

Chapter5

Market Integration, Economic Intervention of the State and the Decline of Empires:

Austria-Hungary and Russia

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Oscar Jaszi's famous book on the dissolution of the Habsburg Monarchy formulated the following thesis: "By 1913, the Austro-Hungarian Monarchy was already a defeated Empire from the economic point of view, and as such it went into the World War in 1914."¹ The origin of this statement came from speculations on the "tragedy of the free trade-policy" of the Habsburg Monarchy, in a chapter where the free-trade was discussed as one of the centripetal forces in the Monarchy. The book was written in the late twenties and Jaszi was one of the followers of the idea of the "Danubian Confederation," i.e. a multinational political and economic integration."

Forty years later, in a "historical contribution to the current integration-problems" Krisztina Maria Fink considered that "das retardierende Moment eigentlich vom 1867er Vertrag in den Ablauf der Dinge gebracht wurde."² From the base of the institutional "Grossraumwirtschaft" her main argument compared the Monarchy directly to the European Economic Community: "... [sie] in der dritten, zweistaatlich-konstituellen Phase keine tFbertragung auf eine von beiden Teilen anerkannte supranationale Organisation fanden, deren Entscheidungen auch ohne Zustimmung der Mitgliedsstaaten für dieselben verpflichtend gewesen waren."³ From this point of view the peak of the process of the economic integration in the Habsburg Monarchy was undoubtedly the period of Neoabsolutism (1849-1860). (We can take for a great

fortune, that Fink choose as a forerunner of the EEC not the last years of the Russian Empire.)

Whether we put the starting point of the preponderance of centrifugal economic forces in the Monarchy at 1867 (Fink) or at the beginning of the 20th century (Jaszi) in a global institutionalist view the political dissolution ought to be preceded and prepared by the economic disintegration.

The Hungarian version of the law of 1867 sharply differentiated the *common affairs* (foreign and military affairs and the related financial matters) from *the affairs of common interest*. The former resulted from the law called Pragmatica Sanctio (1723), but the latter came from affairs newly founded during the neoabsolutist period. If we look more thoroughly at these affairs of common interest, we can find in this "basket" of the Compromise exclusively economic matters: the apportionment of the Habsburg state debt, the railway lines built across the border between the two halves of the Empire, the consumption taxes imposed according to the same principle in both parts of the Monarchy, the contractual form of the customs union and the common monetary system.

Different regulations applied to the several historically rooted types of affairs. Finances related to the common affairs (after all tariff revenue had been applied to) fell to the two halves of the Monarchy in a ratio (the so called 'quota') following principally the distribution of the number of citizens and their taxpaying capacity. Actually the quota was set by political negotiations (1868 - 70 : 30; 1899 - 65.6 : 34.4; 1907 -63.6 : 36.4). To the payment by installments — from the official Hungarian point of view the Habsburg debt was undertaken without Hungarian approval — Hungary contributed only "from fairness, and political considerations." By the unification of debt denominations in 1868 the two partner-states settled for Hungary yearly a fixed amount of payments. While after 1873 the rate of interest diminished for a long period, this way of installments became unfavorable for Hungary (although the idea came originally from the Hungarian minister of finance). Concerning the so called

affairs of common interest the Compromise was subject to renewal at stated intervals (as a rule every ten years).

The periodical renewal of the agreements has been judged differently by contemporaries and by historians. From one point of view the discussions in the press, in the parliaments and at the governing level shook and destabilized the Monarchy every ten years.⁴ According to the opposite view, without the periodical renegotiations the rigid system of Dualism would have collapsed earlier than it did. In this opinion, the periodical renegotiations formed the dynamic element of the Dual Monarchy.⁶

Moreover after 1867 in the areas not covered by the affairs of common interest, there were articulated *autonomous Austrian and Hungarian economic policies* (disregarding at the moment the other ethnic and provincial corporative economic interests). Neoabsolutism introduced the interest guarantee system to construct an imperial railway network centered on Vienna. The Hungarian government adopted it after 1867 to build Budapest centered radial main lines in Hungary. The direct tax-system of the Empire formed in 1850-1851 did not belong to the affairs of common interest after 1867. It became different step by step in the two parts of the Monarchy. The Hungarian acts for the industrial promotion (1881, 1890, 1899, 1907) contained tax exemption, interest-free credits, and later the subsidies clearly intended to substitute for Hungary's lack of her own protective tariffs.

