The Austrian School of Economics and the Gold Standard Mentality in Austrian Economic Policy in the 1930s*

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> “All right,” said the Cat; and this time it vanished quite slowly, beginning with the end of the tail, and ending with the grin, which remained some time after the rest of it had gone.
>
> Lewis Caroll, *Alice in Wonderland*

Introduction

Eric Hobsbawm, the famous British historian, once chose Austria as an example of the inverse relationship between “the supply of good economists” and “the fortunes of national economies”:

> Pre-1938 Austria, where such theorists were plentiful, distinguished and consulted by governments, was not an advertisement for economic success until after 1945 when, as it happens, it had lost all its distinguished older theorists without acquiring comparable replacements.[1]

This quotation hints at the question to be dealt with in this paper, namely, the extent to which Austrian economic policy in the 1930s was shaped by the power of Austrian liberal ideas. Furthermore, it suggests a possible answer, namely, that by relying on the advice given by the Austrian economists policy-makers fell victim to the inadequacies of orthodox economic thought.[2] However, before we can scrutinize the relationship between economic thought and economic policy in the 1930s, we must identify the economists, the ideas attributed to them, and the point of view from which economic policy will be examined. Broadly speaking, we will limit our question to the influence of the so-called “Austroliberals” on Austrian economic policy regarding its handling of the Great Depression of the 1930s, and we will concentrate on the link between theory and policy as provided by the “gold standard mentality.”[3]

In the following sections, we will begin by defining more precisely these elements of our inquiry. Then we will try to establish the connection between the economists’ policy recommendations and actual economic policy, where it will be convenient to distinguish between two phases: the first one from 1929 to 1933—the beginning of the downturn, the *Creditanstalt* crisis and the slump into deep depression; and the second one from 1934 to 1938—the weak recovery under the changed conditions of the “corporate state.”[4]

The Austrian Economists

To begin, we will review briefly those Austrian economists relevant for our story.[5] First, there is what may be termed the "liberal core" of the Austrian school of economics, whose tradition goes back to Carl Menger and Eugen Böhm-Bawerk.[6] In the interwar period this core consisted of Ludwig Mises (of the third generation of the Austrian school) and Friedrich August Hayek, Fritz Machlup, and Gottfried Haberler (of the fourth generation)[7] as well as some lesser known economists like Richard Strigl, Erich Schiff, and Martha Stephanie Braun,[8] to name but a few. These economists were, at least up to the middle 1930s, the main protagonists of liberal economic discourse, which ranged from the debates in the numerous "private circles" existing outside the university to their academic and non-academic publications and pamphlets.[9] Among them, Ludwig Mises was the dominant figure in theory as well as in policy. As the secretary (up to 1934) of the Chamber of Commerce he shaped the opinion of this interest group and thereby influenced actual policy-making. Picturing himself in his recollections, Mises avowed: "I was the economist of the country." [10] Mises also initiated the founding of the Austrian Institute for Business Cycle Research in 1927, which, due to grants from the Rockefeller foundation, could sustain some independence from interest groups and government interference and so turned into a significant source of policy monitoring, if not advice. Friedrich Hayek was the first director of the Institute, from 1927 to 1931, and Machlup and Haberler were temporarily affiliated with it.

Next we turn to the margin of Austroliberalism, that is, to a strand within the Austrian school of economics that was, in contrast, more skeptical towards liberalism than was the core of Mises and his followers. This part of the tradition derives from Friedrich Wieser,[11] and in the 1930s it was represented foremost by Hans Mayer and Oskar Morgenstern. Hans Mayer, a pupil of Wieser, was the sole member of the Austrian school to hold a chair at the University of Vienna. In the 1930s, however, he spent most of his time in intrigues, and his scientific contributions as well as his influence on economic policy must be considered negligible.[12] In the 1920s, Oskar Morgenstern, after a short spell under the influence of Othmar Spann, turned to the Austrian marginal utility school and worked as an assistant to Mayer. When he returned from a three-year Rockefeller fellowship abroad, he joined Hayek at the Institute and finally succeeded him as director from 1932 until 1938. Furthermore, though formally under the supervision of Mayer, he in effect acted as managing editor of the *Zeitschrift für Nationalökonomie*, the single Austrian (and, after 1933, German-language) economics journal of international reputation.[13]

Finally, for the sake of comparison we must also take account of those Austrian economists who adhered to the traditions of the historical or romantic schools of thought.[14] Again, we shall distinguish two groups. In the first one we put those influenced by Catholic social teaching, who later turned into faithful supporters of the Austrian corporate state. As two representative examples we pick out Josef Dobretsberger, who for a short time acted as Minister of Social

Administration and then became university professor in Graz, and Richard Kerschagl, a member of the State Council from 1934 to 1938 and professor at the *Hochschule für Welthandel* in Vienna starting in 1937. The economic thought of both might be characterized as syncretistic and theoretically not very rigorous, to put it mildly.[15]

The second group is that of the so-called universalistic school, most prominently represented by its founder Othmar Spann and his disciple Walter Heinrich.[16] Spann, professor of economics at the University of Vienna, was involved in a never-ending struggle with the untiring Mayer. Spann was the main source of an anti-liberal and anti-democratic movement, especially among intellectuals and academics.[17] Although he was one of the leading propagators of the idea of a corporate state, his version was closer to the Italian style of fascism than to the homegrown one. Because he was more interested in the great issues (e.g. of transforming liberal democracy into the "true" ideal state), the specific contributions of universalistic doctrine to economic theory and its influence on economic policy in a narrower sense were only marginal. The influence of the universalistic school on economic policy is, therefore, neglected in this study. We should, however, be aware that members of this school might be excepted when we impute unanimity of opinion to Austrian economists.[18]

How, then, may members of the Austrian school of economics have influenced actual economic policy? The first and direct way is, of course, by acting more or less formally as policy advisors. This is the role that Mises played with some success throughout the period from the beginning of the First Republic to his resignation from the Chamber in 1934. Then, in the era of the corporate state the position of policy advisor was to some extent filled by Oskar Morgenstern, one of the few members of the Austrian school remaining in Austria up to 1938.

Yet there is another, indirect way to influence economic policy, namely, by shaping public opinion on economic matters. To do so, the scientific debate that proceeds in monographs and contributions to scientific journals must be transformed into the simple lessons and catchy phrases of journalism. And, indeed, the members of the Austrian school were heavily engaged in this activity of educating public opinion in the truths of Austrian economics. A few striking examples will suffice. From March 1932 to May 1934, Fritz Machlup ran a weekly column in the Viennese daily, *Neues Wiener Tagblatt* titled "Zwei Minuten Volkswirtschaft" (Economics in two minutes).[19] Between 1931 and 1933, the same newspaper regularly published comments on current problems of economic policy supplied, according to a formal contract, by Machlup, Morgenstern and some collaborators from the Institute. These comments were partly anonymous, under the title "Beiträge zur wirtschaftlichen Vernunft" (Contributions to Economic Reason), partly signed by the authors.[20] As a final example we might mention the project, on a much smaller scale, of Julius Meinl's *Wirtschaftliche Rundschau*, where for the first year (1934) Morgenstern worked as managing editor.

Austrian Economic Theory and the Gold Standard Mentality

One of the unique features of "Austrian economics" consisted of the specific theories on which its adherence to the gold standard mentality rested. The common point of reference was that of a frictionless economy without money as laid out in the contributions of Menger and Böhm-Bawerk.[21] In such an economy the capital market succeeded perfectly in transforming "true" savings into capital formation (in modern terms: investment), where the capital structure of the economy was described, according to "Austrian" capital theory, by the "roundaboutness" of production. In this sense, net investment tended to lengthen the period of production and thereby to make the economy more productive. The seminal contribution of Mises[22]—later on elaborated and refined by Hayek and others[23]—was to introduce money into this system and to relate it to the question of the business cycle.

The crucial characteristic of such a money economy was that the flows of saving and investment now were transacted in money and intermediated mainly through the banking system. Changes in the stock of money, i.e., inflation and deflation, typically affected the capital market by adding to or subtracting from the supply of savings. Inflation, therefore, meant an additional "artificial" flow of capital supply that lowered the money rate of interest to a level below the equilibrium rate, i.e. what it would have been if only true savings were coming to the market, and induced an increase in investment. As the resources of the economy were supposed to be already fully employed, the increase in investment (i.e., the lengthening of the period of production) could only be realized if and as long as continuing injections of money enabled the entrepreneurs to bid away the factors of production from their use in the production of consumption goods and redirect them to the production of capital goods, the so-called process of forced saving. However, for a variety of reasons this situation could not be sustained indefinitely. Yet, as soon as inflation stopped, the funds supplied to the capital market were reduced to true savings, which was not sufficient for maintaining the capital structure. This was said to be "too roundabout," hence the notion of "overinvestment" and a theory to explain the onset of crisis. Due to "capital shortage," which was in effect a shortage of savings, capital goods must be liquidated and factors of production reshuffled to the production of consumption goods; because of the immobility and specificity of capital goods and, possibly, labor the consequence was unemployment and idle capacities. Furthermore, when the banks began calling back loans, a process of deflation was started. However, if deflation and depression could run their course, equilibrium—as the "Austrians" maintained—would be safely restored. Ultimately, depression would lower wages sufficiently to make production again profitable and would encourage saving by redistributing income, so that after the necessary adjustments the deflated capital structure could be maintained again.[24]

This cyclical explanation of the depression was supplemented by a structural one that referred to a more long run perspective. This was again based on the view that the supply of true as opposed to forced savings was a precondition for furthering investment and economic progress, and, in turn, that profits are the main source of savings. In this regard, high taxes and social duties, budget deficits, and excessive real wages (resulting from the activity of the trade unions) were regarded as burdens drawing on profits and savings and eventually detrimental to economic growth. At the worst, these burdens might even lead to a decumulation of capital or, as the "Austrians" put it, to "capital consumption," whereby worn out parts of the capital stock could not be replaced due to a lack of savings.[25] In Machlup's vivid description this meant: "We eat up our streets, our railways and our houses. We make a fire with our furniture." [26]

Evidently, both of these "Austrian" explanations of depression and unemployment shared a common message with regard to policy. The business cycle approach considered the depression as the inevitable consequence of the boom, which in turn was caused by inflation. Therefore, as a consequence, a strictly non-inflationary policy was called for as a kind of prophylactic device. As this excluded the possibility of financing budget deficits by money creation, i.e. inflation, such deficits could only be financed by recourse to the capital market. In this case, however, part of the supply of savings would be channeled into presumably unproductive uses by the government instead of into profitable private investments. Furthermore, after the traumatic experience of hyperinflation in the 1920s, any sustained budget deficit even if financed by issuing bonds might, in the end, generate a self-fulfilling expectation of future inflation. Therefore, sound finance, i.e., budgets balanced at a low level of expenditure, was considered a necessary complement to sound money.

