
EUROPE: THE WORLD'S BANKER
1870-1914

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THE WORLD'S BANKER
1870-1914

AN ACCOUNT OF
EUROPEAN FOREIGN INVESTMENT
AND THE CONNECTION OF
WORLD FINANCE WITH DIPLOMACY
BEFORE THE WAR

BY
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With an Introduction by
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TO
EDWIN F. GAY
TEACHER AND FRIEND

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INTRODUCTION

THIS important contribution to economic history traces the outward flow of European surplus capital from 1870 until the war of 1914-18 caused waste and destruction again to usurp the place of creation and thrift. The first aim of the author is that of the economist, namely, to give a tableau of the way in which British, French, and German savings were employed in loans to governments, in financing railways, harbor developments and other public works, in exploring and exploiting the resources of colonies and of undeveloped states or areas, in building railways in India and Africa.

On this purely economic side there were well-marked national characteristics. British capital favored an economic development that would produce the revenue for debt-service or dividends rather than loans to governments or government guaranties, to supply constructive talent and management, to stay with the enterprise and to make it "earn its own keep." Other types of investment of course there were—emissions of loans of foreign governments, of the bonds of American and Argentine railways, and so on—but relatively the British investment emphasis was on control and management.

The volume of this total foreign investment was enormous, rising from the annual investing of £1,700,000 in the five-year period 1875-79—the period of world-wide financial depression and contraction—to the annual investing of £185,000,000 in the four-year period 1910-13, when the annual foreign investment equaled approximately one-half the national savings. At this time the total foreign investment amounted to about four billion pounds, or one-quarter of the national wealth, and produced one-tenth of the national income.* It seems to have

* As Mr. Feis points out, the disproportion is accounted for by the fact that national income includes the return for all forms of productive labor.

been about equally divided between investments within and those without the empire. Obviously it created a preponderating interest that the world should be orderly and peaceful.

French conditions were different. Social habits had determined a life of patient toil, a desire for an unlaborious old age, small families and a stationary population, remaining at home, finding "warmth of assurance in patiently accumulated sums"—in financial terms, a lending rather than an adventuring people. The amount of foreign investment was much less than the English—in the 1909-13 period perhaps \$250,000,000 a year as against a British average foreign investment of \$900,000,000 in the same period; a total in 1914 of about \$9,000,000,000 or one-sixth of the national wealth, as against the British \$20,000,000,000, or one-fourth of the British wealth.

But it is the character of the French investment that differentiates it sharply from the British. For the French there were practically no opportunities for the development of regions colonized by their own people, opportunities to build, to manage, and to profit by the dividends on ownership-management. The investment was that of a lender, who relies upon the general solvency of the borrower rather than upon the success of the enterprise. The first result of this type of lending is the capitalist who is much less concerned as to the use made of his money than if he were the entrepreneur who must earn his dividends. The second result is that until the approach of the borrower's bankruptcy is apparent, the lender, confident in the borrower's general ability to pay, sees ulterior political purposes that can be accomplished through a loan without too great risk to the security of the investment.

This French idea of using the savings of the citizens for political purposes is in direct line of descent from the ideas of Colbert, Louis XIV's Prime Minister. The French Revolution, which broke the continuity of the domestic political system of France, exerted little effect on the re-

lation between state policy and economics. As in the time of Colbert, policy between 1870 and 1914 was directed primarily by two sets of conditions and desires. French industry was lagging in its growth behind that of rival states; French foreign investment must serve to aid it. French political destiny was being worked out from day to day in a world that included enemies; French foreign investment was seeking forces by which the destiny of France might be made a safe, perhaps a triumphant one. French capital and enterprise, in greater measure than either English or German capital, "was shaping political alignments—making the fortunes of a new day." The French bankers, even the ordinary French investors, were dealers in "Affaires."

