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## GOVERNMENT EXPENDITURE AND BANKING DEVELOPMENTS

In the preceding sections we have described the changes in the banking structure effected by the Nazi government to help finance its military program, and the methods and techniques applied in raising funds through taxes, borrowing, and miscellaneous revenues. While it was possible to trace with a certain degree of accuracy the structural developments in the financial system of Nazi Germany, it is much more difficult to secure reliable and comprehensive information about the actual operation of that system. The nearer we get to the immediate past, the larger are the gaps in the statistical material and the greater the difficulties in interpreting it. In only a very few instances do we possess statistical series which cover the entire ten-year period that has now elapsed since the beginning of German war preparations. In addition, the figures that are available become less and less comparable since their coverage changes and since we are not able to make necessary adjustments. Because Nazi Germany began incorporating foreign territories into the Reich in 1935, the consistency of statistical time series has been destroyed in many instances. We hardly need to mention that these difficulties multiply with the outbreak of war when Germany started to overrun many European countries. "An important factor during 1940," says the Bank for International Settlements,<sup>147</sup> "was the extension of the banks' business to incorporated and occupied territories." And the London and Cambridge Economic Service stated in July 1943 in discussing German financial statistics that "it is not always clear how far recent German figures refer to the area including the incorporated parts of France, Belgium, Poland and Yugoslavia or to the 1939 frontiers."<sup>148</sup> Hence the reader may well appreciate how difficult it is to interpret the changes that have taken place in banks' deposits, or note circulation, or government securities owned by banks.

There is another problem that should be mentioned. Figures on financial conditions in Germany no longer have the significance which similar statistics have in a traditional capitalist economy. In an economic system as completely dominated and planned by the

<sup>147</sup> *Eleventh Annual Report* (1941) p. 115.

<sup>148</sup> *London and Cambridge Economic Service* (Memorandum No. 95) p. 21.

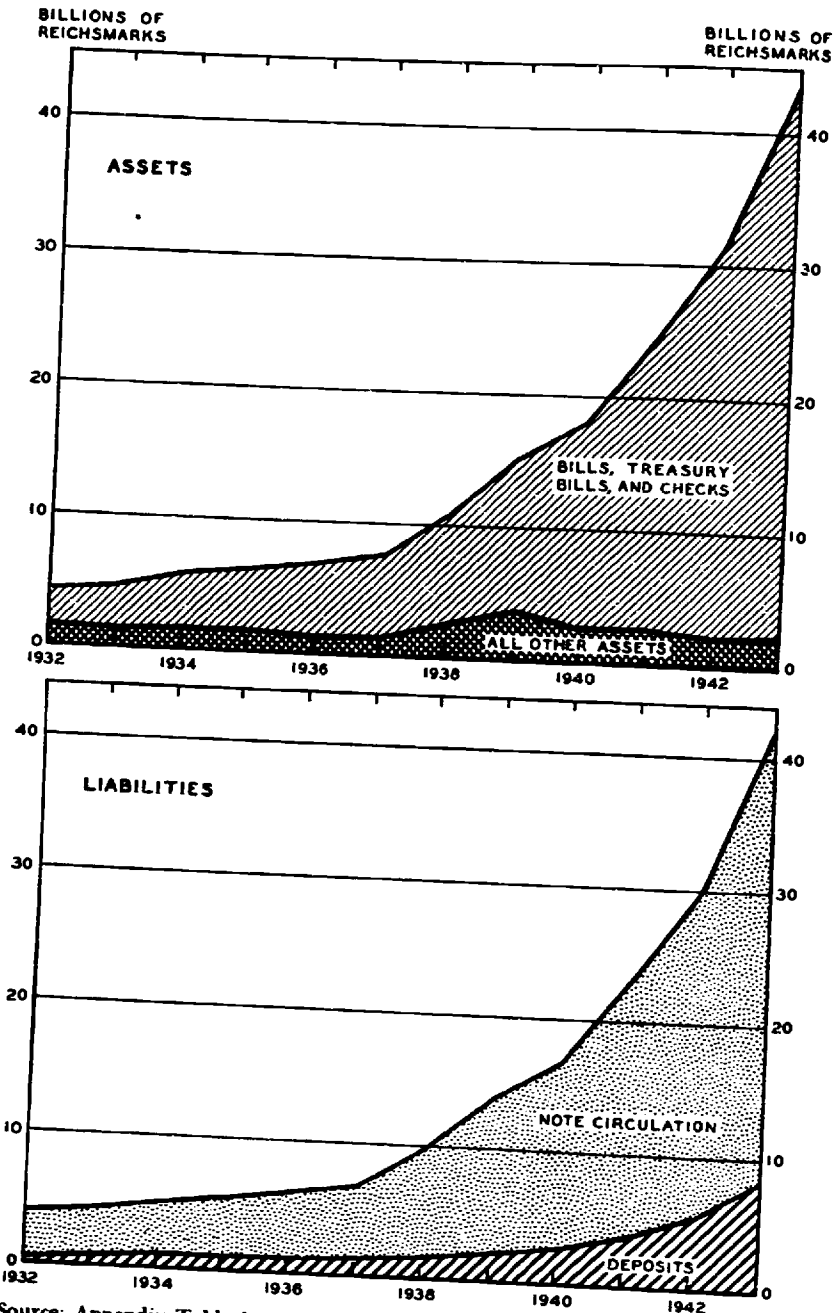
government and as thoroughly regulated by direct controls as the Nazi economy, an increase in the public debt or changes in the balance sheets of banks have lost much of the importance usually attached to them. While they still register performances in the economy, they no longer operate as major barometers and guides to the government. Since all significant decisions to produce, invest, and consume are made in the light of minute statistics of available resources and potentialities, indications of financial developments no longer serve the purposes that they fulfill in an economy based on the traditional market mechanism.

