The European Economy in the Interwar Period

The First World War devastated Europe with millions of casualties and the destruction of land and property. A slow process of economic recovery began in the years following the war. Any such recovery, however, was short-lived, as European economies suffered under the depression of the 1930s.

The 1920s: Reparations, Inflation, and Weak Recovery

The belligerent countries had spent countless billions on the war effort and relied on loans, in addition to the sale of war bonds to their citizens, to finance the war. In contrast, the United States was the sole country to escape the war without any debt and instead supplied credit and food to Europe. Most European countries, in an attempt to increase their supply of money during the war, abandoned the gold standard. This move rapidly devalued their currency, causing inflation. By peacetime, therefore, European economies were unstable and heavily indebted.

The peace treaties signed to end the war included harsh economic penalties for the Central Power aggressors. Reparation payments forced the Central Powers to assume financial responsibility for the damage caused during the war. In 1921, the Inter-Allied Reparations Committee determined that Germany should pay 269 billion marks, or approximately 100,000 tonnes of pure gold. This sum was later reduced to 132 billion marks. Germany was unable to follow the schedule of payments. Its treasury was emptied of all precious metals to pay the debt, which then devalued the currency completely. The German government printed large amounts of currency causing a state of hyperinflation. For example, a cup of coffee cost 14,000 marks. At the peak of inflation, the rate of exchange was one trillion marks to one dollar. With the intervention of the United States under the Dawes Plan in 1923, Germany borrowed 28 million marks, its yearly payments were reduced, and the state of hyperinflation receded. (The last of the reparation payments was made in October 2010.)

While the economy of the United States flourished in the Roaring Twenties, European economies took much longer to recover and grow. It was not until the mid-1920s that European economies surpassed prewar figures of production. Newer industries like automotive, radio, and commercial aviation spurred growth, as did the implementation of standardized mass-production in industry. This growth, however, could not compare with the surging economy of the United States, and the percentage of the world market held by European countries declined.

While European countries entered a period of economic growth from about 1925 to 1929, the gains they made were modest. Unemployment was still high, and the benefits of growth were unevenly shared. The gap between rich and poor increased, a situation that was exacerbated by a rise in the general population. Most people, therefore, had not improved their financial situation much when depression hit in the 1930s.

The Great Depression

Much of Europe's survival and prosperity in the 1920s relied on American loans. When the U.S. stock market crashed in October 1929, American credit disappeared, which drastically affected European businesses. In Germany, where the recovery had been particularly weak, the depression hit particularly hard. Six million Germans were unemployed in the early 1930s. In 1931, when the German and Austrian economies seemed in danger of collapse, the United States brokered a deal to place a moratorium on reparations payments.

The deal did not do much to help either country's economy, but it hurt other European countries instead. The British, who relied partly on German reparations payments to make their own repayments to the U.S., suffered a near-collapse of their financial system.

European governments also responded poorly to the onset of depression. The British, who relied heavily on external trade, raised tariffs and abandoned free trade in general. The French, meanwhile, reduced the civil service as well as payments to former members of the military. Both actions – raising tariffs and thereby discouraging trade, and reducing the civil service and thereby destroying jobs – have since been determined to have deepened the Great Depression. The difficulty was that governments across Europe followed the same pattern in dealing with the Depression. The continent therefore remained mired in depression for the rest of the decade.

Fascist Economies

In the wake of the economic downturn of the 1930s, a more authoritarian form of political governance increasingly appealed to Europeans. While fascist political parties gained adherents throughout Europe, in Germany, the National Socialists, or Nazis, a fascist party, succeeded in obtaining power. Fascism was based on the idea that the masses should participate directly in the state, not through a legislative body such as a parliament, but through a fusion of the population into one "spirit." The individual was insignificant, and the nation-state was the supreme embodiment of the destiny of its people. The fascist government controlled every aspect of the lives of its citizens. The ideals of economic stability and social peace could be obtained only through dictatorship and tight control over the press, education, police, and the judicial system.

Fascists had enjoyed political success before the Nazi seizure of power in 1932-33. In the 1920s, Benito Mussolini's fascist movement gained control in Italy with much popular support. By 1929, as the Great Depression loomed, there was a new sense of order in the Italian economy and society. Mussolini's popular support, however, plummeted after he failed to implement effective social change in the 1930s.

The 1930s witnessed the rise of fascist control in Germany. Under the leadership of Adolf Hitler, the Nazis implemented a major state-directed economic plan aimed at jump-starting the economy. Hjalmar Schacht, a former German Democratic Party member, created the plan. Schacht introduced price controls and borrowed heavily to finance large public-works projects. Rearmament was a major component of Schacht's plan, but there were also major projects, such as the construction of the Autobahn and production of the Volkswagen. These projects were moderately successful in creating growth and also reduced unemployment significantly. The economic success of the Nazis was one of the reasons that the Nazis won respect from many people in Depression-ridden Europe. It also solidified the support and loyalty of the German people.

In 1936, Hitler replaced Schacht with Hermann Göring. Göring was ordered to make the German army ready for war in four years, even though specific provisions in the Treaty of Versailles prohibited Germany from rearming after World War I. The military build-up that followed stimulated the German economy tremendously. German industry enlisted in the Nazi economy as well, and the country increased in prosperity as well as self-confidence, in marked contrast to democratic Europe.

