Second World War, the quarter century that has now passed since the end of the Cold War invite considerable comparison. In 1945, the old political order that had continued in 1918, albeit within new borders for Southeastern Europe, was gone. On the Western side, the American economic predominance was even greater than in 1918 and its leaders were now determined, even before the start of the Cold War not repeat the earlier postwar retreat from European recovery. This was the major lesson of post-1918 period, as frequently stated by US authorities. UN membership was accepted, not rejected as with the League of Nations, and most of the aforementioned UNRRA aid came from the United States. Nor was the Soviet side, although weakened by its war effort, ready to retreat from Eastern Europe. The need for rapid reconstruction justified the demands of its allied or subordinate Communist parties for exclusive political control. Then Cold War competition between the two sides led to direct American aid to Greek agriculture and Yugoslav infrastructure that advanced their economic development. Soviet support in Bulgaria, Romania and now Albania pushed heavy industry ahead and opened the large Russian market to Bulgarian agriculture and light industry. The financial imperatives of the post-

1918 years were secondary at best, and there was no interest in restoring the interwar monetary order or the gold reserve standard that it had discarded in the 1930s.

The end of the Cold War left only the Western side standing. The initial economic failings of the successor regimes in the now independent Yugoslav republics as well as in Bulgaria, Romania and Albania brought back the Western emphasis on financial stability as the first step to postwar recovery. Weak or politically dependent central banks could not prevent pyramid schemes and catastrophic inflations in Bulgaria and Albania as well as Serbia. Crony capitalism that left large enterprises, even if formally privatized, in the hands of political insiders, cut short what appeared to be promising increases in Croatia and Romania in Gross Domestic Product (GDP). Western aid, primarily from the European Union, and rising EU trade helped to reduce balance of payments deficits, uniformly exceeding the limited totals for foreign direct investment (Lampe, 2006, p. 291). Here was evidence to support the so-called Washington Consensus established in the World Bank and the International Monetary Fund (IMF) from their experience with inflationary Latin American economies in the 1980s. Then with the end of the wars of Yugoslavia's dissolution in 1999, the EU and the World Bank jointly agreed on further aid to what was now called the Western Balkans, the Yugoslav successor states minus Slovenia plus Albania. Dubbed the Stability Pact, its major aim was to create the financial stability that would open the way not just to competitive privatization, increased trade and direct foreign investment but most importantly the path to EU membership that had been previously opened only to Slovenia.

Regional attraction to this open door combined with an upsurge in direct foreign investment to increase growth rates in the Western Balkans and bring Slovenia, Bulgaria and Romania into the EU before the international financial crisis of 2008 set them all back. It is this most recent postwar period that raises the major issues for useful comparison to the post-1918 period. Let me draw on my own recent scholarship, which has been primarily concerned with these past 15 years, to put forward a number of positive differences, suggesting lessons learned, and several unfortunate similarities, suggesting lessons yet to be learned (Cohen and Lampe, 2011, pp. 386-447 and 462-73; Lampe, 2014, pp. 270-308). Obviously, the existence of three new international institutions, the EU, the World Bank and the IMF, were major differences and I think advantages, especially when they soon stepped away from deflationary austerity and supported what its representatives called the Post-Washington Consensus. The EU provided the most financial assistance, rising to 5 billion Euros for 2000-2006

and 10 billion for 2007-13. World Bank and IMF lending promoted the fiscal reforms and restraints in state spending that limited budget deficits with some reduction in public employment before the financial crisis and helped to survive reduced revenues since then. No crash programs like Stojadinović's to restrict Yugoslav note issue in the 1920s were undertaken. Instead, the region's various central banks used the independence that Norman had promoted in the 1920s to assemble professional staffs, advise their Finance Ministries and maintain stable exchange rates. Their rising reputations in the international financial community served their economies well, especially after the financial crisis. And all sides were assisted by the determination to proceed ahead with free trade and access to EU and regional markets, consciously avoiding the turn to protective tariffs that been so common in the 1920s. Instead, the magnetic attraction of European integration as the only alternative to the divisions of the 1930s has survived even under its recent trials.

Against these positive features and lessons learned, we must acknowledge a mixed record for the foreign banks that became even more prominent in the region than in the 1920s. More troubling has been the export burden from exchange rates stabilized around an overvalued Euro, and the failure of Greece, an EU member since 1981, to avoid the worst debt crisis faced by any European economy in 2008. The largely West European and Greek banks that provided much of the credit for the 2002-7 boom stepped into former Communist economies where banks had functioned only as secondary agents for distributing state funds for investment. The arriving foreign banks thus provided services closed off to domestic banks before 1989. At least they did not collapse or leave as their counterparts did after 1929, but high interest rates and newly restrictive terms have kept the credit supply reduced since 2008. The attraction of earning profits in currencies at rates of exchange matching an increasingly overvalued Euro has not served to keep large inflows of foreign direct investment in place any more than it did for the more limited foreign funds of the late 1920s. In the meantime, the region's trade deficits have risen with the effect of the general European slowdown on overpriced exports. With FDI reduced as well, regional governments have been pushed back into more borrowing. Croatia's foreign debt recently surpassed GDP, matching the Yugoslavia's troubled level in the early 1980s.

But the region's major debtor remains Greece. Here we should resist the temptation to blame the large Greek banks, with a couple of exceptions. The major source of the Greek problem has ironically been a state sector and employment expanded significantly in the 1980s and supported by informally forced loans from the large banks since then. Making matters worse were the missing standards for

accurately reporting national accounts, otherwise well observed in the region under EU and central bank observance. Still, as Greek reforms now proceed ahead under the hardest austerity imposed on any of the region's populations, we may hope that the various postwar lessons learned in the rest of the region will allow it to contribute to representing what is now the southern European side in working with the German-led northern side and finding a way forward to a banking union and a common fiscal framework. Relying solely on a financial framework based on a stable exchange rate holds no more promise than it did after the First World War.

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