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WAR FINANCING OF GERMANY IS BUT A PAPER EDIFICE

Foundation is Confidence in Success of Her Arms—No Reserve Strength—Whole System May Crumble Up with the Coming of Peace, Which, is, Therefore, Likely to Be More Terrible Than War.

(By W. W. Tarn, Fellow of Trinity College, Cambridge.)

Professor Jastrow of Berlin, in his book "Gold und Kredit im Kriege," says that the German system of war finance rests on no foundation but confidence in the success of German arms. He is rather proud of the fact, but, at the same time, he admits that, as German credit rests on "Stimmung" (a state of mind), it might fall with it. Much the same admission was made a year ago by the Frankfurter Zeitung, the soundest upon finance of the German papers; "as long as confidence can be maintained," it wrote, "the technique of war finance holds out, especially as paper and the printing press are not only able to produce money for the time, but are an admirable means of producing a brilliant deception regarding the actual impoverishment by artificially producing buying power." It is agreed, that while the war lasts, Germany will continue to find the necessary money so long as the people retain confidence in the Government: that is, war finance, like much else in Germany, will only break down as the consequence of military defeat. The moment war was declared Germany took to an irredeemable legal-tender paper currency with German thoroughness. The measures of August 4, 1914, annulled the obligation of the Reichsbank to redeem its notes in gold, while leaving them legal tender, made the notes of other banks of issue redeemable and legal tender, and allowed the Reichsbank to hold notes of the Imperial Loan Banks (Darlehenskassen) as part of its reserve against its own notes. The system was adapted to meet a short and victorious war ending with a great indemnity. The prolongation of the war has had the natural result of an increase of paper beyond all bounds; instead of the statutory one-third reserve to be kept by the Reichsbank against its notes, on July 7 last the gold reserve was \$22,444,150, against notes in circulation amounting to \$273,800,000, a proportion of 18.09 per cent. only. There are also in circulation \$244,000,000 of Treasury and Loan Bank notes. It does not matter while the war lasts, but it will matter exceedingly afterward.

Peace More Terrible Than War. For, so far as concerns finance and all that it implies, peace to Germany is going to be much more terrible than war. Count Rendow is quite right in his outcry that without a huge indemnity, Germany will be ruined, perhaps irretrievably. And the situation grows more desperate with every month that Germany uselessly prolongs the war. The depreciation of the mark is the measure of the world's opinion of Germany's financial position; but, before we consider what this depreciation means, it may be worth indicating briefly what that position is.

Germany has voted her war credit

its and raised her internal loans with regularity; there is, as the saying goes, "plenty of money" in Germany. The war industries have made large profits, and to some extent the profits are genuine, that is, they represent the labor of the German people. But there is another aspect of the matter. Much of the money poured by these industries into the German war loans represents, not profits, but the depletion of German stocks of material of all kinds. Existing stocks have been sold out or used up, and they must be replaced at enormous prices after peace. Germany is becoming an "empty cupboard." For instance, it was stated at the beginning of the war that Krupp possessed a stock of copper sufficient for all demands for five years. Part of Krupp's "profits" represents merely the using up of that irreplaceable stock of copper. Similarly, repairs and renewals of railways and rolling stock have fallen very much behind. All this will tell at the peace.

The actual total of the war credits already voted is ninety-four milliards of marks, say \$4,700,000,000 and Germany is now spending at the rate of \$5,000,000 marks a day. The boast of Germans that they have made war cheaply is quite unjustified. According to a recent expert calculation the net war expenditure from Aug. 4, 1914, to Feb. 24, 1917, was about \$300,000,000 greater in Germany than in Britain, deducting each country's loans to its allies; and, whereas Britain's loans are good, we should not like to say much about safety of Germany's loan to Turkey. With every month that the war now lasts, says the Frankfurter Zeitung, Germany's future yearly burden of taxation for interest on debt is increased by some \$7,500,000. The Minister of Finance for Wurttemberg, in a speech on Aug. 1, calculated that the interest on the German war loans, with the expenditure on war pensions, amounted yearly to seven milliards of marks and said it was "extremely difficult to form a picture of the economic effects on the empire which would result from raising this sum, together with the five milliards yearly which were raised before the war." That is to say, he takes the amount Germany now requires to raise annually at \$600,000,000 nominal, or about one-third of the total annual taxable income of the country before the war. Other calculations have made it much more even \$800,000,000. But even \$600,000,000 is probably a good deal more than one-third of a day for a German authority has recently calculated that the capital wealth of Germany has decreased 20 per cent., i.e., from 350 to 280 milliards of marks, so that Germany is back to where she was in 1900.

Daily Expenditure Increasing. We may add that the war is not yet over, and that, during the last year, Germany's daily expenditure has increased out of all proportion to what it was in the first two years of the war. And this is by no means the whole story; an enormous burden has also been thrown on the municipalities, part of which is repayable by the Government, and on the separate States. Germany has made no serious effort to meet the interest on her loans by taxation, as interest has been met in Britain; she has gambled upon a war indemnity. No one supposes that she can possibly raise yearly a good deal more than one-third of her total taxable income, and the question of a capital levy after the war ranging from 25 per cent. even to 50 per cent., has been freely discussed as an alternative to repudiation.

Naturally the state of Germany's finances has been reflected in the foreign exchanges. The depreciation of the mark has made steady progress. At the end of 1915 it stood at about 20 per cent. discount; in December, 1916, at about 30 per cent. discount; the average for June was about 44 per cent. In August it was about 50 per cent. In September, it was about 54 per cent.; that is, anything that Germany purchased in, say, Sweden, costs her twice the price of that article in Sweden. It will be noticed that the acceleration in the fall during 1917 has been very great. And the foreign exchange is not the whole of the matter.