The range of effect of these converging and diverging tendencies in the area of the institutional system and the instruments of economic policy was determined by the framework of the *market*. Until the war the institutions and the economic policy operated solely through means conforming to the market system. The development of the market in the Austro-Hungarian Monarchy is one of the preferred topics of the latest cliometric researches. Examining the wholesale prices of the Empire David F. Good reinforced the earlier formulation, that the commodity-market integration peaked in the 1850-1860s.⁶ The institutional and political background

behind the price convergence which is usually mentioned is the formation of the customs union and the building of the main railway lines of the Empire.

An other important finding of Good's work is the money-market integration of interest rates within the Monarchy during the first half of the 1880s. The institutional framework included a uniform interest rate policy at the branches of the Austro-Hungarian Bank and the newly prescribed legal maximum interest rate. Through the inconvertible "parallel currency-system" (with fluctuating rate of exchange between the "paper currency" and the silver Gulden) the Monarchy before 1892 (and in Russia till 1895) fit in a contradictional way into "the fragmented international capital market."⁷

As for Russia the institutional approach of the Empire would indicate the permanent growth of centripetal forces. There was no sign of any "Compromise" in this respect, the trend has been the opposite to the Austrian "bicentralisation." "Self-government" given for conquered territories at the first period after that they "joined" to the Russian Empire was lost. "Sooner or later, for one reason or another, the privileges granted to conquered peoples were retracted, contracts were unilaterally abrogated, and subjects, together with their territories, were incorporated into the regular administration of the Empire."⁸ It is true, the latest step in this respect was made namely in the field of economic matters. The Finnish constitution for example was suspended in 1899, followed by the centralization of taxes only in 1910, during the so called "campaign against Finland."⁹

Behind the bureaucratization and centralization the market integration emerged in Russia as well. Measuring with different methods the bias of agrarian prices the pioneers of Soviet "new economic history" also pointed out that "to the 1880s comes to the end the formation of the unified all-Russian agrarian market."¹⁰ From our comparative point of view the exact timing of the fulfillment of the process is not so relevant as the statement, that the market integration in Russia

developed slower and later than in the "bicentralized" Monarchy.

Intending to emphasize centrifugal forces as the greatest economic problems of the Austro-Hungarian Monarchy before the War, authors usually deal more with the international balance of payments and trade of the customs union as a whole than with the commodity and capital turnover between the two halves of the Dual Monarchy. Jaszi's main economic argument mentioned at the introduction of this paper also was based on the statistical observation that after 1907 the balance of trade of the Monarchy became passive, followed by an increasing indebtedness. Actually the growth of imports into both parts of the Monarchy from outside the customs territory was much quicker than that of exports during the last prewar cycle (1908-1913 trough to trough). But the situation was the same during the previous period of time (1901-1908) as well. The principal reason for the passive balance of trade of the whole Monarchy was the turn to deficits in the Cisleithanian commodity balance (Graph I).

Since 1901 we can follow the customs inland traffic between the two halves of Austria-Hungary not only from Hungarian, but also from Austrian statistical sources. In this "Zwischenverkehr," after some years of Hungarian active balance in the first years of the century (the data are different in the Austrian and Hungarian statistics, presumably because of diverging pricing methods), from 1905-1906 a large Hungarian deficit accumulated. The growth rate of turnover decreased somewhat in the period 1908-1913 in comparison to 1901-1908, but it does not show any dramatic breakdown or irreversible change. Behind the increased customs barriers of 1906, the two countries of the newly formed "customs alliance" maintained the same traditional commodity trade to which they had become accustomed in the well proved division of labour within the Habsburg Empire since the late 18th century. The real foreign trade outside the Austro-Hungarian customs territory is indivisible from the inland traffic between the parts of the Monarchy. "The Monarchy's striking import

surplus — the result of massive Austrian imports of raw cotton and wool, plus yarn and thread — never attained the absolute size of Austria's export surplus of textile goods in her trade with Hungary." The accelerating exports outside of the customs area consisted first of all of new products, which find their way abroad.¹¹

Concerning the capital account, the negative balance of commodity trade almost as a matter of course coincided with an increase in security export before the War. We know from summary estimates that the outflow of bonds and shares from the Monarchy was obviously higher, while data collections disregarded direct emissions and considered short term monetary movements to be unmeasurable.¹² In the Austro-Hungarian Monarchy, with its inconvertible crown-currency belonging to the outer periphery of the international gold standard, according to a contemporary analysis during "external drains" when "the Bank of England redeems its notes in gold, the Austro-Hungarian Bank in gold bills, viz., gold in foreign hands... To have the requisite stock of Devisen and able to meet any demand, the bank sends gold abroad and procures bills in exchange."¹³