These financial studies constitute a major contribution to the problem of the causation of the World War, disintegrate Article 231 of the Treaty of Versailles which imposes sole "war-guilt" on Germany and perpetuates the myth of a planned and deliberate aggression against a peace-loving world. Nothing, of course, can cleanse the scutcheon of the Dual Monarchy from the blot of having put the match to the powder magazine, or relieve the German Reich from the responsibility of having in July, 1914, backed an ally in dealing a vendetta blow, blind to the frightful aftermath; but as for the deeper causes of the War these financial studies underpin the conclusion of Lowes Dickinson, "that the War was caused by the system of international anarchy involved in alliances, armaments, and secret diplomacy," and show how that system called to its aid the financial strength of the counter-intriguing nations.

The Franco-Russian connection was not more iniquitous than other such alliances, but it is more easily traced and more spectacular in the essential cultural and institutional antitheses that existed between the ramshackle autocratic government of Russia, heading blindly for the abyss, and the thrifty egalitarian close-knit French re-

public. The France of republicanism, liberty, and equality, was gradually harnessed to decaying Russian imperialism, oppression, and corruption; and French peasants of the blue blouse, French shopkeepers of the black coat, bowed their backs, pinched their household budgets, and hoarded their francs with the effect of enabling Russian despotism to resist the pressure of the Duma for constitutionalism and a peaceful revolution. A common hatred and fear of the common neighbor bound these antitheses together and themselves became a factor in bringing on the cataclysm against which they were intended to protect.

This is not to blame a France which had suffered from such master-intrigue and master-preparation for the war of 1870 as Bismarck's. Indeed, it was the later intrigue of Bismarck in the financial field, seeking by a refusal of credit to Russia to bring her into humiliating subservience to Germany that first threw Russia into the arms of France. The first Russian loan, 500,000,000 francs, was floated on the Paris Bourse in December, 1888, after the approval of both governments, and was quickly followed by one of 700,000,000 francs and another of 1,200,000,000. French financial help to Russia, once begun, increased rapidly as the Czardom brought its Danaïdean jar to be continually refilled at the inexhaustible French spring. In 1902 French investments in Russia were approximately 7,000,000 francs and by 1914 had become 11,300,000,000 francs, about one-quarter of the whole French foreign investment; over 9,000,000,000 francs of French-owned Russian securities were obligations of the Russian Government. The distribution in France was extraordinary; after the war the Property Office established by the French Government "received some 1,600,000 individual declarations from owners of Russian securities."

The huge French investment in Russia came to be guided almost exclusively "by the stir of political arrangements"; the weaker Russia became in her financial and domestic affairs, the higher price did she put on her mili-

tary friendship, until, as may sometimes happen, the ulterior purpose of the borrowing endangered the financial interest of the lender. About 37 per cent of the Russian railways were built primarily for political and military, not economic, reasons. Isvolsky in 1911 boasted of the way in which he had forced the French Government to subordinate the financial interests of the French banks to the needs of the dynasty and the strategic requirements of the far-stretching military fronts of Russia.

The Franco-Russian illustration has been selected, I repeat to avoid misunderstanding, because the red military entries are so conspicuous among the plain black-and-white entries of humdrum finance, but not because the case was otherwise with the Central Powers. Germany, too, was throwing gold and the sword into the same scale, and in the various phases of the Moroccan controversy backed German enterprise with a resolution which shifted questions from the terrain of finance to that of irreducible prestige,* and with a recklessness which enlarged the universal fears and set camp against camp in prepared array.

The chapter on the Balkan railways shows how financial interests were entangled in the web of politics and nationalism, each financial maneuver contributing to the suspicions and antagonism that brought on the Balkan wars and thereby the cataclysm that began at Sarajevo. The chapter on Japan's financing, on the other hand, leads out of the atmosphere of constant intrigue, and by coincidence of the period studied with that of Japan's own phenomenal expansion, gives the financial side of the drama of Japanese development from a local to a first-rank power.

