# 1
# Introduction: some perspectives

The story of the German economy between 1929 and 1938 is a critical one in the history of modern Germany. Historians and economists still debate the issues of the depression in the hope of showing that different economic policies might have stopped Hitler. The economic recovery that followed raised then, and since, important questions about the relationship between state and economy, questions that have come more clearly into focus with renewed emphasis in recent years on markets rather than state initiative in the developed economies. More controversially, the economic recovery stands at the centre of any 'positive' view of the Third Reich. If there is still disagreement about how the Nazi economy should be interpreted, there is a general consensus that recovery did occur at a faster rate and to a higher level than almost anywhere else in Europe. Since a central feature of the revival was the regime's willingness to undertake schemes of deficit financing, the myth has taken root that Hitler was a Keynesian before Keynes, and being so won widespread support inside Germany in the years of peace and returning prosperity.

While there is some truth in this picture, it is in general misleading. The economic recovery must be placed in a wider perspective. Indeed the very term 'recovery' is in some sense ambiguous. The German economy was relatively stagnant in the inter-war years. Two short bursts of high growth (1925–8 and 1937–9) punctuated a general picture of slow growth, economic discontent and painful adjustment to the changed and unhealthy climate of the inter-war world economy. There is no disputing the fact that the German economy recovered from the disastrous trough reached in business activity in 1932. But throughout the

Table I *Annual average growth rates in Germany of selected economic indices 1870/1913–1950/70*

| | 1870–1913 | 1913–50 | 1913–38 | 1950–60 | 1950–70 |
|---|---|---|---|---|---|
| Growth of total production | 2.9 | 1.2 | 2.6 | 7.6 | 6.2 |
| Growth of output per capita | 1.8 | 0.4 | – | 6.5 | 5.3 |
| Growth of output per man-hour | 2.1 | 0.9 | 1.3 | 6.0 | 5.0 |
| Growth of exports (volume) | 11.0 | –2.4 | –1.6 | 16.0 | 12.8 |
| Fixed investment as % of GNP (excl. housing) | 15.6* | – | 9.7* | 16.1 | 17.7 |

* Figures for 1900–13 and 1920–38.

inter-war years the German economy failed on average to match the growth rates of pre-1914 or the high rates achieved after 1950. Trade revived slowly in the 1920s and collapsed in the 1930s. Domestic consumer demand responded sluggishly in both decades. Productivity improved significantly only with the so-called 'rationalisation' movement in the mid-1920s, and then for a limited range of industrial sectors. Full employment later in the 1930s paid the price of a slower and more uneven growth of productivity. Wages barely recovered to the level of 1913 in real terms. It was the exceptional decline of the depression years from 1929 to 1932 which gave the subsequent revival its rosy complexion. Table I sets out the long-term growth record. Average annual performance compared poorly with other industrial states, even with Mussolini's Italy. International comparisons are set out in Table II. The German economic miracle was very much a product of the post-Nazi era, not of the 1930s.

The recovery must also be contextualised in other ways. It is sometimes suggested that the recovery was a product of a specific 'fascist' economic strategy, which distinguished it from the recovery

Table II *Comparative economic performance of selected countries 1913–1937/8 (1913 = 100)*

| | GNP (1937) | Ind. output (1937–8) | Output per man-hour (1938) | Real wages | Annual rate of growth* |
|---|---|---|---|---|---|
| USA | 171.9 | 164 | 208 | 153 | 2.9% |
| Sweden | 174.0 | 231 | 143 | 150 | 2.2% |
| Italy | 154.2 | 196 | 165 | n.a. | 1.3% |
| UK | 146.5 | 139 | 167 | 133 | 1.7% |
| Germany | 136.4 | 144 | 137 | 109 | 1.2% |
| France | 120.8 | 119 | 178 | 128 | 0.7% |

* 1913–50.

efforts of other capitalist states. While few would disagree that the Nazi regime had a number of clear ideological preferences when it came to the economy (or that these came to determine the direction that the economy was to take by the late 1930s) the policies actually pursued in 1933 had much in common with those adopted in other countries, and with the policies of the pre-Hitler governments. The control of foreign exchange movements, work-creation and intervention in the formation of prices and wages were all in fact the products of the pre-Hitler period, modified or extended by the new regime after 1933. The German economy traditionally enjoyed a higher degree of state regulation or intervention than the more liberal western economies. Under the impact of war, defeat, hyperinflation in 1923 and the crash in 1929, state involvement became more widespread and increasingly necessary. In the 1920s state spending was double the pre-war levels.