Since the time has not yet come to make an exhaustive study of developments in the money and capital markets during the Nazi regime, we shall have to limit ourselves to indicating in broad outline the effects of government expenditure on central and commercial banking. Although the information which has become available is scanty and incomplete, it throws some interesting light on the development of Nazi war finance. Not only does it portray those characteristics of wartime banking that on the whole are common to all belligerent countries—*increase in deposits, note circulation, and bank holdings of government paper*—but it suggests some additional observations.

#### THE REICHSBANK

Two developments are characteristic of the German money and capital markets both before and during the war: the increasingly large use of central bank credit to cover government expenditure, and the exploitation of all the resources of the credit mechanism for the same purpose. The reader may recall our discussion about the changes in banking legislation in the prewar period of the Nazi regime. We emphasized that most of these changes were made in view of the government's intention to prepare for war and to adapt the banking system to the financial requirements of a military conflict. This, we said, was particularly true of the "reform" of the Reichsbank Law. The development of the Reichsbank's status bears out our interpretation (Chart 1). The Reichsbank became the solid basis upon which German war finance has been operating. The provision enabling the Reichsbank to use government obligations in unlimited amounts as cover for the notes with which they were bought was the key to German war finance and to the "liquidity" of

**CHART 1— PRINCIPAL ASSETS AND LIABILITIES OF THE REICHSBANK, DECEMBER 31, 1932-43**



Source: Appendix Table 1.

the credit system<sup>149</sup> for the Reichsbank could purchase at any time any amount of government paper that the public and the banks were not willing or able to buy. And the Reichsbank was compelled to make increasing use of that provision.

Even in the very early years of war preparation, the Reichsbank took active part in financing armament expenditure. By the end of 1937, the total amount of bills held by the Central Bank—which were to a large extent Treasury bills or government-guaranteed paper—was more than twice as much as its holdings in bills in the boom years before the 1929 depression when the Reichsbank portfolio consisted largely of commercial paper. After 1937, the Reichsbank “bill” portfolio grew at an accelerated pace. From the outbreak of war until December 1943, the Reichsbank gained over 30 billion reichsmarks in bills of all types (the “bills” were chiefly government paper<sup>150</sup>) while its note circulation grew by about 23 billion during the same period. By the end of 1943, the Reichsbank held in its portfolio about 20 percent of the entire Reich debt, an indication of how important the purchase of government paper by the Central Bank had become for the financing of the war. Taking the decade of the Nazi regime since 1933 as a whole, the figures on Reichsbank holdings of government paper are an interesting corollary to the available information about German expenditure for military purposes presented in the next section. The Reichsbank statistics offer an illustration that German military preparations gained momentum beginning in 1937. The total amount of bills held by the Reichsbank more than trebled in the seven years from the end of 1932 until the outbreak of war; and it increased four times in the next four and a half years, from the beginning of war until the end of 1943.