How was this all related to the gold standard? Ideally, the aim of preventing an inflationary boom would be achieved by following a policy of "neutral money," which was, apart from a few complications, equivalent to stabilizing the effective quantity of money (i.e., the left-hand side of the so-called quantity equation) or the level of factor prices (e.g., wages).[27] However, when for lack of empirical knowledge this ideal could not be accomplished, the gold standard was seen as a practicable though second-best alternative. Because a gold standard meant that the gold price of the currency was fixed, this left little room for inflationary policy; it worked as a "golden brake" on credit creation. Furthermore, the gold standard system also implied a policy of no interference with international capital flows, so that again the central bank of a single and, moreover, small country did not have much leeway for manipulating the rate of interest, e.g., in pursuing a policy of "cheap money." So in the view of the "Austrians" the gold standard was the best system available for safeguarding against inflation.[28]

Due to this latter property the gold standard was also regarded as a means of securing confidence in monetary stability, or, as Bordo and Rockoff put it, a "good housekeeping seal of approval." [29] Conversely, infringements of the gold standard were bound to shake confidence.

However, the problem with this confidence argument is that it is a circular one. Adherents to orthodox theory argued that some measures of policy (e.g., a devaluation) would shake confidence for fear of its negative effects because they supposed that confidence was shaped by orthodox theory, which predicted just these negative effects. So, indeed, the greater the success of orthodox theory in influencing relevant opinion, the more self-fulfilling its predictions might become.

Besides these (to use anachronistic terms) macroeconomic features of the gold standard, two aspects of a more microeconomic nature must also be noticed. First, the gold standard had to fulfill not only the internal task of preventing inflation but it was supposed to serve also as the prerequisite for the external aim of free trade to which the "Austrians" fully subscribed. Free trade (meaning the absence of tariffs, export subsidies, import restrictions etc.) was considered both a source of growth and of an efficient allocation of resources.[30] For bringing about all the necessary adjustments (e.g., to eliminate the disequilibria stemming from trade deficits, transfers or reparation payments), the "Austrians" relied on the workings of the classical mechanism, that is—given the fixed gold parity—flexibility of prices and wages.[31]

Second, the gold standard was associated with the system of liberalism in general, not only with regard to foreign trade. This meant, again, minimal interference with and regulation of markets, e.g., in the realm of industrial policy. The Austroliberal twist on this issue was mainly due to Mises, who singled out the labor market and the activity of trade unions as one of the fields of utmost concern. In this regard the uniqueness of Mises' hostility towards the trade unions must be emphasized. According to him, their capability of fixing wages was based on their use of force (strikes and the possibility to prevent idle workers from undercutting the wage bargain)[32] and on the provision of state-financed unemployment benefits. In the end he considered the abolition of the power of the trade unions as an inevitable concomitant for the restoration of prosperity.

Furthermore, in Mises' view liberalism was the only viable economic system. As to its rivals, interventionism and socialism, neither was viable. On the one hand, in order to fulfill its aims, interventionism could not stop short of outright socialism after a never ending spiral of one intervention (e.g., the fixing of prices) necessitating a still graver next one.[33] On the other hand, as he tried to prove in the so-called calculation debate, a properly working socialist system was impossible because of its lack of a measuring rod for balancing benefits and costs.[34] Therefore, any deviations, even small ones, from liberalism pure and simple had to be rejected.

To summarize, the policy goals as recommended by the "Austrian economists" consisted of sound money and finance, free trade, and generally free markets, where the gold standard was considered as a means for pursuing these goals, in particular the macroeconomic ones. This implied that the burden of adjustment to any disturbance had to be laid on the flexibility of prices and wages as compared with the rigidity of rules to be followed by policy. "Rigid doctrines and flexible prices" is how P. Clarke described it, as contrasted with the "Flexible doctrines and rigid prices" of the Keynesian alternative.[35] This set of policy prescriptions has recently been termed "the gold standard mentality," [36] and it is the consensus view of economic historians (or at least of the economists among them) that this mentality was the decisive factor responsible for the depth and the length of the Great Depression. In the following section we will examine the extent to which Austrian economic policy conformed to that mentality and the extent to which it reflected the policy advice of Austroliberal economists.

The Economists and Economic Policy: The Depression

The world economic crisis that started in 1929 as a seemingly normal cyclical downturn only to degenerate from 1931 onwards into the deepest depression ever experienced by the capitalist economic system hit the Austrian economy especially hard.[37] At the bottom of the depression gross national product was 23% down from its pre-depression level and unemployment amounted to 25%.[38] In this section, after a short overview, we will concentrate on economic policy and on the advice given by the "Austrian economists" with regard to two particularly important questions: the handling of the *Creditanstalt* crisis and its consequences, and the problem of deflation.

Applying their theory, the "Austrians" [39] identified the general causes of the depression to be (1) overinvestment as a consequence of prior inflation, (2) capital consumption due to excessive taxes and social duties as a remnant from the social legislation at the beginning of the Republic, and, in particular, (3) high wages as a cause of unemployment. Therefore, in the first stage of the depression the policy recommendations of the "Austrians" were the usual ones: to cut production costs and to abstain from inflation.[40]

In the already gloomy state of the Austrian economy the breakdown of the *Creditanstalt* in May 1931 had the effect of a first-order economic catastrophe.[41] It immediately turned out that the bank was not just illiquid, in which case the usual lender-of-last-resort operations would have saved the situation, but insolvent. Thus, the choice for policy was either to accept bankruptcy and liquidation or to undertake a bail out – and taking account of the fact that a large part of Austrian industry was in some way controlled by the *Creditanstalt*, the government opted for the latter. However, until a solution was reached eventually in the bargaining with foreign owners as well as creditors, a run on the bank developed that soon turned into a run on the currency.[42] This left the central bank (under its president Richard Reisch) in the unfortunate position of, on the one hand, supplying liquidity to the *Creditanstalt* by increasing its bills portfolio and, on the other hand, of losing its exchange reserves.[43] After watching the deteriorating situation more or less passively for almost half a year, finally, when the central bank had almost run out of its reserves, the government introduced exchange controls, which quickly developed into a bureaucratic system that stifled Austrian foreign trade. Meanwhile, Reisch had fallen victim to a controversy about the limits of the central bank's support of the *Creditanstalt* and was replaced by Viktor Kienböck, who, on short notice, returned to a restrictive policy. Finally, after the introduction of a moratorium on foreign payments, the Austrian government in 1933 managed through the Lausanne Protocol to receive a foreign loan, which was primarily used to pay back short-run government debts to the central bank, thereby replenishing the bank's exchange reserves. The price to be paid for the loan was, however, the reestablishment of external custody of Austrian economic policy.

The reaction of the "Austrian economists" to the measures taken by the government and the central bank were predictably negative. They were unanimous in declaring the ongoing increase in the bills portfolio of the central bank to be an example of irresponsible inflation that had to be stopped as soon as possible.[44] To them the loss of reserves and the eventual depreciation of the Schilling clearly signaled the inflationary nature of these policies. Machlup rendered the "official" statement of this position in a League of Nations memorandum on the credit crisis.[45] His paramount advice was for the central bank to intervene by no means without inflation there would also be no threat to its exchange reserves. In order to protect illiquid banks from withdrawals of (foreign) deposits he considered the imposition of a moratorium as justified, yet in the case of insolvency (as of the *Creditanstalt*) there was no alternative to liquidation.[46] In any case, if the central bank intervened and injected liquidity, it must be ready to accept the ensuing depreciation of the currency, i.e., it must be prepared to go off gold and float its currency—although Machlup regarded this outcome as decidedly inferior to the non-interventionist policy.[47] The worst Machlup envisioned a central bank could do was exactly what the Austrian national bank did do: to intervene and use exchange controls to prevent the necessary depreciation.[48] Therefore, from the point of view of the "Austrians" the handling of the *Creditanstalt* crisis must be considered a disaster; in the end, economic policy preferred to preserve the letter instead of the substance of the gold standard.

Now that the disaster had happened, what could be done? In effect, after Kienböck had replaced Reisch as president of the central bank, the "Austrian economists" staged a campaign intended to make the best of a bad situation, a campaign that turned out to be surprisingly successful—probably not only due to their own powers of persuasion but also to a little help from external pressure.[49] The aims of this campaign were threefold. First was the restoration of a restrictive monetary policy. Second was the elimination of exchange controls, at least with regard to foreign trade, if not to financial transactions. This was the more urgent as the free-market rate of the Schilling[50] had declined markedly in comparison with the official parity, so that trading at the overvalued official rate had the effect of subsidizing imports and taxing exports. Furthermore, in the attempt to make these controls effective a host of regulations had to be introduced, which further crippled Austrian exports. And third, as a consequence of the first two steps, the "Austrian" economists pushed for pegging the Schilling again to a gold parity. Regarding the latter point, there was some controversy among the "Austrians" (and in the business community) about whether monetary restriction should be intensified in an attempt to return to the old parity—predictably this was Mises' point of view [51]—or whether some depreciation should be accepted.[52] Finally, when all three aims were realized after a long drawn-out process, the Schilling was stabilized at 20% under par, which meant that it had somewhat appreciated from its lowest free-market level. Yet the most important aspect of this episode was not that even the adherents to the gold standard were ready to accept some devaluation of the currency (or, conversely, admit that a greater devaluation might have been helpful) but that by the fixing of a parity the exchange rate was reintroduced as a guide for or an intermediate target of monetary policy.[53] Thus the gold standard, although already limping at this time, could again act as a brake to inflationary policy.