The illustrative material selected in this introduction only indicates the illuminating mass of facts which the author has brought together from a great variety of

* "Vital interests and national honor" is the American euphemism for the will to dominate.

xiv *Europe: The World's Banker: 1870-1914*

sources and many archives. The book presents the major episodes of the financial contribution to the war-drift without moralizings, but the author is by no means oblivious of the implications of the facts presented; these are so ordered that they might well serve as material for a philosophical inquiry into the relation between man's organized acquisitiveness and the political anarchy of a world of stubborn "sovereignties." The export of capital raises profound questions both in the economic and in the political spheres, which bring us, as the author says, "close to questioning the whole of modern history, its motives, dominant national ideals, new industrial life and methods."

The volume is published under the auspices of the Council on Foreign Relations, which has undertaken to bring out occasional special studies in addition to its annual *Survey of American Foreign Relations and Political Handbook of the World*; it follows H. Foster Bain's study of *Ores and Industry in the Far East* and James W. Angell's work on *The Recovery of Germany*.

New York
July, 1930.

Charles P. Howland,
Director of Research
Council on Foreign Relations.

PREFACE

WHEN in the stillness of some distant, uninhabited valley the steam shovels and pneumatic drills pound out the path for steel rails and the locomotive, a drama of new life is begun. Human power is applying itself to an intricate creation. One world is destroyed, another founded.

Before the World War the capital of western Europe was impelling forward this drama of change upon a limitless stage. Through the savings of a few countries the power of industrial civilization was carried from its first home to all other lands; the world of machines, of organized, time-consuming production, of large-scale exchange, of numbers, extended itself. The financial journals stand as birth registers of the continuous union of capital, technical skill, and purposeful planning of the capital-accumulating countries, and the resources and labor of the rest of the hemisphere. Western Europe, through its spared accumulations of capital, impregnated all other regions with the growing cells of its civilization. The economic and political arrangements of the world were thereby permanently changed.

To study the main trend of this migration of capital, to measure and record it, was the original purpose of this volume. But preliminary study soon revealed that its connections with the political and diplomatic events of pre-war days were numerous and important. The world from which the capital moved was made up of highly ambitious, competitive national states. The regions to which it moved varied enormously in the character of their peoples, their powers of self-government, their ability to put borrowed capital to good use, their political strength. The place of many of these regions in the political arrangement of the world was, even then, in the balance. Their transactions with foreign capital often settled the outcome. In short,

the financial transactions between western Europe and other areas were an important element in political affairs. They became all the more important because the official circles of lending countries gradually came to envisage the foreign investments of their citizens, not as private financial transactions, but as one of the instruments through which national destiny was achieved. Financial force was often used to buy or build political friendship or alliance, was often lent or withheld in accordance with political calculations.

The lines of political division in pre-war Europe, the situations which were created and which led ultimately to the War, can be understood only by taking account of the borrowing-lending relations which existed. On the other hand, the action of capital, seeking return, can be understood only by taking account of the national influences to which it was subject. The volume, it is hoped, reveals the strength of the tendency of capital to move over national boundary lines in search for opportunity, and at the same time amply illustrates the special risks, controls, and pressures to which such capital movement has been subject.

These are the reasons for believing a study of lending and borrowing relations in the pre-war years worth undertaking. But additional point may be given to the effort by the fact that the United States has taken its place with western Europe in supplying capital to other lands. It has become, and will remain, a great, perhaps the greatest, center from which the revolutionizing force of accumulated capital and machine technique will travel outward. The account which follows proves, I think, that a capital-lending country should possess a policy, or at least a carefully defined attitude, toward this process of foreign investment and the situations it creates. Some instruction may be in the record of policy and experience of pre-war Europe.