### COMMERCIAL BANKS

Since publication of official banking statistics was greatly curtailed in 1939,<sup>151</sup> information on the effect of government expenditure upon commercial banking does not exist for the entire period of the Nazi regime. The only available data covering the development

<sup>149</sup> This mechanism for government borrowing which the Reichsbank Act of 1924 deliberately sought to prevent, resembles very much the system used during the last war and in the inflationary period until the fall of 1923.

<sup>150</sup> League of Nations, *Money and Banking 1939-40*, Vol. I, p. 52.

<sup>151</sup> League of Nations, *Money and Banking 1940-42*, p. 118.

from 1933 to the end of 1942 refer merely to the "Big Five,"<sup>152</sup> which were the five leading banks in Berlin, leaving out the many other banks in the country. The increase in government paper and in deposits of these five banks was very small until the outbreak of war. Although their "bill" portfolios contained increasing amounts of various types of government-guaranteed bills instead of commercial paper, the leading banks do not seem to have helped a great deal in financing war preparation directly. This changed, however, with the outbreak of hostilities. Since the beginning of war until the end of 1942, the deposits of the five leading banks more than doubled and their holdings in government paper increased about five times. (See Chart 2.) We have no way of knowing whether the change in assets and liabilities of the "Big Five" may be considered a fair indication of the trend of developments in all commercial banks after 1939. We know, however, that before 1939, starting almost with the beginning of the Nazi regime,<sup>153</sup> both deposits and holdings in government securities and government-guaranteed paper by *all* commercial banks, including the "Big Five," increased considerably more than in the "Big Five" alone. Going a step further and including also the many other banks that existed in Germany, such as *Girozentralen*, state and provincial banks, workers banks, agricultural banks, land banks and savings banks, we will find<sup>154</sup> that the share in the prewar debt of the government, which was not placed with either the public or the insurance companies, was considerably larger than the statistics on "commercial" banking suggest. For the period after the outbreak of war, we know from an official source that about four-fifths of the increase in the short-term debt from September 1939 to the end of 1941 was placed with the banking system (including the Reichsbank) and that the percentage of long-term paper bought during the same period by the entire credit apparatus (including savings banks and insurance institutions) was not much smaller.<sup>155</sup>

The statistics on Nazi banking just described, however incomplete they may be, make it clear that the government war expenditure