This points to the next subject of our inquiry: the nature of monetary policy. The main question here is, of course, the extent to which monetary policies in the 1930s, and in particular in the Kienböck era, are to be considered as deflationary. Obviously, an answer presupposes a clarification of terms. As already pointed out above, the contemporary meaning of inflation and deflation was simply that of an increase or decrease in the effective quantity of money. This shifts the problem to the definition of what is to be counted as money; fortunately, the "Austrian" position is quite clear cut in this respect. According to Machlup, "Money is what acts as a medium of exchange," and therefore a broad definition of money is warranted that includes both currency and cash deposits, but not savings deposits.[54] He contrasts this with a (too) narrow definition that identifies money with "central bank money," that is, currency and the reserves held by the banks (see column B in Table 1 below).[55]

Table 1: Austria 1928-1936

Monetary Aggregates (end of year) and real GNP

	M1	M2	B	GNP
1928	99.0	95.8	94.4	98.6
1929	100	100	100	100
1930	97.6	103.3	100.2	97.2
1931	75.2	83.3	111.6	89.4
1932	61.9	76.3	105.8	80.2
1933	59.5	75.1	100.5	77.5
1934	54.9	73.2	107.2	78.2
1935	55.8	75.9	111.8	79.7
1936	53.7	75.3	112.4	82.1

Sources: M1 and M2: Schubert (1991, 104); B: "Notenumlauf und Giroverbindlich-keiten der Nationalbank", *Monatsberichte*, various issues; GNP: Butschek (1985, 46), own calculations.

As a next step we will take a look at the facts as they are now known to us. Table 1 exhibits the development of three different monetary aggregates throughout the 1930s. Besides central bank money, the table shows what is now called M1, that is, currency plus cash deposits, the aggregate most likely to represent the definition used by the "Austrian economists," and M2, a still broader aggregate that includes savings deposits also.[56] To be fair, it must be noted that to contemporaries only data on central bank money were directly available; however, as has been variously pointed out, it would not have been difficult to calculate at least raw estimates of the other numbers.[57]

In Table 1 we recognize the inflationary momentum of 1931 in the 10% increase in central bank money, which was, however, swiftly counteracted and more than compensated in its effects on the broader aggregates when the public switched out of bank deposits and into cash.[58] So the depreciation of the Austrian currency was due less to an increase in the quantity of money than simply to the distrust caused by the fear of future rises in prices amidst an international environment of falling prices. The net result of the inflationary episode followed by stabilization was that the increase in central bank money had nearly been reversed, whereas the broader monetary aggregates had decreased by as much as 45% and 25%, respectively. Evidently, combined with relatively rigid prices and wages, this produced a nearly equiproportionate decrease in production.[59] And, as can be ascertained from the table, this situation was not destined to improve much henceforth.

This was not, however, the way things were looked upon by the "Austrian economists." Contrary to what might have been expected, having in mind their definition of money, they concentrated on the behavior of central bank money. There they saw inflation in 1931 followed by stabilization. Yet, as the amount of central bank money remained disproportionately high in comparison to production, this stabilization was always considered to be prone to a revival of inflation.[60] Instead of taking into account the drastic decrease in bank deposits they preferred to stress the existence of "hoarded money," i.e., money in the hands of the public withheld from transaction purposes. (For a transitional period there was indeed some such phenomenon, in particular with regard to abnormally high holdings of 1000-Schilling notes). Such hoards were seen to pose a permanent danger to monetary stability, and the Austrian central bank was warned to be ready to sterilize any influx of hoarded notes into circulation by a restrictive policy.[61]

Although it is not certain that the "Austrians" were aware of the true extent of their apparently contradictory explanation of "inflation" in the face of a sharp shrinkage in the quantity of money (M1 or M2) and production, the closest they came to resolving this puzzle was to distinguish between "deflation" and "deflationary policy," or, in Amonn's terms, between "contraction" and "restriction." [62] The latter referred to a decrease in the quantity of money deliberately caused by actions of the central bank, e.g., by decreasing central bank money. The former was thought to be a quasi-automatic process resulting from the depression, e.g., the shrinking of bank money as caused by the repayment or the writing off of loans. In this sense the "Austrians" felt justified to state that Austria certainly experienced deflation but not deflationary policy. For example, Machlup flatly stated that "no country has pursued a deflationary policy." [63] And, moreover, in their view this kind of automatic deflation was an inevitable part of the depression, necessary to fulfil a kind of cleansing function and to force structural adjustments upon the economy.[64] With no recovery in sight, the stubborn refusal of the economy to behave accordingly was not blamed on ill-chosen remedies—that is, the passive response to automatic deflation—but on the economy's lack of flexibility, in particular of wages and prices.[65]

Fiscal policy followed a pattern similar to that of monetary policy. The onset of the depression led to a considerable budget deficit as early as 1930 that was exacerbated by the bail-out of the *Creditanstalt* in the following year. Yet, as part of the deflationary turn of Austrian economic policy in general, an almost balanced budget was realized in 1932 by means of severe cuts in expenditure and the introduction of new taxes. Extraordinary circumstances—the eventual reconstruction of the Austrian banking system, additional expenditures in connection with the civil war, and a moderate program of public works—led to higher deficits in the next years, all tolerated by the foreign supervisors, until in 1936 under the ministry of Ludwig Draxler an austere budget policy was pursued once more. Thus, fiscal policy might not appear as unambiguously deflationary in character as monetary policy.[66] Yet, it must be noted that the actual budget deficit is a misleading indicator when the economy operates significantly below normal (or full) employment, in which case even an unchanging deficit level will aggravate economic fluctuations. In addition, a more expansionist policy would have been difficult to finance, taking into account the dearth of a domestic capital market and the refusal of the central bank to participate in such financing. Furthermore, when in 1933 the *Trefferanleihe* was successfully floated, the decision to use part of its proceeds for the repurchase of bills from the central bank obviously had a deflationary effect, equal in principle to restrictive open-market policy. Therefore, despite some moderate deviations from orthodoxy, the generally deflationary stance of fiscal policy in the 1930s cannot be questioned.

Thus, when the Austrian economy reached the bottom of the depression in 1933, monetary and fiscal policy had settled for an orthodox course. However, in the aftermath of exchange controls foreign trade and industrial policy emerged as highly regulated fields, farther away than ever from the liberal ideals. Therefore, despite the ostensible return of economic policy to the rules of sound money and finance, the position of the "Austrian" economists was one of distrust and skepticism, not one of triumph.

The Dissolution: From Austroliberalism to Austropragmatism

The following part of the paper examines the time span from 1934 onwards. It will be argued in this section that this year approximately marks a break in the development of "Austrian economics." [67]

The primary cause for the change that the economics community underwent in these years was, of course, the emigration of the most prominent members of the Austrian school.[68] The reasons for emigration were manifold, ranging from growing anti-Semitism to the push and pull of career opportunities in Austria and abroad. For example, Hayek emigrated in 1931 when, on the initiative of Lionel Robbins, he was offered a professorship at the London School of Economics, obviously an offer too good to be rejected. Haberler spent a year (1931/32) as a visiting professor at Harvard and, after a short interlude in Vienna, worked for two years at the League of Nations in Geneva, eventually in 1936 becoming full professor at Harvard. Machlup spent two years as a Rockefeller fellow in the United States and Great Britain (from 1933 to 1935), and when his habilitation was unduly delayed by the usual intrigues, he decided in 1936 to accept an appointment as professor in Buffalo. Finally, in 1934, having reached retirement age, Mises took leave from the Chamber of Commerce in exchange for a professorship in Geneva.

As a consequence, the leadership among those economists remaining in Austria switched from Mises (and the other core members) to the young Oskar Morgenstern.[69] Morgenstern's role derived from his now dominant position within the Austrian economics community. He had already succeeded Hayek as the director of the Institute and consequently as the editor of the

Monatsberichte.[70] Furthermore, he was, due to the inactivity of Mayer, the sole managing editor of the *Zeitschrift für Nationalökonomie* and a referee for the important *Springer Verlag*. Moreover, the Institute provided one of the rare employment opportunities for economists outside academia, and, due to his excellent contacts with the government as well as with the Rockefeller foundation, he also had control over the necessary funds.

However, in the context of our study it is Morgenstern's role as a policy advisor that is of utmost concern.[71] First, in these years, in particular in 1936/37, he occupied numerous official positions among the proliferation of such within the Austrian administration. For example, he worked as an official advisor to the Ministry of Commerce, giving rise to a memorandum on the choice of transport system (railroads vs. automobiles), and as a member of the price commission.[72] Yet, to judge from Morgenstern's diary, it was the informal relations that mattered most. In this regard two connections stand out. On the one hand, he was very close to the president of the Austrian central bank, Kienböck, who dominated Austrian economic policy in general,[73] and, during the period of a decidedly austere budgetary policy, to the Austrian minister of finance, Draxler. It is in this time span that he supplied the government with a memorandum on the policy alternatives in the face of the devaluation of the gold bloc currencies. On the other hand, he was also a member of the (partly overlapping) circle of Julius Meinl, who relentlessly pursued the quest for a less tightly regulated and more liberal economy.[74] Although Morgenstern seems to have been open in all directions, an attempt to relate him to parts of the *Heimwehr* failed because he considered their proposals too "dreadful." [75]

The crucial aspect of this transition from Mises to Morgenstern was that Morgenstern turned away to some extent from the foundations on which the Austrian school had based its policy advice. This change took place on different levels. Most importantly, Morgenstern rejected the aprioristic foundation of liberalism advocated by Mises. Instead, he argued that the validity of economic theories must be determined on empirical grounds and that policy advice must be purely technocratic, i.e., free of value judgments. Therefore, Morgenstern strongly objected to the idea that economic theory could "prove" the superiority of a liberal policy. To the contrary, in his view the economist as a policy advisor had to accept the aims that were determined by the political process.[76] Furthermore, he endeavored to make economics an "exact science" by using mathematical tools, which the other "Austrians" generally abhorred.[77]

With regard to the substantive issues, Morgenstern was also rather critical of some basic tenets of "Austrian economics." This is highlighted when looking at the three important controversies in which the Austrian school was involved in the 1930s: on business cycle theory and policy (vs. Keynes), on capital theory (vs. Knight), and on socialist calculation (vs. Lange).[78] Morgenstern remained largely agnostic in the last one, and he sided (in Morgenstern 1935) with Knight against the "Austrians" on capital theory.[79] His position with regard to the macroeconomic debate, as we may now term it, is more ambiguous, as he rejected Keynesian theory as well as the expansionist policy conclusions derived from it. Yet, he did not endorse a specifically "Austrian" theory of the business cycle but contented himself with an eclectic notion of the depression being an inevitable outcome of prior inflation. In some sense his belief in the appropriateness of the orthodox rules persisted, although he had turned away from their "Austrian" foundations.[80]

Even though Morgenstern's criticism of "Austrian" and traditional theory was often trenchant, he did not put forward a clear-cut alternative. He directed his main efforts towards a mathematical treatment of economics that should account for the peculiar role he attributed to the elements of time and risk, and of power and interdependence in situations of imperfect competition—considered as typical of modern economies. In any case, in those busy days in the 1930s Morgenstern was not able to accomplish his aim of writing the book to revolutionize economic theory; yet, some of his ideas found their way into the mainstream critique contained in the introduction to the *Theory of Games*. [81]

Having noted these developments within Austrian economics, we must now take account of the fact that the major event of 1933/34 in the political sphere was, of course, the end of democracy and the erection of the corporate state.[82] Therefore, it appears legitimate to comment briefly on the relationship of the Austrian school to democracy and to the corporate state, respectively.