The enormous growth of the passive balance of trade and the rapid increase of discounting bills at home sharpened the situation on the foreign exchange market (Graph II). The balance sheets of the Austro-Hungarian Bank show the radical parallel diminution of the metallic reserve and the stock of gold bills during the years 1910-1912. The bank had to raise its rate of interest which peaked in 1913. In the year 1913 — according to the normal path of the business cycle — the stock of gold and gold bills started to increase. It was the direct result of diminishing discount at home and that of the decrease of import surplus. The gold buying activity of the bank, was totally missing in years 1912-1913.¹⁴

Examining Russia from a strictly economic point of view and disregarding the level of indebtedness the position of this empire looks less problematic. The Russian balance of trade remained continuously active up to the war, which means

Russia was able to counterbalance the flow of foreign loans by his forced agricultural exports.¹⁶

This way the question related to the economic "defeat" raised by Jaszi seems insolvable in itself and at a comparative level too. Neither the institutions and the economic policy, nor the structure and cyclical movements of the market predetermined the economic dissolution of Austria-Hungary before the war. The Austro-Hungarian Monarchy dissolved not for economic reasons, but it was dissolved. Could have such a few influence the centripetal, integrative forces of the market?

We could not accept the argument of the relatively "close correlation" between economics and military forces of powers — represented by Paul Kennedy. "While it would be quite wrong, then, to claim that the outcome of the First World War was predetermined, the evidence ... suggests that the overall course of that conflict... correlates closely with the economic and industrial production and effectively mobilized forces available to each alliance during the different phases of the struggle."¹⁶ Our comparison of Austria-Hungary and Russia suggests other consequences.

Alexander Gerschenkron's famous thesis on the role of "relative backwardness" in Europe contrasts the German and Russian type industrialization. It is "common place" now in economic history, that in Germany the bank, and in Russia the state substituted the factors required for the so called "great spurt." It is not so well known, that in Gerschenkron's concept the Austro-Hungarian Monarchy was divided into two halves from the point of backwardness and substitution: Austria (Cisleithania) belonged to the German-type, Hungary (Transleithania) to the Russian-type development.

When we talk of the economic activity of the state in Austria-Hungary and Russia during the World War I, some comparative questions and points are evident. The first point

comes immediately from Gerschenkron's above mentioned thesis: the difference in the tradition and practice of the state interventionism in the two empires. There are, of course, some common features of backwardness in the central and eastern part of Europe. Some of them (the low level of internal capital accumulation, the traditional structure of society) was emphasised very strongly in the last decades in the historiography. "It is not the peculiar and specific role of the state, but the import of capital, promoted and motivated by the state activity, which may be regarded as a feature distinguished Eastern Europe from the rest of the Continent in the modern transformation of the economy."¹⁷

But on the eve of World War I, the contrast in the state activity seems to us much stronger, as similarities. Not only between Austria and Russia, but between Austria-Hungary together (as an economic entity) and Russia as well. The indices of the financial system of the two empires sharply differ: the amount of assets of financial institutions in comparison to the GNP was higher in Austria-Hungary, namely 220%, while in Russia only 158%. From the other side, the foreign indebtedness of Austria-Hungary reached 50%, that of Russia 65% of the GNP. The different level of the monetarisation required different redistributive activity by the governments.

The income side of the state budget shows very well the differences too. In Austria-Hungary the state revenues based mainly on tax system, which differed in direct, but were identical in indirect taxes in the two halves of the empire. In Russia before the War the main items of government income came from tax on vodka-distillation and the state railways (26 and 24% respectively). The weight of the defence expenditures marks also important differences: "The proportion of armaments expenditure to national income on the eve of the war amounted in Germany to 3.5%, in Britain to 3.6% and in Austria-Hungary to about 4%. Russia engaged in even higher armaments expenditure: some 6% of national income."¹⁸ Low level of monetarisation, restricted possibility of modern

taxation, high level of military expenditures and foreign indebtedness — this is the background of Russian war finance before the war.

