

Roman Holec: The Great Depression of 1929 – 1933 from the point of view of Czechoslovak financial experts and economists

I.

According to Mitchell, the index of Czechoslovak gross national product in 1929 exceeded that of 1913 by 52 points. The index for the Czechoslovak manufacturing industry was higher than the average for 18 European countries; a more favourable index was achieved only by Greece, Finland, the Netherlands and Italy. The Czechoslovak index, perhaps a little overstated, reached 172 points (with 1913 equal to 100), whereas in Austria and Hungary it did not exceed 118 and 114 points respectively.

A chronic problem throughout of interwar years, which had negative national and political effects, was the economic and social heterogeneity of the Czechoslovak Republic. There were considerable differences in the economic structure of the Czech Lands and of Slovakia. Until 1938, Slovakia – and the extremely underdeveloped Carpathian Ruthenia – was little more than an agrarian appendage of the Czech Lands, supplying it with raw materials. **Map**

The crisis hit the industrialized and export oriented Czech Lands harder than agrarian Slovakia, where, in addition, agriculture was oriented towards consumption in kind. On the other hand, in Slovakia the depression raged in a social environment where living standards had been far from satisfactory before 1929, so that even though the living standard of the Czech population, it proved much more burdensome.

The foothold gained in the West for the exports of manufactured products in the 1920's played a positive role during the world economic depression after 1929. Czechoslovakia then suffered her greatest losses in her traditional markets, partly because of the tremendous decline in the national income of the East Central European agricultural countries and partly because of the autarkic policies that reduced her commercial relations within this region to bilateral bargaining. Within three years, between 1929 and 1932, the value of Czechoslovak exports to East Central Europe declined by more than two thirds. But her trade with Western Europe remained at about half its predepression value and declined by less than one third with the rest of the world.

Czechoslovakia also had an export surplus with other European countries and a deficit in her trade with the rest of the world. But over the entire period there was an overall surplus in the merchandise balance of trade in all but three of the interwar years: 1919, 1932 and 1933. The

net outflow of capital was used in great part for industrial investment abroad to acquire new sources of income, as rising tariffs were reducing export trade.

The soundness of Czechoslovakia's balance of payments and of her economy depended to a great extent on a well-functioning world trade and payments network. The breakdown of this network in the 1930's severely damaged the country's ability to maintain a free economy with a minimum of restrictions. The volume of exports, which rose during the 1920's to reach its prewar level by 1929, fell drastically thereafter, and in 1933 was less than 40 % of the 1929 volume. Even after the rest of the economy had recovered from the depression by 1937, exports recovered scarcely two thirds of the 1929 level. This in turn had two implications: first, the ability to control imports was crucial in maintaining a balance of trade surplus; second, foreign demand played less important role in economic recovery in the period between 1934 and 1937 than during the preceding decade.

Chart. 1

After 1929 the graph shows a clear separation in the growth path of gross national product and development in these other sectors. While the volume of foreign trade and industrial output fell sharply, and investment activity exhibited typical features of an acceleration model, gross national product declined comparatively less.

In the early depression years, the government followed a deflationary monetary policy that aggravated the crises, but the emergency fiscal measures that had to be taken in response to the distressed conditions and political pressures were in contradiction to the deflationary monetary principles and brought some relief. Among such factors was the persistent budget deficit. As the depression gained momentum, budget revenues fell more sharply than expenditures, because of the increase in transfer payments. Although employment outside of agriculture declined by about 25 percent at the lowest point of the depression in 1934, unemployment benefits increased more than 20 times by 1933. In addition, other benefits accrued to the unemployed, such as the free distribution of food, Christmas bonuses, and care of their children, all of which increased aggregate demand.

Other important countercyclical policy measures were taken in the field of agriculture. Under the pressure of falling agricultural prices and the rising burden of farm indebtedness, and in response to political pressures of the well-organised Agrarian-party, various measures were introduced to support agricultural prices, such as increased customs duties and import restrictions. With the continuing distress of the farm population, especially in grain farming, these piecemeal measures finally culminated in 1934 in the centralization of all purchasing and distribution of grain products within a state grain monopoly agency, which provided the

small farmers with a guaranteed sale of their harvest at relatively stable prices. These measures prevented the income of the sizable farm population from falling to a much lower level and, in addition, increased domestic aggregate demand for agricultural commodities by import substitution.

With the onset of the world depression, the Czechoslovak economy suffered a setback from which it had barely recovered by 1937. During this period economic policies were not directly aimed at internal economic expansion. Rather, goals were formulated in terms of the classical view: maintenance of stable exchange relations and an adjustment of domestic prices and wage levels to this effect. The deflationary policy pursued undoubtedly contributed to the severity and length of the depression in Czechoslovakia.