The position of the Austroliberals is ambiguous at least. To begin with, Mises professed himself an adherent to democracy as the only political system consistent with liberalism, in contrast with dictatorship or a corporate state, which he rejected because they ultimately cannot safeguard against the danger of civil war and revolution.[83] However, his position became blurred as soon as he distinguished between democracy proper—that is, one enlightened by the spirit of liberalism—and that kind of democracy that is dominated by political parties in pursuit of special interests.[84] In any case, in Mises' view, Austrian democracy was permeated not only by special interests but by the descent into socialism and the use of violence, so it could not prove viable. This view was attested to by Machlup, who, in a speech on the "Political Situation of Austria," described Austrian democracy as one in which the conservative majority was not allowed to govern due to the leftists' threats of force.[85] On the other hand, the Austroliberals entertained no illusions about the corporate state. For example Max Mintz, a member of the Mises seminar, characterized the corporate state by its "clericalism" and "lack of economic freedom": "Never in the last 80 years was political and economic liberalism as dead as now." [86]

Morgenstern added a distinctive shade to the "Austrian" view. Drawing on his *Grenzen der Wirtschaftspolitik,* he argued for the necessity of a strong state to discipline the special interests otherwise prevailing. In particular, he considered democracies as less able than autocratic governments to take the necessary steps in case of a deep depression, e.g., to execute sharp cuts in the budget.[87] In this regard his judgment echoed that of those responsible for the end of parliamentary democracy in Austria.[88] Moreover, he maintained "that an absolutist-autocratic form of government, far from being necessarily inconsistent with a liberal economic policy, actually gives it ... much better chances than it has elsewhere." Yet, the economic policy of an authoritarian state might face the danger "that a particular group... will obtain control over the government and then use it shamelessly to its own advantage, or simply that there will be incapable, ignorant people and charlatans at the helm who may do untold harm out of their lack of understanding." [89] In this regard there was a clear discontinuity between Mises and Morgenstern, the former arguing for a kind of "minimal state," the latter for a "strong state" ready to intervene against the pursuit of special interests.[90]

Accordingly, despite their doubts on the efficacy of Austrian-type democracy the relations of the members of the Austroliberal core to the corporate state were somewhat strained, whereas Morgenstern—and more so the devout adherents to the new form of government—did not feel uncomfortable in lending their expertise to the solution of day-to-day economic problems. Conversely, the exponents of liberalism and the policy advice they rendered were considered with suspicion by the new regime, which had committed itself to an anti-liberal course. Under these circumstances it cannot be much of a surprise that the influence of the more pronounced Austroliberals evaporated after 1934. Apart from the fact that only the lesser known had remained in Austria, their career opportunities were hurt, both inside academia, where the only two vacant professorships in economics were awarded to Dobretsberger (in Graz) and Kerschagl (at the *Hochschule für Welthandel*),[91] and outside, in Morgenstern's recruitment for the Institute. Among the younger economists affiliated with the Institute after 1934—Ernst John, Reinhard Kamitz, Josef Steindl, Gerhard Tintner and Abraham Wald—none had close ties to the liberal tradition. As a final bit of evidence we might point to the petering out of the journalistic activities of the "Austrians." Machlup, for example, decided to close his regular column after the newspaper in too many cases refrained from publishing his contributions.[92]

The Economists and Economic Policy: The Recovery

The main characteristic of the development of the Austrian economy during the regime of the corporate state was that the recovery from depression was weak not only in absolute terms but also when compared to other countries.[93] In the following we will try to relate this lack of success in economic policy by singling out three topics: public works, the deflationary hard-currency policy, and industrial and trade policy.

The first topic I will address is that of public works, about which debate indeed stretched from the time of the Lausanne loan in July of 1931 until the end of the corporate state in 1938.

However, as the relevant views did not change much over time, a summary discussion is justified. Although there were a few attempts at fighting unemployment by public works (financed by parts of the proceeds from the "*Trefferanleihe*" of 1933, the "*Arbeitsanleihe*" of 1935 and the "*Investitionsanleihe*" of 1937), there was a broad consensus against them on economic grounds. Even when the government had opted for a public works program, at least some of its exponents, such as Kienböck, agreed to it only for reasons of political propaganda, not on its economic merits.[94]

The consensus against public works presupposed that they must be financed either by loans or by taxes, as any other kind of financing (e.g., by taking recourse to the central bank) would be inflationary, with all the well-known harmful consequences. In connection with the hotly debated Deutsch-Vertes plan[95] and the possibility of such inflationary finance for it, Haberler commented that the mere announcement of such a plan would already lead to a currency crisis.[96] On this occasion the "Austrians" also dismissed the theory of the secondary effects of public works, i.e., an early version of Keynes's "multiplier," as "primitive" and "naïve." [97]

Under non-inflationary conditions, the rejection of public works rested on two straightforward arguments, first, that "labor is merely shifted from one production to another" because "under given conditions and with a fixed wage level only a certain number of workers can be employed with a certain amount of capital," [98] and, second and even worse, that profitable private investment is replaced by unproductive government expenditure. The "Austrians" were seconded in their arguments by R. Kerschagl, who attacked public works as an example of an "ill-guided policy to use taxes and loans for investments that are from the very beginning doomed to yield no return," and by J. Dobretsberger.[99] Morgenstern noted with satisfaction that Kienböck was able to prevent the excesses of public works programs, and he reported a lecture by Wilhelm Röpke (one of the few expansionists among liberal economists) that was ill-received in the *Nationalökonomische Gesellschaft*.[100] Morgenstern also played a role in what should turn out to be the final episode in this regard. When in January, 1938 Ernst John tried to place a contribution into the *Monatsberichte* that argued for some public works, he was censored following an intervention by Kamitz and Morgenstern (then already in the United States). Eventually, John's article surprised the reader by taking an unexpected turn half-way in the argument and concluding with a reaffirmation of the importance of a stable currency.[101]

Next we turn to monetary policy.[102] As argued above, with the benefit of hindsight the data on broad monetary aggregates show that it was deflationary even after 1933. However, after the reconstruction of the Austrian banking system the peculiar characteristic of the loan and money market was its growing independence from central bank policy.[103] As the banking system, dominated by the *Creditanstalt*, which had acquired a quasi monopolistic position, had plenty of reserves and was extremely cautious in granting loans, the central bank could not have exerted much of an expansionist pressure even if it had intended to do so.[104] Thus, loans to businesses remained scarce and expensive in this period. Many contemporary and present-day observers blamed the *Creditanstalt's* monopoly behavior—raising prices and restricting quantities—as the main culprit, and undoubtedly there is a valid point in this view. However, such a "credit deadlock"[105] with a high yield spread between short-term and long-term has been found to be a typical phenomenon, in particular in countries that experienced banking failures, even in the absence of a monopoly bank.[106] In any case, this failure of the banking system to fulfil its task of intermediation was another cause contributing to the weakness of the recovery.

The deflationary stance of monetary policy was, of course, intimately connected to the stabilization of the currency and an austere budget policy. In both regards 1936 was a crucial year. First, after the deficits in the preceding years, the ministry of Draxler achieved an almost balanced budget. And second, in spite of the eventual breakdown of the gold bloc (then consisting of France, Switzerland and the Netherlands) and the devaluation of its member currencies, Austria chose a policy of inaction, i.e., not to devalue but to keep the parity. These decisions were the more significant as they came when Austria had ultimately acquired autonomy in its economic policies.[107]

Examining the policy advice from economists, we again start with that of Morgenstern. Indeed, it was just in these times that his contacts were closest to the inner circles of government, particularly to Kienböck and Draxler.[108] Apparently, the primary message he tried to convey was the necessity of urgent action. Only when he felt that time was going by without any such action taking place did he outline his view on the currency question in a memorandum, a modified version of which was published.[109] There Morgenstern made clear that the devaluation of the gold bloc in any case would impose sacrifices on the economy and that the alternative reactions to this event differed only in the way these burdens would be distributed. The alternatives were external vs. internal adjustment. External adjustment would be a devaluation of the Schilling. This would fail to relieve the budget (as a stable currency might do, because of the foreign currency denominated debt), it would undermine confidence, and, by sparking off price increases, it would hurt workers and alpine farmers. The preferred alternative was internal adjustment, that is, a policy of lowering prices, directly by means of price controls (with regard e.g. to agricultural prices) and indirectly by eliminating trade restrictions and opening up markets to foreign competition.[110] The byproduct of such a policy of *Auflockerung* would have been a step towards a more liberal economic system. As it turned out, the currency was not devalued; however, to Morgenstern's disappointment, none of the measures proposed for internal adjustment were realized to any reasonable degree.

Another aspect of this episode is noteworthy. In his diary of 24 July 1937 Morgenstern wonders that many "foreigners" have criticized the decision not to devalue. And in fact, Haberler (then already at Harvard and also with some intellectual distance from the Austrian school) in no less than four consecutive letters to Morgenstern did firmly argue that now the time had come to devalue. Unfortunately, Morgenstern's replies have not survived, yet the motives for the government's decision were referred to in the same diary entry as political obstacles, especially those of agricultural policy.[111]

However, the atmosphere of the debate on devaluation would be misrepresented if it were confined only to the technocratic level. In fact, the arguments for the hard currency policy were, as a rule, dogmatic if not delusive. A few examples will suffice. Dobretsberger, under the title "Conservative monetary policy-constructive economic policy," reaffirmed the validity of the old rules of monetary policy, which "have nothing to do with liberalism," as against "modern fibs," and he ended up with unqualified praise:

> Austrian economic policy since March 1933, the beginning of the authoritarian state, represents a powerful achievement that has been fully appreciated abroad. Primarily the monetary policy ... is the greatest capital of our economy.[112]

Even the more coolly tempered Morgenstern did not stop short of telling of the "admiration" felt abroad for Austria's monetary and financial policy: "If policy keeps to these principles in the future, again success cannot fail." [113] And the *Monatsberichte* in 1938 gave the following picture of this hoped-for success:

> As a consequence of a sound monetary and a cautious credit policy and by avoiding any kind of overinvestment Austria has achieved a much greater stability against future crises than those countries that now experience a very advanced phase of an excessively stormy boom.[114]

Indeed, it is true that Austria in these years never had to worry about such a stormy boom.