A higher level of state economic intervention cannot be regarded as intrinsically fascist, and indeed German strategy for combating the slump has been compared with the anti-depression policies pursued in Roosevelt's New Deal [36; 107]. State deficit-financing, the regulation of trade and currency transactions, state stimulation of heavy industry and construction, and the supervision of banking and capital markets could all be found in one mix or another in the anti-depression armoury of the rest of the world. They were the product of circumstantial pressures as much as ideology – the decline of world trade, the collapse of world prices, high unemployment, and the unwillingness of private investors to plough their money into the productive sectors.

Why then should the German recovery have occasioned so much debate? Part of the answer is economic. The German experience in the inter-war years was an extreme manifestation of the business cycle in operation. Explanation for both the severity of the collapse and the speed of the revival offered lessons to modern economists wrestling since the 1970s with a slower and more uneven pattern of growth in the developed world. Another answer lies in the apparently demonstrable links between economic performance and radical politics in inter-war Germany. The depression was inextricably bound to the course of German party politics; economic policy choices were shaped by political expectations as much as by economic circumstance. The rise of Nazism as an electoral force is widely regarded as a direct consequence of the failure of government economic strategy during the slump. The consolidation of the Nazi dictatorship between 1933 and 1936 was eased by the subsequent business revival, which secured for Hitler a broader base of approval than he had enjoyed in 1932 [87]. To understand the business cycle, so the argument goes, is to understand the political cycle too.

There are, finally, profound disagreements about how to interpret both the causes and course of the recession, and how to explain the recovery that followed. In what follows, the international and political contexts feature where appropriate, but the main focus is on the economic explanation for the fall and rise of the German economy in the 1930s.

# 2
# The German economy from war to depression

On the eve of the First World War Germany possessed all the features of an advanced and expanding industrial economy. German trade was on the point of exceeding that of Great Britain. Output had increased at the rate of almost 3 per cent a year for forty years. German industry was highly competitive and was supported by a banking system and educational structure particularly favourable to industrial growth. Economic modernisation was reflected, too, in the changing social structure. Bismarck's Germany in 1871 had been predominantly rural; Germany in 1913 was predominantly, though by no means completely, industrial. The Great War did not reverse the direction taken by the German economy in any permanent way, but it did seriously distort the trajectory of economic development. A combination of territorial losses, particularly the industrial regions of Alsace-Lorraine, Silesia and the Saarland, together with the collapse of German trade and the shortage of capital, contributed to a decline in industrial output in the years 1919–24 to between half and three-quarters of the level of 1913. The costs of war and reconstruction also fuelled a high rate of inflation, which led to the collapse of the German mark in 1923 and the loss of half a century of accumulated savings.

In the years following inflation the economy struggled to regain the achievements of 1913. The revival of industrial output, though it lagged behind that of the rest of Europe and far behind that of the United States, did lead by 1928 to a restoration of the output and trade levels of the pre-war period. The revival rested heavily on foreign investment which provided the resources that the domestic capital market lacked following the inflation. Foreign funds made possible a limited modernisation programme for sections of German industry. Between 1925 and 1929, output per man-hour in the major industrial sectors expanded by 17 per cent; large industrial plant was built, to exploit modern production methods. Technological innovation, which had been slowed down by the impact of war, once again became an important component in the growth of Germany's industrial core [33; 50].

The recovery in the 1920s disguised many structural weaknesses. It was a fragile revival, restoring pre-war achievements but exhibiting few signs of sustained expansion and buoyant growth as in the years before 1914. Looked at in the long-term, it is difficult to dispute Petzina's conclusion that the 1920s, or for that matter much of the inter-war period as a whole, was for Germany a period of relative economic stagnation. Whereas GNP doubled in Germany between 1890 and 1913, and trebled between 1950 and 1970, it increased by only 4 per cent between 1913 and 1929 [75: *10–74*]. The causes of sluggish development were many. The terms of the peace settlement in 1919 were designed to hold back German economic revival: the territories lost to Poland and France contained three-quarters of Germany's iron ore, and one-third of her coal; 90 per cent of the German merchant fleet was confiscated; all Germany's overseas assets, totalling 16 billion marks, were forfeited. Above all the victors insisted that Germany pay for their war losses, and imposed a final bill for reparations of 132 billion gold marks.

