FIXED IDEAS OF MONEY

Most European countries are rather small, yet we know little about their monetary history. This book analyzes for the first time the experience of seven small states (Austria, Belgium, Denmark, the Netherlands, Norway, Sweden, and Switzerland) during the last hundred years, starting with the restoration of the gold standard after World War I and ending with Sweden's rejection of the Euro in 2003. The comparative analysis shows that, for most of the twentieth century, the options of policy makers were seriously constrained by a distinct fear of floating exchange rates. Only with the crisis of the European Monetary System (EMS) in 1992–1993 did the idea that a flexible exchange rate regime was suited for a small open economy gain currency. The book also analyzes the differences among small states and concludes that economic structures or foreign policy orientations were far more important for the timing of regime changes than domestic institutions and policies.

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Small States and Exchange Rate Regimes in Twentieth-Century Europe

TOBIAS STRAUMANN

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To Manuela, Emil, and Jakob

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Preface

Few topics have been more popular among economic historians and political scientists than the monetary history of Western Europe, and the industry is still alive and well. Yet, as with any industry, some paths of discovery have been followed more frequently than others. Most important, scholars usually have focused on the large European countries because, obviously, France, Germany, and the United Kingdom have been the driving forces in Europe's monetary history, and therefore, the experiences of small European states have been neglected. This blind spot is the main reason for this study. It attempts to make a first step toward a more comprehensive understanding of the monetary history of seven small, economically developed countries: Austria, Belgium, Denmark, the Netherlands, Norway, Sweden, and Switzerland.

Given that almost every small state has its own language and has produced a bulk of literature on its monetary history, I decided to restrict the study in two ways. First, I focused on the question of exchange-rate regime changes, and second, I confined the period under study to the interwar years and the decades after the end of Bretton Woods because the regime changes were particularly frequent during these two periods. This restrictive approach enabled me to cope with the huge amounts of primary and public sources and to tell a coherent story. My main finding is that for most of the twentieth century, small European states preferred having their exchange rates fixed or pegged and that the reason for this preference was not institutional or economic in nature but rather the result of a deeply rooted fear that a floating exchange rate would hamper trade and complicate monetary policy.

Because of this strong preference for fixed rates, I have chosen to call this study *Fixed Ideas of Money*. The expression is not meant in negative terms, however, although these fixed ideas sometimes proved counterproductive, especially during the Great Depression of the 1930s. As I try to show, the fear of floating was based on considerations about possible risks of foreign exchange markets. In retrospect, this fear may seem exaggerated, yet it was entirely rational at the time, given that the goals of policy makers were to make controlled adjustments and to avoid short-term fluctuations. The corporatist ideal of keeping the power of markets within clearly defined limits was reflected directly in the way small European states chose their exchange-rate regimes during the twentieth century.

During the current crisis, there are signs that the trend toward floating exchange may become less popular among small states. In particular, Iceland, once overwhelmingly sceptical toward Brussels, is now considering adoption of the euro. Such a move would not question the basic argument of this study, however. First of all, Iceland is a very small country, counting only 320,000 inhabitants, and therefore hardly comparable with Belgium, Sweden, or Switzerland. Second, Iceland is not considering a return to the traditional monetary order by introducing fixed exchange rates. Policy makers know well enough that the old regime of the twentieth century would not have shielded them from the recent turbulence. On the contrary, it is very likely that a fixed-exchange-rate regime would have harmed the economy even more, similar to what happened in Argentina in the final phase of the currency board period. The "fixed ideas" of the twentieth century are not experiencing a comeback.

Needless to say, all this research could not have been done without the help of others. First of all, I would like to thank Albrecht Ritschl, through whom I discovered the monetary history of Europe, and Brad DeLong, Barry Eichengreen, and Tim Hatton, who introduced me to Europe's economic history during the twentieth century. Without the encouragement of all these inspiring teachers, I hardly would have approached this complicated topic. I am very thankful to Harold James for his great support. He read the manuscript, helped me to improve the basic argument, and endorsed the publication. I also profited from critical comments made by members of the scientific committee of the University of Zurich who reviewed my thesis: Volker Bornschier, Jörg Fisch, Dieter Ruloff, Jakob Tanner, and Ulrich Woitek. Last but not least, I would like to thank the editors of the series, in particular Michael Bordo and Scott Parris, for their interest and encouragement.

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