At this stage we might remark that the case for orthodox policy was based on the strength of orthodox opinion as well as on the weakness of the heterodox one. As not only the liberals but also Austromarxists (up to 1933) and the conservative adherents to the corporate state were hostile to "Keynesian" policies, the agitation for a reformist policy was left to monetary cranks and to those who were not afraid of following Nazi Germany and its economic experiments.[115] Therefore, most of the alternative proposals could be easily dismissed as irresponsible.

Finally, we take a look at the microeconomic level: how is the policy of the corporate state with regard to foreign trade, agriculture and industrial relations to be evaluated from a liberal point of view? In this regard historians and independent contemporary observers agree that, contrary to its announcements, the policy of the corporate state was more than ever dominated by certain special interests. The special interest of prime importance was obviously that of agriculture, where interventions abounded.[116] The aim of autarky combined with the stabilization of prices by controls eventually led to an intricate and overly expensive system (*Marktordnung*) of quantity controls, export subsidies and so on, which seemed to be taken from Mises' textbook description of the failure of interventionism. In any case, it was clear that the burden resulting from the preference granted to agriculture fell (in terms of higher prices) both on industry and on workers.

Similarly, in industry the ideal of free competition was paid only lip service, whereas in practice the tendency towards cartelization and monopolistic behavior was strengthened.[117] On the one hand, this was furthered by the existing trade restrictions (tariffs, prohibition and restriction of imports) that sheltered many industries from foreign competition, and, on the other hand, the very institutions created by the corporate state for the sake of "self-organization" (*Bünde, Kammern*) turned out to be ideal places for planning collusive actions. The result was high and stable prices, which, when combined with the deflationary effect of monetary policy, could not but weaken the recovery. Moreover, this development on the price side contrasts sharply with that of wages. The weakening of the trade unions and the increased "flexibility" of labor markets led to a decrease in the wage bill and henceforth of consumption demand.[118]

Again, Morgenstern's response appears to be typical of most Austrian economists. As was already pointed out above, he acknowledged that the prevalence of imperfect competition made some state intervention into industrial policy inevitable; he also backed away from the earlier proposal of the "Austrians"of a unilateral return to free trade, deeming it unfeasible under the current situation of international trade and incompatible with the ideology of the corporate state. However, he considered the elimination of price rigidities as the only way to a stronger recovery and to improved international competitiveness.[119] The easing of trade restrictions was the means that he urgently suggested. After the gold bloc devaluations, Morgenstern formulated with diplomatic skill:

> As the competent agencies of government ever have declared that most of these measures only resulted from the emergency situation of the time when they were introduced, it must be reckoned that the *Auflockerung*, as it fits in with the needs of the present, will not be long in coming. [120]

When Morgenstern's hopes failed, he resigned from the price commission.[121] It seems that his interests turned away then from policy advice, and he began earnestly to consider some of the invitations from American universities. Eventually, in 1938, he went as a visiting professor to the United States, whence he would not return to Austria. Yet, in the meantime, before his departure, his criticism of economic policies became more sharp. In the last speech that he delivered in pre-*Anschluss* Austria, on "The conditions of Austria's economic ability to survive," after a short reference to the great successes of economic policy, he castigated the tendency to treat those who favored more economic freedom as enemies of the regime. Consequently, he proposed a more liberal trade and industrial policy, including steps toward free trade and an end to exchange controls, and, in a final remark, criticized that economic policy had been determined only within small circles and without public discussion.[122] One year later, after the *Anschluss*, Morgenstern's characterization of the corporate state was devastating when he blamed it for "creating hosts of 'corporate bodies'... the practical result [of which] is that they tend to eliminate every trace of new competition which might appear." It should therefore be relegated to the "great field... which might appropriately be called the 'pathology of economic policy.'" [123]

Conclusion

In this final section an overall evaluation of the power of "Austrian" ideas with respect to policy-making in the 1930s will be undertaken. Thereby, we take up the distinction between the depression and the recovery phase.

In the depression phase, when the reputation and influence of the liberal core of the Austrian school certainly had reached its peak, Austria's ability to make a policy of its own was relatively unconstrained, and, in fact, under the extraordinary circumstances of 1931 it exercised this power to diverge rather widely from the path prescribed by adherence to the gold standard. However, as a consequence of its policies Austria became dependent on foreign capital supplied by international financial institutions. The supervisory power of these institutions and the policy advice of the "Austrians" combined to reintroduce the gold standard policies that were willfully followed by Austrian economic policymakers henceforth.

In the recovery phase, the position of the Austroliberals had severely weakened, on the one hand due to the emigration of their most eminent representatives, on the other hand due to the outright renunciation of liberalism as a doctrine by the corporate state. The policy choice of the corporate state might be described—by paraphrasing Clarke's dictum quoted above—as "rigid doctrines and rigid prices." In this regard the rigid doctrines represented the continued adherence to the gold standard rules, while the rigid prices resulted from the attempt of the corporate state to install a densely regulated system of production, particularly in the fields of agriculture and foreign trade. The first aspect was rather unanimously favored by Austrian economists, that is, not only by the remaining liberals among them, whereas the high level of regulation was obviously in direct contradiction to anything liberal economists would have advised. Furthermore, it is important to note that economic policy clung to the rigid doctrines of the gold standard even after some autonomy had been regained in 1936.

The persistence of the gold standard mentality right to the end of Austria's existence as an independent state, therefore, constitutes somewhat of a puzzle. It persisted even though in general the liberal tradition in Austria always had been rather weak. It persisted even after most of the Austroliberals had emigrated and had no way (and little intent) to influence directly Austrian politics. It persisted even after the League of Nations control of Austrian economic policy had ceased, the gold bloc had broken down, and Austria had regained its autonomy in monetary policy. And, finally, it persisted although, due to the nature of the corporate state as a kind of "government dictatorship," there was no need to worry much about public opinion.[124] Apparently, the gold standard mentality had acquired a life of its own and was kept alive even after its foundations had vanished – just like the "grin without a cat."

Thus, in conclusion, although the gold standard mentality owes to the "Austrian economists" a number of high-brow theories and low-brow propaganda pieces in its favor, holding them responsible for the awkward economic policy to which Austria committed itself in the 1930s would be a clear exaggeration of the power of their ideas. To the extent that Austrian economic policy in dealing with the *Creditanstalt* crisis could be realized autonomously, it broke many of the liberal rules without, however, following a clear plan. Only after supervision by foreign creditors became effective again did the rules of the gold standard regain their decisive influence on Austrian economic policy and were once more defended as a means of safeguarding monetary stability against the danger of inflationary excesses. Yet, at this point Austroliberalism had already lost much of its former grip on the policy making process. In fact, in most countries the gold standard mentality was only overcome when the politicians in power were overturned.[125] In this regard, the continuity of economic policy in Austria in the 1930s was a consequence of the continuity in the rule of conservative governments, not of the doubtful continuity of liberal economics.

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Footnotes

[1] E. Hobsbawm, *On History* (New York: The New Press, 1997), 100.

[2] This presupposes the feasibility of policies based on non-orthodox ("Keynesian") theories, a proposition which has been questioned with regard to the Weimar Republic by K. Borchardt, *Wachstum, Krisen, Handlungsspielräume der Wirtschaftspoliti:. Studien zur Wirtschaftsgeschichte des 19. und 20. Jahrhunderts* (Göttingen: Vandenhoeck und Ruprecht, 1982). Some authors, e.g. S. Mattl, "Die Finanzdiktatur: Wirtschaftspolitik in Österreich 1933–1938," in *Austrofaschismus: Beiträge über Politik, Ökonomie und Kultur 1934–1938* (Wien: Verlag fur Gesellschaftskritik, 1984) 133–160, put the blame for the lack of room for maneuver on "financial dictatorship" exemplified by the League of Nations' supervision of Austrian economic policies. For an alternative view of League of Nations activities in Austria cf. P. Berger, "The League of Nations and Interwar Austria: Critical Reassessment of a Partnership in Economic Reconstruction," *Contemporary Austrian Studies,* vol. 11 (New Brunswick: Transaction Publishers, in press).

[3] This phenomenon is explored in B. Eichengreen and P. Temin, "The gold standard and the Great Depression," *Contemporary European History* 9 (2000): 183-207.

[4] In the following unless otherwise indicated all translations from German-language sources are my own. References to the Fritz Machlup Papers, Hoover Instititution Archives, Stanford University and the Oskar Morgenstern Papers, Rare Book, Manuscript, and Special Collections Library, Duke University are abbreviated by FMP and OMP, respectively.

[5] The biographical information used in this section is taken from H. Janssen, *Nationalökonomie und Nationalsozialismus: Die deutsche Volkswirtschaftslehre in den dreißiger Jahren* (Marburg: Metropolis, 1998) and from the contributions in H. Hagemann and C.-D. Krohn, eds., *Biographisches Handbuch der deutschsprachigen wirtschaftsw issenschaftlichen Emigration nach 1933* (München: K.G. Saur, 1999).

[6] On the intellectual history of the Austrian school see E. Streissler, "The Intellectual and Political Impact of the Austrian School of Economics," *History of European Ideas* 9 (1988): 191–204. The term "Austroliberalism" is borrowed from K. H. Müller, "Die Idealwelten der österreichischen Nationalökonomen," in *Vertriebene Vernunft I: Emigration und Exil österreichischer Wissenschaft 1930–1940* (Wien: Jugend und Volk, 1987), 238–75.

[7] Joseph Schumpeter is not included in this list because he was not a true member of the Austrian school and had no influence on Austrian policy after he had left the country in 1925.

[8] On the female Austrian economists of this period see J. Nautz, "Zwischen Emanzipation und Integration: Die Frauen der Wiener Schule für Nationalökonomie," in *Die Frauen der Wiener Moderne* (Wien: Verlag für Geschichte und Politik, 1997), 64–82.

