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POSTWAR ECONOMIC RECONSTRUCTION OF EUROPE

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~~before the~~

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Western civilization is a civilization of industrial countries, as distinguished from agricultural countries. The characteristic feature of an industrial country is that it imports raw materials and foodstuffs, and that it exports manufactured goods, which are for the most part manufactured from imported raw materials.

What made the countries of Western and Central Europe industrial countries was not so much their natural resources as accidental historical factors. Western Europe has developed political and economic ideas that have given rise to an organization in which modern capitalism can flourish. Economic liberalism and its corollaries, capitalism and political democracy, had their origin in the West, and from there, in the course of the 19th century, slowly spread to the other parts of the world. The head-start thus gained by Western Europe explains why these Western countries, up to the outbreak of the first World War, were by far the richest. Their capital had already begun to accumulate at a time when other countries were still following backward methods in government and production.

It is important to realize that the advantage thus gained by Western and Central Europe was temporary only, and that it was doomed to be overtaken by the development of natural resources in other parts of the world. Viewed from our present state of geographical and geological knowledge, the cradle of modern capitalism must appear poorly endowed indeed. There are many varieties of raw materials and foodstuffs which cannot be produced at all in these countries, and there are many others which can be produced only with a greater expenditure both of capital

and labor than is required elsewhere. With the realization of these disparities of natural endowment, and with the practical adoption of modern methods of government and production by the formerly more or less barbarous but, ^{backward countries which nature had} better endowed countries, capital and labor concomitantly migrated from Europe.

This transfer of capital and labor, by which Western Europe gave and all the rest of the world only received, ^{has long since stopped} ~~was the greatest historical event of the most glorious epoch in human history so far. It made North America, great parts of Latin America, Australia and a large area in South Africa the white man's home. It transformed the economic and social structure of Japan, China and India. It left no part of the world untouched. It made international the outer trappings, the paraphernalia of modern civilization. We may deplore the fact that this internationalization did not concurrently include the political and moral ideas of English and French 19th century liberalism, and that, far from eradicating the innate propensities to violence, it only provided the non-European nations with more efficient and more terrible instruments. But this failure is only to be ascribed to the replacement of these old liberal ideas, today stigmatized and laughed at as "orthodox," by so-called more realistic doctrines of power politics.~~

It was this "Realpolitik" which brought the period of laissez faire and laissez passer to an end. Today, international migration is practically impossible, and it may be that, in the not too distant future, migrations will even be hindered within the boundaries of every country by the same factors which have already reduced international migration figures.

The mobility of labor had created a tendency toward an equalization of the marginal productivity of labor. The great disparities in wages and standards of living among different areas of the world gradually diminished. Today, labor is practically country-bound. This fact has the tendency not only to perpetuate but to aggravate the inequalities in standards of living and civilization among different nations. Wages are today much higher in the United States and in the British

Dominions than even in England; in Europe wages are lower the further we go eastward and southward from England.

It has changed
~~Still more serious~~ is the situation with respect to the supply of capital.

Foreign investment was based on the assumption that the rights of private property would be respected. Precisely the opposite was the case. We may safely say that expropriation of the rights of foreign investors and the repudiation of foreign loans are considered a regular means of economic and financial policy. It is an accepted and generally tolerated practice of governments to use their sovereign powers for the sake of the nationalization of enterprises held by foreigners. It is a common rule to establish foreign exchange regulations in order to nullify the claims of foreign creditors.

Looking back over the history of foreign investment and international credit, we may observe that, but for the United States and the British Dominions, capital ~~marched~~ on a one-way route. Only ~~childish~~ ^{naïve} optimism could believe that the fate which the foreign investors and creditors will meet in China and British India will differ essentially from what has befallen them in Russia, in Germany and in the Balkans.

Until the outbreak of the first World War, Western and Central Europe financed their purchases of imported food and raw materials to a great extent by the interest on foreign loans and by the earnings of foreign investment. This will no longer be the case. That part of foreign assets which has not already been lost by ~~confiscation and repudiation~~ ^{the} has been confiscated ^{of its creator} by governments ^{and nations} and used for the financing of war expenditures. The present war will leave Europe without foreign assets.

This makes
Now we ~~may realize~~ the ~~critical~~ ^{critical} situation which the Western countries of Europe will have to face. On the one hand, an industry without adequate equipment. Machinery used up and not properly replaced, machinery for the production of arms and military necessities which cannot be used for the production of goods which

buyers in peace time demand. On the other hand, no way to provide the capital required. It is unlikely that the American investor, after all the experiences he has had with foreign stocks and bonds, and with the unpleasant memory of foreign exchange restrictions, will be anxious to run the risk anew. But, even if he should be ready, his government will hinder him. It is nowadays one of the items on the labor program of creditor countries to stop the outflow of capital in order to render higher the domestic level of wages.

This state of affairs spells the doom of European labor. ^{Men} They will have to work in factories whose equipment is much poorer than the equipment of the competing plants abroad. The European entrepreneur will have to pay on the world-market the same price for raw materials as his competitors overseas, who ~~work~~ ^{produce} under more favorable conditions. He will, moreover, have to sell his products at a lower price than his competitor who will be sheltered in his home market by protective import duties. The result will be low wages for industrial workers, which will depress their standard of living to something like Japanese levels.

