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No. 12

# GERMAN, COMMERCIAL POLICY

B.

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## NOTE

SINCE its establishment in 1927, the Graduate Institute of International Studies at Geneva has organized, in addition to its regular instruction, certain series of lectures by experts from outside its own staff. In spite of the original character of most of these lectures, the Institute cannot publish all of them.

The Directors believe, however, that they ought to make certain of them available to a larger public.

The first of these publications were a series of monographs on the policy of different States in the League of Nations. They were followed by three studies concerning various other topics of international interest. The present monograph is the third of a new series relating to the recent commercial policy of different States, the first of which was devoted to Belgium, the second to Italy. Both were published in French. ~~†~~

For these studies, as well as for all which may follow, the task of the Directors of the Institute is limited to the selection of their authors. The authors have been left complete freedom of thought, and naturally, therefore, they bear the sole responsibility not only for their opinions, but also for the form of their expression.

PAUL MANTOUX.  
W. E. RAPPARD.

## PREFACE

THIS book presents the revised reproduction of a series of lectures which I gave at the Graduate Institute of International Studies in Geneva in the beginning of February, 1934. I have done everything to make this monograph on German commercial policy as up to date as possible, but things in Germany are changing so rapidly that, when it comes out of the press, it may possibly no longer correspond, in every detail, to the actual situation. I believe, however, that the main arguments will be corroborated rather than refuted by further developments. In particular, I am firmly convinced that the economic development of Germany during the last years is a sort of experimental verification of the reasoning of those who thought it their duty to warn the public against the autarkistic tendencies, and an irrefutable proof of the vital necessity of foreign trade for a country like my own.

I am very much indebted to Professor Jacob Viner who kindly corrected the English manuscript.

WILHELM RÖPKE

UNIVERSITY OF ISTANBUL

*May, 1934*

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## CHAPTER I.

### INTRODUCTION.

ALMOST precisely one hundred years ago from this moment, an event occurred in Germany which marks the beginning of a German Commercial Policy in the proper sense of the term. In the present days the attention of all of us is so entirely absorbed by the enormity of the actual problems, both economical and political, and by the breathless speed with which they are following each other, that a centennial of this kind is very apt to be overlooked, even if it is the centennial of an event the importance of which cannot easily be overrated. What I have in mind is, of course, the fact that, on the New Year's Eve of 1833-34, the German Zollverein went into effect. It was one of the merriest New Year's Eves which the German nation has seen. Precisely at the moment when the church bells all over the country chimed in the new year the good old turnpikes were lifted, from the Baltic Sea down to the Bodensee, to the infinite enjoyment of the people who got rid thereby of the internal customs barriers which otherwise would have strangled the growth of the later colossus of German industry. Everybody was happy except the smugglers because everybody was to gain except the smugglers. An era of freedom and unimpeded enterprise had been initiated.

It would have been a fine thing if the centennial of the Zollverein could have been celebrated by a similar act of liberation and clean-up, by something which would do for Europe and for the world what the Zollverein did for Germany one hundred years ago. But even to imagine such a thing seems rather like a cynical irony on the miserable



reality of ever-growing customs barriers and all the new-fangled devices such as quota systems, exchange control systems, import trading boards, currency tampering, and so on, which are threatening to break up that densely woven net once bearing the proud name of world economy into small fragments of more or less independent national or even regional units. What a difference between 1834 when the world was moved by anticipations of a new era of economic liberty and world-wide solidarity, and 1934 when the very foundations of our economic and social system are beginning to weaken, when national isolation and State intervention of the crudest kind are shattering those hopes to pieces, and when the mentality of 1834, even in its noblest parts, is decried as a strange abomination.

Nothing could be more instructive, indeed, for a better understanding of this change of a century than a thorough-going analysis of the development of the commercial policy of Germany, of its underlying causes and its far-reaching effects. For we must understand that the commercial policy of a country is like a mirror reflecting all the economic, political and social determinants of the time. The larger and the more important the country, the better and the more distinctly will the mirror reflect those determinants. That is the reason why the commercial policy of Germany is such a fascinating subject that it will arouse the most vivid interest even of those who can have no use for the highly technical details which, in the case of Germany, are very apt to bewilder everybody except the specialist. Therefore, it must be my purpose, in these lectures, to confine my treatment of the subject to the more general lines and to go into technical details only in those cases which have a special bearing on the general tendencies.

There is something else which we must bear in mind. I am referring to the question of guilt and responsibility. Commercial policy has that in common with international policy in general that it is a play of actions and reactions. The student of the theory of international trade may deny

that most emphatically, saying that to treat commercial policy as something akin to the policy of alliances, armaments and war-making is just the terrible mistake which is responsible for the greatest part of the errors and misconceptions of the commercial policy of the times of the mercantilism and again of our own times. He may point out that there is no sense in imitating the high protectionism of other countries and that free trade remains the best, *i.e.* the most rational, commercial policy even when the other countries are adopting a policy of protection. I would be the last to deny the truth which is at the bottom of this theory, but we are not concerned here with what the nations ought to do but with what they are actually doing. In this respect, nobody can dispute the statement that commercial policy, like international policy in general, is a play of actions and reactions. It is very natural, then, to raise the question as to who is responsible for a wave of protectionism,—as it is very natural to raise the question as to who is responsible for a wave of armaments or for a war. Natural, yes. But not always very well-guided. Leaving aside the question of war guilt (where we should come to similar conclusions), we perceive that the set of actions and reactions characterizing the commercial policy is a very complicated one where causes and effects are interwoven. As a matter of fact, it very rarely happens that we can heap all the blame—or, as the case may be, all the glory—for a new trend in the commercial policy of the leading countries on a single country. True, we see a certain country taking the first step in the new direction or taking the initiative for the collective step of several countries. But, on the other hand, it must not be forgotten that this initial act was the result of ideas and circumstances of an international character. Sooner or later, something of this kind was bound to happen as long as those ideas and circumstances were prevailing. It is necessary to stress this point because the commercial policy of Germany has sometimes been held responsible for a certain turn of international

commercial policy to a greater extent than it really deserved. Much has been made, for instance, of the German tariff revision of 1879 as the initial act which brought about the new era of protectionism. This tariff revision of 1879, marking the end of free trade in Germany, was, indeed, a turning-point in the tariff history of modern times. It would be unfair, however, to suppress the fact that the first step in the new direction had been made by the tariff changes in the United States during the Civil War and—more important still—that the German tariff revision was the result of an atmosphere which had been prepared and of circumstances which were noticeable throughout the western world. Austria and Italy had actually preceded Germany in the new policy, and the French were already busy in drafting a new tariff Act when the Bismarck Tariff of 1879 went into effect. We shall see later that we have to apply the same sense of fairness in order to find out the real share of responsibility which Germany has to bear for the new wave of protectionism and isolationism since 1928. I do not want to leave you under the impression that I am following the very bad example of pointing to the mote in other people's eyes and not seeing the beam in our own eyes, a practice which is almost the common rule in all discussions about commercial policy, but I shall try to do my best to be an impartial and unprejudiced judge both of the achievements and of the errors of German Commercial Policy.

That leads me to another question with which I may be permitted to deal by some remarks of a more general character. The comparison between the commercial policy and the external policy of a country has already presented itself. Commercial policy is in a formal sense a part of the whole external policy of a country, because it deals with the economic aspect of the international relations. But that is only one side of the matter. The other side is the fact that the commercial policy is also a part of the general economic policy of a country, just as is a policy of price-fixing, of subsidies to special industries, of encouragement to certain

lines of investments given by the State and the like. Now, the very fact that the commercial policy is part of the general economic policy of a country and has the appearance of being a part of the general external policy and of being in the same class with alliances, armaments and war-making, is extremely apt to darken the real issue. People are led to believe that in all matters of commercial policy the interests of the different nations are lined up against each other like two hostile armies, so much so that every concession made in commercial treaties appears as a sacrifice made by the whole nation to the foreign country. The vocabulary of the more vulgar type of protectionism is full of military expressions and metaphors which are all very useful for conducting the water of legitimate and honest patriotism over the mill-wheels of protectionism and for creating the impression that protectionism and patriotism are identical. For the same reasons, criticism of the commercial policy of one's own country from a liberal point of view is regarded as a regrettable lack of patriotism or even as high treason. Everybody is familiar with these tricks of the prevailing economic nationalism which is poisoning the atmosphere all over the world, tricks played on the ignorance and thoughtlessness of the people. We have progressed so far at this moment of the centennial of the Zollverein that to buy foreign goods is considered a crime from which one may be acquitted only under exceptional circumstances. And even to point out that it is nonsense to talk of our good money given away for the import of such luxuries as perfumes, oranges and Christmas toys is something which subjects one to grave suspicion. All that, of course, is nothing short of degrading that noble passion which we call patriotism. We may call it downright commercialization of patriotism, intentional or unintentional. The truth is that, in all questions of commercial policy, the interests are lined up in an entirely different manner. The interests of the native producers wanting protection are lined up against the block of interests both of the consumers and

of all other producers. Thus, in all disputes on commercial policy, the real clashes of interest do not coincide with the frontiers of the State, but run right across the country. Therefore, every concession made in commercial treaties is in reality a sacrifice which those whose protection is diminished by this concession are forced to make in the interest of the nation as a whole. The fact that this true conflict of interests has the appearance of a conflict between the native and the foreign country is the explanation of why the attempts to identify the protectionist interests of a small part of the population with the common interest of the nation and the appeals to patriotism in this respect prove always so extremely successful.

## CHAPTER II.

### THE COMMERCIAL POLICY OF GERMANY AS RELATED TO ITS GENERAL ECONOMIC DEVELOPMENT.

TURNING now definitely to my subject, it is not my purpose to deal at length with the earlier stages of the history of the German Commercial Policy. I shall confine myself to an attempt at giving a rough outline of the development of German Commercial Policy against the background of the general economic development of Germany.

During this century, from 1834 to 1934, on which we are now looking back, Germany has run, in a most conspicuous manner, the course of a country which has changed from an agricultural country to an industrial country. In a hundred years an industrial superstructure has been built upon the agricultural basis to make room for an increase of population, and all this in dimensions which were considered as unique until quite recently the Japanese development has even surpassed the German example. What happened in Germany can be summed up in this way: Under the ever-increasing pressure of population and driven by forces the mystery of which will never be unveiled in these cases, Germany has diverted a growing proportion of its productive means to industry, commerce and the other non-agricultural activities, procuring thereby not only a gainful employment for its teeming millions, but also augmenting rapidly the economic welfare of the masses. Germany—like Japan to-day—had to emancipate itself from the limits imposed on its productive capacity by the scantiness of the German soil, and it did so by building up a broad industrial superstructure on a relatively small agricultural basis. What

Germany achieved in this way may be roughly illustrated by the statement that from 1800 to 1900 the German population increased by 250 per cent., while the increase of the national income may be estimated at 1000 per cent., so that the average income per head has been quadrupled. While the absolute importance of agriculture has remained almost stationary, the relative proportions between the agricultural and the non-agricultural sections of the population have, of course, changed tremendously during this period. The share of the farming population in the total population has continuously decreased from 40 per cent. in 1882 to 23 per cent. in 1925, whereas the share of the industrial population has increased from 35 per cent. in 1882 to 41·3 per cent. in 1925 (earlier dates are not available). The percentage for the population engaged in commerce and transport has increased from 9·7 to 16·9. This development meant, of course, at the same time growing urbanization. In this respect it is remarkable that during the last sixty years the proportion between the rural and the urban population has been exactly inverted, for in 1871 almost two-thirds of the German population (63·9 per cent.), while in 1933 only one-third (33 per cent.), were living in rural communities. The entire increment of population during these sixty years has been added to the urban population, and that mostly to the population of the big cities. The result is that to-day almost every third German (30·2 per cent. of the total population) is living in the big cities. In contrast to the development in England, this has been going on without any visible signs of decay of agriculture. On the contrary, German agriculture has not only held its ground but has made steady progress and has remained absolutely healthy. But the vital point is that the enormous growth of the other sections diminished the *relative* importance of the agricultural section correspondingly. The industrial section is still more ahead in the net value of production which, in a calculation recently made by the Verein der Deutschen Maschinenbauanstalten, is estimated for the "Wirtschaftsjahr" 1930-31 at

approximately 20.3 milliards RM., against about 11 milliards RM. for the net value of the agricultural production.

This process of rapid industrialization amounted not only to a process of urbanization, but also to a process of *internationalization*, that is to say, to a process of growing importance of foreign trade. While everybody knows that Germany has won one of the first ranks in the world commerce from which even the World War could not definitely displace her, it is extremely difficult to give an exact measure of the degree in which the German economic structure depends on foreign trade. We are touching here a problem that is being feverishly discussed at present in connection with the well-known question of Autarky which I shall deal with later on. It is possible, to be sure, to find out the approximate proportion between the volume of internal production and the volume of foreign trade or to calculate the volume of foreign trade per head of the population, and to compare the data for various countries or for different periods. It may suffice here to say that the volume of foreign trade in Germany shows a steady increase from 1860 to the World War, so much so that in 1912 only Great Britain ranked above Germany as the country with the largest share of the world trade. This upward trend was of necessity interrupted by the war and the post-war disturbances, but from 1925 on until 1930 the pre-war trend was resumed with a remarkable steadiness until the present crisis started a downward development which it is still extremely difficult to interpret. It cannot be denied that in the recent years, under the influence of the crisis and of the protective measures at home and abroad, the relative importance of foreign trade has somewhat diminished. It is interesting, however, that as recently as 1931 36.4 per cent. of the industrial net production was exported, which, under certain reasonable assumptions, leads to the conclusion that almost 10 millions of Germans—that is 15 per cent. of the total population—were dependent on export. But even that is not sufficient to



show the true importance of foreign trade for Germany. The truth is that the present proportion between domestic and foreign trade cannot be varied very much in favour of the domestic trade without jeopardizing the very foundations of the German economic structure. It must not be forgotten that that part of the industrial production which is exported is just that part which, according to the law of mass production, is absolutely essential for the maintenance of the industrial production as a whole. Further, it must not be forgotten that for most of the raw materials and for an important part of the foodstuffs Germany is absolutely dependent on import and, therefore, on the export of finished and half-finished products. It has been one of the favourite arguments of the advocates of Autarky in Germany to ridicule this dependence, but the experience of the last months has been sufficient to turn this spirit of mockery into greatest anxiety. It has become clear to everybody that any significant increase of industrial activity in Germany depends entirely on a considerable increase of the import of raw materials which must be paid for by increasing exports of finished goods or by new foreign credits. As it could be predicted long ago, the whole economic future of Germany hinges now upon this point.<sup>1</sup>

This short sketch of the economic development of Germany would be incomplete without any reference to the development of the German *balance of payments*, in which foreign trade constitutes only one, though the most important, item. Leaving aside the international balance of railway and water transport charges and similar items, we find that the structure of the balance of payments is mainly determined by the balance of capital movements, in such a way that a surplus of the balance of trade is a reflex of a deficit of the balance of capital movements and vice versa. A *deficit of the balance of capital* movements may have a double meaning. It may mean that the country in question is

<sup>1</sup>Cf. W. Röpke, "Trends in German Business Cycle Policy," *The Economic Journal*, September, 1933.