[9] The most relevant circles were the Mises *Privatseminar*, the so-called *Geist-Kreis* and the seminars of the *Nationalökonomische Gesellschaft*. See for example E. Craver, "The Emigration of the Austrian Economists," *History of Political Economy* 18 (1986): 13–18.

[10] L. Mises, *Notes and Recollections* (Spring Mills, Pa.: Libertarian Press, 1978), 74. These recollections of Mises were written already in 1940; their self-serving character and lack of reliability as a historical source should be noted.

[11] On Wieser see E. Streissler, "Arma virumque cano: Friedrich von Wieser, the Bard as Economist," in *Die Wiener Schule der Nationalökonomie* (Wien: Böhlau,1986), 83–106.

[12] Cf. Craver, "Emigration of the Austrian Economists," 10–13.

[13] On Morgenstern's intellectual development in the interwar period—in connection with his future involvement in game theory—see U. Rellstab, *Ökonomie und Spiele. Die Entstehungsgeschichte der Spieltheorie aus dem Blickwinkel des Ökonomen Oskar Morgenstern* (Chur: Ruegger, 1991) and R. J. Leonard, "From Parlor Games to Social Science: von Neumann, Morgenstern, and the Creation of Game Theory 1928–1944," *Journal of Economic Literature* 33 (1995): 730–61.

[14] In the following, we distinguish between Austrian economists in general, members of the Austrian school (denoted as "Austrian economists," i.e., in quotation marks), and, occasionally, the still smaller subset of Austroliberals.

[15] It should be noted that these two men represented quite different strands within the corporate state, as Dobretsberger stood for the "left wing" of the Christian Socialists, while Kerschagl was affiliated with the *Heimwehr*. On Dobretsberger see O. Rathkolb, "Überlegungen zum Exodus der 'Jurisprudenz,' " in *Vertriebene Vernunft I: Emigration und Exil österreichischer Wissenschaft 1930–1940,* (Wien: Jugend und Volk, 1987), 292–3. On Kerschagl see B. Dachs, "Richard Kerschagl: Zur Geschichte der Volkswirtschaftslehre an der Hochschule für Welthandel" (master's thesis, Wirtschaftsuniversität Wien, 1995), whose classification of Kerschagl as an "Austrian economist" is, however, untenable.

[16] On Spann and the politics and economics of universalism see J. Haag, "Othmar Spann and the Quest for a 'True State,' " *Austrian History Yearbook* 12–3 (1976/77): 227–50 and K. Milford and P. Rosner, "Die Abkoppelung der Ökonomie an der Universität Wien nach 1920," in *Zur deutschsprachigen wirtschaftswissenschaftlichen Emigration nach 1933* (Marburg: Metropolis, 1997), 479–502.

[17]Othmar Spann's most influential work in this regard was *Der wahre Staat: Vorlesungen über Abbruch und Neubau der Gesellschaft* (Graz: Akademische Druck- und Verlagsanstalt, 1972); he did not, however, embrace the Austrian corporate state, which he called a "weird carnival joke," O. Spann, *Kämpfende Wissenschaft* (Graz: Akademische Druck- und Verlagsanstalt, 1969), 5.

[18] We also neglect the Austromarxist contributions as, for obvious reasons, their influence on economic policy was nil. On the Austromarxist debate see U. Weber-Felber, *Wege aus der Krise: Freie Gewerkschaften und Wirtschaftspolitik in der Ersten Republik* (Wien: Europa, 1990), pt. 2.

[19] F. Machlup, "Zwei Minuten Volkswirtschaft," *Neues Wiener Tagblatt*, various issues 1932-34. For a more detailed account of Machlup's journalistic writings see H. Klausinger, " 'Austrian Economics in Two Minutes.' Fritz Machlup as a Journalist" (paper presented at the meeting of the History of Economics Society, Winston-Salem, North Carolina, 2001).

[20] For the contract see *Neues Wiener Tagblatt* to Morgenstern, undated (Jan 1931?), OMP, box 6. See also F. Machlup, "My Early Work on International Monetary Problems," *Banca Nazionale del Lavoro Quarterly Review* 133 (1980): 135.

[21] See C. Menger, *Grundsätze der Volkswirtschaftslehre* (Wien: Braumüller, 1871) and E. Böhm-Bawerk, *Kapital und Kapitalzins: Positive Theorie des Kapitals* (Innsbruck: Wagner, 1909).

[22] L. Mises, *Die Theorie des Geldes und der Umlaufsmittel* (München: Duncker und Humblot, 1912); L. Mises, *Geldwertstabilisierung und Konjunkturpolitik* (Jena: Gustav Fischer, 1928).

[23] F. A. Hayek, *Geldtheorie und Konjunkturtheorie* (1929; reprint, Salzburg: W. Neugebauer, 1976); F. A. Hayek, *Prices and Production* (London: Routledge, 1931).

[24] For a more elaborate analysis of "Austrian" business cycle theory see H. Klausinger, "Schumpeter and Hayek: Two Views of the Great Depression Re-examined," *History of Economic Ideas* 3 (1995): 93–127. It should be noted that nowadays even after the revival of classical liberal, and in particular "Austrian," ideas in the last decades "Austrian" business cycle theory is considered outdated by the vast majority of economists.

[25] Among others, L. Mises, *Die Ursachen der Weltwirtschaftskrise* (Tübingen: J.C.B. Mohr, 1931); Mises, *Geldwertstabilisierung und Konjunkturpolitik;* and Hayek, *Prices and Production,* 111–12 identified capital consumption as a cause of economic stagnation. For—indeed heroic—attempts at estimating the amount of capital consumption in Austria see O. Morgenstern, "Kapital- und Kurswertänderungen der an der Wiener Börse notierten Aktiengesellschaften 1913 bis 1930," *Zeitschrift für Nationalökonomie* 3 (1931): 251–55; N. Kaldor, "The Economic Situation of Austria," *Harvard Business Review* 19 (1932): 23–34; and F. Machlup, "Professor Knight and the 'Period of Production,' " *Journal of Political Economy* 43 (1935): 577–624.

[26] Machlup, "Zwei Minuten Volkwirtschaft," 3 July 1932.

[27] For a discussion of neutral money as a policy goal see Hayek, *Prices and Production,* 90–109; and G. Haberle, "Price Stabilization and the Business Cycle," (discussion leader) in *Reports of Round Tables* (Chicago: The Norman Wait Harris Memorial Foundation, 1932), 370-411.

[28] For endorsements of the gold standard along these lines see Hayek, *Prices and Production,* 110–11; F. A. Hayek, "Das Schicksal der Goldwährung," *Der deutsche Volkswirt* 6 (1932), translated in F. A. Hayek, *Good money. Part I: The New World* (London: Routledge, 1999), 153–68; F. Machlup, *Führer durch die Krisenpolitik* (1934; reprint, Wien: Manz, 1998), 150–60; and Mises, *The Theory of Money and Credit* (New York: Harcourt and Brace, 1935), 275.

[29] M. D.Bordo and H. Rockoff, "The Gold Standard As a 'Good Housekeeping Seal of Approval,' " *Journal of Economic History* 56 (1996): 389–428.

[30] For a treatment of free trade within the context of liberal foreign policy see L. Mises, *Liberalismus* (Jena: Gustav Fischer, 1927), ch. 3, especially 115–20.

[31] Based on his belief in the classical mechanism, Machlup (e.g., "Zwei Minuten Volkwirtschaft," 16 October 1932 and 11 June 1933) even advocated a unilateral pursuit of free trade policies.

[32] "The labor unions use force to attain their goals ... Workers who would like to work [in spite of work stoppages] ... are forced by acts of violence to give up any such plan. ... the characteristic feature of modern governments is that they have capitulated to the labor unions." Mises, *Money and Credit,* 188. See also Mises, *Liberalismus,* 73–74; L. Mises, *Kritik des Interventionismus* (Jena: Gustav Fischer, 1929), 12, 60.

[33] Mises, *Kritik des Interventionismus,* especially 11–2.

[34] L. Mises, *Die Gemeinwirtschaft: Untersuchungen über den Sozialismus* (Jena: Gustav Fischer, 1922). For a re-evaluation of the so-called socialist calculation debate see D. Lavoie, *Rivalry and Central Planning: The Socialist Calculation Debate Reconsidered* (Cambridge: Cambridge University Press, 1985).

[35] P. Clarke, *The Keynesian Revolution in the Making, 1924–1936* (Oxford: Clarendon Press, 1988), 28, 162.

[36] B. Eichengreen and P. Temin, "The Gold Standard and the Great Depression," *Contemporary European History* 9 (2000): 183.

[37] For a broad overview of Austrian economic policy in the 1930s see, e.g., D. Stiefel, *Die große Krise in einem kleinen Land* (Wien: Böhlau, 1988); H. Kernbauer, *Währungspolitik in der Zwischenkriegszeit: Geschichte der Oesterreichischen Nationalbank von 1923 bis 1938* (Wien: Oesterreichische Nationalbank, 1991); and the contributions in E. Tàlos, H. Dachs, E. Hanisch, and A. Staudinger, eds., *Handbuch des politischen Systems Österreichs: Erste Republik 1918–1933* (Wien: Manz, 1995).

[38] The numbers are from F. Butschek, *Die österreichische Wirtschaft im 20. Jahrhundert* (Stuttgart: Gustav Fischer, 1985), 46, 42.

[39] E.g., Mises, *Weltwirtschaftskrise,* 14–17.

[40] See F. Baltzarek, "Ludwig von Mises und die österreichische Wirtschaftpolitik der Zwischenkriegszeit," *Wirtschaftspolitische Blätter* 28 (1981): 127–39 on the role of Mises in the *Wirtschaftskommission* of 1930.

[41] For a more detailed account see A. Schubert, *The Credit-Anstalt Crisis of 1931* (Cambridge: Cambridge University Press, 1991).

[42] Schubert, *Credit-Anstalt Crisis,* 58–64 argued that by the state guarantee for the bank due to its sheer size public distrust was not abated but merely shifted from the bank to the state (and the currency), and so the banking crisis was transformed into a currency crisis.

[43] In retrospect, R. Reisch, "Die neue Geld- und Kreditpolitik," *Zeitschrift für Nationalökonomie* 8 (1937): 423 justified his expansionist policy by the necessity to protect the "wealth of the depositors and of the little man."

[44] See for example Mises, *Notes and Recollections,* 91.

