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Ludwig von Mises, *“Finance and Banking in the Austrian Empire and the Republic of Austria”* [1921]



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The 11th edition of the *Encyclopedia Britannica* was the last edition which appeared before the First World War destroyed the old liberal order in Europe. The next edition, the 12th, reproduced the 11th edition with the addition of 4 supplementary volumes which covered the war and its immediate aftermath. This article is part of the supplementary volumes.

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Austrian Empire [Excerpt From Volume XXX, Pp. 323–324.]

Finance and Banking.—The third licence granted to the Austro-Hungarian Bank expired on Dec. 31 1910. It was at first extended provisionally, as it was impossible to reach a settlement between Austria and Hungary regarding the continuance of common currency and banking arrangements. In Hungary a strong majority, which the Government could not afford to ignore, insisted on the formation of an independent Hungarian bank; on the other hand the advantages accruing to Hungary through the community of the financial and banking organization were quite obvious. There was an important divergence of opinion between Austria and Hungary concerning the constitution of the bank. Since the closing years of the 19th century the Austro-Hungarian Bank had pursued a policy which had in the main the object of making the Austrian *krona* a gold exchange standard. It was decided, however, by the Austrian financial authorities that the obligation of the Austro-Hungarian Bank to convert its notes into gold on demand should remain suspended as hitherto, owing to fear lest the renewal of the obligation of the bank to cash its notes in gold should lead to a rise in the rate of interest. Hungary, on the other hand, striving for access to the money markets of the West, desired that the obligation of the Austro-Hungarian Bank to cash its notes should be explicitly mentioned in the law, in order to make the public loans rank as easily negotiable securities on foreign *bourses*. In the banking law of Aug. 8 1911 a compromise was formed on the following lines. The suspension of cash payment by the Austro-Hungarian Bank was continued, but the bank was bound to provide, by every means at its disposal, that the value of its notes as quoted on foreign *bourses* should be permanently secured in proportion to the parity of the legal mint standard of the *krona* currency. Hungary's wishes were met by the introduction of a specially prompt procedure for the eventual future abolition of the suspension of the bank's obligation to cash its notes. By the same law, besides other less important provisions, the amount of the bank's tax-free issue of notes was raised from 400 to 600 millions of *kronen*, and the conditions formerly attached to the issue of 10 and 20 *kronen* notes were sensibly relaxed.

A 4% bank-rate had been uninterruptedly in force from May 8 1908 to Oct. 23 1901. From Oct. 24 1901 to Feb. 3 1911 it was 5%; on Feb. 4 1911 it was reduced to 4½%, and on Feb. 23 1911 further to 4%. From Sept. 22 1911 to Oct. 25 1912 the bank-rate was again 5%; on Oct. 25 1912 it was increased to 5½%; and on Nov. 16 1912 a rate of 6% came into force and so remained until Nov. 27 1913, when it was lowered to 5½%, falling on Jan. 20 1914 to 5%, on Feb. 3 1914 to 4½%, and finally on March 12 1914 to 4%.

These changes in the bank-rate show that Austria passed through a financial crisis and credit difficulties in 1912–3, from the consequences of which she had only just recovered at the outbreak of the war. The stringency of the money market and the crisis had their commencement as early as the spring of 1912. The Balkan War, which broke out in the autumn of 1912, did not occasion the crisis, but it made it more acute. The number of trade insolvencies in Austria-Hungary had reached its height in 1912. The Vienna Creditors' Association for the protection of claims in bankruptcies had in 1909–11 fresh failures with liabilities of 45, 40 and 43 millions of *kronen* respectively. In 1912 the value of fresh claims involved rose to 112 millions of *kronen*; in 1913 it still amounted to 73 millions. One obvious sign of a crisis was the demand for loans against security from the Austro-Hungarian Bank, which was the result of the unfavourable position of investments on the *bourse*. In each of the five years, ending Dec. 31, from 1909 to 1913 the loans granted by the Austro-Hungarian Bank against securities amounted to 90, 149, 187, 355 and 311 millions of *kronen* successively. The bank-note circulation rose in proportion. Notwithstanding the fact that the banking law raised the tax-free note issue in 1911 from 400 to 600 millions of *kronen*, in 1913 the bank was unable to avoid incurring tax payments for notes issued in excess of the amount allowed free of tax, a state of affairs which had no parallel in the bank's history. From Aug. 23 1912 to Jan. 23 1914 the bank return showed no tax-free reserve of notes.