lending or investing more capital abroad than it is borrowing or receiving under any other title from abroad (first stage for a lending country). Or it may mean that the country in question has to pay more as interest, amortization, and dividends abroad than it is receiving under any other title from abroad (second stage for a borrowing country). Also a *surplus of the balance of capital movements* may have a double meaning. It may mean that the country in question is receiving more capital as interest, amortization, and dividends from abroad than it is sending abroad under any title (second stage for a lending country). Or it may mean that it is borrowing more capital abroad than it is sending abroad under any title, especially as interest, amortization and dividends on the old debts (first stage for a borrowing country). It is easy to see that the first stage for a lending country and the second stage for a borrowing country are equally characterized by an active balance of trade, and that the second stage for a lending country and the first stage for a borrowing country are equally characterized by a passive balance of trade. The economic history of Germany shows that the development of the German balance of payments has run through all these four stages. Starting with the year 1860, we see in the first period a considerable excess of imports which must be explained as an excess of imports due to a surplus of capital import (first stage of the borrowing country). This was only a natural reflex of the early economic expansion of Germany financed to a great extent by foreign capital. This period came to a sudden end in 1880. From then on the balance of trade became active, marking thereby the transition from the first to the second stage for a borrowing country, and later on to the first stage for a lending country. The transition from the first to the second stage of the lending country came slowly at the end of the 'eighties, together with the first signs of the upward swing which became more and more accentuated during the 'nineties. The active balance of trade remained relatively steady until the outbreak of the Great War, fluctuating

about the level of 1 milliard of marks. The<sup>2</sup> position of Germany as one of the great lending countries had been definitely established, its foreign investments amounting to something between 25 and 30 milliards of marks. After the smoke of the war and the inflation had been dissipated, we see Germany enter again into a period of a passive balance of trade, but this time of the type indicating the first stage for a borrowing country. Thus Germany had been thrown back to the position at which it had started in 1860. Corresponding to the gigantic capital import into Germany in the years 1925 to 1929, the passive balance of trade reached enormous heights, with a maximum of 2.8 milliards of marks in 1927. Germany had been forced into the rather doubtful position of the leading borrowing country of the world. But, in contrast to the passive balance of trade of the second stage for a lending country, the passive balance of trade of the first stage for a borrowing country can of necessity never be permanent, since sooner or later a point will be reached when the curve of the increasing payments for interest and sinking fund on the old debts will cross the curve of the new capital borrowings flowing in, the more so because of the reparation payments. This point had been definitely reached in 1930, and in 1931, under the pressure of the great crash, a net active balance of nearly 3 milliards of marks was attained, teaching thereby an unforgettable lesson to those who will not believe in the remarkable elasticity of the balance of trade even under the most unfavourable circumstances.

## CHAPTER III.

### A GENERAL APPRAISAL OF THIS DEVELOPMENT.

SUMMING up our all too short survey of the economic development of Germany as the background for the development of its commercial policy, we may say that Germany is a striking example of a country which has become tremendously populous, rich and powerful by building up a second story of an industrial and commercial character upon an agricultural foundation. This "second story" principle means industrialization, urbanization, commercialization and—last, but not least—internationalization so as to interlace more and more the German economy with the world economy. Much can be said about the disadvantages of this development, which were at all times during the last fifty years fervently pointed out by the more conservative economists, not to mention the philosophers like Nietzsche, who perceived with growing uneasiness the high tide of mass civilization threatening to submerge the more aristocratic values of occidental culture. Just at the turn of the century a group of economists, including men like Adolph Wagner and Ludwig Pohle, were striking an extremely pessimistic note, emphasizing the increasing instability and the top-heaviness of an economic system relying too much on industry and foreign commerce. This famous dispute about "Agrarstaat" and "Industriestaat" has become known to every student of the subject. It is not to be wondered at that a second and still more powerful wave of pessimism swept over Germany during the present crisis, culminating in the demand for a drastic reagrarization and nationalization of

the German economic structure, for which purpose the old slogan of the advocates of the "Agrarstaat," *i.e.* "Autarky," was repolished with tremendous success.

It would be foolish to deny that we have to pay a price for everything. We cannot have something for nothing. We may grant that the price to be paid for the gains derived from industrialization and internationalization is a very heavy one. Moreover, we may even grant that the price is much too high to justify such an adventure. But it is one thing to grant this and quite another willingly to turn back the wheels of history. For it must never be forgotten that this development created the conditions necessary for the enormous increase of the German population and for a standard of living which cannot be brought down to the level of a century ago without fatal effects. The additional millions of Germans are there. They have come to stay, and it is impossible to destroy afterwards the conditions which brought them into existence. That is what the whole question is simmering down to. "Beim ersten Schritte sind wir frei, beim zweiten sind wir Knechte." Fifty years ago Germany had a free choice, but to-day it has no alternative whatever, no less than has Japan to-day. This state of things was clearly conceived, in the 'nineties, by the Reichskanzler Caprivi when he coined the famous phrase which was destined to appeal to the reason of the rather violent partisans of agricultural protection: "We are forced to export either goods or men." But even this alternative is no longer available, since most of the outlets of emigration have been closed by the restriction of immigration abroad. If ever we have a right to speak of an inexorable fate, it is here and nowhere else. *Fata volentem ducunt, nolentem trahunt.* What is true of Germany is equally true of most of the other leading nations of the world, though in a varying degree. As the whole world is hearing frenzied cries for Autarky, these remarks have a universal meaning.

It is well known that the transition of Germany from the agricultural to the industrial stage went on under a régime

which, in comparison with the present practice all over the world, might be regarded as fairly liberal and which, at the close of this period, was free trade pure and simple. It is interesting to note that it was Prussia that, under the leadership of a broad-minded and liberally-tinged bureaucracy, paved the way for this liberal commercial policy, the first stage being the Prussian tariff of 1818 with relatively low rates, the second stage the foundation of the Zollverein in 1834, the third stage the commercial treaty between Prussia and France in 1862 with the subsequent tariff reductions. In this historic mission the Prussian Government was aided by the fact that the landed aristocracy were advocates of free trade as long as Prussian agriculture was on an export basis, and very ardent advocates at that. By the 'seventies the transition had been completed. From this time onward the history of the German commercial policy can be conceived as the resultant of two forces: the inherent necessities forced upon a country with the economic structure of Germany on the one hand, and certain interests and considerations striving against these necessities on the other hand, the one aiming in the direction of a liberal, the other aiming in the direction of an illiberal commercial policy. The history of German commercial policy is the history of the struggle between these two sets of forces and of the peculiar circumstances assisting sometimes this side, sometimes the other.

There is one thing that is made clear by this history, and that is something worthy to be remembered in these days of international protectionism going on on an unprecedented scale. I am referring to the fact that three times during this history the second set of forces has been able to set its mark on the commercial policy, each time in a more powerful manner. Leaving out of account the altogether abnormal period of the Great War and the time immediately after it, we find that these three triumphs of protectionism occurred during the three great economic crises which have shaken Germany in the course of the last fifty years. The crisis of

the 'seventies, starting in 1873 as a financial<sup>o</sup> and commercial crash, then prolonged as a tenacious industrial depression and finally supplemented by the great agrarian crisis of that time, bred the tariff reform of 1879 marking the end of unreserved liberalism in German commercial policy, although the duties were at the beginning moderate. Bismarck adhered strictly to his policy of unmitigated protection, sticking to the famous most-favoured-nation clause of the peace treaty of Frankfurt and refusing any tariff concessions or consolidations. But the commercial policy of the 'nineties took the direction of a marked mitigation of protection, which was brought about by the so-called Central European commercial treaties, a line running parallel to the general economic prosperity of that decade. The economic depression which followed at the turn of the century was marked again by a reversal of the liberal tendency in commercial policy, realized in the tariff revision of 1902 which went into effect in 1906. This liberal direction of commercial policy was resumed, without considerable change, in 1925, after the interval reaching from the outbreak of the war to the recovery of full autonomy in commercial policy. And again a great economic depression brought this period of moderation to a sudden close, this time the world crisis which began in 1929. There is, then, perhaps, no better illustration of the close interdependence between the trade cycle and the direction of commercial policy than the history of the commercial policy of Germany. We shall not enter upon the question as to which is cause and which is effect. Very probably cause and effect are intertwined as usually in these matters. But the experience of the German commercial policy seems to prove at least that the prospects for a liberal commercial policy are never more hopeless than during a pronounced depression. It is all very well to tell the people that protection is making the depression worse rather than better. They will not believe it unless the first signs of recovery are being felt. Relieve the economic pressure by credit expansion before you appeal to wisdom

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and reason, and the appeal has some chance of success. The other course means putting the cart before the horse. That is one of the main reasons why the great and laudable effort of the late World Economic Conference was doomed to failure.



## CHAPTER IV.

### THE CASE AGAINST AUTARKY.

IT has been argued that the course of German economic development has by an inexorable logic demanded a liberal German tariff policy, notwithstanding all the rather noisy claims for the opposite. We may even go further than that by asserting that the development of Germany is only a part of a more general development. What I had in mind in the case of Germany was that the industrialization and internationalization of this country has, after a while, become a *fait accompli* which, willy-nilly, had to be respected. Now, I want to add that also this process of internationalization was not a more or less fortuitous event, but the outcome of a much wider set of forces and therefore completely in accordance with the inner logic of the universal development of the last centuries. To-day the world is full of neurotics who seem to derive much pleasure from detecting gloomy handwritings on the wall of our civilization. They tell us that all this economic internationalization was a foolish departure from the natural course of things and that now the present world crisis has been inflicted upon us as a sort of Nemesis for our sins against logic and nature. We cannot deny that this attitude is not altogether incomprehensible. But, on the other hand, there is no getting away from the fact that logic and nature are entirely on the other side. The last few years of terribly dwindling world trade and of retreat from international division of labour are nothing compared with the trend of centuries, and this trend of centuries is characterized by what might be termed growing economic integration. The space over which men have

been intertwined economically has, in the long run, grown continuously and the interpersonal economic relations have been steadily intensified on the growing geographical scale. It has been said that such internationalization is so unnatural that it has never been tried before in history, conveying obviously the contention that it is an unheard of experiment which was bound to fail, sooner or later, like the tower of Babylon. One has no need to be a scholar of ancient civilization to know that the Imperium Romanum was very much like the world economy of to-day. From what we know of that time according to the more recent investigations, it is absolutely wrong to suppose that a journey from Byzantium to Geneva would have been much less common than to-day—if only the people at the Eastern Metropole would have known that little hamlet on the Lacus Lemannus. The delegates went to the famous Concilium Œcumenicum of Chalzedon—the Kadiköy of to-day where I am living at the moment—in A.D. 451 much like the delegates who come to Geneva. No, the experiment has been tried before, and with tremendous success, for more than 500 years. Ancient civilization has declined for reasons which have nothing to do whatever with the pretended lack of naturalness of the world-wide economic system, and what came after this decline is certainly not enticing enough to induce us wantonly to abandon the elements of international economic organization which still survive.

Of course, the modern world-wide economic system is unique as far as its dimensions are concerned. But then the increase of population during the last century is also unique and something that the world has never seen before. These additional millions who came into being under this system have every right to protest against their being classified as something unnatural. Their origin is of the most natural kind. They are anything but products of the much despised rationalism. On the contrary, they are of a most irrationalistic origin. All this talk about the unnatural character of our world-wide economic system,

about the ugliness of industrialism, about the romantic loveliness of the open country and about the rejuvenating forces of an anti-industrial national economy is futile as long as the advocates of this new policy do not suggest any satisfactory solution of the problem of how to dispose of those unfortunate millions who depend on the present system.

There is another point so banal that I have some reluctance to mention it here, but as it is equally important and apt to be overlooked, I may say a word about it. I refer to the enormous progress of the technique of transportation and communication as one of the most powerful forces behind this process of economic integration. With the most modern branch of this technique, the technique of broadcasting, a point has been reached where national boundaries simply do not count any more, and no customs barriers, no quota and exchange control systems can hinder the people from switching from Russian radio lectures to an opera performance in Milan or to a symphony in Leipzig. I wonder how many realize that hailing the "Graf Zeppelin" and advocating a policy of national economic isolation are acts incompatible with each other. People may not care whether it is a contradiction or not. It may be that a logical contradiction will not prevent the railways and ports of the world from crumbling away and the highways from decaying as they decayed after the decline of the ancient world, but it is certainly not a small thing that there is such a contradiction and that it can be explained to the people. There is one of those *faits brutaux* which even the most ardent advocates of national economic isolation cannot ignore.

On the whole, I believe that the opponents of this modern drift towards Autarky let themselves be intimidated too easily by the blaring propaganda of the isolationists. They are lacking in courage to stick to the excellent reasons which they have in stock, and to prick the fine bubbles of the isolationist philosophy. It is very easy to show that economic

institutions which have the inner logic behind them are always forcing their way against all obstacles. Capitalism in general—if we may use for a moment this much-abused word—is one of the examples. It obviously takes a good deal to kill it. Ten years ago, perhaps nobody would have believed that capitalism would outlive the deadly blows administered to it during these years, and yet it lives, however crippled and bruised—like the unfortunate eel which has been stabbed, skinned, dressed and in spite of all this is jumping in the pan. Another example is the tenacity well known among the economists with which the price-system is always coming again to the surface after having been submerged by all kinds of interference. There is such a thing as the “*Eigengesetzlichkeit der Wirtschaft*” (after the German terminology), which cannot be ignored, and which is always leading to the question whether and how far a certain measure of State intervention is really effective. With rare exceptions all systems of price maxima or price minima have broken down. The State control of foreign exchanges is circumvented by illegal dealings, and so forth. The same reasoning, now, may be applied to the international trade. Here I am not speaking of the smugglers, although the economic importance of this trade is in an inverse proportion to its respectability and in direct proportion to the height of the customs barriers. I am speaking rather of the fact that in the last fifty years the volume of world trade on the one hand and the restrictions of foreign trade on the other have increased together. Therefrom we are allowed to draw the conclusion that the forces behind the development of the international economic system must have been immensely powerful to overcome the increasing restrictions and to make room even for an increase of world trade. A superficial glance at modern tariff history seems to prove that in the struggle between liberalism and protectionism the former has been driven to the wall. But this first impression is evidently misleading, since the growth of protectionism did not succeed in preventing the realization





of the ideal of the early liberalism on a scale which has certainly outrun the previous expectations. Until very recent times, therefore, the intrinsic logic has conquered the opposing forces, and there is no convincing reason for not expecting that it will be again triumphant after the present crisis has been dissipated.