[45] F. Machlup, "Die Währungs- und Kreditkrise," *Schmollers Jahrbuch* 62 (1932): 373–88. See also F. Machlup, "Die Theorie der Kapitalflucht," *Weltwirtschaftliches Archiv* 36 (1932): 512–29.

[46] Note that the distinction between a bank being insolvent or just illiquid is crucial for the effects of rescue operations by the central bank. In the latter case, when the run on the bank has been stopped, money will flow back so that the inflationary increase in central bank money is only temporary, whereas in the former case (as with the *Creditanstalt*) the increase is permanent. In the 1930s, Machlup's position was uncompromising in both cases, yet in retrospect he conceded that the rescuing of merely illiquid banks was legitimate; see Machlup, "My Early Work," 133.

[47] He called it "unjust" and "more harmful than the distress sale of the assets of the actual debtors"; Machlup, "Währungs- und Kreditkrise," 379.

[48] Even if not fully agreeing with the position of the "Austrians," it is obvious that much would have been gained by imposing exchange controls as long as the central bank was still in a position of strength, i.e., with sufficient reserves. For an analogous argument with regard to the German currency crisis of 1931 cf. T. Ferguson and P. Temin, "Made in Germany: The German Currency Crisis of July 1931," (Working Paper, Department of Economics, M.I.T., 2001): 39-40.

[49] This campaign was one of the main objects of the journalistic activities of Machlup and Morgenstern referred to above. See as examples Machlup, "Zwei Minuten Volkwirtschaft," 9 October 1932 and O. Morgenstern, "Der Weg zu freier Schilling-Kursgestaltung," *Neues Wiener Tagblatt*, 10 September 1932, 11. For a retrospective account see O. Morgenstern, "Entstehung und Abbau der österreichischen Devisenbewirtschaftung," *Nationalökonomisk Tidsskrift* 75 (1937): 34–56.

[50] Before the introduction of "private clearing" the free market rate was that of the Schilling at the Zurich exchange. The highest disagio of the Schilling in black markets amounted to 44% in November 1931; Schubert, *Credit-Anstalt Crisis,* 92.

[51] And that of the Chamber of Commerce as reported by Kernbauer, *Währungspolitik in der Zwischenkriegszeit,* 344. See also M. Kröll, "Währungsanleihe oder Investitionsanleihe?" *Neues Wiener Tagblatt*, 27 January 1932, 12.

[52] F. Machlup, "Sie wissen nicht was Inflation ist," (1932?) typescript, FMP, box 86, folder 3 argued that the authorities should eventually accept the depreciation of the Schilling due to their prior inflationary policy, but the newspaper did not publish this column possibly as a result of (self-)censorship.

[53] As commented in the *Monatsberichte* of the Institute for Business Cycle Research, "the central bank is again in the position to judge the expediency of its actions by the movement of the exchange rate"; "Rückblick auf das Jahr 1933," *Monatsberichte des Österreichischen Instituts für Konjunkturforschung* 8, no. 2 (1934): 23.

[54] Machlup, "Zwei Minuten Volkwirtshaft," 21 May 1933.

[55] For similar definitions see e.g. Machlup, *Führer durch die Krisenpolitik,* 40-1, 61 and F. A. Hayek, *Monetary Nationalism and International Stability* (1937), in Hayek, *Good Money: Part 1,* 44–5. Apart from these explicit definitions, "Austrian" business cycle theory is based on the view that banks can "produce" money and therefore necessarily embraces a broad definition.

[56] Money demand in terms of M2 was shown to be more stable than in terms of M1 by Schubert, *Credit-Anstalt Crisis,* 126, therefore M2 is included here. The close relation between M2 and GNP can also be ascertained from Table 1.

[57] F. Steindl, *Monetary Interpretations of the Great Depression* (Ann Arbor: University of Michigan Press, 1995), 61–2 makes this point with regard to U.S. data.

[58] Schubert, *Credit-Anstalt Crisis,* 109 calculates the decline in the deposit-currency ratio in 1931 as about 52% (for M1) and 39% (for M2).

[59] In this regard Austria conformed almost perfectly to the classic explanation of M. Friedman and A. J. Schwartz, *A Monetary History of the United States, 1867-1960* (Princeton: Princeton University Press, 1963).

[60] Cf. again the *Monatsberichte*: "Money in circulation [identified with central bank money] has considerably increased while simultaneously the volume of production and general business activity had severely contracted," "Rückblick auf das Jahr 1931," *Monatsberichte des Österreichischen Instituts für Konjunkturforschung* 6, no. 2 (1932): 18. And one year later they ask whether "money in circulation is not still excessive with regard to the maintenance of the exchange rate," "Rückblick auf das Jahr 1932," *Monatsberichte des Österreichischen Instituts für Konjunkturforschung* 7, no. 2 (1933): 16. By the way, economic historians often have accepted this "Austrian" interpretation unquestioned, cf. e.g. Butschek, *Die österreichische Wirtschaft,* 56–57; Stiefel, *Die große Krise,* 306; and Kernbauer, *Währungspolitik in der Zwischenkriegszeit,* 402.

[61] On the problem of hoarded notes see Machlup, "Zwei Minuten Volkwirtschaft," 24 Apr 1932 and "Rückblick auf das Jahr 1932," 19–20. In consequence, the argument went against mobilizing these hoards for purchases of government bonds.

[62] A. Amonn, "Zur gegenwärtigen Krisenlage und inflationistischen Krisenbekämpfungspolitik," *Zeitschrift für Nationalökonomie* 5 (1934): 4.

[63] Machlup, "Zwei Minuten Volkwirtschaft," 25 Mar 1934.

[64] On the necessity of automatic deflation and the dangers of reflation see, e.g., Hayek, *Good Money: Part I,* 64; M. Braun, "Das Schlagwort 'Re-Deflation,' " *Neues Wiener Tagblatt*, 2 March 1932, 11; F. Machlup, "Zur Frage der Ankurbelung durch Kreditpolitik," *Zeitschrift für Nationalökonomie* 4 (1932): 404; and R. Strigl, "Währungspolitik in der Krise," *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 13, no. 11-12 (1931): 304.

[65] To contrast the "Austrian" view on deflation and depression with the views of modern monetarism and contemporary "Old Chicago" see Klausinger, "How Far was Vienna from Chicago in the 1930s? The Economists and the Depression," *Contemporary Austrian Studies,* vol. 11 (New Brunswick: Transaction Publishers, in press).

[66] Butschek, *Die österreichische Wirstschaft,* 55–6.

[67] In a companion paper I argue that this break increased the diversity of opinion within the school to such a degree that it ultimately led to its dissolution; H. Klausinger, "The Austrians on Relative Inflation: Some Evidence on the Dissolution of the Austrian School," (paper presented at the History of Economics Society Meeting, Davis, California, 2002).

[68] On the emigration of the "Austrians" see Craver, "Emigration of the Austrian Economists"; E. Craver, "Patronage and the Directions of Research in Economics: The Rockefeller Foundation in Europe, 1924–1938," *Minerva* 24 (1986): 205–22; L. A. Coser, *Refugee Scholars in America: Their Impact and Their Experiences* (New Haven: Yale University Press, 1984), ch. 4; and the sources listed in n. 2 of the present paper.

[69] One might note a similarity between Mises and Morgenstern in that both had the ambition to become Minister of Finance; see F. A. Hayek, *Hayek on Hayek: An Autobiographical Dialogue,* ed. S. Kresge and L. Wenar (London: Routledge,1994), 70 and O. Morgenstern, diary, 21 Nov 1936, OMP, box 13.

[70] *Monatsberichte des Österreichischen Instituts fürKonjunkturforschung,* (Wien: 1927-1938).

[71] By 1933, Morgenstern was already close to becoming the secretary of the Association of Austrian Industry, an attempt that failed due to an ugly campaign that accused him of being of Jewish origin, a liberal and a disciple of Mises; see OMP, box 1.

[72] See for example Morgenstern diary, 18 Apr, 17 Jul and 12 Oct 1936, OMP, box 13. For the railroad question see O. Morgenstern, "Die Einordnung der Verkehrspolitik in die allgemeine Wirtschaftspolitik," *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 18, no. 1-2 (1936): 11–23.

[73] See e.g. J. Nautz, ed., *Unterhändler des Vertrauens: Aus den nachgelassenen Schriften von Sektionschef Dr. Richard Schüller* (Wien: Verlag für Geschichte und Politik, 1990), 173–4.

[74] Including, of course, a decrease in the coffee tax; see Morgenstern diary, 22 Nov 1934, OMP, box 13.

[75] Morgenstern diary, 21 Nov 1936, OMP, box 13.

[76] O. Morgenstern, *Die Grenzen der Wirtschaftspolitik* (Wien: J. Springer, 1934), 4, 9; on p. 57 he illustrated his position by an example where free trade is not a feasible option because policy-makers have decided to protect an important group of the population from foreign competition.

[77] Morgenstern diary, 19 Apr 1935, OMP, box 13. Morgenstern's turning away from "Austrian" methodology became visible also by his being a frequent member of two other famous Viennese "circles": Moritz Schlick's "Vienna circle" of philosophers and Karl Menger's (the son of the founder of the Austrian school) "Mathematical Colloquium."

[78] On these controversies see M. Blaug, *Not Only an Economist* (Cheltenham: Edward Elgar, 1997), 87–94.

[79] For the "Austrian" view of the capital controversy see F. Machlup, "The Consumption of Capital in Austria," *Review of Economic Statistics* 17 (1935): 13–9.

[80] See the transcripts of a lecture series on the business cycle, "Konjunktur-Vortrag," Jan 1936, OMP, box 26. Morgenstern's eclecticism also shows up in the descriptions of the "Austrian" business cycle in the *Monatsberichte* of the Institute. As P. Rosner, "The Austrian Research on Business Cycles," *History of Economic Ideas* 7 (1999): 221–2 has pointed out, these are often in contradiction to the "Austrian" theory, which is no surprise if we acknowledge the fact that Morgenstern was no (more) part of the "Austrian" mainstream.

[81] J. von Neumann and O. Morgenstern, *The Theory of Games and Economic Behavior* (Princeton: Princeton University Press, 1944), ch. 1. On the development of Morgenstern's heterodoxy see Rellstab, *Ökonomie und Spiele,* ch. 6.