On July 23 1914 the gold reserve of the Austro-Hungarian Bank amounted to 1,238 millions of *kronen*, its silver to 291 millions. In its portfolio, were discounted bills to the amount of 768 millions of *kronen*. It had loans on security outstanding to the amount of 186 millions, and the bank-notes in circulation amounted to 2,130 millions of *kronen*.

The outbreak of the World War compelled the bank to raise its rate on July 27 1914 from 4 to 5%, on July 31 to 6% and on Aug. 2 to 8%. The public rushed to the bank to obtain advances by pledging securities. On Aug. 4 1914 the Bank Act was suspended by imperial ordinance having the force of law. In this manner the bank was converted into an institution which could supply the Government, by fresh issues of notes, with loans to an unlimited extent. The legal forms under which this source of credit was assured were various, but the actual result was in every case the same. The bank-rate was reduced to 6% as early as Aug. 20 1914; and the granting of credit on depositing securities was facilitated by extending the limits of the securities accepted.

The note issue was as follows:—

Dec. 31 1914 5,137 millions of *kronen*

“ 1915 7,162 ”

“ 1916 10,889 ”

“ 1917 18,440 ”

“ 1918 35,589 ”

In proportion to the increase of the notes in circulation prices and wages rose, and the *krona* depreciated on the foreign exchanges. The Government tried to oppose the rise in prices by penal measures, and in public attributed the rise of foreign rates to

speculation. A Central Securities Board (*Devisenzentrale*) was set up on Feb. 24 1916; and regulations were issued on Dec. 19 1916 and June 18 1918, attaching a series of conditions to dealings in foreign money, bills and securities, which amounted actually to a monopolizing of all such operations by the *Devisenzentrale*. These measures had no success. The value of the American dollar, in terms of Austro-Hungarian paper *kronen* with legally fixed value, varied in fact, as shown by the Swiss exchange market, as follows:—

End of Aug.	1914	5.12
End of Dec.	1914	5.76
" "	1915	7.85
" "	1916	9.56
" "	1917	8.40
" Oct.	1918	11.83
" Dec.	1918	15.77

State Finances.—The revenue from taxation rose, year by year, partly owing to the increased profits of industry, partly to fresh increases in taxation. From the year 1902 to the financial year 1914–5 the State revenues doubled, rising from 1,730 millions of *kronen* to 3,460 millions of *kronen*, but this increase in revenue could only be achieved by placing an extraordinary strain on the taxable capacity of the country. In the financial year 1913 the amount of estimated expenditure rose to 3,461 millions of *kronen*. Of the estimated net revenue of 2,102 millions of *kronen*, 432 millions (20.5%) came under the head of receipts from direct taxation, 905 millions (43%) under the head of receipts from indirect taxation and taxes on commerce, while 294 millions (14%) were the proceeds of State property and State institutions. Of the direct taxes the land tax produced 52 millions, the house taxes 127 millions, the taxes on industry 127 millions and the income tax 102 millions. Of the taxes on consumption the spirit tax produced 95 millions, the beer duty 85 millions, and the sugar duty 76 millions. The State debt amounted to 11,340 millions of *kronen*. On the outbreak of the war it was at first impossible to contemplate meeting the cost of the war by raising existing taxes or by imposing fresh taxation. The costs of the war were in the first place met by loans and the assistance of the note-printing press. The means of carrying on the war were obtained by the State becoming the debtor of the Austro-Hungarian Bank, in so far as credit was concerned.