All these remarks, which may seem somewhat of a digression, are in fact necessary for a better understanding of German tariff history, especially in its latest phases. As I said earlier in my lecture, the tariff history of Germany can be conceived as the resultant of two components: the logic forced upon a country with the economic structure of Germany on the one hand and the considerations striving against this logic on the other hand, the one aiming in the direction of a liberal, the other aiming in the direction of an illiberal commercial policy. It was further stated that, three times in the course of its history, the second set of forces has been able to set its mark on the commercial policy, each time in a more powerful manner: firstly, in 1879, secondly in 1902, and thirdly in the period from 1928 onward, each time during an economic depression. As is the rule in these matters all over the world, the struggle between the two parties has sometimes been a rather wild and noisy one, each party putting forward its case with the exaggerations which are only natural in this field, giving thereby the impression that the issues were of a much greater importance than they were in fact. All the wildness of this struggle cannot conceal the fact that, even at the very crest of the protectionist waves, Germany has paid its tribute to logic and reason—sometimes, forsooth, a very niggardly and reluctantly given tribute, but nevertheless a tribute. That is, perhaps, best illustrated by the most recent developments to which I have already had several occasions to refer. Since about 1930, all forces inimical to a liberal tariff policy have been let loose on an entirely unprecedented scale. Several circles of Conservative Radicals—if I may use this term—gaining rapidly in strength and influence, especially among the younger generation, were conducting a very

clever propaganda in favour of almost complete economic independence. Very prominent at one time in this propaganda was the circle around the monthly *Die Tat*, commonly called "Der Tat-Kreis." For about two years the influence of this group was very great, especially during the chancellorships of Papen and Schleicher. Their general attitude was not very different from the attitude of the National-Socialists, except that they had a certain inclination towards Russia and that they were lacking the characteristics of a mass movement like the National-Socialist movement. At all events, the National-Socialists made, in their propaganda before they came to power, the widest use of the popular sentiments towards economic nationalism. Thus, at one time, the word "Autarky" was nothing short of a national slogan. And yet, it cannot be said that the victory of the National-Socialist movement has been the victory of unmitigated economic nationalism. On the contrary, an unprejudiced examination shows that, while a more popular propaganda is still going on, the new leaders have made some unmistakable efforts to silence the wildest fire-eaters and to make it clear that they realize the vital necessity of foreign trade. As in economic policy in general, so also in the tariff policy of Germany, there have not been any revolutionary changes since the victory of the National-Socialist movement. What has been done in the way of shutting off Germany from the world economy has been done to a great extent under the previous Governments and even under social-democratic leadership, and there seem to be even certain signs of growing awakening to the truth that several of the tariff fortifications built up during the last years will prove quite untenable if the programme of economic reconstruction is to be carried out successfully. Deprecating liberalism does not mean, after all, that with the term also the real content of economic liberalism has been discarded. That is not said in an excessively optimistic vein, but only to show that, to all appearances, economic liberalism is not just a caprice, but something much deeper and much more in accordance with the inner logic of things.



## CHAPTER V.

### INDUSTRIAL PROTECTION IN GERMANY.

Now, at last, the ground has been thoroughly prepared for a closer examination of the more intimate details of the German commercial policy. From the Bismarck tariff of 1879 up to the present day, Germany has had a protective tariff with a continuous upward trend of rates until they reached the sky-high dimensions which is the fashion in these days. What were the real forces behind this trend? For the sake of simplification, we are entitled to concentrate our attention on two main branches around which the protectionist movement in Germany has centred up to the present day, viz. the iron and steel industry (Schwerindustrie) and agriculture. We may even carry the simplification still further by saying that the commercial policy of Germany from 1879 to almost the present day can be compared to an ellipse, the focal points of which are iron and rye. That looks like a rather strange combination, requiring further explanation for which a short historic review will be a great help. From all we know of the circumstances leading to the tariff reform of 1879, it seems certain that it was the iron and steel industry that was pressing most actively for a change from free trade to protection, while the agrarians remained at the beginning rather inactive. The situation was rather like this: The iron and steel industry, politically organized in the new National-Liberal Party, wanted protection, but they could not get it without the consent of the mostly agrarian Conservatives who had been free traders up to then. It was not until the outbreak of the great agricultural crisis brought about by the crushing

competition of the virgin soils of America that the agrarian Conservatives joined definitely the protectionist block of the manufacturers. At that moment the scales had been turned in favour of all-round protection. The case of the duties on iron and steel is not very difficult to be comprehended. The immediate aim was to mitigate the situation engendered by the economic depression which was, as usually, most pronounced in the iron and steel industry. Moreover, attempts were made to apply the infant industry argument—the idea of the “*Erziehungszoll*” of Friedrich List—to the German *Schwerindustrie*. This reasoning sounded rather plausible since at that time the German *Schwerindustrie* was only in the first stage of development. But there is perhaps no better illustration of the weakness of the reasoning of Friedrich List than the subsequent development which ensued after the tariff reform. As everybody knows, the crucial point of the infant industry argument is the question of how to get rid of the educational duty after it has fulfilled its mission of protecting the industry during its infancy. It will prove extremely difficult to find any example in the tariff history of any country where the educational duty has been abolished after having fulfilled its mission. As far as I know, the nearest approach to this ideal case has been the way in which, after the stabilization of the mark, the German automobile industry has been protected temporarily against the crushing competition of the automobile industry abroad. Under the altogether artificial conditions of the war time and the inflation period, the German automobile industry had remained far behind the progress made abroad. The unrestricted import of foreign cars would have ruined the German automobile industry while, on the other hand, it was reasonable to assume that, in a very short time, it could make up for the advance of the foreign production. Thus it was almost an ideal case for tariff education or, rather, re-education, assuming that guarantees were given that the protection would not become permanent. To secure this, it was provided that, in several stages determined

in advance, the tariff should decrease automatically. It seems that Friedrich List relied on a kind of automatic disappearance of the educational duty, his reasoning being that once the home industry had grown so far as to suffice for the demand of the home market the competition of the home producers would make the duty ineffectual. This reasoning was quite sound, but he did not take into consideration that competition might be replaced by monopoly. That is exactly what happened in the case of the German *Schwerindustrie*, as well as in the United States. The duties on iron and steel proved a very strong incentive for the formation of monopolistic organisations (among which the well-known *Kartell* became the most favourite form) since it was only in this way that the iron and steel manufacturers could secure themselves against the efficacy of the duties being gnawed off by the growing output of the iron and steel industry. The tariff, moreover, became indispensable to fortify the monopolistic position of the *Kartells* on the home market, as it enabled them to raise the prices for home consumers above the prices on the world market by the amount of the duty, and to gain thereby the means for selling cheaper abroad, practising thus a policy which has been termed, in a rather loose way, "dumping." In this way, there was established a mutual interdependence between protectionism and monopolism, the former instigating the latter and the latter instigating the former. The tariff had changed its function. What once had been a protective tariff had now become a *Kartellschutzzoll*. While formerly the tariff had the function to protect the industry against foreign competition on the home market, now a device had been invented to extend the protection to the foreign markets. The originally defensive tariff had become an aggressive one. It is, of course, an exaggeration to say that there is perfect correlation between protectionism and monopolism, but that the coefficient of correlation is a rather high one nobody can deny. It is of no avail, in this connection, to point to the example of England where, even in the

glorious time of free trade, industrial combinations were by no means totally absent. It is obviously irrefutable that as long as a product is unprotected, it is impossible for an industrial combination to raise the price on the home market above the price on the world market by more than the relatively small margin of the cost of transportation. Therefore, the industrial combinations in England could, generally, not be called monopolistic as long as there was no duty, with the exception, of course, of those products for which the English producers had a natural or a legal monopoly so that foreign competition was practically non-existent.

The relation between protectionism and monopolism which I have referred to seems important enough to justify some further remarks of a still wider range. In the great trial against capitalism now going on all over the world one of the main charges against the defendant is the alleged degeneration of capitalism by rampant monopolism. For the sake of the argument, let us assume that monopolism is a degeneration of capitalism (what, in certain defined cases, might well be disputed). Does that mean that the basic principles of our economic system are responsible for this? It will be an extremely difficult task to prove that convincingly. In this, like in the greater part of similar cases of degenerative tendencies of capitalism, it can be shown that at the bottom of it there is almost always some act of interference with the economic process. In other words, in a surprisingly great number of degenerative tendencies of capitalism the fault is on the part of acts and ideas which are congenial with the attitude of the anti-capitalists. Thus it is one of the plain cases where the plaintiff is turning into the defendant. Those who are charging capitalism with rampant monopolism are mostly the same persons who never tire of ridiculing the philosophy of free trade and of invoking not less but more protection, not realizing that, in doing so, they are fortifying still further the position of monopolism. Instead of recommending the logical remedy, viz. : lowering the tariff, they demand that the Government shall take over

the monopolistic industries or control them. . Or they even go further and say that capitalism as a whole is rotten and must be replaced by socialism or—to use the new euphemistic word—by a planned economy.

Of course, our theory about the close relationship between protectionism and monopolism no longer holds water if the monopolistic movement becomes international in character as it has more and more become during the last decades, and especially in the later 'twenties, under the leadership of the German and French *Schwerindustrie*. If a strong international Kartell exists it is no longer sufficient to abolish protection for the products in question, since foreign competition cannot work freely any more. That is not to say that the duties have now become useless for the protected industry. On the contrary, they are an integral part of the whole international monopolistic system just as they were formerly an integral part of the national monopolistic system. Only their functions have changed. While, formerly, they had the function of making possible a national monopoly by limiting foreign competition, they have now the function of fortifying the position of the national Kartell in the negotiations with the foreign national Kartells with the object of forming an international Kartell. Thus the duty, instead of being a *national* Kartellschutzzoll, has now become an *international* Kartellschutzzoll. The connection between protection and international monopolism has still another aspect. We found that protection and national monopoly, both interdependent, have made possible the policy of dumping on a large scale. In mentioning this policy of dumping, we are touching on a subject of a most complicated nature about which an extended literature has sprung up in recent years. The impression one gains in reading this literature is that it is very difficult to make up an exact balance-sheet of the advantages and disadvantages of dumping from the different points of view. However that may be, two things are certain. The one is that there is no copyright on dumping, but if all countries are practising the

same thing it becomes a nuisance for all which every country concerned has an interest to abate. The other thing is that, even if the policy of dumping is not adopted by any other country, the foreign producers of finished goods will profit by the dumping prices of raw materials and half-finished goods and thus be enabled to undersell the home producers of finished goods at home and abroad, the more so since the latter will have to pay the enhanced home prices of raw materials and half-finished goods. Thus it is a very complicated situation which has to be faced, illustrating excellently the wide repercussions of protection. It is not to be marvelled at, then, that in Germany the duties on iron and steel have aroused from the beginning until the present day the opposition of the manufacturers of finished products (the engineering industry, the hardware industry, etc.) and that an endless dispute arose between these two groups. In order to make politically possible the duties on iron and steel it was absolutely necessary to appease the manufacturers of finished products in one way or another. Some mitigation of the conflict was brought about by the process of vertical amalgamation between iron and steel producing firms and manufacturing firms. The problem was really tackled when the great iron and steel Syndicates and the Kartells of the iron-fabricating industries agreed upon the payment of drawbacks computed for the exported part of the production of iron and steel goods and destined to compensate somewhat for the enhanced home prices of the raw materials. After the war this agreement was replaced by an agreement between the Deutsche Rohstahlgemeinschaft and the Arbeitsgemeinschaft der eisenverarbeitenden Industrie (Avi). According to the abbreviated name of the latter association the drawbacks are now called "Avi-Rückvergütungen." The details of this agreement are very complicated, and the whole scheme is far from working satisfactorily, owing to the irreconcilable conflict of interests. Now, it is clear that as far as the international Kartells are eliminating the policy of dumping they are also serving the interest of the more

advanced fabricating industries. For, since the practice of dumping is eliminated for the countries covered by the international Kartell, the damage done to these more advanced industries by iron and steel protection is greatly diminished.

The connection between protection and monopoly can clearly be seen in the fact that the pre-war attempts at framing an international monopolistic organization of the Central-European iron and steel industries were resumed only after Germany had regained its tariff autonomy in 1925. In the autumn of 1926 the iron and steel industries of Germany, France, Belgium, and Luxemburg founded the Internationale Rohstahlgemeinschaft (IRG). This was a simple Kartell of the type which in the German literature is called Quotenkartell. That is to say, the participants agreed only upon fixed maxima of the national production without any provision for prices and export regulations. The latter was attained in 1930, but the subsequent depression made the provisions work rather unsuccessfully, and the IRG came to an end in 1932. More successful were the international Kartells framed for a number of half-finished products (bar-iron, girders, rolled plates, tubes, pipe, etc.). Very recently (June, 1933) the old IRG was re-established under the name "Internationale Rohstahl-Export-Gemeinschaft" (IREG) with the expressed purpose of regulating the *export* of steel products of the national Kartells belonging to this organization. Together with the international Kartells for the half-finished products, an intricate monopolistic system for the European steel industry has been worked out which some enthusiasts are already regarding as the outline of a "Paneuropa" for the iron and steel industry. Whether Europe will be made happier by that is a question on which the opinions will be somewhat divided, but into which we cannot enter here.

The Avi-Rückvergütungen which I have mentioned cannot conceal the fact, of course, that steel protection and monopoly combined are a very heavy burden for the rest of the German economy. How far the internal price level of

steel products is above the world price level may be gathered from a more recent price list of the German producers. According to this list<sup>1</sup> the export price for bar-iron of the IREG is, from July, 1933, onward, about 60 RM., and the inland price 112 RM., and for the other products correspondingly. The *Avi-Rückvergütung* has not been deducted from the inland price, but even then the difference is surprisingly great, since the price accorded after this deduction is still 79 RM. To this it must be added that the *Rückvergütung* is paid only upon certain conditions and only for a part of the home consumption. There is no denying the fact that the rest of the German economy is paying an extremely heavy bill for which several computations have been made, one of these estimating the burden laid upon Germany by protection and monopoly combined at about 1½ milliards of Reichsmark for the period from 1925 till 1929.<sup>2</sup> This estimate may be exaggerated, but the real damage done is greater than can be calculated numerically and more subtle in character. It would not be so bad if the economic burden of iron and steel protection consisted only in conducting a stream of money from the consumers to the producers of iron and steel. But the economic burden means more. It means lack of elasticity of the whole system of prices and costs, and it means faulty investment of capital on a huge scale. I am convinced that both factors have contributed heavily to the special severity of the economic depression in Germany in the last years, a conviction that has become almost *communis opinio* in Germany. As far as I have been able to familiarize myself with the conditions in other countries, I believe this to be a German specialty. It was really disastrous that, until the later stages of the depression, the German monopolies for the most essential raw materials did not adapt their price policy sufficiently to the changed circumstances. It was with reference to this monopolistic price policy that the Institut für Konjunkturforschung

<sup>1</sup> *Die Wirtschaftskurven der Frankfurter Zeitung*, July, 1933, p. 172.

<sup>2</sup> *Magazin der Wirtschaft*, 1929, No. 49, p. 1836.



pointed to the divergence between the free and the fixed prices so detrimental to the elasticity of the economic process during the depression. In view of this experience it may seem strange that, in the past, the Kartells were sometimes regarded as a stabilizing factor smoothing the business cycle. This opinion was not very well founded, indeed. For it is obvious that holding certain prices rigid is not identical with economic stabilization but rather detrimental to it, since the downward movement of the uncontrolled prices is thereby accentuated, and since stability of prices in a certain industry means unstability of production and employment. The experience made in Germany in recent years has confirmed this simple reflection. It is equally easy to see that monopoly profits are very apt to lead to faulty investments, in contrast to the view which has been held by many industrialists, that corporate surplus was the best form of saving of capital. The corporate surplus, however, is very apt to be invested in the corporation's own plant, even if the profit gained therefrom is lower than the interest gained from investments placed on the capital market.<sup>1</sup> The formation of capital by investment of corporate surplus in the corporation's own plant ("Selbstfinanzierung") is by no means the best, but rather one of the more dubious forms of the formation of capital. This also has been corroborated by the recent experiences in the German iron and steel industry. For this we have no less an authority than the official Enquêteausschuss which, in a special report published in 1930, made the heaviest charges against the iron and steel industry for having built up a plant with a capacity of production far ahead of the potential demand. Thus

<sup>1</sup>The subject has been dealt with at greater length in my book: *Die Theorie der Kapitalbildung*, Tübingen, 1929. On rather similar lines, the investment of corporate surplus has been attacked by Professor Francesco Vito in his very stimulating article "Il Risparmio Forzato e la Teoria dei Cicli Economici," *Rivista Internazionale di Scienze Sociali*, January, 1934. He goes so far as to expose this investment of corporate surplus as one of the major causes of the cyclical disequilibrium between saving and investment.

protection of the iron and steel industry in its direct and indirect effects has caused waste and friction on an appallingly great scale.