[82] On the politics and economics of the corporate state see E. Tàlos and W. Neugebauer, eds., *"Austrofaschismus": Beiträge über Politik, Ökonomie und Kultur 1934–1938,* 4th ed. (Wien: Verlag für Gesellschaftskritik, 1988) and G. Bischof, A. Pelinka, and A. Lassner, eds., *The Dollfuss/Schuschnigg Era in Austria: A Reassessment,* Contemporary Austrian Studies, vol. 11 (New Brunswick: Transaction Publishers, in press).

[83] Although L. Mises, *Liberalism: A Socio-Economic Exposition* (Kansas City: Sheed Andrews and McMeel,1978) 45 declared that even if democracy is "on the road to destruction, ... force is never a means to overcome these difficulties," there is a disquieting aside where he acknowledged that, although ultimately to be rejected because of the above argument, "Fascism and similar movements ... are full of the best intentions and that their intervention has, for the moment, saved European civilization"; *Liberalism,* 51.

[84] Note that the potential conflict between democracy and liberalism and the "rule of law" is an ever-present theme in the writings of Hayek turned social philosopher; cf. F. A. Hayek, *The Political Order of a Free People* (Chicago: University of Chicago Press, 1979).

[85] Machlup, 1938?, FMP, box 86. Mises, *Notes and Recollections,* 88 speaks even of "the terror apparatus ... of the Social Democratic Party."

[86] Max Mintz to Machlup, 9 Dec 1934, FMP, box 53.

[87] Morgenstern, *Grenzen der Wirtschaftspolitik,* 129.

[88] Already in mid-1932 this was the opinion shared by Dollfuß, Kienböck, Rost van Tonningen and Schuschnigg; see e.g. Kernbauer, *Währungspolitik in der Zwischenkriegszeit,* 389. Viktor Brauneis (of the Austrian national bank) voiced a similar concern to Morgenstern; Brauneis to Morgenstern, 5 Aug 1932, OMP, box 4. Morgenstern's reaction was evading, but not negative.

[89] O. Morgenstern, *The Limits of Economics* (London: Hodge, 1937), 143-4. However, on p. 145 Morgenstern, the director of the Institute of Business Cycle Research, knew a remedy: "Governments need advisers in economic matters."

[90] In this regard M. Braun, review of *Die Grenzen der Wirtschaftspolitik*, by Oskar Morgenstern, *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 16, no. 1 (1934): 23 noted: "This is a point where Morgenstern will be much misunderstood, too; for critics will reproach him for advocating fascism in the interests of sound economic policy" a subtle comment as of January 1934. See also Hayek's heavy criticism; Hayek to Morgenstern, 2 Apr 1934, OMP, box 5.

[91] Morgenstern received the title "*außerordentlicher Professor*" in 1935.

[92] See his correspondence with the *Neues Wiener Tagblatt,* FMP, box 55, folder 18. The Machlup papers contain ten typescripts of contributions not published (FMP, box 86, folders 3 and 4), most of them from early 1934. The latest one was titled "Good or Able men?" (14 Apr 1934). Small wonder it was censored by the Catholic regime, as Machlup opted for the latter. On censorship see also the correspondence between Machlup and Morgenstern; 26 Mar and 4 Apr 1934, FMP, box 54.

[93] For example, Austria's gross national product in 1937 was below the pre-depression as well as the pre-war level, a unique feature among Western industrial countries; cf. Butschek, *Die österreichische Wirtschaft,* 46.

[94] Kernbauer, *Währungspolitik in der Zwischenkriegszeit,* 393.

[95] On the plan see O. Deutsch and A. Vertes, *Aufbau, nicht Abbau* (Wien: Staatsdruckerei, 1932). It is noteworthy that G. Haberler, "Mit oder ohne Inflation: Zu 'Aufbau, nicht Abbau,' " *Der Österreichische Volkswirt* 25, (5 November 1932): 136-7 was joined in his attack on the plan by Karl Polanyi, "Ein gefährlicher Aufbauplan," *Der österreichische Volkswirt* 25, (5 November 1932): 133–6, who was certainly not an Austroliberal. On the debate see also F. Butschek, "Pre-Keynesianism in Austria," *History of Economic Ideas* 5 (1997): 107–19.

[96] "... a country devoid of exchange reserves ..., where every increase of money, be it ever so small, will immediately be transmitted to the exchange rate, ... a country with a population that has experienced inflation [can] not allow itself such experiments ... as their mere announcement would lead to a flight from the currency"; G. Haberler, "Mit oder ohne Inflation," 137.

[97] F. Machlup, "Industrialisierung, Autarkisierung, Arbeitslosigkeit," *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 14, no. 11-12 (1932): 279.

[98] Machlup, "Zwei Minuten Volkwirtschaft," 7 May 1933.

[99] R. Kerschagl, "Probleme der Arbeitsbeschaffung," *Die Industrie* 8, no. 3–4 (1933): 3; J. Dobretsberger, "Bemerkungen zu den Arbeitsbeschaffungsplänen," *Jahrbücher für Nationalökonomie und Statistik* 137 (1932): 260–74.

[100] Morgenstern diary, 5 Dec 1936, OMP, box 13; Morgenstern to Haberler, 10 Sep 1935, OMP, box 5 and Morgenstern diary, 7 Sep 1935, OMP, box 13.

[101] This story is told by J. Steindl, "Zeitzeuge," in *Vertriebene Vernunft II: Emigration und Exil österreichischer Wissenschaft* (Wien: Jugend und Volk, 1988), 400, who worked at the Institute in 1938. The article in question is in all probability "Österreich und die Weltkonjunktur," *Monatsberichte des Österreichischen Instituts für Konjunkturforschung* 12, no. 1 (1938): 6–10 with its distinctly Keynesian flavor.

[102] On the following see also G. Senft, "Geld- und Währungspolitik unter dem Kruckenkreuz," in K. Bachinger and D. Stiefel, eds., *Auf Heller und Cent: Beiträge zur Finanz- und Währungsgeschichte: Festschrift für Herbert Matis* (Frankfurt: Ueberreuter, 2001), 453–69.

[103] See Stiefel, *Die große Krise,* 306–12 and Schubert, *Credit-Anstalt Crisis,* 129.

[104] The only way out would have been to resort to open market purchases, preferably for financing public works a "modern" policy instrument deemed to be inflationary and not in conformity with the law (the *Nationalbankgesetz*). See also Butschek, *Die österreichische Wirtschaft,* 57.

[105] The term was coined by R. Hawtrey, "The Credit Deadlock," in *The Lessons of Monetary Experience* (New York: Farrar and Rinehart, 1937), 129–44.

[106] The new view of B. Bernanke, "Nonmonetary Effects of the Financial Crisis in the Propagation of the Great Depression," *American Economic Review* 73 (1983): 257–76 located the cause of this deadlock in a lack of credit supply due to an increased perception of risk; B. Bernanke and H. James, "The Gold Standard, Deflation, and Financial Crisis in the Great Depression: An International Comparison," in *Financial Markets and Financial Crises* (Chicago: University of Chicago Press, 1991), 33–68 established a connection to prior banking crises.

[107] The League of Nations ended its control of Austrian economic policies formally in November, 1936 and, according to P. Berger, "Meinoud Rost van Tonningen, Vertreter des Völkerbundes in Österreich: Ein Forschungsbericht," *Zeitgeschichte* 18 (1990/91): 351–78, had already eased some of its grip earlier.

[108] Morgenstern's position is to be contrasted with the low esteem in which Dobretsberger and Kerschagl apparently were held by Kienböck, cf. Morgenstern diary, 13 Jun and 21 Jun 1936, OMP, box 13.

[109] Morgenstern diary, 25 Nov 1936, OMP box 13; O. Morgenstern, "Währung und Preise," *Österreichische Zeitschrift für Bankwesen* 1 (1936): 166–71.

[110] Morgenstern, "Währung und Preise," 168-9. In this account, the effect of devaluation most stressed by modern interpretations is notable by its absence, namely, that of facilitating a more expansionist monetary policy.

[111] Morgenstern diary, 24 July 1937, OMP, box 13; Haberler to Morgenstern, 30 Oct, 20 Nov 1936, 9 Jan 1937, and undated 1937, OMP, box 5.

[112] J. Dobretsberger, "Konservative Währungspolitik—konstruktive Wirtschaftspolitik," *Neues Wiener Tagblatt*, 26 August 1935, 15. Dobretsberger was also the president of the Union for Sound Currency. For another defense of the hard currency policy see J. Dobretsberger, "Zur Frage der volkswirtschaftlichen Liquidität," *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 17, no. 3-4 (1935): 57–66.

[113] Morgenstern, "Währung und Preise," 171.

[114] "Österreich und die Weltkonjunktur," 10.

[115] With regard to Germany, H. Janssen, *Nationalökonomie und Nationalsozialismus,* 396–413 convincingly proved the close relationship of many of the so-called "reformers" to the NSDAP.

[116] The special treatment of agriculture is emphasized by Stiefel, *Die große Krise,* 363–75 and G. Senft, "Economic Development and Economic Policies in the Ständestaat Era," *Contemporary Austrian Studies*, vol. 11 (New Brunswick: Transaction Publishers, in press).

[117] D. Stiefel, "Utopie und Realität: Die Wirtschaftspolitik des Ständestaates," in *Tirol und der Anschluß* (Innsbruck: Haymon Verlag, 1988), 403–33.

[118] On a macroeconomic level this differential development of the intensity of competition in product and labor markets expressed itself in a decline in the share of wages in national income. Cf. Stiefel, "Utopie und Realität," 417.

[119] O. Morgenstern, "Free and Fixed Prices during the Depression," *Harvard Business Review* 10 (1931/32): 62–8 and O. Morgenstern, "Konjunktur-Vortrag", part 5, OMP, box 26.

[120] Morgenstern, "Währung und Preise," 169.

[121] "It will ... come to nothing ..." Morgenstern diary, 24 July 1937, OMP.

[122] O. Morgenstern, "Die Bedingungen der wirtschaftlichen Lebensfähigkeit Österreichs," OMP, box 22, p. 17.

[123] O. Morgenstern, "The Experience with Public Regulation and Public Monopoly Abroad," in *Monopoly and Competition in Industry and Labor* (New York: Academy of Political Science, Columbia University, 1939), 39.

[124] H. Wohnout, *Regierungsdiktatur oder Ständeparlament? Gesetzgebung im autoritären Österreich* (Wien: Böhlau, 1993), 434.

[125] Eichengreen and Temin, "Gold Standard," 185.