The great dimensions of the matters which I have attempted to study may help to excuse the shortcomings of the result. Within the covers of one volume it has been im-

possible to give attention to many of the aspects of this course of capital movement which are of greatest interest to economists and international lawyers: to cite a few in the economic sphere, the operation of the financial mechanism by which the capital is transferred from lender to borrower, the effect of such transfers on trade balances and prices; or to cite one in the legal sphere, the consequences of the spread of the doctrine within borrowing countries that those who invest capital within their borders must accept the same status as domestic capitalists. It has also been impossible to traverse the whole area of lending and borrowing. Only the capital investments made by the British, the French, and the Germans, with the concomitant government activity, are included: the ventures of the Dutch, the Belgians, and the Swiss, as much as they deserve consideration as part of the historic process, could not be adequately reviewed without virtually doubling the task and the consequent number of pages.

So much for the pretensions and limitations of this volume. For assistance given I am heavily indebted to many individuals and groups. The necessary study in Europe was undertaken with the aid of a fellowship award of the Guggenheim Foundation. The Graduate School of the University of Cincinnati also made some grants for the work. The advice and encouragement of Professor F. W. Taussig greatly helped me to plan the study. The critical reading of the manuscript by Professor William R. Langer and Professor Parker T. Moon enabled me to understand and partly to correct its faults. Among those who aided me by giving information or putting material at my disposal I take the liberty of mentioning, as grateful acknowledgment, M. Cousin, of the Association Nationale des Porteurs Français des Valeurs Mobilières; M. De Mouy, formerly of Lazard Frères, Paris; M. Masson, Director of the Crédit Lyonnais; M. Joseph Caillaux, formerly Prime Minister and Minister of Finance of France; M. Fernand Faure, Editor of the *Revue Politique et*

xviii *Europe: The World's Banker: 1870-1914*

Parlementaire; H. G. Hawtrey, Esq., of the British Treasury; B. I. G. Lloyd, Esq., of the British Board of Trade; Hartley Withers, Esq.; Walter T. Layton, Esq., Editor of the *Economist*; Douglas Reid, Esq., of the Council of Foreign Bondholders; Sir Josiah Stamp; Sir George Paish; Sir Alexander Kleinwort; Henry M. Andrews, Esq., of J. H. Schröder, London; Herr Ernst Kahn, of Lazard Speyer-Ellissen of Frankfort. To the authorities and staff of the École des Sciences Politiques, the London School of Economics, and the New York Public Library, I owe thanks for unfailing courtesy and aid.

H. F.

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TABLE OF CONTENTS

| | PAGE |
|-------------------------------------|------|
| Introduction, by CHARLES P. HOWLAND | ix |
| Preface | xv |

PART I

THE RECORD OF CAPITAL MOVEMENT

Chapter

| | |
|--|----|
| I. British Foreign Investment | 3 |
| The greatest free financial force | 3 |
| The geographical spread of the investment | 17 |
| The character of the investment | 26 |
| II. French Foreign Investment | 33 |
| The world of saving and the world of lending | 33 |
| The rôle of the French banks | 39 |
| The growth of the foreign investment | 43 |
| Where the investment was made | 49 |
| The character of the investment | 57 |
| III. German Foreign Investment | 60 |
| Two needs for every mark | 60 |
| The German great banks and their allies | 62 |
| The growth of the investment | 68 |
| The zones of investment | 73 |
| The character of the investment | 78 |

PART II

RELATIONS BETWEEN FINANCE AND GOVERNMENT IN THE LENDING COUNTRIES

| | |
|--|----|
| IV. Finance and Government in Great Britain | 83 |
| Legal freedom and informal intercourse | 83 |
| The adjustment of financial and political policy | 88 |
| The colonial stocks act | 92 |

xx *Europe: The World's Banker: 1870-1914*

| | |
|--|-----|
| The Government's concern with foreign opportunities for British capital and enterprise | 95 |
| The Palmerston circular and subsequent policy | 102 |
| The investors endeavor to help themselves | 113 |
| Concluding observations | 117 |
| V. Finance and Government in France | 118 |
| The texts | 118 |
| Supervision for economic ends | 122 |
| The search for political advantage | 133 |
| Favor for the colonies | 142 |
| The Government's part in securing concessions | 144 |
| Government protection of foreign investment | 146 |
| The organization of the investors | 154 |
| Some general observations | 156 |
| VI. Finance and Government in Germany | 160 |
| The growth of a doctrine | 160 |
| Means and methods | 163 |
| The actual exercise of government influence | 169 |
| Government aid in securing concessions | 176 |
| German capital and the colonies | 181 |
| The protection of the foreign investment | 183 |
| Concluding observations | 186 |