During the interwar period little was changed in great disparity of development between the western and the eastern parts of the country, which gave rise to considerable political dissatisfaction in the less-developed provinces. The major reasons were due in part to a lack of understanding of the nature of regional underdevelopment and in part to the pressure of other post-war issues, which focussed attention on international, rather than domestic, problems.

II.

The centre of gravity of the cycle 1929 – 1937 was not a boom but a crisis. Revival came slowly and a series of countries, including Czechoslovakia, did not succeed in surpassing the level of the macro-economic indicators from 1929.

The basic features of the crisis:

- Decline of gross domestic product, decline of industrial production and raw material industries;
- interweaving of the crisis in industry with an agrarian crisis;
- Collapse in international trade, growth of protectionism and economic nationalism;
- Currency crises, abolition of the convertibility of currencies into gold, the origin of currency blocs, clearing, competitive devaluation;
- The extraordinarily severe social impact of the crisis.

Economic theory and economic policy sought a remedy to the crisis in Keynesianism. Liberalism was replaced by a strengthening conviction of the inevitability of state intervention, which was further reinforced by the transition to a war economy. The idea of national economic planning was ever more attractive.

In Czechoslovakia the deepening crisis led to sharper disputes between the political parties, making it more difficult to maintain internal political equilibrium. The resignation of the minister of finance, technocrat and important economist Karel Engliš was a reflection of all this. Engliš did not succeed with his programme of state regulation of prices and imports or with intervention against cartels. In currency policy, he could not overcome the position of the Živnobanka, which did not want to give up the link of the crown to gold.

In 1932, the economic crisis grew into a political crisis. The new government meant a new wave of state interventionism. Apart from the Agrarians, it was supported by the Social Democrats with an emphasis on state investment, returning the unemployed to productive work, regulation of prices and intervention against cartels.

Theoretical groping and great differences in practical solutions appeared in the analysis of the crisis and the search for ways out of it. They were mostly ideologized and the republic did not find an adequate consensus.

III.

Next, we will look at the views of the individual parties, groups and individuals, starting with the above mentioned important national economist **Karel Engliš** (1880 – 1961).

As an adherent of equilibrium in the national economy, he thought that state intervention in the economy disturbed this equilibrium. Therefore, he opposed intervention. He saw the main problem of the crisis in incorrect monetary policy and in deflation. He saw two ways out of the crisis. The first meant compensating for deflation by reducing all the economic indicators, including wages, pay and especially interest rates. He demanded a reduction of prices in the interest of exports. However, he quickly understood that “deflation to the results”, while maintaining the gold standard, was not a possible way out of the crisis. Therefore, he chose a second route: to end deflation by devaluing the crown, but still retaining the gold standard. Devaluation came in the last stage of the crisis, when the Czechoslovak economy was in a deep depression. Therefore, it did not bring the expected boom. The orientation to France remained a problem. The French hesitated to devalue, leading to various exchange rate shifts for Czechoslovakia. Revival came only in 1936, and the pre-crisis value of the economy was not reached.

The **National Democrats (Right)** originally supported Engliš. They saw the causes of the crisis in structural changes caused by the First World War, and so in disequilibrium between development in different countries. They rejected state intervention and the creation of jobs at

the expense of a deficit. They rejected Engliš's theoretical concepts, but in practice they finally supported many of his steps.

The **Social Democrats** led by the economist Jozef Macek (1887 – 1972) saw the causes of the crisis in bad monetary and credit policies, derived from an incorrect understanding of money.

Macek did not recognize the linking of money to gold or to another precious metal.

He proposed departure from the gold standard. A low interest rate would facilitate private business and reduce the interest on the state debt. Cheap long term credits would stimulate enterprise. He also proposed an extensive programme of public works.

Macek saw the second cause of the crisis in the maintenance of a fixed value of the currency in relation to gold, which led to a protectionist customs policy, a selfish policy of cartels and monopolies, and a tendency towards autarchy. He proposed the removal of barriers to foreign trade.

The Social Democrats wanted to give workers a share in the profits of their companies and so increase their interest in success. The influence of Keynes and of the Swede Ohlin on their theory was obvious. The anti-crisis measures applied by the New Deal and in the Scandinavian countries were important models.

In the agrarian sphere they aimed to build up production and consumer cooperatives. Closeness to the agrarian programme was a pre-condition for the traditional red-green coalitions. They wanted to implement their demands in coalition with other political parties.

The **left wing of the Social Democrats** thought that capitalism was incompatible with democracy so they criticized the policy of the party leaders, who participated in government.

They supported state intervention, even state economic planning. In this area they approached the position of the Communists. Strengthening of enterprise autonomy as a basis for economic democracy was closely connected with this. They proposed socialization of some branches of industry.