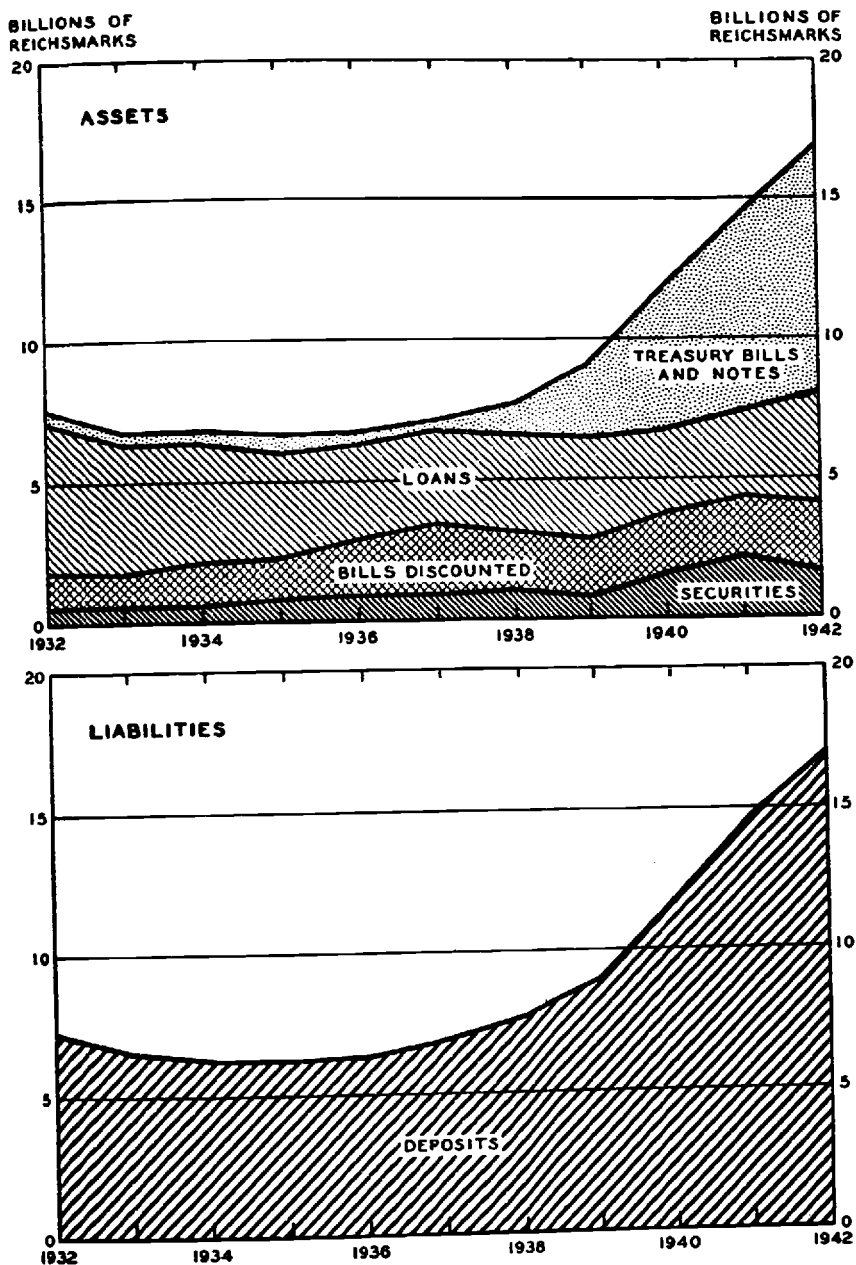
<sup>152</sup> Deutsche Bank, Dresdner Bank, Commerz- und Privat Bank, Reichs-Kredit-Gesellschaft, Berliner Handels-Gesellschaft.

<sup>153</sup> League of Nations, *Money and Banking 1938-39*, Vol. II, p. 91.

<sup>154</sup> *Ibid.*, pp. 82-88.

<sup>155</sup> *Wochenbericht des Deutschen Instituts für Wirtschaftsforschung*, Vol. 15 (1942) p. 41.

**CHART 2 — PRINCIPAL ASSETS AND LIABILITIES OF THE "BIG FIVE"  
COMMERCIAL BANKS IN BERLIN, DECEMBER 31, 1932-42**



Source: Appendix Table 2.