Prohibition of vodka-distillation at the very beginning of the war and permanent chaos in the railway traffic very early reduced the government revenues in Russia.¹⁹ There was an other possibility to raise the income, to increase the direct taxation of the firms and the population, which was carried out extensively. In introducing new taxes (for example the income tax) the tsarist government was not very active. Only in 1916 did they start to impose them. Issuing war obligations — because of the weak development of financial institutions and the low rate of saving - was not a great success. From the beginning of the war to the February Revolution they issued 6 domestic bonds: in nominal value some 8 billion rubles. Due to the creditor activity of the Allies, Russia also received substantial foreign loans during the war. In constant price we can say that these measures were only enough to hold the of pre war expenditure level.²⁰

Austria-Hungary - belonging to the Central Powers — had not had the same opportunity to use the foreign stock market for war finance purposes. The Austrian and the Hungarian Governments exploited domestic sources to a greater extent. The 8 War Loans in both side of the Monarchy (35 billion K in Cisleithenia; 18 billion K nominal in Hungary) increased the importance of the domestic state debt.²¹ This process, however, diminished the possibilities to increase the state-revenue through new taxes. In this respect the difference between the two halves of the Monarchy was not without importance: Austria employed since 1896 a modern personal income-tax system, which was introduced very late, only in 1916 in Hungary (incidentally in the same year as in Russia). All these measures lead — in a different way from Russia — in constant prices, to the same result: roughly to the pre-war expenditure level of the dual Monarchy. In this respect we can formulate a very modest conclusion of the above discussed problems about the war finance. The tradition and earlier

practice of the state intervention in two relatively backward empires determines usually only fiscal techniques, rather than the final success of the war financing.

Looking in another field to research the economic activity of the state (and the market) we can cast a glance at the regulation of the food supply during the war. The intervention of the government - maximising food-prices, regulating the grain trade by two, semi-state-owned companies — was earlier and more efficient in Austria-Hungary, than in Russia. What is extremely interesting in Russia, — partly an agrarian export country and partly that of famine — that during the war enormous reserves of food were accumulated in the grain producing areas. In this respect we can mention the old Austrian accusation against the Hungarian agriculture too, use of the Austrian food shortages during the war. "...in 1916 Hungary supplied no more than 100,000 tons of grain and flour to Austria, as against 2.1 million tons yearly before the war, and deliveries of other foodstuffs were likewise drastically reduced."²²

More serious measures were taken in both empires only in the second half of 1916. In Hungary a decree of 24 August controlled the surplus product, and the possibility of requisitioning it.²³ After the weak yield of the grain-collection a new decree of 27 November 1916 ordered two more requisitions with a centrally determined contingent for every county. This measure was the first sign of the decisive change in the government's economic policy.

In Russia a decree of 29 November 1916 ordered the so called "*prodrazverstka*" the collection of grain for national defence purposes.²⁴ The declaration of the State Monopoly of grain remained the duty of the Provisional Government in 25 March 1917, but was introduced only after the Bolshevik takeover.²⁵

To sum up the points: during the war the economic activity of the state was weaker and more muted in the field of fiscal and food policy in Russia than in Austria-Hungary. It suggests to me, that in opposition to the Gerschenkron thesis

in wartime not the difference of "relative backwardness" between the two empires was really the impetus for the state intervention. In Austria-Hungary, where the market and the economic infrastructure were deeply articulated this intervention could rather *substitute* during the war-time missing market factors.

According to some remarks, "by 1917 ... Austria-Hungary and Russia were racing each other to collapse."²⁶ This race was won undoubtedly by Russia in 1917. But the war was won by the Allies. Consequently the Habsburg-Monarchy disappeared from the scene of history and Russia received possibility once more to reorganize (for more than a half century) a new form of (soviet) empire.

Notes

- 1 Oscar Jászi, *The Dissolution of the Habsburg Monarchy* (Chicago, 1961), p. 202.
- 2 Krisztina Maria Fink, *Die österreichisch-ungarische Monarchie als Wirtschaftsgemeinschaft Ein historischer Beitrag zu aktuellen Integrationsproblemen* (München, 1968), p. 35.
- 3 *Ibid.*, p. 45.
- 4 *Ibid.*, p. 58.
- 5 Galántai József, *A Habsburg-Monarchia alkonya* (Bp., 1985), pp. 154-155.
- 6 György Szabad, "Das Anwachsen der Ausgleichtendenz der Produktpreise im Habsburgerreich um die Mitte des 19 Jahrhunderts," in V. Sándor & P. Hanák (eds.), *Studien zur Geschichte der österreichisch-ungarischen Monarchie* (Bp., 1961), pp. 123-137; David F. Good, *The Economic Rise of the Habsburg Empire 1750-1914* (Univ. of California Press, 1984), pp. 108-123.
- 7 There are two different interpretations: Leland B. Yeager, "Fluctuating Exchange Rates in the Nineteenth Century: The Experiences of Austria and Russia," in R. Mundell & A. Swoboda (eds.), *Monetary Problems of the International Economy* (Chicago, 1969), pp. 61-89; and John Komlos, "The Diffusion of Financial Technology into the Austro-Hungarian Monarchy toward the End of the Nineteenth Century," in J. Komlos (ed.), *Economic Development in the Habsburg Monarchy in the Nineteenth Century* (Boulder, New York, 1983), pp. 137-165.
- 8 Richard Pipes, *The Formation of the Soviet Union* (Atheneum, 1980), p.3.