While the iron and steel industry, from the beginning to the present day, has been, among the industrialists, the main stronghold of protection, the greater part of the finished products industries has, for very obvious reasons, been more inclined to a liberal tariff policy. Operating mostly on an export basis, and being more or less unable to form strong Kartells, they are or rather should be natural advocates of a liberal commercial policy. Furthermore, as they use much man-power of a rather skilled kind, they represent one of the most important assets of the German economy on which it has to rely for earning the greater part of the foreign exchanges necessary to meet the exigencies of import and foreign debt service. On the other hand, these industries do not possess strong organizations for pushing forward their case, nor even the sense to realize clearly their own position. In this respect, however, a certain change has been noticeable in recent years. Particularly conspicuous has been the activity of the engineering industry, whose central organization, the "Verein der deutschen Maschinenbauanstalten," has become more and more the focus of the more liberal tendencies, presenting the case against excessive protection in a remarkably able and constructive manner. This industry was especially entitled to do this, as it is the most important export industry of Germany. (This term "export industry" needs a short explanation, since it has a double meaning. Firstly it may be applied to an industry exporting a great part of its production, in other words, operating on an export basis. Industries exporting more than 50 per cent. of their production are the glass and pottery industry, the musical instruments industry, the toy industry, and the like.<sup>1</sup> Industries exporting between 20 and 50 per cent. are the hardware industry, the paper industry, the chemical industry,

<sup>1</sup> *Vierteljahrhefte für Konjunkturforschung*, 1927, No. 4, p. 32 ff.

the iron and steel industry, the silk industry, the engineering industry, and similar industries. Only a minor part of their production is exported by the main textile industries, the cement industry, etc. Essentially domestic trades are the industry of food and kindred products, the clothing industry, the lumber industry, etc. In a second sense, the term "export trade" may be applied to industries which contribute a large share to the total export of the country. And here the engineering industry heads the list, although in the first sense it is an export industry only in a less degree. Using the foreign trade figures for 1932 (the figures for 1933 are not yet available), we find that 73 per cent. of the total export of Germany consisted of finished industrial products, and that the export of machines ranks first, the export of chemical and pharmaceutical products second, and the export of textile goods third. This order of relative importance is, of course, always changing within certain limits according to the vicissitudes of foreign trade. Thus it seems likely that the relative importance of the engineering industry will be found to have somewhat diminished during the last year, owing to the wholesale cancellation of Russian orders.)

It may well be asked why the engineering industry, although to be classified as an export industry only in the second sense of the term, has become such an outstanding advocate of a liberal commercial policy, since, important though the export of machines is from a national point of view, the home market is still much more important than the foreign markets for this industry. Why, then, does not the engineering industry take the same stand as the iron and steel industry? The very simple answer to this question is that the special character of the engineering industry makes it impossible to organize it in strong Kartells, and that the great variety of machines makes it less important for the engineering industry to be protected against foreign machines, which are more or less non-competitive, than to gain free access to the foreign markets and to have the lowest possible costs, both aims being fulfilled by a liberal com-

mercial policy. (We have, of course, to differentiate between the separate branches of the engineering industry and to distinguish those making machines exposed to more or less strong outside competition and those where the international division of labour is most pronounced, and the machines in question are a German specialty, such as machine tools and the like. In the latter case there is, of course, a clear balance against protection.) Here we come to the category of those industries where Germany has what is sometimes called in a rather loose way a monopoly on the world markets. The outstanding example is perhaps the optical industry, at least as far as the more refined articles are concerned. You cannot make a Leica anywhere else in the world, at least not at the moment nor perhaps for many years to come. Curiously enough, there are in Germany a number of industries of the very opposite character which nevertheless are more or less without competition from abroad, viz. the industries producing cheap fancy-goods and glass-ware, wooden articles, imitation jewellery, etc., with the aid of workers combining great poverty with hereditary skill. The only competitors for this industry—which you find mostly in the mountains of Saxony, Thuringia and Bavaria in a form known as "Heimindustrie"—are nowadays Czechoslovakia and Japan. It goes without saying that the interests of all these industries are, on the whole, on the side of a liberal commercial policy, but their voice is too feeble to be heard by the side of the big megaphones of protection. As for raw materials, Germany has no monopoly, with the one important exception of potash, after the pre-war monopoly had been re-established in a sense after the war by the agreement between the German and the Alsatian potash industry. Here, in the case of the potash industry, we have a rare example of the discrimination between domestic and foreign prices being the reverse of dumping, viz. low domestic and high export prices.

A special case is that of the textile industry, where the guerilla warfare between the protectionist and the anti-

protectionist interests is going on all the time, without attracting much attention in the wider public. Here the conflict between the iron and steel industry and the finishing industry is reproduced on a smaller scale by the conflict between the spinning industry and the upper stages of production. While the economic structure of Germany as one of the great workshops of the world is truly reflected in the fact that her imports consist mostly of foodstuffs and raw materials, and her export mostly of finished goods, there is one great exceptional item on the side of import, viz. yarns of cotton, wool and silk. These are mainly imported from England, which still has an unchallenged position in the production of the finer grades of yarns, due to the climate and to other circumstances. It is obvious that the tariff on yarns is a great handicap to the finishing stages of the German textile industry. A special story is the case of artificial silk, characterized by the close relationship between protectionism and international monopolism which has been made familiar to us by the case of iron and steel.

While the great chemical industry, being mostly an export industry, belongs, on the whole, to the liberal side in the tariff controversy, the protection enjoyed by certain chemical products in which the German producers have to meet strong foreign competition has recently become conspicuous. Protection of this kind is, of course, especially dubious, since the products in question are mostly more or less essential raw materials for a great number of other industries. A striking example is the high tariff on mineral oils which have become so important with the modern motorization. Although Germany has no petrol tax, the price of petrol is extremely high (the more so as, until recently, the German car owners had to pay, in addition to that, an equally high automobile tax). The main reason for this is the high tariff on mineral oils which has been raised continuously in the recent years, not as a duty for revenue but as a protective duty. The quantity of mineral oil

produced in Germany is negligible as far as natural resources are concerned, but it is well known that the production of synthetic mineral oil has been very much developed during the last years under the protection of the high tariff. When you drive with your car through Germany you will see everywhere billboards urging you to use German petrol. About this case one could write a voluminous economic treatise, as it illustrates, in an illuminating way, a number of points of general interest. People are very apt to admire inventions of this kind without giving due attention to the question of the cost of production. Generally, they will understand even in these more enlightened days of economic nationalism, that producing oranges in Scotland—technically possible though it may easily be with the aid of hot-houses—means self-inflicted impoverishment. But if you present to them an invention in which a tremendous amount of incomprehensible and scholarly thinking has been invested, and if you add that this has been done in the interest of the nation, you are very likely to override the common-sense view of the matter. Now, we have every reason to admire inventive genius, just as we admire the theory of quanta, but nobody dreams of giving products made on the application of the theory of quanta special tariff protection because it costs more to produce them. As a matter of fact, we must carefully distinguish between the technological and the economic side of production and be on guard against the illusion that solving the technological side means solving the economic side too, which is identical with the crucial problem of the cost of production, *i.e.* with the problem of whether the productive forces of the country are better used here or somewhere else. It is just this kind of reasoning which must be applied to the German protection of the production of synthetic mineral oil, because the fact that it was possible to develop this production and to maintain it only by continuously raising the tariff is an irrefutable proof that it is highly uneconomical. In view of the ample and cheap production of mineral oil abroad it is highly

improbable that its synthetic production will ever become economical. At least, the very small degree of probability to the contrary does not justify the heavy burden laid on the consumers of mineral oil at the present and for the near future. It is somewhat disquieting to think that all this would not have happened if some technical genius would not have made the scientific discovery which has made this production of synthetic mineral oil possible. We shudder to think what would happen if somebody discovered a way of producing synthetic copper or cotton, whose production would not cost more than 150 per cent. of what it costs in the countries of its natural production. In all countries where this discovery was made use of we would hear the familiar slogan: "Use the products of your own country!" and again everybody would be made so much poorer. That is certainly a variety of the old theme "Progress and Poverty" which would be new even to Henry George. It would perhaps not be a bad idea to grant no one a patent unless he binds himself never to demand protection for the production based on his invention.

The high price of petrol in Germany which I mentioned presents still another aspect which is a good illustration of how complicated things have become nowadays. The law provides that a certain percentage of alcohol sold by the German monopoly of alcohol (Reichsbranntweinmonopol) has to be mixed with the petrol. This may sound rather curious. The explanation of it is that the monopoly of alcohol has a tremendous surplus of alcohol which it is trying to get rid of in one way or another. To understand this is really a science of its own. The gist of it is that alcohol in Germany is, under the restrictions laid upon industrial distilleries, mostly produced by agricultural distilleries which are considered an indispensable part of the agricultural system prevailing in Eastern Germany as providing an outlet for the surplus of rye and potatoes. Now, it has become one of the objects of the policy of the Reich monopoly of alcohol to give to this agricultural system a special aid by buying

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large quantities of rural alcohol at satisfactory prices. This policy, in turn, has led to the great surplus of alcohol which is now by force being partly conducted to the carburettors of our cars. Not everybody realizes that in driving a car he is helping Eastern agriculture, although sometimes the motor does, protesting against this policy by knocking badly. Having found in the tariff on mineral oil the link between industrial and agricultural protection, we now can pass definitely to the very important question of agricultural protection in Germany.



## CHAPTER VI.

### AGRARIAN PROTECTION IN GERMANY. GENERAL APPRAISAL.

FOLLOWING the rule that it is the essence of science to simplify complicated and, therefore, confusing matters by setting the essential points in the foreground, I ventured the simplifying statement that, from the beginning, the main pillars of the German commercial policy have been the duties on iron (or steel) and rye. The Bismarck tariff of 1879 was based on the union sacrée of the iron and steel industry and of the great grain-producers of Eastern Germany. This union had a distinctly feudal flavour in it and has conserved it to the present day. This statement should not be held to imply any judgment of ultimate values, on which it is rather difficult to arrive at a common agreement. But the statement is intended to convey the idea that it is perhaps less possible in the case of German commercial policy than in the case of any other country to come to a real understanding without due consideration of the political and sociological elements involved therein. That will become quite clear when we consider the situation of the later 'seventies and the 'eighties, at the time when the framework of the modern commercial policy of Germany was being built.

As in a great number of other European countries, the backbone of German agriculture was the production of grain when the great agrarian crisis of the 'eighties shook European agriculture in its foundations. In this crisis two courses were open for the different countries. The one course, followed by Denmark, Holland and Belgium, was that of adapting the agricultural system to the new conditions by

restricting the production of grain and developing that part of agricultural production which the Germans call *bäuerliche Veredelungswirtschaft*, *i.e.* stock-raising, dairy-farming, fruit-growing, and truck-farming, based on the utilization of grain and green fodder grown on the farm or bought on the market, and mainly in the hands of the small farmers. In this way the countries mentioned could face the competition of the cheap American grain without protection, though after a painful period of transition. Germany, like Austria or France, did not go this way of "Danization" but followed the other course of preserving the old agricultural system by aid of protection. That was the meaning of the Bismarck tariff of 1879 and of the further course of German commercial policy. Preserving the old agricultural system, however, meant at the same time preserving the old social system of German agriculture which was and is still characterized by the fact that Western Germany is predominantly a district of peasant farms and Eastern Germany is predominantly a district of large estates, owned by families who have always exerted a great political influence (which they had to share later on with the great Western industrialists). It is this dualism of the German agricultural system, with the Elbe as dividing line, which we must always keep in mind. Eastern Germany is essentially colonial land with a history of its own, and has preserved some of this character up to the present day. Western Germany is in its greater part densely populated, is the principal seat of German manufacturing industry, and in its agricultural sections is dominated by the peasant farm. Eastern Germany, on the other hand, is still a district with wide open spaces, very little industry, and very few peasants. Common opinion in Germany has, almost without any exception, come to regard this state of things as unwholesome and to look upon an agrarian reform which would break up a great number of the big estates into small peasant farms as one of the most important objectives of a far-seeing policy. Long before the war attempts were made in this direction, but not much progress had been

made, for several reasons, among which the apparent contradiction between this policy of land reform and the agrarian tariff policy, aiming at preserving the economic basis of the great estates, is, perhaps, the most important one. When in 1918 the Revolution changed the political structure of Germany, at last the great chance had come for an agrarian reform on a large scale like the agrarian reforms which at that time swept all over Central and Eastern Europe. It is still one of the great mysteries of our times why nothing of this sort occurred in Germany, and why the parties of the Left made no use of this heaven-sent opportunity of doing something big and important which would have changed the economic and social structure of Germany in a most wholesome manner, giving Eastern Germany back to the peasants and attaching thereby this most important class to the new régime. Nothing perhaps illustrates better the inner weakness of this régime which now belongs to the past. True, more has been done in the policy of peasant settlement than before the war. But since after 1925 the agricultural protection of the pre-war days, concentrated on the protection of grain, was resumed with ever-growing resoluteness, it was impossible to change the agricultural system of Eastern Germany thoroughly. In addition to this, the bureaucratic clumsiness of the policy of peasant settlement was a lamentable obstacle to any conspicuous progress. It is well known that even the wholesale bankruptcy of the Eastern estates in the last years, though a sure sign that this agricultural system was no longer tenable, brought about no visible change, since subsidies were paid in enormous sums in order to enable the bankrupt landowners to carry on. Reichskanzler Brüning tried to stop this, aided by one of the more far-seeing of the landowners themselves, Schlange-Schönningen, but that was just his last act before his Government was overthrown, as it was the last act of the Reichskanzler von Schleicher to permit an investigation by the Reichstag into the possible misuse of the Osthilfe. There is nothing at the moment which warrants the assumption that this

state of things has been changed since the new Government came into power, although some of the National-Socialist leaders have shown a sincere desire of moving against the great landowners.

It has sometimes been said that this agricultural system of Eastern Germany, whose preservation has always been the main objective of German agricultural protection, cannot be altered without the greatest damage to agricultural production, since it is the result not of historical, but of natural conditions. One refers to the climate and to the more sandy soil prevailing in the East, which are supposed to leave as the only alternatives, growing grain and potatoes, or using the soil for forest culture. The prominence given to rye in the German agricultural protection has again and again been explained by these alleged inferior qualities of climate and soil in the East. Although there is an element of truth in these claims, one can point to facts proving that the agricultural system is not condemned for ever to this rather uninviting alternative of grain (specifically rye) and potatoes, or pine trees. The first fact is that there is really no great difference between the natural conditions in the East and those in many parts of Denmark and of the Baltic countries, where a system of diversified farming has been developed. The second fact is that there are many districts in Eastern Germany not differing in soil and climate from the rest, where smaller farms have long been doing quite well with dairy-farming and stock-raising. What is lacking in many parts of Eastern Germany are well-irrigated meadows, but this gap could have been filled by melioration schemes, the cost of which would have been covered by a small fraction of the gigantic sums poured out for the preservation of the old system in the form of tariffs and subsidies. Finally, it must be said that only an elementary knowledge of economics is sufficient to show that it is the function of the rent to regulate the use of the soil. If the soil is inferior, the rent will be lowered until it pays to cultivate it or, if not, the soil will be left to forestation or hunting grounds.