There are two forms of depreciation: that abroad and that in purchasing power at home, and according to the calculation of an American writer, A. C. Whitaker, at the time when the mark stood at 20.7 per cent. discount in terms of American dollars, it had lost 43 per cent. of its purchasing power in Germany. When it stands at 50 per cent. discount abroad, the home depreciation must be gigantic. It is worth noting that one of the many blessings which Austria owes to Germany is an even worse depreciation of her currency; during June the krona averaged 58 per cent. discount, or 14 per cent. worse than the mark.

The situation is now taken very seriously in Germany. From time to time that country has taken measures to deal with the depreciation, but they have had little effect. In March, 1915, exchange operations were confined to twenty-six private banks, but there were gaps in the legislation: non-commercial transactions, post office business, and the transmission of notes abroad remained uncontrolled, and purchases

of goods abroad for delivery after the war was not provided against. In December, 1916, steps were taken against this last by limiting remittances abroad by postal cheque or notes to 225 in January, 1917, the importation of goods into Germany without license was prohibited. In February, 1917, a decree consolidated and expanded the existing measures. Control was extended to cover all dealings in foreign currencies, notes, bills, credits, etc., non-commercial transactions were included, and even debts abroad could not be collected without the consent of the Reichsbank. The export of mark currency, the use of mark credits in favor of residents abroad, and the incurring of indebtedness abroad through purchase of goods, etc., were prohibited without the like consent. The Chancellor was empowered to demand the notification of all holdings of foreign currency, claims against foreign currencies, and mark credits granted to foreign countries, and to order their sale to the Reichsbank.

But the decree did not prevent the mark falling faster than ever. A census of foreign securities held in Germany was taken in September, 1916, and it is understood that a good deal has been done in the way of exporting them; but it has produced no effect either. At last the Government has decided the export of gold. A little gold had been exported from time to time, but had been made good by collections in Germany. For instance, Germany had adopted the cheque system, and her people before the war used to hoard gold. For the week ended June 22 there was a decrease in the gold reserve of \$2,325,500; and in the first week of July a warning was issued by the Secretary of the Treasury, who stated that the decrease was "not yet alarming," but that more gold must be exported, and that he was "led to suppose" that there were still several hundred million marks of gold jewelry and coins in Germany. For the week ended July 23 this reserve again decreased by \$2,811,800, bringing it

to \$120,074,250. (If the German total of the reserve be not exaggerated), a decrease in gold compared with the corresponding period in 1915 of \$350,600,000 marks (\$30,000) instead of "several hundred millions."

Germany's Vicious Circle. Peace will bring to a head the financial troubles of Germany. With a currency depreciated 50 per cent.—it will probably be far more if the war lasts another year—she will have to find vast sums of money, while loans abroad will be impossible, or the terms ruinous. Apart from the stupendous interest on her war loans, her debt to her municipalities already reaches hundreds of millions of pounds. Hamburg estimates that \$75,000,000 will be

needed for shipping subsidies alone, an enormous sum will be required to restart her sugar industry. How she can revive the system of bonuses and subsidies on which her export trade was built up does not quite appear. But the vital question at first will be imports.

That the adverse exchange will compel her to restrict her imports (as she will have to pay at least twice their value) is being emphasized in Germany. But she will have to export all she can, and quickly, for the sake of improving the exchange "the watchword" said the Wurttemberg Finance Minister, "must be export, export and import little." But she must export suitable things, not her cheap bulky coal, for her shipping space will be

very limited, if it exists at all, and for neutral tonnage the allies will overbid her. She is drained dry of many raw materials, and she cannot manufacture properly for export unless she first imports raw material, and she must restrict imports, even if, again, the allies do not outbid her for available stocks. A finer "vicious circle" cannot be imagined—to export she must first import, but to import she must first export.

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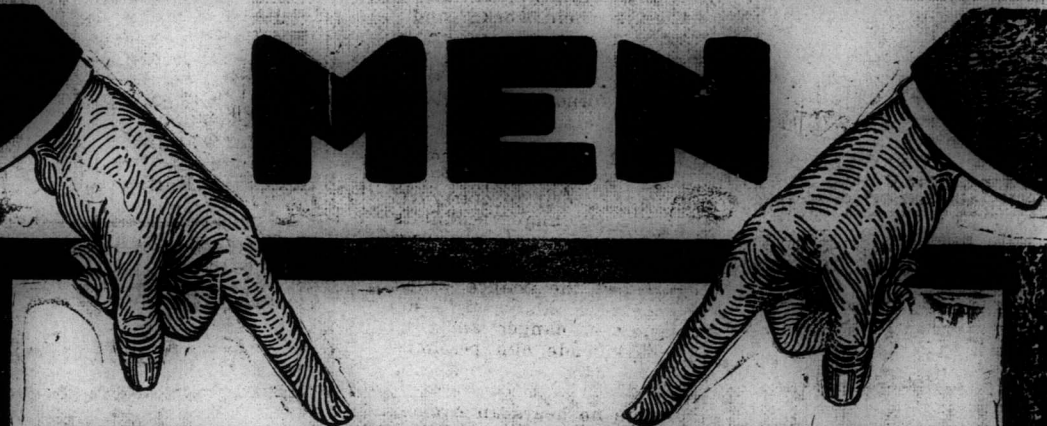
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