The Communist Economy

To the depressed economies of Europe in the 1930s, Communist Russia's economy also seemed like a major success story. By the beginning of the 1920s, Russia's economy was ruined because of the First World War and several years of civil war. Industrial production dropped to 18% of prewar levels, agriculture was less than half of prewar levels, and unemployment was rampant. Years of war, famine, and disease left many orphans wandering city streets. Robbery by packs of little children was an ordinary fact of life.

It was difficult for the Bolsheviks to digest the fact that the international Communist revolution had not materialized. After a great deal of hesitation, they declared that Russia had entered a transitional stage on the route to Communism. Marx had spoken about such a stage, but he indicated that it would not last long. As a result, the Bolsheviks announced the New Economic Policy (NEP) in 1921. Under the NEP, the state stopped confiscating businesses (which it had done during the civil war), the market was opened (though to small business only), and currency was restored. The government maintained its monopoly in heavy industry and the major means of production. Thus, from 1921 to 1928, a market economy existed in Russia.

The NEP pleased the peasants, who finally brought their grain to market. The peasant revolts stopped. The economy revived immediately and the living standards of both workers and peasants improved. Food rations were no longer necessary, and the famine was over.

Though the NEP seemed like a good policy, it was problematic for the Bolsheviks. They had viewed its passage as a necessary step backward on the road to a Communist paradise, and eventually they would have to move forward. The NEP set the stage for an unequal distribution of wealth and also foreshadowed one of the great problems the Communists would face. Marx had theorized that workers would overproduce when they owned the means of production, but they didn't.

When Joseph Stalin came to power in the second half of the 1920s, he therefore began to move the USSR away from the NEP. His new policies involved large-scale industrialization and collectivization. Stalin realized that Russia had been crushed in the First World War because its industry was not developed enough, and claimed that Russia was 50 to 100 years less industrialized than the Western powers. To survive the coming assault, they needed to be ready in ten years. (Stalin was right, ironically, since Hitler attacked Russia about 13 years after the first Five Year plan began.) The government therefore developed a series of Five Year Plans with unreachable objectives to govern the economy.

According to Communist theory, industrialization would also increase the number of "progressive" workers (workers were considered to be progressive because they were traditionally the strongest supporters of Communism) and decrease the number of peasants (who were considered to be less enthusiastic supporters of Communism). Since the entire economy had to be planned (instead of the unplanned and volatile capitalist economy), all businesses were nationalized. Almost all economic resources were moved to heavy industry; if there were ever surplus materials, they always went to heavy industry (Class A) instead of light industry (Class B). Constructing houses was a luxury, so few were constructed. This created massive strains in the cities as peasants flooded in.

Industrial output quadrupled during the 10 years covered by the first two Five Year Plans. Considering that it happened at the same time as the Great Depression, it was a signal to many that capitalism would indeed be replaced by Communism. (Westerners did not see the human and material waste that accompanied such spectacular growth; millions died as a result of the Communist reengineering of society, and parts of the country were despoiled because of industrial production.)

Workers toiled with tremendous enthusiasm, thanks to propaganda promising that their rewards were only a few years away. The Communists began a number of enormous projects that could only have been completed with the help of the workers. They also succeeded in electrifying the entire region. The Soviets produced their own tractors at an astonishing rate; they made the best tanks in the world in incredible numbers; they created their own aircraft industry, and the Soviet air force was equal to the Luftwaffe by the outset of the Second World War.

Collectivization, however, proved less successful than industrialization. Collectivization had both economic and political aims. It enabled the government to make agriculture into an industrial enterprise, which would theoretically produce more because of economies of scale. Politically, the Communists hoped that collective farms would eliminate the peasants as a separate class. According to the Communist understanding of history, social classes would always struggle against each other. Peasants were presumed to be more conservative than workers; since peasants owned their farms, employed workers, and kept profits (in Communist lingo, they were *bourgeois*), they did not fit into the Communist system. By creating collective farms, the Communists hoped to eliminate the peasant class and replace it with a rural working class. This would bring an end to class warfare (since everyone would be a worker) and help to usher in the workers' paradise that the Communists desired.

Though in theory all Russians owned the collective farms together, in practice the government administered them. The government had a plan for how much each farm should produce. It would take a quota that amounted to at least the majority of that production and divide anything that was left among the farmers. The farmers could either consume the surplus, or they could sell it on the open market. In practice, many collective farms produced less than the small farms had. The government had to meet the planned quota, so it took everything from the less productive farms. The peasants who worked these farms essentially worked for free, and had to depend on their own land to survive. As a result, the 1930s was a period of terrible starvation across the USSR, though these tales rarely reached Western audiences.

Summary

- European economies were heavily damaged by the First World War, and took a long time to recover. Their recovery in the late 1920s was sluggish and quickly destroyed by the Great Depression.
- When the Nazis took power in Germany, they attempted to inject new vitality into the economy as part of their Fascist agenda. The massive military buildup that they demanded helped to bring Germany out of depression.
- The Communists also enjoyed economic success in the 1930s. Large-scale industrialization efforts developed the Russian economy very quickly and made the USSR the envy of the West. What foreigners did not realize, however, was the extent of the sacrifices demanded of Russian citizens.