Germany is not rich enough to afford the luxury of cultivating every patch of land, no matter how much it costs to do that. People have no vested prerogative to grow rye, no matter where and how and how much, and to let the rest of the country pay for it. As a matter of fact, the most inferior soils of Eastern Germany were not turned into farm land until after the increase of the duties on grain by the Bülow tariff of 1902, and there is no reason why they should not be turned back into woodlands, however painful such an operation may be. After much money has been wasted to avert this necessity, the process of shifting is now slowly going on.

Now, we are able to reach the conclusion that it was the main fault of the agricultural protection of Germany since 1879 that it aimed not only at preserving but even of increasing the production of grain, and especially rye, consolidating thereby an agricultural system which it cost milliards every year to preserve against the tendencies inimical to it. It really looked as if growing rye *was* considered a vested prerogative. The grain-producers got the lion's share of agricultural protection, while the peasants had to pay higher prices for grain used for feeding purposes. The worst of it was that German agriculture was being accustomed to looking for help from the State, so much so that the initiative of the farmers was lulled. Everybody agrees to-day that the vocational education of the farmers was badly neglected up to the present day, and that the farmers became more interested in the intricacies of the tariff than in improving their marketing organizations. Lobbying was considered more essential than marketing and bringing down the cost of production, and everybody who dared to suggest that a solution of the agricultural problem should be sought in these latter directions was attacked fiercely and accused of being an enemy of agriculture or even of something worse. In the technique of production German agriculture was able to hold its place, but in economic adaptability it was far outrun by countries like Denmark and in some respects also

by the United States. Thus it happened that when after the war the reorganization of German agriculture became more urgent day by day, it was generally felt that it was those countries from which the German farmers had most to learn.

When we look for the reasons given for this system of agricultural protection, we must be somewhat struck by their vagueness. It is really very difficult if not impossible to deal scientifically with the common phrases about agriculture being the foundation of the nation because all these phrases are more or less question-begging. It had to be proved that there was really no other alternative than that between this policy and the ruin of agriculture, and this proof was not forthcoming in a convincing manner. To point to the discouraging example of England was not sufficient, because it can be shown that the case of England is different, being characterized by the coincidence of a number of special circumstances, among which the social side of English agriculture is perhaps most prominent. The cases of Denmark and Holland, moreover, prove that free trade in agriculture may mean the very opposite of ruin. It seems fairly certain that German agriculture would not have been ruined in the absence of protection, but would have changed in a manner that would have given the family farm a more prominent place, and would have fortified German agriculture to a much greater degree against the agricultural crisis of the present day. In this connection it must be remembered, however, that industrial protection must also have gone if agriculture was not to have been handicapped. The best way, therefore, to keep agriculture as the backbone of the nation would have been free trade all round instead of all-round protection.

In this connection, it has also to be borne in mind that the real foundation of a nation is not agriculture in the general sense of the term, but agriculture run by peasant farmers, while for any sort of bonanza or plantation farming the old saying of Pliny holds always true: *latifundia perdidere*

*Romans.* It is not always duly recognized that the industrialization and urbanization of Germany could not have proceeded as rapidly as it did without the agricultural system of Eastern Germany. The German peasant farmer is a man who sticks to his soil under any circumstances whatsoever. As long as he owns his soil he does not leave his farm. If he has not any land he will prefer farming to any other occupation provided that you offer him a patch of land. That is the reason why the drift to the cities, which has always been duly lamented over, has never been in Germany a drift of farmers but a drift of two other groups of persons: firstly, of agricultural labourers coming from the great estates in the East, and, secondly, of farmers' sons without soil. In both cases, the agricultural system of the East was at the bottom of it. It drove the labourers who would not endure the social and economic pressure connected with the big estates away to the cities, and it withheld the soil for which the farmers' sons were longing. Both groups went not only to the cities, increasing there the industrial proletariat, but also to the virgin countries overseas, where they became most valuable pioneers in cultivating the American and Canadian plains. The agricultural labourers leaving the great estates in Eastern Germany were more and more replaced by Polish and Russian labourers. Now, agricultural protection in Germany was one of the most powerful means for preserving this agricultural system of Eastern Germany. It is really driving the joke too far to present this system of agricultural protection as a system fortifying German agriculture as the backbone of the nation—a system that was to a great extent responsible for the fact that Eastern Germany remained a region of big estates very sparsely populated, and for driving away to the cities and oversea every year thousands and thousands even of these few people, and for replacing them partially by Slavs.

*Prima facie* another line of argument which has always been very popular in Germany sounds more impressive. This argument boils down to the assertion that agricultural

protection was necessary in order to make Germany, in case of war, as little as possible dependent upon imported supplies of foodstuffs. This argument is, of course, not essentially unsound, but it is not absolutely watertight. First, it may be said that the scarcity of food was one of the main reasons of the defeat of Germany in 1918, a scarcity which the pre-war agricultural protection had not averted. It may be replied that this only proves the insufficiency of the pre-war agricultural protection, but I believe that it proves quite another thing. It proves that it is impossible to build up an industrial system like the German and at the same time develop agriculture so far as to render the country independent in the provision of food. But for the purposes of war the former is just as essential as the latter. Furthermore, if Germany gets involved in a war which shuts it off from the outside world its fate is doomed anyway, as the World War has amply shown. It is better to avoid such a war than to try the impossible. But, in spite of all this, the demand for "*Nahrungsfreiheit*" is still very popular in Germany. (I may mention in passing that this is a very curious word for a state of affairs which is characterized by the absence of liberty in buying the kind of food we want.) This demand for self-sufficiency is based to-day not only on military arguments but also on the idea that the necessity of importing foodstuffs involves also a sort of *economic* dependence. Needless to say that this idea is like other similar ideas in being just as wrong as it is popular. If Germany is dependent on other countries in the import of foodstuffs, those other countries are dependent on Germany in the import of industrial products. It is just that mutual dependence involved by the division of labour system which is the basis of our total economic and social system, and this sort of dependence is obviously less intolerable than that awaiting us if we would make, like the Hindoo peasant, our bare subsistence dependent on the mercy of the weather.

Another question is whether the object of making



Germany independent in the import of foodstuffs is attainable within practical limits. This question has always been hotly debated, with many exaggerations on both sides, though more on the optimistic than on the pessimistic side. The efficiency with which German agriculture has been able to contribute a large share to the total amount of foodstuffs needed by the growing population is astounding and altogether to the credit of the German farmers. Certain facts, however, are very apt to be overlooked. The first fact is that this result could have been obtained only by concentrating agriculture on the production of products most suitable for the conditions in Germany and by leaving the production of others more and more to foreign countries. It must not be forgotten that, in the past, German agriculture, like the agriculture of the other European countries before the industrial era, provided the population not only with food but also with most of the raw materials for clothing. This, of course, has been totally changed. Sheep pastures have become a rare thing in Germany, and so has flax acreage. The gap has been filled by foreign wool, hemp, cotton and silk. It is darkening the issue to be silent on this problem because clothing is on the margin just as important as food. It would need a two-story agriculture to provide both. The same holds true for oil-seeds and leguminous vegetables, of which by far the greater part has still to be imported. That leads us to the second point, the essence of which is that the intensive agriculture which has been developed in Germany could not be carried on without large imports of feedstuffs, especially of oil-seeds, maize and barley. The third point is that even as far as foodstuffs only are concerned, attention has too much been concentrated on the unquestionable fact that agricultural protection in Germany has at last succeeded in securing the supply of grain for food purposes out of German soil, while too little is said about the wide gaps between domestic needs and domestic supply still open for many other agricultural products. According to an estimate recently made by the

Institut für Konjunkturforschung<sup>1</sup> the share of domestic production of the total consumption of food in 1932 has been as follows : for sugar, grain for nourishing purposes, brewery barley, potatoes and veal, between 99 to 100 per cent. or more (for rye appreciably more) ; for pork and beef, between 97 and 98 per cent. ; for butter and cheese, between 80 and 90 per cent. ; for fruits and poultry, between 70 and 80 per cent. ; for eggs and fish, between 60 and 70 per cent. ; for lard and leguminous vegetables, between 50 and 60 per cent. ; for fats of every sort, between 40 and 50 per cent. (for margarine, between 3 and 5 per cent.). In this estimate no regard has been given to the feedstuffs which had to be imported to attain even this result. If we reckon this in corresponding amount of pork and dairy products, we get the result that only 80 to 90 per cent. of pork and 60 to 70 per cent. of dairy products consumed in 1932 have come from German farms. Even if allowance is made for the possibility of a further increase of the productivity of German agriculture, it seems to be a fair conclusion that the achievement of agricultural independence is a task which has been beyond the powers even of the gigantic system of agricultural protection built up in the last decades. It is remarkable that the weakest point is still the supply of fats, whose shortage was also the sorest point in the food problem during the World War.

The list of reasons given above for agricultural protection in Germany is far from being complete. Some must be omitted, but a new line of reasoning which has been developed during the present crisis will be dealt with later. To expose the inner weakness of all these arguments is not to say that no case could be made at all for agricultural protection since 1879. If we do not want to appear as dogmatic adherents of the free trade doctrine, we must admit that agriculture has problems of its own arising from its peculiar character which make agriculture a rather loosely

<sup>1</sup> *Wochenbericht des Instituts für Konjunkturforschung*, 30 Aug., 1933.

working part of the whole economic process of our times.<sup>1</sup> This is not the place to work out a theoretical system of agricultural economics, which, by the way, is badly needed. Two points, however, have to be mentioned here. The first is that agriculture is of necessity perhaps less elastic and adaptive than any other part of the economic society and that, therefore, the process of adaptation takes a long time, implying great losses and far-reaching effects. The pricing process does not work as smoothly and perfectly as we have a right to assume for other economic branches. A high degree of inelasticity of demand, an equally high degree of inelasticity and of irregularity of supply, all this and many other elements are working together in bringing about the effect that ever since agriculture has become part of the modern capitalistic system its status has almost never ceased to be a subject for worry. That is the first point. The second is that this worrying about agriculture is especially justified since agriculture is really more than just an ordinary business which we can regard with cool detachment. On these and similar lines it can at least be made plausible that some kind of State intervention, if carefully and rationally conducted, might do more good than evil, provided that it aims not at preserving an untenable position but at smoothing the way for that new equilibrium which the natural tendencies are working to bring about. I believe it to be a great mistake to say that we are sinning against the spirit of liberalism by admitting that there are kinds of State intervention which are rational and useful, and I believe further that that is just the mistake which has discredited economic liberalism so much in these days.<sup>2</sup> What we need is a theory of the maxims of rational interventionism that while denouncing in a forceful manner interventionism as a whole, and mercilessly exposing its inconsistencies and even follies, would

<sup>1</sup> The subject has been touched upon at greater length in my articles "Das Agrarproblem der Vereinigten Staaten," *Archiv für Sozialwissenschaft*, Vol. LVIII, 1927, and Vol. LIX, 1928.

<sup>2</sup> *Vide* my article "Staatsinterventionismus" in the *Handwörterbuch der Staatswissenschaften*, 4th ed., Supplementary Volume, Jena, 1929.

work out certain general principles for exceptional cases where intervention could not be classified as sand thrown into the complicated machinery of our economic system, as it generally must. As I believe this kind of interventionism to be compatible with the general trend of economic liberalism I would like to call it "liberal interventionism."<sup>1</sup> One of the first principles of liberal interventionism should be that State intervention should never be conducted against the natural tendencies of economic development, but only in harmony with them, in order to bring about unavoidable changes with the least possible hardships and losses. Applying this kind of reasoning to the case of German agriculture, we must start with the statement that during the last fifty years the natural tendencies were distinctly working against the economic position of grain production in the old industrial countries in general and in Germany in particular, for reasons the general character of which might be sufficiently indicated by referring to J. H. von Thünen and his well-known theory about the localization of agriculture. At the same time the natural tendencies of the times were equally distinctly working against the economic position of the large-sized estates all over Europe, for reasons partly akin to the reasons of the declining grain production, partly derived from the changes of the economic and social structure of a country that is rapidly being industrialized.<sup>2</sup> In short, the natural tendencies were working against a great part of the German agricultural system both in its economic and in its social aspects. A sudden change of the economic and social structure of agriculture, however, is not a mere trifle to be dismissed in a light-hearted manner. To make the transition

<sup>1</sup> I am borrowing the term from Professor Rüstow (now at the University of Istanbul) who made use of it in his excellent speech at the annual conference of the Verein für Sozialpolitik in 1932 (*Schriften des Vereins für Sozialpolitik*, Vol. 187, 1932, p. 62).

<sup>2</sup> Very little has been written on this most important subject. The only treatment that has come to my notice is that by Arnold Dániel in his article "Das Vordringen der Agrardemokratie in Europa und die Lage des Grossgrundbesitzes in Ungarn," *Archiv für Sozialwissenschaft*, Vol. LXII, 1929.

more smooth might be, therefore, a legitimate object of liberal interventionism. Consequently, much might be said, on purely theoretical lines, for a well-dosed and carefully conducted policy of agricultural protection in Germany long before the war, with the sole object of smoothing the process of the transformation of the old agricultural system into a system with less grain production, and with more peasant farmers producing dairy products, meat, eggs, fruits and vegetables. But the point is that agricultural protection in Germany has done nothing of this sort. It did the very opposite of it: it did everything to *increase* the production of grains, and thereby to discourage the growing of other products. It did even more than that, giving thereby the impression that perfection should be achieved in going the wrong way: among the different varieties of grain it gave a distinct preference to that variety which, because of changing habits of nourishment, was especially doomed, *i.e.* rye. After the war and after the inflation, Germany could have made a fresh start in its agricultural policy. All disinterested experts, and even several of those who had been advocates of the old agricultural protection before the war, joined their voices in demanding an agricultural protection on the lines indicated above or even free trade in agricultural products. The tragedy was, however, that all this advice was more or less haughtily waved aside. From 1925 onward the pre-war system of agricultural protection was not only resumed but brought to a climax with an uncanny consistency deserving of a better cause. What has been done especially—moreover, under social-democratic guidance!—in the case of rye has become an excellent text-book example of ill-advised interventionism, surpassed perhaps only by the coffee valorization in Brazil. In the years 1925 to 1929 there was still time to adopt a more rational policy without exceedingly great losses, as the general prosperity would have given a strong foothold to agriculture. And yet, Germany let slip even this last chance of averting the disaster. Then happened what was bound to happen:

the old agricultural system became untenable just at the moment of the worst general economic crisis which Germany had ever seen, *i.e.* at a moment when the non-agricultural sections of the nation were less able than ever before to support the cracking pillars of German agriculture. The industrial and the agricultural crisis got so much intertwined that it is difficult to decide which is cause and which is effect. However that may be, it seems certain that much of what happened in Germany in the last ten years economically and even politically must be understood as the direct or indirect result of the effects of the German system of agricultural protection.