These conditions - a comparatively unfavorable state of material resources for production, an extreme scarcity of capital, the impossibility of emigration for the excess population, and trade barriers in the foreign markets - will make it impossible to continue the prewar economic ^{policies} policies. These were characterized by a disregard of vital necessities and by ignorance of the principal requirements of business. What people are accustomed to call a progressive socio-economic policy consisted mainly in measures resulting in a reduction of output and in the consumption of capital. Modern labor policy was designed to reduce hours of work, to raise wages above the level which industry could bear, and to confiscate a part of the capital invested in order to spend it. The most outstanding instances of this policy are the unbalanced budgets and the practice of embarking upon public works regardless of the profitability of the enterprise. It was a misguided class policy which did not understand the meaning of profitability within the framework of

a capitalistic society. If capital is withdrawn from branches of business where it could pay, and invested in activities where it does not pay, the result is waste of capital and the creation of a privilege for minority groups. If capital is consumed or wasted, it is not only the entrepreneur and the capitalist who pays the bill. Other things equal, more capital means higher marginal productivity of labor and therefore higher wages.

All the measures of modern social legislation which effectively restricted the quantity of capital available and the output, were, in the last analysis, measures against the masses, both as wage earners and as consumers.

~~But I do not wish to discuss the incidence of labor and tax legislation.~~
What I wish to say is only this: for policies of this type there will be no room left in postwar Europe. This--let us say "Victorian"--policy was one of taking away something from the entrepreneur and the capitalist. Where there is a tremendous shortage of capital and where the entrepreneur lacks the means for a better equipment of his plant, for the purchase of raw materials and for the payment of wages, nobody can tax him or interfere with his management, if the wheels of the mills are to continue turning. ~~I do not see~~ ^{there is no} under such conditions a field where trade-unions could operate. There will be left no other taxpayer than the wage-earner and the consumer. Everybody will easily understand the problems involved, and the somewhat metaphysical aphorism, "the State should pay this or that," will lose its undeserved prestige. Where all the taxes must needs be paid by labor, because there are no rents and business profits to tax, every increase in public expenditure will immediately shorten labor's capacity to consume. The budget will be based on something like head taxes on great masses of extremely poor workers. The old slogans, "tax the rich, subsidize the poor," are void of meaning where everybody is a have-not and where the only goal of a reasonable economic policy has to be to facilitate the accumulation of capital. The labor policy of the traditional type, and the activities of trade-unions will become obsolete.

The same will hold true for the prewar agrarian policy. In the industrial countries of Europe, high import duties, the quota system and rigid prohibitions of imports on the one hand, and subsidies and tax exemptions on the other hand made the farmer live at the expense of the consumer. Domestic food prices were often three times or even more higher than world market prices. It will be impossible to maintain this system to the disadvantage of an extremely impoverished non-agrarian population. This means the disappearance of the greater part of agricultural production in these countries.

Nor will conditions be better for urban real estate. An impoverished people will hardly be able to pay rents sufficient for the maintenance of the buildings.

With the decline in the value of real property and the income derived from it, mortgages will be defaulted. Savings banks and insurance institutions will go bankrupt because their assets will depreciate.

Of course there is no doubt that, notwithstanding the military and political result of the war, all bank assets will be valueless. Their foreign assets have been expropriated by the government. Their holdings of commercial paper, of loans on collateral, of government bonds and debentures and of mortgages will likewise lose their value.

The day after the cessation of hostilities will therefore ^{mark the beginning} be the ~~blackest~~ ^{blackest} ~~Friday that ever dawned.~~ ^{and deep depression} Total war will result in total bankruptcy. It would be wrong to attempt to refute this by citing the armistice day of 1918. At that time there were not only many European countries which had not suffered at all, but even in the belligerent countries the structure of the apparatus of production was unshattered. And a very important difference is this: that the Jews have been practically eliminated from business. ~~What that means, no American can realize.~~ It means in Central and Eastern Europe that everybody who is business-minded has been removed, and that those remaining expect every improvement from the action of

a ~~metaphysical entity, the State.~~ The quick reconstruction of economic life in Europe after 1918 was the work of business men, among whom in Central Europe more than 50 per cent and Eastern Europe more than 90 per cent were Jews.

~~This dark prospect becomes still worse if we consider the mentality of~~
the people involved. ~~They~~ will not be ready to face stark reality and to understand that nothing else can lead them back to prosperity than restless work. They will look for some artificial remedy, for some magic wand to change dust into food and clothes. Decades of demagogy have given them the conviction that there is some panacea against all economic ills. They believe that it is the duty of the government to discover it. They believe superstitiously in the power of financial ~~arcana,~~ be it stamp money, social credit, or ~~what you will.~~ ^{anything else.} They believe in everything but in what they call orthodox economics. If someone explains that capital can be accumulated only by saving, they call his advice "dismal science."