The debt of the Austrian State to the Austro-Hungarian Bank in direct loans made by the bank to the State amounted at the end of 1919 to 25,088 millions of *kronen*. But, besides this, the bank had also afforded credits to the State in other forms. In return for bonds given by the Austrian and Hungarian State they issued Treasury bills, and transferred the proceeds from them to the two finance departments. The total amount of such Treasury bills in circulation at the end of 1918 was roughly 7,400 millions of *kronen*.

The Post Office Savings Bank was also made to serve the financial needs of the State. Whenever a war loan was impending it accepted advances from the members of the Banking Consortium, which had to place the war loans, and as soon as the

subscription was closed they were compensated for the underwriting. At the end of June 1919 these advances still amounted to 2,605 millions of *kronen*.

Foreign credit also was laid under contribution by the Austrian State. On Oct. 31 1918 the amounts of outstanding debts incurred abroad during the war were as follows:—

2,696 millions of German Reichsmarks

42.9 " Dutch florins

20.6 " Danish kroner

7.9 " Swedish kroner

3.6 " Bulgarian levas.

The home money market was approached by the Government through the issue of war loans. The total number of such war loans was eight. They bore interest at 5½%. The first issue took place on Nov. 1 1914, and from that time onwards a fresh war loan was issued about every six months. In this way a State debt of 35,069 millions of *kronen* was accumulated.

Up to Sept. 1915 no increases in taxation were introduced in Austria, except a slight, increase in the duty on beer; neither were any new taxes created. Even the reform of taxation carried out in the autumn of 1915 (modification of the inheritance and donations duty and the taxation on insurance policies and legal charges) cannot be regarded strictly as war taxes, as they had been planned a considerable time before the outbreak of the war and had only been delayed by the inability of Parliament to continue its work. It was not until 1916 that increases took place in every field of taxation. The price of tobacco and the tariff of the State railways were considerably increased, special, war increases were introduced in the direct taxes, and in April 1916 an entirely new tax was imposed—the “war profits tax,” the name of which was subsequently altered to “war tax.” But all these taxes and increases of taxation were quite inadequate to meet the enormous expense of conducting the war. War finance was not able to dispense with the printing of notes.

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Republic Of Austria [Excerpt From Volume XXX, Pp. 348–349.]

Finance and Banking.—When in the last days of Oct. 1918 the various parts of the Austro-Hungarian monarchy constituted themselves on one side independent states (the Austrian Republic, the Czechoslovakian Republic, Hungary, and the republic of West-Ukraine), and for the other part decided on joining already established nations (Italy, Rumania, Yugoslavia); or joined territories detached from other states. and forming new states (Poland), there existed in all these territories one uniform paper currency in circulation, *i.e.* the notes of the Austro-Hungarian Bank, enjoying a fixed rate. It was clear that such conditions could not be maintained for any length of time, and that, in view of the connexion between paper money of fixed rate and State finance, it was impossible to continue this unity of currency. All the states concerned, which succeeded the Austro-Hungarian Monarchy, were in such financial straits that they considered the continued recourse to the issue of notes a necessity. The note-printing press, however, was in Vienna, and the Austro-Hungarian Bank was actually under the deciding influence of the new German-Austrian Government. It was urgently necessary for the new states to obtain an independent currency, *i.e.* to make themselves independent, so far as the printing of notes was concerned, of the Vienna note-printing press. This was comparatively easy for those who had joined already existing states, but more difficult for the newly formed states which were obliged in the first instance to create a new currency. In these conditions the money problem, at the moment of the dissolution of the Austro-Hungarian Monarchy, was merely a technical problem of printing, and the question how to obtain printing-plates, banknote-paper and printing-ink appeared for the moment the most important points of currency policy. After the Italian Government as early, as Nov. 1918 and the Rumanian Government in Feb. 1919 had made the necessary preparations to substitute respectively the *lira* and the *lei* for the Austro-Hungarian "*krona*," in the territories occupied by them, the Government of the Serbo-Croatian-Slovenian State proceeded in Jan. 1919 to mark the Austro-Hungarian notes circulating within their territory by stamping them. On Feb. 25 1919 the Czechoslovakian Government followed suit by stamping the *kronen* notes circulating in their country. Then the Austrian Government could not remain idle. It could not wait until all the other states had passed from the Austro-Hungarian *krona* to a national *krona*. It had to get rid of the Austro-Hungarian *krona*, in order to avoid the danger of such notes as for one reason or another had not been stamped by the other states returning to German Austria and there increasing the inflation. The *kronen* notes circulating in German-Austria were therefore also specially marked, and, by a regulation of March 25 1919 having the force of law, it was decreed that all notes not so marked would not be legal tender within the German-Austrian State.