## CHAPTER VII.

### THE TECHNIQUE OF AGRICULTURAL PROTECTION IN GERMANY.

LITTLE has been said so far of the details of the system of agricultural protection in Germany. I preferred to give first an idea of the general principles and of the underlying reasoning. But now it is time to have a closer look at this formidable machinery of protection which has been built up piece by piece in the last fifty years, sometimes with something approaching ingenious inventiveness.

The beginnings were rather mild and almost timid. The first dose of heroin was 1 mark for 100 kg. in 1879 both for wheat and rye. It was increased to 3 marks in 1885, and to 5 marks in 1887. This duty was decreased to 3.50 marks in 1891 by the commercial treaties with Austria and Italy, signed by the Reichskanzler Caprivi, and the reduced duty was applied, by virtue of the most-favoured-nation clause, to all other countries (with the exception of Russia for the duration of the famous tariff war between Germany and Russia in the early 'nineties). This more liberal commercial policy of Caprivi aroused the fierce opposition of the agrarians, who had founded, in 1893, the famous "Bund der Landwirte" which became one of the most powerful and influential factors in commercial and even in general policy. The first success of this agrarian opposition (in which, of course, the great landowners of the East were most prominent) was the introduction of an ingenious system destined to make the duties on grain more efficacious. This system was the so-called Einfuhrschein system (system of import debentures) the working of which is not quite easy to ex-

plain. But as it has lost nothing of its importance up to the present day, something must be said about it here. The Einfuhrschein was a transferable debenture given to the exporter of grain, and entitling him or the bearer to import a corresponding amount of grain (later also of other products) free of duty. The effect of this was manifold. First, it was a means whereby the exporter of grain could also share in the profits of protection. This was very important for the Eastern grain-grower whose natural market was in the Scandinavian countries. He could sell his Einfuhrschein to a Western grain importer, usually at a price in the neighbourhood of the amount of the duty. The second effect was that now the domestic prices of grain were raised almost always by the full amount of the duty, since whenever they tended to fall below this level, it became profitable to export grain and thus to relieve the domestic market. The third effect was that the Einfuhrschein tended to become an outright export bounty, with the further result that, immediately after each harvest, the German grain market was cleared to a great extent by heavy exports while, later on in the year, large amounts of grain had to be imported again. If we remember in this connection that the German system of agricultural protection has always been presented as a means of securing ample grain supplies in case of war, the contradiction between this pretension and the effect of the Einfuhrschein system becomes apparent. In reality, the Einfuhrschein system must be understood as a device invented to make the duties on rye and wheat (especially rye) as efficacious as possible and to extend the boon of protection also to those parts of German agriculture that were operating on an export basis. Needless to say, this system involved the Government in a good deal of net expense. It therefore obtained the doubtful honour of being put, in all public discussions on commercial policy, on the list of the so-called "Liebesgaben," or gifts liberally and lovingly disseminated among the landowners.

Another example of the ingenious inventiveness in which



agricultural protectionism is very apt to excel and another victory of the agrarian opposition of the 'nineties was the Meat Inspection Law of 1900, which provided that the carcasses of meat animals should not be admitted unless the (highly perishable) internal organs were still attached thereto.

The final victory of the Bund der Landwirte was the Bülow tariff of 1902, which went into effect in 1906. The duties on agricultural products were almost doubled. Furthermore, it was provided that the duties on grain should not be lowered in commercial treaties below a minimum stated in the tariff act. Small wonder that the new commercial treaties negotiated on the base of the Bülow tariff were far from being satisfactory.

At the outbreak of the World War practically all restrictions on the import of agricultural products were removed, as the logical result of the food shortage in Germany during the war. It was only in 1924 that the issue of agricultural protection became again a matter of lively interest, as the stabilization of the mark and the approaching end of the limitations set on the German commercial policy by the Peace Treaty—these limitations were to expire on January 10, 1925—marked the return to more normal and stable conditions. A great part of public opinion and the almost unanimous vote of the academic economists was on the side of a distinctly liberal policy. This remarkable renaissance of economic liberalism in Germany was not successful, however, since the pre-war system of protection was resumed, though in a somewhat moderated manner at first, in the tariff act of August, 1925. This system remained essentially unchanged until in 1928 it became more and more apparent that it was no longer able to attain its time-honoured aim of preserving the old agricultural system of Eastern Germany. The exceptionally good harvest of 1928-29 made it all too obvious that the consumption of grain all over the world was lagging badly behind the increasing production. As far as rye was concerned the situation was becoming

nothing short of desperate, since people were rapidly shifting from rye bread to wheat bread, more rapidly outside of Germany than in Germany itself. Prices of rye, therefore, tended to drop to the level of fodder. At the same time there was a good deal of dumping of grains on the part of the Russian Government and—last but not least—cost of production had been considerably lowered in the Western parts of the United States and Canada by means of the tractor, the combine and dry-farming. That was the moment when the German Government had to make its final decision as to which way they were going, *i.e.* whether the German agricultural system should now at last be adapted, by one great and final effort, to the new circumstances after the Danish example, or whether protection and intervention on behalf of the old agricultural system should be carried to extremes and all energy and inventiveness should be concentrated on the almost impossible task of maintaining grain production at its existing level. Unfortunately, the Government preferred to go the latter way, blind to the fact that it was now embarking on a policy which was eventually to shake the total economic structure of Germany to its foundations. Since the traditional methods of tariff protection seemed no longer to suffice, a new and powerful machinery of protective intervention was built up to deal with the new situation, the old story of interventionism being repeated that one step in this direction is always liable to lead to other and still bolder steps until, in the end, a maze is created in which only a few experts can find their way, with the greater part of the public groping its way in the dark, not knowing what it is all about. It is a curious fact that while the great landowners were pulling the strings as they always had done, the real work has been done to a great extent by people belonging to the Left parties, *e.g.* by the democratic minister, Dr. Dietrich, and by the Reichsgetreidekommissar, Dr. Baade, who belonged to the social-democratic party. It seems that it was easy to persuade these circles that this protective machinery had

distinctly socialistic aspects, which should make it attractive to Socialists no matter how much it helped incidentally the great landowners. In other words, some Socialists and radical democrats in Germany fell into a trap which, as so many recent experiences in a great number of countries have shown, is all too easily ensnaring our more or less well-meaning anti-capitalists.

Without going too much into details, I think it worth while to describe in a general way the construction of that protective machinery. The main task was to make room on the markets for the formidable surplus of rye. This was done, firstly, by a number of measures destined for the ruthless restriction of the import of grains competing with rye. The duties on all kinds of grain were raised again and again until they reached the present height. Then came, in 1929, the new device of forcing the German flour-mills to use a certain percentage of German wheat (*Vermahlungszwang*), a device that has since become popular also in a number of other countries. A national advertising campaign in favour of rye bread was launched too. Special care was taken to substitute rye for such fodder grains as barley and maize. To this end the duties on barley and maize were considerably raised, and finally the Reich monopoly of maize established (1930). On the other hand, rye for feeding purposes was cheapened by an intricate system of measures. In order to keep this sort of rye from the market of rye destined for human nourishment, it was dyed with Eosine (*Eosinroggen*). A host of other measures, covering almost all branches of agriculture, were invented in order to make the system as watertight as possible. The rest was left to a vast valorization scheme for rye in order to take off the surplus of rye from the market and dispose of it in some way or another. Two big attempts were made in this respect, but each time it was a complete failure after much money had been wasted on it. Finally, after several years nature took its course in reducing the acreage of rye, so much so as to make it no longer a patriotic

duty to eat rye bread. The new protective system has achieved the result, however, that the extent of grain production as a whole has been considerably increased since 1925 so as to make Germany now practically self-sufficing in the provision of bread grains. This has been achieved by isolating the internal grain market almost entirely from the world market. The price level of wheat and rye in Germany was raised to 200 and sometimes even to 300 per cent. of the level of the world prices. In order to give an idea of the dimensions of this new protective system, I may mention that the duties on wheat and rye have reached almost 300 per cent. of the import prices, the duty on barley a little above 200 per cent. (twenty times as great as the pre-war duty). It is characteristic of the whole system of protection to-day in Germany that agricultural protection has far outrun industrial protection. The highest duties on industrial products, viz. those on bar-iron and similar products, amount to about 50 per cent. of the import price, while the majority of the other industrial duties do not exceed 20 per cent. The one great exception is the duty on mineral oil which I discussed earlier in my lectures; the duty on petrol, *e.g.*, is about 220 per cent. of the import price.

But all that is only a small part of the whole story. We must deal, now, with the direct and indirect repercussions of this protective system. The first and most direct repercussion has been felt by the other branches of agriculture. The economic position of the Veredelungswirtschaft has been prejudiced in two ways. Firstly, the ruthless protection of grain production was conducive to bringing down the prices of fodder grains on the world market and to raise them on the home market, so as to make it more and more difficult for the German Veredelungswirtschaft to compete with the foreign producers of butter, cheese, pork, eggs, etc. Secondly, since in consequence of the ruthless protection of grain the consumers had—at least relatively—to spend considerably more money for these products, the demand for which is highly inelastic, they necessarily had less money to spend

for the other products, such as butter, meat, etc., for which the demand is rather elastic. This tendency was the more marked, as the industrial crisis was contracting more and more the general amount of spending power. Thus it happened that the agricultural crisis which had begun in the grain districts of Eastern Germany was now invading the *bäuerliche Veredelungswirtschaft* of the other parts. The burden had been shifted from the shoulders of the great landowners to those of the peasants, becoming more and more crushing in character with the advancing general crisis. However, for reasons which it is for the sociologist to elucidate, it proved possible to divert the exasperation of the peasant farmers from the landowners to the Government and the parties representing it, and to persuade them that what was needed was not to abandon this system of one-sided and ill-advised agricultural protection, but to complete it by equal protection for the farmers. The Government yielded to the ever-increasing pressure exerted by the united front of the landowners and the farmers (the "Grüne Front"), and embarked on the bold policy of extending to the other farm products the degree of protective intervention which had already been applied to grain production.

The first step was to increase the duties on these products above anything that had been thought possible before the war. For purposes of illustration, it may be mentioned that in the beginning of 1933 the duty on hogs had risen to about 160 per cent. of the import price, against 4.4 per cent. in 1913, the duty on butter to about 55 per cent., against 8.8 per cent. in 1913. This policy, however, met with the greatest difficulties, because the countries from which Germany imports the greatest part of the imported *Veredelungsprodukte* are just those countries which are most important for the German export of industrial products, especially Holland, the Scandinavian countries, Switzerland, Belgium, Czechoslovakia, Austria, Jugoslavia, Hungary, Italy, France, and the Baltic countries. The existing commercial treaties between Germany and these countries,

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accordingly, had been negotiated on mutual tariff concessions, affecting, on the part of Germany, mainly the duties of the more advanced agricultural products, and, on the part of the other countries, the duties on a great number of industrial products. For this reason, the import of those agricultural products could not be restricted without new negotiations with the object of reducing these mutual concessions. Consequently, the progress of agricultural protection was now seriously to threaten the existence of the German manufacturing industry, and thus the total economic structure of Germany. The industrialists, who had hitherto been all too indulgent to the vast scheme of grain protection, were now showing some concern, since the clash between the agricultural and the industrial interests was now too apparent to be easily dismissed by semi-patriotic phrases about agriculture being the backbone of the nation, and about a prosperous home market being essentially in the interest of industry, and so forth. The history of agricultural protection in Germany during the last years, therefore, is characterized by continuous and tenacious attempts on the part of the German Government to force a way through all these difficulties.

A good illustration is the case of butter. The duty on butter had been bound by the commercial treaty between Germany and Finland in 1926, and this reduced duty had, according to the most-favoured-nation treatment, to be applied to the other countries in question. By the new treaty negotiated with Finland in 1930, Finland assented to a considerable enhancement of the duty on butter on the understanding that a quota of 5,000 tons should be imported at a lower duty. The German Government claimed that the requirements of the most-favoured-nation clause were satisfied by granting the same absolute quota to Denmark and the other countries, while these countries which exported ordinarily a much greater amount of butter to Germany than did Finland, charged the German Government with gross unfairness in interpreting the most-favoured-nation

clause. The exasperation of the Scandinavian countries was still further intensified by the subsequent introduction of special anti-dumping duties on butter against the countries of the sterling group. The climax of this policy was reached by the establishment of a Reich monopoly for dairy products, oils and fats, recently established under the Hitler régime. An especially interesting phase of this development has been the attempt (in the autumn of 1932) to restrict the import of special products such as vegetables, fruits and animal fats by means of real quotas (in contrast to the tariff quota accorded in the German-Finnish treaty). A special delegation of Government representatives—derisively called the "Tomatenkommission"—were sent to Holland and the other countries concerned in order to negotiate this project, while in Germany a violent discussion about its feasibility ensued between the representatives of the Grüne Front and those of the export industries. The atmosphere which the Tomatenkommission found in Holland, Belgium and Denmark, and the boycott movement conducted against German industrial products in those countries, showed plainly that the limit had been reached, the agitation incited by the whole scheme being one of the factors leading to the overthrow of the Papen Government in November, 1932.

How far did this policy help to alleviate the position of the *bäuerliche Veredelungswirtschaft*, and how did it affect German economy as a whole?

To every impartial observer it was quite clear that the main reasons for the bad position of the peasant farmers were on the one hand the ruthless grain protection, increasing the price of fodder and lessening the amount of purchasing power of the urban population available for the other agricultural products, and on the other hand, the absolute shrinkage of urban purchasing power due to the industrial crisis. That this diagnosis is not incorrect is proved by the fact that the German import of this category of agricultural products showed, even before the new restrictive measures set in, a steady and very marked decline, and by the further

fact that the downward curves of the purchasing power of the industrial workers and of the prices of the Veredelungsprodukte show an unusually high degree of correlation. Therefore, one had every reason to be highly sceptical about the effects of the new import restrictions on peasant agriculture. It was maintained, with very good reason, that the restrictions would bring about a further shrinkage of urban purchasing power, because it was obvious that they would of necessity operate to diminish the export of industrial products, intensifying thereby the industrial crisis. It was further maintained that, in consequence of the high elasticity of demand for these products, any tendency of rising prices would frustrate itself as long as the general amount of urban purchasing power was not augmented by a rising industrial activity. Finally, it was argued that any upward tendency in the prices of the products concerned would bring about an increase of production, and thus defeat its own purpose. The conclusion was that it was quite impossible to combine protection of grain and protection of the other agricultural products, and that the position of the peasant farmers could be bettered only by a reduction of the costs of production (including the cost of fodder, but also technical modernization of production and marketing) and by a policy aiming at increasing industrial activity. One of the most efficacious means to attain both aims with one stroke would have been a liberal tariff policy.

I believe this reasoning to be fundamentally sound, although I would concede that one or another of the arguments adduced in its support were not absolutely watertight. There was, however, one possibility which seemed quite remote and theoretical in character some time ago. It seems, of course, possible to raise the price level of those products permanently, if in some way or another the production could be effectively controlled. To this end, the idea of bringing agriculture under some sort of a Kartell was discussed for some time, but was finally abandoned as not feasible. It was only after the present system of strongest



political discipline had been established, aided by the enthusiasm of the peasants, that it became possible to try this extremely bold experiment of imposing on agriculture the Kartell principle. Although it is very difficult to reduce the present economic policy of Germany to its essentials, it seems that that is what the agrarian policy boils down to. The most important measure in this respect is the Reich monopoly for dairy products which has been established very recently. It is the purpose of this monopoly to control the amounts of dairy products brought on the market. They have first to be offered to the monopoly or its agencies; the products refused by these agencies must not be sold anywhere else under any circumstances. The monopoly fixes the prices. By means of this system the prices of dairy products have considerably risen so as to enhance the cost of living quite sensibly, the more so since the price of margarine has also risen as the result of a number of measures introduced with this objective in view.