- 9 Richard Pipes, *Russia under the Old Regime* (Penguin, 1979), pp. 250-251; *Istoriia SSSR*, t. VI (Moscow, 1968), p. 360.
- 10 I.D. Koval'chenko & L.V. Milov, *Vserossiiskii agrarnyi rynek XVIII-nachalo XX veka* (Moscow, 1974), p. 239. According to an other research the equalisation of Russian and world grain prices came to the end only at the turn of the century. M.B. Mironov, "Faktoy dmamiki khlebnykh tsen v evropeiskoi Rossii v 1801-1914 gg. i kolichestvennaia otsenka ikh vliiania," in *Matematicheskie metody v issledovaniakh po sotsial'no-ekonomicheskoi istorii* (Moscow, 1975), p. 201.
- 11 Scott M. Eddie, "Economic Policy and Economic Development in Austria-Hungary 1867-1913," in P. Mathias & S. Pollard (eds.), *The Cambridge Economic History of Europe*, Vol. VIH (Cambridge Univ. Press, 1989) p. 838; Scott M. Eddie, "Mit bizonyitanak az 1882-1913-as export-statisztikai adatok: Magyarorszag valoban csak a Monarchia "eleskamraja" volt? [What Do the Export Statistics for 1882-1913 Prove: Was Hungary Really Only the "Pantry" of the Monarchy?]," *Történelmi Szemle*, No. 3 (1982), p. 424.
- 12 Eduard März, *Österreichische Bankpolitik in der Zeit der großen Wende 1913-1923 Verlag für Geschichte und Politik* (Wien, 1981), pp. 50-51; Fritz Bartsch, *Statistische Daten über die Zahlungsbilanz Österreich-Ungarns vor Ausbruch des Krieges Mitteilungen des K. K. Finanzministeriums XXII* (Wien, 1917).
- 13 Ludwig V. Mises, "The Foreign Exchange Policy of the Austro-Hungarian Bank," *The Economic Journal*, No. 6 (1909), p. 208.
- 14 Köver György, "Az Osztrák-Magyar Bank 1878-1914," in T. Bácskai (ed.), *A Magyar Nemzeti Bank története I.* (Bp., 1993), p. 332.
- 15 B.R. Mitchell, *European Historical Statistics 1750-1970* (London, 1975), p. 496.
- 16 Paul Kennedy, *The Rise and Fall of the Great Powers Economic Change and Military Conflict from 1500 to 2000* (New York, 1989), p. 274.
- Ivan T. Berend & György Ránki, *Economic Development in East-Central Europe in the 19th & 20th Centuries* (Columbia Univ. Press, 1974), p. 92.
- 18 Gerd Hardach, *The First World War 1914-1918* (Penguin, 1977), p. 150.
- 19 The weakness of infrastructural network was clear from military point of view too. P. Kennedy, *op. cit.*, p. 239.
- 20 Hardach, *op. cit.*, p. 153.
- 21 Teleszky János, *A magyar dllampenzügyei a háboru alatt* (Bp., 1927), pp. 264-265; Eduard März, *Österreichische Bankpolitik in der Zeit der großen Wende 1913-1923* (Wien, 1981), pp. 198-199.
- 22 Hardach, *op. cit.*, p. 121.

- 23 Puskás Julianna, "Adatok a hadigazdálkodás kialakulásához és rendszerehez Magyarországon az első világháború idején," *Történelmi Szemle*, Nos. 1-2 (1958), p. 140.
- 24 Rev István, "A nagy hisztéria, avagy az önmagát beteljesítő jóslat," *Medvetánc*, Nos. 3-4 (1987), p. 169.
- 25 E.G. Gimpel'son, *Voennyi kommunizm: Politika, Praktika, Ideologija* (Moscow, 1973), pp. 56-57.
- 26 F. Kennedy, *op. dt.*, p. 263.