Germany entered the world market again after the war already disadvantaged. But the slow revival of world trade, and the worsening terms of trade for primary producing countries in particular, hit the German economy harder than most because of its high export dependence. Before the war, exports supplied 22 per cent of the national product; in 1928 the figure was only 16 per cent. In the German boom of the 1950s and 1960s the export quota reached 25 per cent [59: *15*]. Germany's share of world exports fell 31 per cent between 1913 and 1927–9, even further than Britain's. Germany's trade with primary producers fell by more than a third over the same timescale. The decline in European capital export in the 1920s also hit German trade, because it reduced demand for German goods in markets financed before the war by British and French credits. The poor trade performance exaggerated the reparations problem, which constituted an additional burden on the German balance-of-payments. If it can be argued that Germans exaggerated the economic burden of reparations in the 1920s for political reasons, it cannot be ignored altogether. War debts were a constant source of friction between Germany and the victor states, who had expected reparations to be paid out of a growing German trade surplus. In fact Germany ran a trade deficit for most of the 1920s; reparations ended up being paid, in effect, by foreign investors attracted to Germany's high interest rates [92]. The reliance on foreign credit tied Germany into a dangerous dependency on the world's financial markets at a time when there existed serious structural weaknesses in the world monetary and payments system [25].

Germany's troubled relationship with the world economy was compounded with significant domestic constraints on growth, producing what Borchardt has called 'the crisis before the crisis' [59]. A basic problem lay with the German capital market. After the inflation, German interest rates remained at what were then perceived to be exceptionally high levels. The high cost of money reflected a shortage of savings following the inflation, and an understandable reluctance to run risks on the part of German investors. Although capital shortages were made good to some extent by large imports of money from abroad, the investment ratio in the 1920s remained well below the pre-war level, while smaller industrial producers, artisans and peasant farmers were left short of capital or were forced to pay for funds at usurious rates. Since craftsmen and peasants made up well over one-third of the working population, the problems they faced acted as a serious drag on the overall performance of the economy.

The sustained industrial and trade growth of the pre-war years had disguised the survival of large numbers of smaller and more marginal producers. The unhappier economic climate of the 1920s exposed the social and structural imbalance of the German economy. German agriculture was unable to compete with more efficient farmers in Europe or against cheap overseas imports. Much of it was small in scale – more than three million holdings – and relatively unmodernised. The long-term decline in agricultural prices in the 1920s, coupled as it was to growing farm indebtedness – an increase from 4.6 billion marks in 1924 to 11.5 billion in 1929 – and to higher taxes and social payments, reduced agricultural incomes and the demand for goods from rural areas. The deterioration of terms of trade for Germany's own primary producers meant that they could afford to buy fewer manufactured goods than before the war. While manufactures increased in price by 57 per cent between 1913 and 1929, farm products increased by only 30 per cent [75: *107*]. There were few gains in agricultural productivity. Mechanisation was held up through the shortage of funds, and farm labour stayed put. The farming population, which had declined more or less continuously as a proportion of the employed population between 1850 and 1913, remained at roughly the pre-war level until 1933. The slow revival of domestic demand during the 1920s owed a good deal to the survival of a numerous, but relatively poor, rural community [75: *104–6*].

Things were not much better among the small shopkeepers and craftsmen. Since they too constituted a sizeable proportion of the German population, some 13 per cent in the 1925 census of occupations, and since they were, like the peasantry, suffering a relative decline throughout the 1920s as they competed with cheaper foreign products and the switch to factory production at home, it is fair to assume that artisan hardships also served to depress domestic demand. Some craftsmen, it is true, found work as skilled factory hands, but many were located away from the main areas of large-scale industry. Nor was the labour market favourable to the displaced craft worker. The modernisation of large-scale industry brought increases in output and productivity, but it left a million workers unemployed [23: *265*; 59: *16*]. The result was low job mobility from countryside to town, or between regions, leading, as Bessel has shown for East Prussia, to significant differences in economic performance both within and between the major provinces [11].