It has now to be asked whether the liberal line of reasoning has been refuted by this recent development. I do not believe so. The first point of doubt is whether with enhanced prices the product of price per unit times the volume of sales has risen accordingly, and if so, how much of this betterment must be attributed to rising industrial activity. Further, the very fact that the Government had to take recourse to this extremely bold step—too bold to have been seriously contemplated some time ago—is ample proof of the fact that the system of agricultural protection had led to an *impasse* forcing the Government to destroy the market mechanism altogether, and to plunge right into planned economy. It will be extremely interesting to watch the further developments. Anyone familiar with the psychology of the peasant, especially in Germany, will have some doubts if even the strongest political discipline will, in the long run, be sufficient to enforce this new kind of Zwangswirtschaft, though it is the very opposite of the Zwangswirtschaft during the war. Last but not least, it remains to be seen how far this

extremely restrictive policy will be compatible with the policy of stimulating industrial activity. I should be surprised if the old Latin saying, *naturam expellas furca tamen usque recurret*, should not come true after all in a very literal sense, but I am afraid after much and partly irretrievable damage has been done. It is, of course, possible to sustain agriculture in all its branches by some cunning and ruthless system whereby the non-agricultural population is made to pay the costs even in the last extremity by inflation, but there is ample reason to fear that the social and political framework of no country would stand the formidable pressure necessary to carry out such a policy.

The moment has now come to pause and to sum up. The time-honoured policy of grain protection in the interest of the great landowners of Eastern Germany has been carried on with a resoluteness proportionate to the growing obstacles, and this very policy has now engulfed the whole economic structure of Germany. That is the essence of all these bewildering happenings. The "battaglia di grano" has been won, but as in the similar cases in Italy and France, and in Germany more strikingly so than in any other case, it has proved a Pyrrhic victory. And there is no denying the fact that this policy did much to poison the international atmosphere of commercial policy during the last five or six years, although I think a number of other countries were as much responsible, and some of them even more. But it is by no means futile to point out what instead would have been the right course to pursue. The right course would have been, and still is, to develop the natural advantages of German agriculture as they would be if it were conducted on the basis of peasant farming. It has always been the dream of the very best German patriots to make German agriculture an agriculture of peasants devoting their energy, thrift, and intelligence to those branches of production which call for these qualities. The German peasant is one of the best in the world. He is a peasant in the sense that he sticks to his soil against all odds, but he is not a mere

stick-in-the-mud bent over his hoe, as the Americans imagine the European peasant to be. He combines conservatism and faithfulness to his occupation with a high degree of intelligence. This rare combination is one of the main reasons justifying the belief that, in the long run, he will withstand any competition as far as the products of the peasant farm are concerned, the more so since for these products the transport costs are high enough to give a sort of natural protection. But to this end the excessive protection of grain production must be definitely stopped, and the estates becoming unprofitable thereby must be converted into peasant farms. And then the farmer must be taught to reduce the cost of production by making full use of the devices of modern marketing and the technique of production which German agricultural science excels in systematizing and developing. Finally, all efforts must be concentrated on bringing about an industrial revival and thus an increase of the urban purchasing power. One of the best means to do this is the return to a liberal tariff policy.

## CHAPTER VIII.

### GERMAN COMMERCIAL POLICY SINCE THE CRISIS OF 1931. COMMERCIAL TREATY PROBLEMS, CURRENT TENDENCIES AND FUTURE PROSPECTS.

It was in the field of agricultural protection that Germany made its first experiments with other methods of protective intervention than the old method of tariff duties, even before the international credit crisis of 1931 initiated a new era of international protectionism. The quota system for home-produced wheat, forcing the millers to use a minimum proportion of German wheat, was introduced as early as 1929, as also the bounty system in favour of rye and the maize monopoly, which later served as a model for the Reich monopoly of dairy products. The special case of sugar has not even been mentioned in my lectures because it is much too complicated to be dealt with satisfactorily in a concise survey like this. Finally it has to be recalled that at the end of 1930 the first experiment was made with the quota system for foreign products, in the form of a quota of butter accorded at lower duty, first to Finland, and then to the other countries enjoying the most-favoured-nation treatment. We may call this a tariff quota, in contrast to the real or quantity quota, which fixes an absolute maximum for the quantity of goods to be imported, without reference to the rate of duty to be imposed.

It must now be our task to investigate the effects of the crisis of 1931 on German commercial policy and to describe the rôle of Germany in the new era of international protectionism to which, unfortunately, this crisis and its after-effects have given rise. To this end, some reflections of a more theoretical character may not seem out of place here.

What happened in 1931 may be described in a sketchy way as an international crisis of national liquidity, leading in turn to a severe shock to the external equilibrium of the countries concerned. The condition necessary for an external equilibrium is that the internal price level, preferably the internal price level of the factors of production, is balanced against the outside price level in such a way as to keep stable the ratio of exchange of the internal currency against foreign currency. If some very simple rules of monetary policy are observed this equilibrium is always tending to be established automatically, and any worrying about the balance of payments, to say nothing of the balance of trade, is quite absurd. But the case of a crisis of national liquidity is different. When milliards of foreign short-term credits are suddenly withdrawn and other millions of home capital flee abroad, the traditional means no longer suffice to maintain the external equilibrium. The most sensible thing to do in such a situation is, of course, the same as the the most sensible thing to be done in an internal crisis of credit, *i.e.* to satisfy the panic demand in the most liberal way and with the least possible delay. I shall not discuss the question as to whether some millions of dollars, judiciously administered in the fatal summer of 1931, would not have spared the world an endless series of misery. Nobody can prove convincingly that it would have worked. Apart from this, three courses are open to weather the storm. The first course is to adjust the internal price level to the new conditions by the severest deflationary measures. The second course is to let things take their course until a new equilibrium is reached at a lower level of the rate of exchanges. The third course is to restrict directly the panic demand for "Devisen" by a number of methods among which standstill agreements, moratoria, transfer restrictions, a severe control of the "Devisen" market, and import restrictions are most conspicuous.

The first course was recommended at that time by several economists in Germany, some of whom even went so far as to

demand a discount rate of 20 or 30 per cent. Fortunately, these recommendations remained, on the whole, unheeded, although a good deal of deflation was carried through by the Brüning Government. The second alternative, as everybody knows, is that followed by England and subsequently by the countries of the sterling group. Germany adopted the third method, combined with a number of deflationary measures, and has adhered to this method up to the present.

To understand the choice made by Germany, the difference between the German and the English situations must be made clear. In the case of Germany it was a clear case of the external equilibrium being disturbed by a panic demand, *i.e.* of a crisis of the national liquidity. It is absolutely wrong to assume that, in the case of Germany, the disturbance of the external equilibrium had anything to do with the German price level being relatively too high. But the case of England was quite different. True, England went off the gold standard under the pressure of a crisis of the national liquidity. But this was only the acute form in which the chronic lack of external equilibrium was made manifest, and this chronic lack of external equilibrium was due to the internal price level (preferably, the internal level of the prices of the factors of production) being too high in comparison with the outside price level, which was in communication with the English price level through the exchange rate of the Pound. In other words, in the case of England the internal price level and the exchange rate of the Pound were out of harmony with each other, so that one or the other had to give way. The English Government had before it only the alternatives of pulling either the exchange lever or the price lever. To prefer the latter would have been absolutely reasonable, quite in contrast to the German case where there was no disharmony between the price level and the exchange rate of the mark. But I believe the English Government is not to be blamed for having pulled the exchange lever. It is beside the point to say that the English price system should have been

adjusted years before. Very probably it should, but it is doubtful whether it was still the right thing to do in 1931 during a severe depression of an extraordinary character. For pulling the price lever meant deflation which, perhaps, could have been rather easily adjusted in 1928, but which would have been nothing short of disastrous in 1931. Thus, I think that England, in the face of the awkward alternative between further deflation and devaluation, did right in choosing the latter.

For Germany there was no sense in trying to weather the storm by a vast deflation. Later on, though, when England and the other countries concerned had gone off the gold standard, the case was different. Now the *permanent* conditions for the external equilibrium of Germany were really changed. For the moment, Germany had only the alternative between the second and the third course. Everybody knows that it preferred the latter, thereby setting an example that was imitated by all countries of South-Eastern Europe from Czechoslovakia down to Turkey, although in several of these countries the conditions were quite different. If we now look back on the avalanche started thereby in 1931, considering that since then the world has sunk deeper and deeper into the morass of economic nationalism, we may well ask whether all these countries have not chosen the wrong way at the cross-roads of 1931. There is much to be said for both sides of the argument. On purely theoretical grounds, there is no reason to assume that the equilibrium would not have been restored by following the second course of letting things go. Needless to say, it is a grave error to stigmatize this policy as inflation, since it is only a policy of giving to the exchange rates the scope necessary for exerting their function of equalizing supply and demand of foreign bills. As there is still to-day a good deal of confusion about these matters, it is very probable that the German Government and the Governments of the other countries following suit, did not see quite through the problem. But even if they did, they had one good reason for shrinking

back from this bold course, and this reason was the fear of the possible repercussions of a perceptible fall of the foreign exchanges on the psychology of the population, which would have been scared to death by anything resembling inflation. Personally, I am of the opinion that even this has been always somewhat exaggerated, and that it would have been quite feasible to damp any possible panic among the German population. First and foremost of all, I always was and am still of the opinion that a drastic and definite "coup d'éponge" for the reparations and interallied debts at that time would have saved the situation.

But it is idle now to speculate on what should have been done and what not. Although the creditor nations are very much to be blamed for not having acted promptly and boldly, the German Government cannot be blamed for having resorted to the third method of the *Devisenzwangswirtschaft* and everything that goes with it, for the pros and cons in this matter were really in the balance. With a good many other countries doing the same thing, and with many other countries letting their exchange rates fall, from now on, the world came to be entangled in a terrific net of interventions and restrictions from which it is not easy to see how it will disentangle itself. A new era of commercial policy with a new outlook and with new methods was started, so destructive in character that nothing less than the future of our whole economic system will depend on whether it is really a new era or just an episode. Let us see now the part that Germany has taken in this development.

To begin with, a severe *Devisenzwangswirtschaft* (foreign exchange control) was established in 1931 and made even more severe in the following years, in striking contrast with the development in Austria where a more elastic course has been recently adopted with great success. It must be noted, however, that the *Devisenzwangswirtschaft* in Germany has never been used openly as a direct tool of import restriction, as it has in most of the other countries concerned. That is to say that in Germany the



"Devisen" are, in principle, equally distributed among the different groups of import goods with the object of satisfying as fully as possible the legitimate demands of the importers and of restricting and controlling only the payments on capital account. Every importer is assigned a certain quota, regardless of the goods imported by him. The Government has been urged time and again to manipulate the distribution of the "Devisen" in such a way as specially to restrict the import of certain groups of goods or the import from certain countries, after the practice of Denmark, Czechoslovakia or Greece, but it seems that until recently it has been possible to check these tendencies. However, even the German system unavoidably exerts a distinct restrictive influence, since with the best intentions in the world the inelasticity of every system of exchange control is bound to bring about a manipulation and restriction of import. But we must give Germany credit for having tried to keep these tendencies within certain limits and to restrict the Devisenzwangswirtschaft to its main object of controlling the transactions on capital account. It is here, as everybody knows, that the attitude of the German Government is severely criticized abroad. While we are not concerned here with this criticism in general, a word must be said about it in so far as it has some special bearing on foreign trade relations.

The criticism starts from the practice developed in the last years of stimulating German export by making use of the different kinds of blocked Reichsmark (Sperrmark), which has necessarily a much lower value than the free Reichsmark. If, in certain cases, the importer abroad is entitled to pay in Sperrmark, which in the hands of the German exporter become Freimark, then we have undoubtedly a clear case of export stimulated by an export bounty which is obviously financed by the difference of value between the Sperrmark and the Freimark, and this difference in turn is created by the transfer restrictions for payments on capital account. While this system has been practised only within

very strict limits, it is now replaced by the "scrip procedure" which has been so widely discussed that almost everybody will be familiar with its essentials. It is based on the fact that the German Government, limiting the transfer of interest on foreign loans to a certain percentage (until recently 50 per cent.), collects the non-transferable part in a common fund (Konversionskasse). Against the balance at the Konversionskasse debentures, bearing no interest—the "scrips"—can be given. These scrips, being quoted now at about 50 per cent., may be used in certain well-defined cases and in a rather round-about way, for paying at least a part of export transactions. Since here also Sperrmark (Konversionsmark in this special case) are turned into Freimark, export is cheapened in the degree to which scrip is acceptable in payment of a particular export transaction.

Though this system of "additional exports" financed in part by the conversion of Sperrmark into Freimark seems rather complicated, its essence is very simple. German goods are in certain cases made cheaper abroad without sacrifice on the part of the German producer, while the difference has to be borne by the foreign creditor. In view of this apparently plain fact, it is not to be wondered at that—to put it mildly—the opinions about it are somewhat divided. It seems to me, however, that there are certain aspects of the matter which must be taken into consideration before the German Government is condemned.

First of all, the foreign indebtedness of Germany presents one of the gravest problems of the present time, and is the main source of all the evil of the past few years. The real point is whether Germany is able to meet at the present all obligations of interest and sinking fund on foreign loans or not. It is not my intention to give a definite answer to this question, but I should like to say that Germany is really in a somewhat awkward position, being between the devil and the deep sea. If Germany wants to bring about a business revival—the task which it is now set upon—it has to meet the difficulty that the import of raw materials will

increase before exports have risen correspondingly. In the face of the fact that foreign short-term credits to cover this lag are not available in the necessary amount, Germany is forced to the alternative either of restricting the demand for "Devisen" for other purposes than for the import of raw materials, or of checking the business revival, or of abandoning the stability of the mark. Since Germany apparently does not want to follow the latter course, it has a choice only between the first two courses. It stands to reason, however, that the first course is also essentially in the very interest of the foreign creditors, since it is only by way of a marked revival of business that a definite solution of the German debt problem can be found. I am not offering this as an answer to our question, but only as a consideration which should be taken into account in a definite answer. This, of course, can be given only after a careful quantitative analysis of the situation. If we assume, however—as we have a right to assume—that Germany is not able at the moment to transfer all interest on foreign loans, the question arises as to whether any attempt at giving the foreign creditor at least something for the non-transferable remainder must be condemned *a limine*. True, the foreign creditor wants full payment, but if it can be proved that he cannot get it, he will concede that something is better than nothing. As a matter of fact, the situation seems to me a rather complicated one, since we have different sets of clashing interests: firstly, the clash between the German Government and the foreign creditors; secondly, the conflict of interests between the foreign creditor preferring something to nothing and the foreign producer driven out of business by the scrip dumping; and thirdly, the conflict of interests between the creditors of the different nations, some of which, having an adverse balance of trade with Germany, can press more strongly for full transfer than others. It would require a special study to ascertain exactly the gains and losses all round, including the consumers' surplus on the part of the buyers of dumped German goods abroad. To analyse

the problem in all these ramifications and complications would bring forth quite a voluminous book from which at least one thing could be learnt : that you get deeper and deeper into the jungle once you have left the golden road of economic liberalism.