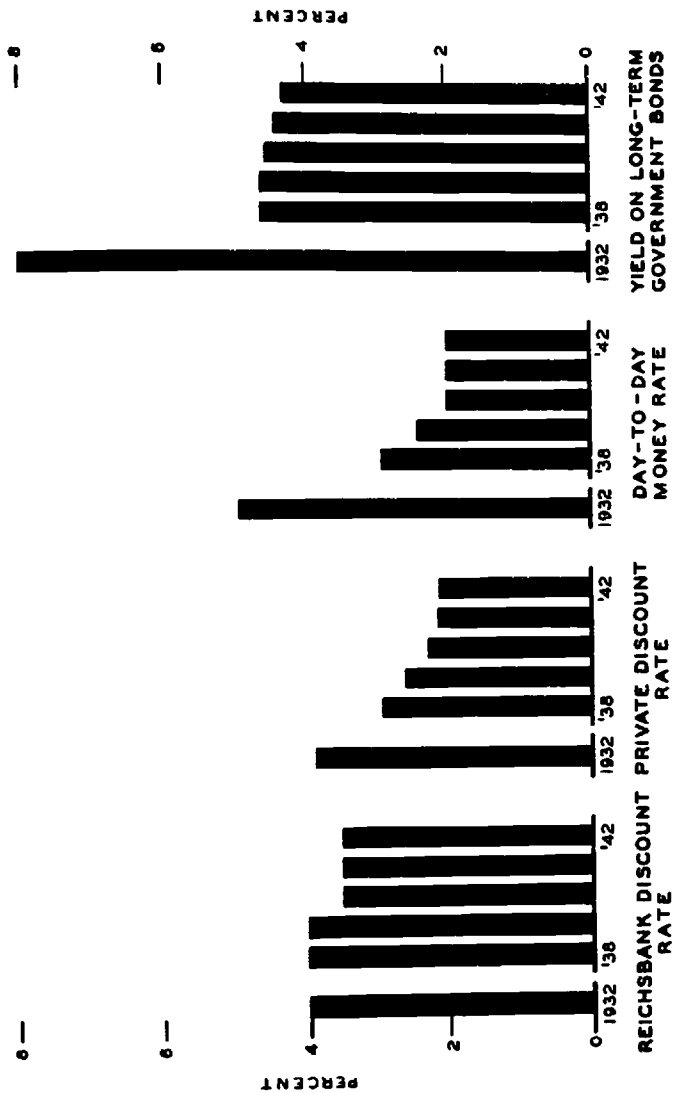
was met to an increasingly large degree through funds provided by the manifold agencies of the credit system. Since we know of the government's efforts ever since the early days of war preparation to reserve the resources of the money and capital market as much as possible for itself, the question might well be asked whether and to what extent credit institutions were able (or permitted) during those years to satisfy financial needs of the country outside government requirements. All the information available on this score, which is as incomplete as any other statistical material about banking, tends to show that the significance of the banking system has changed greatly in providing funds for its private customers. The information on the holdings of commercial bills by banks is exceedingly poor and inconclusive. However, it is frequently suggested in pertinent literature that commercial bills have become less and less significant in the banks' portfolios. There is no doubt that, to put it very carefully, their amount, if anything, has not risen.<sup>156</sup> Similar evidence exists about loans made by banks to their private customers. The total amount of commercial loans and advances made by all commercial banks remained almost stagnant during the period of war preparations and increased slightly in the last few months before the outbreak of war. Information for the war years is again available only for the five leading Berlin banks. In this case, however, they may be considered fairly representative for commercial banking as a whole. The total amount of commercial loans remained about stable during the first two years of war. Then, however, the situation started to change. The total of commercial loans increased rather considerably in 1942. Many pieces of information tend to show that private enterprise then found it more difficult than during the many previous years to self-finance both new investment and the needs of daily transactions, and was compelled to appeal to the money market and also to the capital market. We do not know whether there has been a further development in this direction during 1943 and whether the change just described has any specific significance for Nazi war finance as a whole.

The Nazi government has been very anxious throughout the years of its regime to reduce the rates of interest for the various

<sup>156</sup> League of Nations, *Money and Banking 1938-39*, Vol. II, p. 81.



CHART 3 - INTEREST RATES IN GERMANY, DECEMBER 1932, 1938-42



Source: Appendix Table 3.

types of loans and issues. This was done partly for ideological and political reasons, partly to limit the government's cost in financing the war. It was admitted even by official Nazi sources<sup>157</sup> that the reduction of interest rates, continued during the war years, had no significance upon the size of the credit volume in the economy; it rather illustrated "the desire of the Reichsbank to maintain its easy money policy and was a programmatic demonstration of its fundamental attitude on the interest rate problem." Since we have discussed that policy in greater detail before, it will suffice here to call attention to the movement of interest rates shown in Chart 3 and to emphasize their limited significance for an economic analysis of Nazi war finance.

<sup>157</sup> *Wochenbericht des Deutschen Instituts für Wirtschaftsforschung*, Vol. 15 (1942) p. 32.