PART III

STUDIES IN LENDING AND BORROWING

| | |
|--|-----|
| VII. Introduction | 191 |
| VIII. Nonintercourse between France and the Central Powers | 196 |
| The ban against German securities | 196 |
| Austria-Hungary: the ending of a financial friendship | 201 |
| IX. The Financing of Imperial Russia | 210 |
| The largest borrower in Europe | 210 |
| French capital serves the Alliance | 212 |

Table of Contents

xxi

| | |
|---|------------|
| The German Government intervenes | 224 |
| Upon accord, British investment follows | 229 |
| X. The Financing of Italy by Rival Alliances | 235 |
| XI. The Financing of Portugal—a Debtor with a Noble Past | 243 |
| Default follows upon default | 243 |
| Attention turns to the Portuguese colonies | 247 |
| XII. The Financing of the Balkan States | 258 |
| Serbia is assisted to rise | 262 |
| Creditors' control in Serbia | 266 |
| The development of Roumania | 268 |
| The financing of Bulgarian ambitions | 272 |
| The French Government vacillates | 275 |
| The German Government wins | 279 |
| Creditors' control in Bulgaria | 283 |
| Financing Greece's national career | 284 |
| Creditors' control in Greece | 289 |
| XIII. The Financing of the Balkan Railways | 293 |
| Across the Turkish provinces from Constantinople to Vienna | 293 |
| The Oriental railways live amid trouble | 298 |
| From the Danube to the Adriatic | 302 |
| The Balkan wars bring fresh troubles | 304 |
| International ownership is proposed | 306 |
| Sarajevo—the original terminus of the line | 310 |
| XIV. The Turkish Empire and European Investors | 313 |
| Between war and bankruptcy | 313 |
| The rôle of the powers—Germany | 318 |
| The rôle of the powers—France | 320 |
| The rôle of the powers—Great Britain | 330 |

xxii *Europe: The World's Banker: 1870-1914*

| | |
|---|------------|
| To protect the bondholders—the Ottoman public debt administration | 332 |
| XV. The Financing of Railroads in Asiatic Turkey | 342 |
| The railway progresses toward Bagdad | 342 |
| The project of internationalization fails | 348 |
| German capital goes as far as it can | 353 |
| Opportunity is divided by spheres | 355 |
| XVI. The Financing of Persia: Between Two Imperial Ambitions | 361 |
| The Shah mortgages his domains to travel in Europe | 361 |
| Lending is controlled | 365 |
| Russia and Great Britain divide the field | 366 |
| The Trans-Persian railway project | 379 |
| XVII. Finance and Fate in North Africa | 382 |
| 1. THE FINANCING OF EGYPT | 382 |
| The Khedive goes bankrupt | 383 |
| The creditors take control | 384 |
| The British take charge | 390 |
| 2. THE FINANCING OF MOROCCO | 397 |
| France bargains for a free hand | 399 |
| Germany demands international control | 404 |
| France pushes ahead | 407 |
| On the verge of war | 412 |
| XVIII. Japan Is Helped To Become a Great Power | 422 |
| XIX. The Financing of the Chinese Government | 430 |
| The Chinese Government and the Powers | 430 |
| The financing of government needs | 435 |
| A note on the consortium | 455 |
| A note on the maritime customs administration | 459 |

Table of Contents

xxiii

Concluding Observations—By Way of Apos-
trophe

463