A decree of Feb. 27 1919 had ordered the stamping over of all notes of the Austro-Hungarian Bank circulating within the territory of the German-Austrian Republic, with the exception of the notes for one and two *kronen* (which also subsequently were ordered to be stamped). With the execution of this regulation the German-Austrian

currency was separated from that of the other “succession states,” and there was only one special *kronen* note, which was stamped as recognized legal tender for Austria.

The German-Austrian Republic also used the note-printing press as its chief expedient for covering the national expenses. At the time of the carrying-out of the stamping process, at the end of June 1919, the stamped German-Austrian notes in circulation amounted to 7.6 milliards of *kronen*; at the end of 1920 the circulation had risen to 30 milliards. In consequence there was a further depreciation in the exchange. On Dec. 31 1920 the dollar was quoted in Vienna at 668 *kronen*, as compared to 5 *kronen* in pre-war times.

The republic of Austria at first not only maintained the system of restricting exchange operations, introduced under the Empire during the war, but even made it more severe. Only in the summer of 1920 was any relaxation permitted, in so far as the forced release of foreign currencies obtained for goods exported was generally cancelled. In Nov. 1920 further modifications were made, so that by the end of 1920 the only restriction of money transactions with foreign countries remaining in force was the prohibition to import or export *kronen* notes. The regular exchange operations on the Vienna Bourse were however, not revived. They were replaced by a system of restricted exchange business under the special supervision of the still existing *Devisenzentrale*.

The general political conditions and the depreciation of money had led to such an *impasse* that up to 1921 the whole financial system of the republic was in a state of uncertainty. On the one hand, the Austrian State, by the peace treaty of St. Germain, was made liable toward foreign countries for an amount not specifically determined. On the other, it was found necessary for political reasons to introduce a system of providing the population with cheap victuals. As these had to be obtained almost exclusively against payment in foreign currency abroad, and it was desired to sell at home at the lowest possible prices, there resulted a considerable discrepancy between the expenses necessitated by this part of the State budget and the income derived. At the beginning of 1921 the deficit of the Austrian budget was estimated at hardly less than 50 milliards of *kronen* per annum. To cover this deficit the Austrian State, with the help of the Allied Powers, contracted loans abroad, and for the rest relied on the note-printing press. Only a small part of the expenses of the State could be covered by taxation, notwithstanding that all direct taxes were greatly increased and a new direct tax, an extraordinary property tax, was specially introduced in 1920. Of this property tax, the fixing of which required enormous preparation, it was permitted to make prepayments in Feb. 1920 under specially favourable conditions. Such prepayments brought in over 7 milliards of *kronen*, but more than half of these prepayments were made in war loan. The situation of the Austrian State budget was therefore in 1921 a most unfavourable one. An improvement could only be expected on the one hand by doing away with the system, which could not be permanently maintained, of providing necessaries for the population below cost price at the expense of the State, and on the other by a radical reform of the many State and municipal enterprises (post, telegraph, telephone, State railways, salt mines, tobacco manufactories, town railways, illumination and power works).