The views of the **National Socialists** were connected with the ideas of syndicalism. The theory of managerism, which meant the joint direction of production by engineers and organizers of production, was closely connected with the question of the dispersal of the ownership of capital or "people's capitalism" by means of share ownership. The motive was supposed to be not the maximum profit, but the highest possible productivity of labour.

They saw the origin of the crisis in the results of the war and in the rationalization of production. In their view, the share of capital grew, but consumption was reduced. The National Socialists rejected liberalism and the function of the market. For the planned

management of the economy, they wanted to use monopolies, although they blamed them for the economic crisis.

The **Agrarians** went through two phases in their search for a way out of the crisis. The first, represented by the economist Vladimír Brdlík, was opposed to state intervention in the economy and the managed economy. Like Engliš, Brdlík supported a consistent deflationary policy. In agriculture, which they saw as the basis of the economy, the Agrarians criticized cheap competition from abroad. They strove to achieve the profitability of domestic agriculture, including protective tariffs, a grain monopoly and cheap credit. They saw prices as the key to all solutions.

In the second phase, associated with Rudolf Brož, the Agrarian approach came closer to the position of the Social Democrats. They saw the essence of the crisis in “gold deflation”. According to them, the currency problem was the cause of the crisis. However, they did not conceal that escaping from deflation, meant taking the path of inflation. They increasingly found a model in Germany and its currency policy. A further difference from the Social Democrats was the economic importance attributed to armaments. They increasingly supplemented state intervention in the economy with demands for a regime with a “firm hand”. The young Agrarian intellectuals supported state intervention in the economy, but otherwise identified with the conception of Prof. Brdlík.

The **Communists** saw the way out of the crisis in merciless social struggles leading to the dictatorship of the proletariat. The strike in Most was such an attempt. According to the Comintern it was the most important political action during the crisis in the whole of Europe. With the policy of a united front from above and from below, the Communist Party of Czechoslovakia began to deviate from the dogmatic views of Moscow, but the Comintern quickly put a stop to this. The dogmatic position of the Communists opened the space for the right in the republic.

IV.

We will look further into the Slovak situation, which could be a little different because of the specific economic features of Slovakia. The problem of Slovak development during the interwar period was therefore one of rising from a very low level in the face of acute competition from a much more developed region and in a period of generally slow overall economic growth.

The Slovak political parties did not have their own economic programmes. They looked at all problems from the national point of view and used existing problems as political instruments. Therefore, I will look at two leading economists.

Imrich Karvaš's (1903 – 1981) theoretical ideas developed under the influence of the teleological method of researching the national economy, worked out by Prof. K. Engliš. His academic profile is not reflected only in the further development and application of this method, but also in a wide range of new scientific findings, leading to deviation from the liberal understanding of economic processes and an inclination to a theoretical justification of the combination of macro- and micro-processes, as in the case of state measures to solve unemployment. He thought that the causes of the economic crisis included structural changes in the world economy, the social consequences of the process of rationalizing production, the agricultural crisis, and the resulting unemployment.

From this point of view, he became an important personality in the economic policy of regionalism. He formulated the need to achieve a rate of development in Slovakia that would enable it to overcome the economic difference between it and the Czech Lands.

He associated development of the national economy with cartelization, and support for cooperatives, which represented the penetration of elements of solidarity into the economic system based on individualism. He emphasized the role of the state and its economic policy, which had to defend the interests of the whole population. He published 13 books and 68 articles and tracts on the search for solutions to the current problems in national economic practice.

Ervin Hexner (1893 – 1968), a future functionary of the International Monetary Fund and World Bank, was the first Czechoslovak economic institutionalist, and from this position, he rejected neoclassical economics. In connection with the great economic crisis, he did not research its causes. He was concerned with the search for a way out of it: “It is said that the crisis can be cured in two ways: either by supporting private business, so that in the play of economic forces, it can more easily pass through the period of depression and reach the period of recovery; or by direct effort of the public administration to radically build up the state economy and gradually replace the private sector with the public hand.” Hexner did not incline to either of these possibilities. He studied both in their broad institutional framework and was always concerned with the conceptual system steps. He supported long-term prognoses and short-term decentralized planning. He rejected messianic faith in a planned economy, and so he did not regard state ownership of enterprises as the best solution.

V.

The inability of the politicians to create a unified economic policy programme for the country was obvious. Great differences of view were not overcome and as a result of political radicalization resulting from the errors of the reformist parties and dogmatism of the communists, society began to shift ever more to the right. Perhaps this was a general result of the crisis throughout Europe.

The economic problems of the 1930s led to much keener competition between various groups of capital and to an escalation of social conflicts, which were very often intensified by nationalistic ideas. Decentralizing tendencies, externally encouraged, were growing. The adverse economic development thus contributed to the destabilization of the Czechoslovak republic at a time, when the republic was facing a grave external threat.