Public spending provided some cushion against the slow growth of demand and rising unemployment. In 1928 public authorities were responsible for 47 per cent of all building work in Germany. Road-building, electrification and the development of municipal services all helped to maintain business activity and stimulate demand as they were later to do under the Nazi regime, but they did so at the price of drawing in large foreign loans during the 1925–9 period that left the German economy very vulnerable to shifts in the world economy [28: *54*; 86: *197*].

If there were losers in German society in the 1920s, there were also winners. Because the economic cake had shrunk in post-war Germany, there developed a conflict over how it should be distributed. Creditors lost their slice when the inflation wiped out savings; peasants and artisans remained marginal to the conflict. The chief beneficiaries of the distributional fight were wage earners, particularly the unionised factory workforce. It is now widely argued that the Weimar system was loaded in favour of labour, whose revolutionary potential had to be bought off with high wage settlements and welfare, which were paid for by taxing industry and farmers more heavily. Wage settlements between unions and employers were fixed in the late 1920s at real levels well above the gains in productivity, with the result that profits, and hence investment, were squeezed – not unlike the situation in Britain in the 1970s.

It is certainly the case that the 'wage ratio' – wages as a proportion of national income – was exceptionally high in the second half of the 1920s. The ratio was 70 per cent in 1910–13, but 87 per cent in 1925–9 (in the 1930s it was to fall to 59 per cent). The statistical evidence on real wages and output, though subject to significant margins of error, does suggest that real-wage growth exceeded productivity gains by a growing margin [59: *139–42*]. Von Kruedener has demonstrated that social spending and taxes both rose faster than output. In this sense the Weimar welfare state was more than a low growth economy could afford. The redistribution of the cake to workers and the state had, it is argued, the effect of squeezing profits and investment funds, and reducing the competitiveness of German exports. German workers, it appears, wanted to have their capitalist cake and eat it at the same time [13; 51].

There are a number of objections that might be made to this argument. The exceptionally high wage ratio is characteristic of a stagnating economy with low investment rates, but is not necessarily the cause of that imbalance. The ratio also disguises the timing and distribution of wage increases. For most workers in the 1920s, wages were below the real levels achieved by 1913, often significantly below. Only in the last two years of the decade was the real wage position recovered, and then not for every region or occupation. Workers did not achieve a significantly higher standard of living, but after ten years of war and inflation they wanted to return to the position they had lost. Balderston has suggested that the high wage settlements of 1927–8 actually reflected local labour scarcity rather than union muscle, a product of rigidities in the labour market [7: *401–2*].

It can also be argued that the low level of productive investment was as much a product of high interest rates, excess capacity and poor expectations of the market as it was of high unit labour costs. The same holds for export competitiveness. Balderston has again shown that German exports were not particularly price sensitive – many were high-value, custom-built products – but were depressed by the poor state of overseas markets or were victims of tariff discrimination. He sees high wages as an effect of export growth rather than a cause of export decline. Holtfrerich has taken the argument about confusing cause and effect one step further: the problem of the German economy in the late 1920s can be seen not as one of high wages, but as one of managerial conservatism and entrepreneurial caution. During the 1920s German industry became highly cartelised, protecting the weaker and less efficient producers, keeping prices artificially high and reaching domestic and international market agreements to limit competition. Its response to a hostile market was to limit damage by collective defence – 'organised capitalism' as it was known – rather than run higher risks and squeeze out the marginal producer [59: *76–8*].

Shifting the blame from workers to entrepreneurs begs other questions about where the investment funds were to be found in order to achieve a more vigorous, modernising capitalism, or where the extra demand for German goods might be generated. It also produces an unnecessary polarity between the two explanations, for they can be seen as complementary rather than as alternatives. Both labour and business in the 1920s were anxious to protect their interests in an uncertain economic climate. They both acted defensively – unions in order to protect nominal wage rates, industry in order to keep up prices and protect market shares. The result was a stalemate: the unions were reluctant to accept the wage restraint which might have generated higher profits and investment and the prospect of future wage increases; business was reluctant to run the risks of more aggressive market capitalism which might have put it, as it did in the 1950s, in the