There is another reason why I do not think it fair to heap all the blame for the present state of things on the German Government. It is a commonplace which I hesitate to mention here but which, nevertheless, is of elementary importance, viz. that Germany has to export in order to meet its debt obligations. I would be the last to deny that Germany itself did not do everything possible to develop its foreign trade relations by a suitable tariff policy. But while the German commercial policy is far from ideal, the commercial policies of the majority of the other nations are at least no better. It would be sheer waste of time even to enumerate the obstacles to foreign trade that have been built up all over the world since 1931. With the prohibitive tariff of the United States, the Empire Policy of Great Britain, the quota systems of France and Switzerland, the ruthless Devisenzwangswirtschaft of all the countries of Eastern and South-Eastern Europe, the higher tariffs everywhere, the growing administrative protectionism, boycott movements, and finally the depreciation of national currencies all over the world, it has really become an extremely arduous task for Germany to maintain even a shabby remainder of its previous export trade. And on top of all this there is the obnoxious tendency to equalize the balance of trade between the different countries by means of clearing and compensation treaties, a tendency based on the crudest misconceptions about the real nature of foreign trade. And finally, the medieval superstition that it is better, let us say, to make pencils at home with which it is impossible to write, and which cost twice as much as those produced abroad, instead of making something else in order to exchange it for foreign pencils,—a superstition which has acquired the air of intellectual respectability like

chiromancy, by being honoured by a Greek scholarly name, *i.e.* Autarky.

This disastrous development has also had a deep influence on the German *policy of commercial treaties*. Among the several points to be mentioned here, the growing encroachments on the most-favoured-nation clause deserve special attention. The tendencies inimical to it have come from different directions. To begin with, the quota system has led to numerous conflicts about the most-favoured-nation clause, among which the recent conflict between Germany and France is the most conspicuous one. The second set of tendencies inimical to the most-favoured-nation system has its origin in the increasing importance of preferential systems. The greatest breach in the most-favoured-nation system of the world has, in this respect, been made by the Empire Bloc framed in 1932 at Ottawa, which has proved a very heavy blow to the German export business. These Ottawa Resolutions and other preferential systems of minor importance, together with the differential manipulation of the quota system, have undermined the most-favoured-nation system to such a degree that it has become doubtful whether the latter must not be scrapped altogether. It is, at least, a question which has given rise to a lively discussion in Germany. The most-favoured-nation system has been especially attacked by those who, arguing that the world is dividing itself rapidly into a number of different and more or less closed blocs, want to bring Germany itself into some preferential system. A little while ago many people in Germany busied themselves in the study of the atlas, and in demonstrating with almost Napoleonic gestures that geography was forcing Germany this way or another. This well-meant geographical romanticism led people to discover that salvation could only be found in the great bloc called "Mitteleuropa" (for the sake of the alliteration, reaching from "Köln to Konstantza") or in another bloc with the rather weird name "Zwischeneuropa," meaning the territory of Germany and Eastern and South-Eastern Europe. Under-

lying all these proposals was a fallacy belonging to that large group which Whitehead has called the "fallacy of misplaced concreteness" and which is one of the more common weeds in the garden of Economics. That is to say: all these geographical romanticists are always apt to confound square miles with purchasing power. Eastern and South-Eastern Europe mean very much in square miles but, unfortunately, very little in purchasing power. As a matter of fact, the economic importance of this territory for Germany has been continuously overrated, while it seems somewhat difficult to make people see the prosaic fact that, on the other hand, Western and Northern Europe are most important for the foreign trade of Germany. It would be a bad bargain, indeed, to sacrifice these business relations for a preferential bloc with Eastern or South-Eastern Europe. One could go further than that and say that if there is any country so diversified in production and in foreign markets that it cannot stake its commercial interests on certain markets alone this country is Germany. Consequently, it cannot be denied that the interests of Germany are best served by a system of commercial treaties based on the most-favoured-nation clause, so that Germany is one of the natural defenders of this system. But it cannot be denied either that the task to defend it has become almost herculean in view of the rising tide of preferentialism and differentialism in modern tariff policy. Therefore, it is not to be marvelled at that Germany is trying to make the best of a muddled situation by making certain concessions of its own to the drift of the times and adopting more and more the principle of reciprocity and differentiation in its tariff negotiations. Some attempts have even been made to bring Germany into some sort of regional combination, but none of them has been really successful. The ill-starred negotiations for a Customs Union with Austria in 1931 are to be recalled in this connection. So also the equally unsuccessful negotiations with Hungary and Roumania about preferential grain duties which could not go into effect because, without the assent

of the great grain-growing countries overseas, they could not be reconciled with the most-favoured-nation principle. A little while ago the Convention of Ouchy, signed by Holland and Belgium (including Luxemburg), with the objective of a reciprocal lowering of duties was hailed in some influential quarters of Germany as a very promising beginning in which Germany could possibly join, but, unfortunately, nothing has come out of that, as everybody knows. In the ill-starred World Economic Conference of London, 1933, Germany seems to have played rather the rôle of a detached observer. It is quite interesting to read now an official statement giving an idea of the attitude of the German Government in this matter which we find in a recent survey on the commercial policy of Germany, edited by the Reichswirtschaftsministerium: "In 1933 a further attempt was made at a wholesale clean-up (Generalbereinigung) of the situation on the basis of the attitude of economic liberalism. The World Economic Conference had the appearance of a world parliament which proved on a larger scale the incompetence of such an assembly. Here as well as in the parliaments of the different democratic countries, the proof is forthcoming that each party is pursuing its own purposes, without any intention of making sacrifices in the interest of the community of nations. . . . The attempt at making comprehensive international conventions between all countries of the world, therefore, was doomed to failure. It would be wrong, however, to say that the World Economic Conference has been an entirely unsuccessful and senseless undertaking. Besides the fact that it must have been very useful for every statesman and delegate coming to London to make the acquaintance of the leading representatives of almost every nation, and to discuss personally the different questions, the conference has made it obvious that the inner structure of the different national economies has been differentiated to-day to such a degree that even in the world economy liberalistic methods have no longer a right of existence. Accordingly, the very few results of the work

of the World Economic Conference are not 'liberations' but on the contrary the first beginnings of a world-planned economy, e.g. the sub-committees for the control of production and distribution of wheat, sugar, and timber."<sup>1</sup> Few will deny that there is a good deal of truth in this statement, although one might object to the misuse so common to-day of the term "liberal" contained in this statement, since it is obviously the very absence of liberalism in the present world which is leading the nations to believe that they are making unselfish sacrifices in lifting trade barriers and which is making them reluctant to submit to these alleged "sacrifices."

It would be wrong, however, to assume that Germany of to-day has already found a clear and definite line in commercial policy. As I remarked earlier in my lectures, the radical change in politics has not yet found an equally radical counterpart in commercial policy, and also the previous discussion still goes on, though with a somewhat changed terminology and in a slightly subdued tone. On the one hand, we have still the autarkistic fire-eaters, though one of the wildest among them, the economic leader of the so-called "Tat-Kreis," Ferdinand Fried, does not raise his voice for Autarky any more. One of the representatives of this school says, for instance, that goods which could be produced at home should not be imported, "even if they seem to be cheaper, for, under the aspect of the national economy, even at a tenfold price the German product presents a net gain, while the simple price, paid to a foreigner, means an irretrievable loss."<sup>2</sup> Views like this, which even an extreme mercantilist of the old days would have rejected as excessive, seem to be more and more superseded by more moderate opinions. At least they do not

<sup>1</sup> *Uebersicht über den Stand der wirtschaftspolitischen Beziehungen Deutschlands im Jahre 1933.* Herausgegeben vom Reichswirtschaftsministerium.

<sup>2</sup> A. Pfaff, *Der Wirtschaftsaufbau des Dritten Reiches*, München, 1932 (cited in *Das Wirtschaftsprogramm des Nationalsozialismus*, by Dr. Karlheinz Rieker, Berlin, 1933).



represent the official attitude as it has been expressed on several occasions. In the declaration of the new Government, made in March, 1933, it was said plainly: "We know that we need the connection with the world and that production for foreign markets means bread for millions and millions of members of the national community." Quite in accordance with this statement is a passage in the already mentioned survey of the Reichswirtschaftsministerium: "The protectionism which, without being established wantonly by any country, has been extended everywhere in the last few years, was bound to lead to an isolation of the national economies more and more severe and to increasing Autarky. In the end, that would have meant the return to the primitiveness of far distant epochs. Such a development cannot be the intention of Germany or of any other nation partaking in world trade. For in spite of all tendencies to make the countries economically independent, it is realized everywhere that the modern technical devices for transport and commerce must be utilized for equalizing the climatic and geological differences of the several continents and countries and for facilitating the spiritual intercourse of nations." Some of the regional National-Socialist leaders have been known to have gone so far as to adopt the free trade principle, which at least at Hamburg seems to remain as popular as before, in view of the fact that more than two-thirds of the exporters doing business in Hamburg before the war have been ruined by the crisis.

The point of view of some influential quarters outside of official circles is perhaps well illustrated by two articles published in the *Deutscher Volkswirt* in the middle of October, 1933, under the title "Geistige Neuorientierung in der Wirtschaftspolitik," the author of which is a member of the staff of the Institut für Konjunkturforschung, Dr. Donner.<sup>1</sup> The author begins with the statement that together with the old political order, with parliamentarism

<sup>1</sup> Dr. Otto Donner, "Geistige Neuorientierung in der Wirtschaftspolitik," *Deutscher Volkswirt*, 1933, Nos. 2 and 3.

and with the party system essential parts of the old economic ideas have also definitely gone to pieces. "However, while the profile of the new political order stands clearly before us, showing in an uninterrupted line all details, the outline of the economic policy has, in its essential parts, not yet taken a clear shape. That is not to be wondered at, since in economic policy all energies of the new state have been first of all concentrated on the solution of the urgent actual problems of mass unemployment and destitution." What this definite shape of the economic policy will be is still open for discussion. According to Dr. Donner, however, the instinct of the people is rising against living men being subjected to such a weird thing as the "Konjunktur" and to the anonymous forces of supply and demand. Therefrom he draws the conclusion that Germany is heading for a severely controlled economy. Curiously enough, it is no less an authority than that of Mr. Keynes that is cited with greatest satisfaction by the author in order to show that the new trend of economic policy is not only in harmony with popular instincts or with romantic visions like Professor Sombart's, but is also in harmony with sober economic reasoning. Dr. Donner finds himself especially attracted by the well-known proposition of Mr. Keynes, that as all countries are willing to take cheap credits from abroad but quite unwilling to take cheap goods, this disharmony between the free flow of credits and the interrupted flow of goods is bound to set the countries which are exporting capital under deflationary pressure. He accepts, without hesitation, the conclusion drawn by Mr. Keynes, that under these circumstances, and in the face of the irregular and haphazard character of international capital movements, the principle of *laissez-faire* must be definitely abandoned as far as the external economic and financial relations of a country are concerned, the more so since, according to Mr. Keynes, the international division of labour has lost much of its importance. This reasoning is ending in the conclusion that free trade and all that goes with it, like the most-favoured-nation treatment, will never

recover from its present marasmus. Preferences, quotas, import and export monopolies, therefore, will not only become the normal instruments of commercial policy, but even gain in strength and number in the future. These are the circumstances, as the author sees them, which are to determine also the commercial policy of Germany.

These articles are quite interesting from various points of view. Certainly not for any originality, since the main ideas are borrowed from Mr. Keynes, proving by the way that the Autarky in economic ideas has not been achieved so far. But they are interesting as an attempt at giving a sort of rational expression and argument to very popular sentiments and, therefore, worthy of an equally rational discussion. It is beyond the scope of my lecture to go into such a discussion. That must be done elsewhere and at another time. All I want to say here is this: If the autarkistic policy of to-day and to-morrow has to be based on reasoning like this, it will be built on rather sandy ground. Nobody can dispute the disharmony between the international flow of capital and the international flow of goods, nor are the formidable difficulties arising therefrom to be denied. It is no doubt here that one of the greatest troubles of the present moment lies. But to admit and even emphasize this is one thing and to deduce therefrom the necessity of an extreme economic nationalism quite another. Moreover, it is extremely doubtful whether the disharmony in question must of necessity exert a permanent deflationary pressure on the countries exporting capital. I am referring, in this respect, to the well-known discussion about the transfer problem between Mr. Keynes and Professor Ohlin some time ago which, in my opinion, has proved that there is no reason to expect any permanent deflation of this kind.<sup>1</sup> On the

<sup>1</sup>The discussion has been conducted mainly in the *Economic Journal* (June and September, 1929) by Keynes, Ohlin and Rueff. For my own opinion I refer to my paper on the transfer problem in the publication of the *Friedrich List-Gesellschaft* ("Das Reparationsproblem," Berlin, 1929) and to my article "Zum Transferproblem bei internationalen Kapitalbewegungen," *Jahrbücher für Nationalökonomie und Statistik*, 1930, pp. 225-240.

whole, I think that the ideas of Mr. Keynes, accepted and adapted by Dr. Donner, are a good illustration of one of the main faults of this school of economic autarkism. This fault is the confusion of short-run with long-run tendencies and that in a double sense: firstly, in the theoretical sense of confounding disturbances of the state of equilibrium with the equilibrium itself, and, secondly, in the more practical and historical sense of adopting the international commercial policy of the relatively short period of the present crisis, in other words, this clumsy system of haphazard and emergency measures, as a long-run policy. There is much to be said about this economics of Autarky, leading me to the conclusion that it is not so much the contrast between the willingness of the nations to accept cheap credits and their unwillingness to accept cheap goods that is paving the way for Autarky, as the contrast between the willingness of the nations to accept unsound economics and their unwillingness to accept sound economics.

It is all very well, however, to decry this international preference for unsound economics and to show that sound economics is on the side of economic internationalism. We must be on guard against the complacency so common among us economists, who are very liable to repeat incessantly our time-honoured truths and then to wash our hands of it. These truths must be repeated again and again, because the untruths are also repeated again and again. But there the matter cannot rest. Try as we might, there is no getting away from the fact that a liberal commercial policy connecting the national economy with the world economy, seems, in the long run, impossible without a world system of more or less settled political relations. World economy and world politics are no watertight compartments, but closely related to each other, and in the course of human history it has happened before that the international economic system has declined together with the disintegration of the international political system, the last great example being the simultaneous disintegration of

both the economic and the political system of the medieval world at the end of the 16th century. Nobody can deny that to-day also the international economic and the international political disintegration are showing a striking simultaneity. Whichever may be cause and whichever effect, we must also combat them simultaneously. If you will permit me to end these lectures on German commercial policy with a patriotic wish, I should like to express the desire of seeing my own country one day at the forefront of this noble combat, thus fulfilling a mission to which it seems to be destined by nature and circumstances. And in order to show you that I am not too pessimistic about the ultimate outcome of this combat, let me add the noble words of one of the great German philosophers of the Pre-Bismarckian era, Friedrich Albert Lange: "Der Realpolitiker behält für den Augenblick recht, den grossen Ideen aber folgen die langen Zeiträume."

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