There is no doubt that Europe will after the war have to go through a long period of extreme poverty. Until new capital is accumulated, the masses will live on a level not better than that of the infancy of modern capitalism. One of the consequences of this relapse will be an increase in the difference in the level of life and civilization between Europe and America.

~~It is obvious that the economic decline of Europe will affect America,~~
too. Europe will no longer be able to buy the quantities of American raw materials, food and other products, which it used to buy formerly. Irrespective of the result of the war, the American farmer will suffer a disappointment. The demand for wheat, lard, cotton, tobacco and other farm produce in Europe will be curtailed. In any case, the international division of labor will be restricted, not because of government established trade barriers, but because of a retrogression in European production. There still are, today, some branches of production where Europe is supreme, i.e., optical instruments in Germany, watchmaking in Switzerland, fashions in Paris, cloth in Great Britain. But ~~I do not see any~~ ^{there is no} reason why the

production of these articles should not receive an impetus in this country which has the advantage of being the biggest market for their consumption.

~~What is true for North America is no less true for Latin America. In~~
poverished Europe ~~will not~~ fulfill the hopes of those South American politicians who expect to find ~~a great~~ outlet for their raw materials and foodstuffs. The fantastic plans for a German penetration of Latin American will fail.

The most important question seems to be whether the United States will be able to contribute to a better and quicker reconstruction of Europe. ~~I do not wish to discuss the chances of a radical change in the immigration policy. I be-~~
lieve ~~that~~ it is unlikely that the American trade unions will in the near future lose their influence or change their mind. ^{as regards immigration} On the other hand, ^{we may} ~~I will~~ assume that the American investor will not be hindered by the government from investing his capital where he likes. But the problem is, whether the reasonable investor would want again to risk his capital in Europe. ~~To me,~~ ^{It} seems indubitable, that all kinds of foreign investment and loans to foreigners are doomed if the present state of international law concerning these matters continues to prevail. This state of ^{affairs} ~~of~~ law is characterized by the following features:

(1) Every government is free to repudiate its obligations or to tax as it likes the yield from its bonds.

(2) Every government is sovereign as far as currency is involved. It may ad libitum devalue its currency, it may make unilateral changes in the value of the money which it owes. It has the right by means of foreign exchange regulations to rob all foreign debtors of their principal and interest.

(3) Every government has the right to expropriate foreigners directly or through taxation. Even undisguised discrimination against foreigners is tolerated if it is presented to the public as a measure against capital and big business.

Of course, it is clear that only countries which will be ready to abdicate their sovereignty in these matters have a chance to attract foreign capital. The

most important financial provision in the new constitution of the League of Nations will therefore have to be the transfer to the League of the competence to legislate on these matters, and the establishment of an efficient tribunal to adjudicate all disputes arising therefrom.

It is obvious that a satisfactory state of international relations which would keep the world at peace would require many more encroachments on national sovereignties. But ~~I do not wish to digress from the limits of my subject in dealing with these matters. And I am fully aware that~~ under the present state of prevailing ideologies, it is simply utopian to demonstrate that peace and good will among the nations is possible only in a world of free trade and private property. It will take some time until mankind will be ripe again for this practice. We have to realize that postwar reconstruction will have to be accomplished in a much less perfect milieu.

Our contemporaries have the strange belief that economists and bankers may discover some magic power which can rebuild the ruins at no expense to society. In the presence of these beliefs, it is the duty of honest economists to repeat again and again that, after the destruction and the waste of a period of war, nothing else can lead society back to prosperity than the old recipe - produce more and consume less.

This is the only way for Europe to reconstruct its economic machinery, as far as it still can be rebuilt.

This reconstruction cannot be undertaken from without, it must come from within. It is not simply a matter of economic technique, still less of engineering; it is a matter of social morale and of ^{Social} ~~racial~~ ideologies. It can succeed only on the basis of a return to capitalism and to the economic methods of the 19th century. Of course, many ~~distinguished~~ contemporaries believe that there is another alternative, that is, socialism. It is not within the scope of this ~~address~~ ^{address} to discuss the pros and cons of both these systems of social cooperation.

The analysis of the theoretical side of this question would lead us far afield. I wish only to emphasize that the experience both in Russia and in Germany is not conducive to a favorable judgment of socialist methods. What is wanted is to secure for Europeans something better than the Russian mode of life.

The first and immediate consequence of the armistice and the demobilization of millions of soldiers will be a tremendous amount of unemployment. Probably some quacks will recommend, as a remedy, public works, labor camps and compulsory labor service. But who should pay for these expenditures? The problem is not busy work, but work which can produce the commodities which the producers of raw materials and food in non-European countries are ready to accept as payment. Such commodities for export no government and no socialist management every could produce. For this production, entrepreneurs are needed.

The spirit of enterprise and the initiative of business has, in the last two hundred years, transformed Europe from a continent of barefooted and half-starved masses into a world of mass consumption of goods once unknown or considered as luxuries. If there is any hope for a new upswing, it rests with the initiative of individuals. ~~Let us not forget that the nationalist parties of Europe have destroyed their civilization in the name of a fight against individualism and liberalism.~~

The entrepreneur will have to rebuild what the governments and the politicians have destroyed.