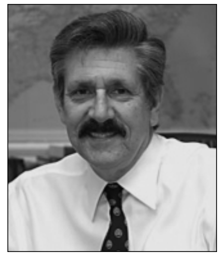

The Great Austrian Inflation

BY RICHARD M. EBELING

Wars always bring great destruction in their wake. Human lives are lost or left crippled; wealth is consumed to cover the costs of combat; battles and bombs leave accumulated capital in ruins; real and imagined injustices turn men against the existing order of things; and demagogues emerge to play on the frustrations and fears in people's minds.

All these factors were at work during and after World War I. In addition, the "war to end war" resulted in the dismemberment of many of the great empires in central and eastern Europe. This war also brought about the destruction of several national currencies in orgies of paper-money inflations. One such tragic episode was the disintegration of the Austro-Hungarian Empire and the accompanying Great Austrian Inflation in the immediate postwar period.

In the summer of 1914, as clouds of war were forming, Franz Joseph (1830–1916) was completing the 66th year of his reign on the Habsburg throne. During most of his rule Austria-Hungary had basked in the nineteenth-century glow of the classical-liberal epoch. The constitution of 1867, which formally created the Austro-Hungarian "Dual Monarchy," insured every subject in Franz Joseph's domain all the essential personal, political, and economic liberties of a free society.

The Empire encompassed a territory of 415,000 square miles and a total population of over 50 million. The largest linguistic groups in the Empire were the German-speaking and Hungarian populations, each numbering about 10 million. The remaining 30 million were Czechs, Slovaks, Poles, Romanians, Ruthenians, Croats, Serbs, Slovenes, Italians, and a variety of smaller groups of the Balkan region.

But in the closing decades of the nineteenth century, the rising ideologies of socialism and nationalism superseded the declining classical-liberal ideal. Most linguistic and ethnic groups clamored for national autonomy or independence, and longed for economic privileges at the expense of the other members of the Empire. Even if the war had not brought about the disintegration of Austria-Hungary, centrifugal forces were slowly pulling the Empire apart because of the rising tide of political and economic collectivism.

Like all the other European belligerent nations, the Austro-Hungarian government immediately turned to the printing press to cover the rising costs of its military expenditures. At the end of July 1914, just after the war had formally broken out, currency in circulation totaled 3.4 billion crowns. By the end of 1916 it had increased to over 11 billion crowns. And at the end of October 1918, shortly before the end of the war in early November 1918, the currency had expanded to a total of 33.5 billion crowns. From the beginning to the close of the war the Austro-Hungarian money supply in circulation had expanded by 977 percent. A cost-of-living index that had stood at 100 in July 1914 had risen to 1,640 by November 1918.

But the worst of the inflationary and economic disaster was about to begin. Various national groups began breaking away from the Empire, with declarations of independence by Czechoslovakia and Hungary, and the Balkan territories of Slovenia, Croatia, and Bosnia being absorbed into a new Serb-dominated Yugoslavia. The Romanians annexed Transylvania; the region of Galicia became part of a newly independent Poland; and the Italians laid claim to the southern Tyrol.

The last of the Habsburg emperors, Karl, abdicated on November 11, 1918, and a provisional government of the Social Democrats and the Christian Socials declared German-Austria a republic on November 12. Reduced to 32,370 square miles and 6.5 million people—one-third of whom resided in Vienna—the new, smaller Republic of Austria now found itself cut off from the other regions of the former empire as the surrounding

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successor states (as they were called) imposed high tariff barriers and other trade restrictions on the Austrian Republic. In addition border wars broke out between the Austrians and the neighboring Czech and Yugoslavian armies.

Within Austria the various regions imposed internal trade and tariff barriers on other parts of the country, including Vienna. Food and fuel supplies were hoarded by the regions, with blackmarketeers the primary providers of many of the essentials for the citizens of Vienna. Thousands of Viennese would regularly trudge out to the Vienna Woods, chop down the trees, and carry cords of firewood back into the city to keep their homes and apartments warm in the winters of 1919, 1920, and 1921. Hundreds of starving children begged for food at the entrances of Vienna's hotels and restaurants.

The primary reason for the regional protectionism and economic hardship was the policies of the new Austrian government. The Social Democrats imposed artificially low price controls on agricultural products and tried to forcibly requisition food for the cities. By 1921 over half the Austrian government's budget deficit was attributable to food subsidies for city residents and the salaries of a bloated bureaucracy. The Social Democrats also regulated industry and commerce, and imposed higher and higher taxes on the business sector and the shrinking middle class. One newspaper in the early 1920s called Social Democratic fiscal policy in Vienna the "success of the tax vampires."

Printing-Press Fiscal Policy

The Austrian government paid for its expenditures through the printing press. Between March and December 1919 the supply of new Austrian crowns increased from 831.6 million to 12.1 billion. By December 1920 it increased to 30.6 billion; by December 1921, 174.1 billion; by December 1922, 4 trillion; and by the end of 1923, 7.1 trillion. Between 1919 and 1923, Austria's money supply had increased by 14,250 percent.

Prices rose dramatically during this period. The cost-of-living index, which had risen to 1,640 by November 1918, had gone up to 4,922 by January 1920; by January 1921 it had increased to 9,956; in January 1922 it stood at 83,000; and by January 1923 it had shot up to 1,183,600.

The foreign-exchange value of the Austrian crown also reflected the catastrophic depreciation. In January 1919 one dollar could buy 16.1 crowns on the Vienna foreign-exchange market; by May 1923, a dollar traded for 70,800 crowns.

During this period the printing presses worked night and day churning out the currency. At the meeting of the *Verein für Sozialpolitik* (Society for Social Policy) in 1925, Austrian economist Ludwig von Mises told the audience:

> Three years ago a colleague from the German Reich, who is in this hall today, visited Vienna and participated in a discussion with some Viennese economists. . . . Later, as we went home through the still of the night, we heard in the *Herrengasse* [a main street in the center of Vienna] the heavy drone of the Austro-Hungarian Bank's printing presses that were running incessantly, day and night, to produce new bank notes. Throughout the land, a large number of industrial enterprises were idle; others were working part-time; only the printing presses stamping out notes were operating at full speed.

Finally in late 1922 and early 1923 the Great Austrian Inflation was brought to a halt. The Austrian government appealed for help to the League of Nations, which arranged a loan to cover a part of the state's expenditures. But the strings attached to the loan required an end to food subsidies and a 70,000-man cut in the Austrian bureaucracy to reduce government spending. At the same time, the Austrian National Bank was reorganized, with the bylaws partly written by Mises. A gold standard was reestablished in 1925; a new Austrian shilling was issued in place of the depreciated crown; and restrictions were placed on the government's ability to resort to the printing press again.

But, alas, government monetary, fiscal, and regulatory mismanagement prevented real economic recovery before Austria fell into the abyss of Nazi totalitarianism in 1938 and the destruction of World War II.