The Scourge of Europe
The Public Debt Described, Explained, and Historically Depicted

L. V. Birck
Written during the early 1920s, at a time when Europe was still recovering from the catastrophe of the First World War, L.V. Birck’s *The Scourge of Europe* examines the economic issues surrounding the existence of public debt, its history, and possible approaches to problems associated with public debt as they were being pursued by the great powers of the time. Birck’s analysis contains a rigorous theoretical exposition and explanation of public debt as it was understood in the crucial period leading up to the Great Depression. This is then followed by an insightful exploration of the role of public debt in European financial and economic history. Finally, some reflections on the policies of England, the United States, France and Germany in the latter part of the nineteenth and early-twentieth centuries are included.

This book will appeal to economic and financial historians, as well as to those generally interested in European policies towards debt from the Middle Ages to modern times.
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The Public Debt Described, Explained, and Historically Depicted

L. V. Birck
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National debt is immoral and destructive; silently undermining the basis of the State, it delivers the present generation to the execration of posterity

Napoleon I
# CONTENTS

## PART I: DESCRIPTION

<table>
<thead>
<tr>
<th>CHAP.</th>
<th>CONTENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. How to Meet a Budget Deficit</td>
<td>1</td>
</tr>
<tr>
<td>II. Basis of Public Credit</td>
<td>8</td>
</tr>
<tr>
<td>III. The Lender</td>
<td>15</td>
</tr>
<tr>
<td>IV. Various Kinds of Debt</td>
<td>26</td>
</tr>
<tr>
<td>V. Conditions</td>
<td>38</td>
</tr>
<tr>
<td>VI. Politico-Economic Conditions</td>
<td>42</td>
</tr>
<tr>
<td>VII. Bankruptcy</td>
<td>50</td>
</tr>
<tr>
<td>VIII. From Debased Coin to Paper-Money</td>
<td>63</td>
</tr>
</tbody>
</table>

I.
*How to Meet a Budget Deficit.*

(The State's expenditure—The State's assets—Extraordinary taxation.)

II.
*Basis of Public Credit.*

(Nature of the credit—Conditions—Authority for loans—Control.)

III.
*The Lender.*

(Subscription—Voluntary loans—Forced loans—Masked subsidies—Union of bond-holders.)

IV.
*Various Kinds of Debt.*

(Administrative and fiscal debts—Funded debt—Floating debts—Consolidated debts.)

V.
*Conditions.*

(Expediency of contracting loans—Effective interest—Redemption—Other conditions.)

VI.
*Politico-Economic Conditions.*

(Financial control—Taxation—The currency—Conversion.)

VII.
*Bankruptcy.*

(Definition—History—Ethical considerations—Question of law—Sanctions.)

VIII.
*From Debased Coin to Paper-Money.*

(The abuse of the coinage privilege—The genesis of paper money—Kinds of paper money—Issuing and calling in.)
PART II: THE EXPLANATION

IX. PAPER MONEY AND INFLATION.

(The effect of debasing the coin—Gold, banknotes, and credit—Effects of inflation—Rates of exchange—Certain phenomena of inflation—The crime of inflation.)

X. BACK TO GOLD!

(Stabilization—Convertibility of the notes—The point of time.)

XI. TAXATION OR LOANS?

(The taxpayer's point of view—The Minister's motives—Principles of sound finance—Loan guarantees—"One hand's debt to the other hand"—Does public debt further capital accumulation?—The national debt and inflation.)

XII. CAN THE PRESENT GENERATION TRANSFER HER BURDENS ON TO THE FUTURE?

(Concrete wealth—Destruction of capital—Domestic or foreign loans.)

XIII. REPAYMENT.

(Astronomical figures—Slow amortisation—Other effects of the continued existence of the debt—Depreciation or bankruptcy.)

XIV. A CAPITAL LEVY.

(It leaves the capital intact—The tax on capital and the rate of saving—How the tax is to be levied—Merchants and theorists.)

PART III: THE FACTS

XV. THE MIDDLE AGES.

(The king's purse—Landed property and pledges—Mercenary troops and advances—)
<table>
<thead>
<tr>
<th>CHAP.</th>
<th>CONTENTS</th>
<th>PAGE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Compulsory loans—Loans from the patricians of the towns and from Jews—The Church's attitude to taking of interest.)</td>
<td></td>
</tr>
<tr>
<td>XVI.</td>
<td><strong>THE ORIGIN OF AN INTERNATIONAL LOAN MARKET.</strong></td>
<td>165</td>
</tr>
<tr>
<td></td>
<td>(The Italian towns—Lyons—The debt of the Hapsburgs—Antwerp—German loan centres—The Fuggers—Loan Policy of the later middle ages.)</td>
<td></td>
</tr>
<tr>
<td>XVII.</td>
<td><strong>THE ERA OF ABSOLUTISM.</strong></td>
<td>184</td>
</tr>
<tr>
<td></td>
<td>(Its Economy—Voluntary loans—Forced loans—The Mississippi Bubble—Organization of the capital market—Public debt in the eighteenth century.)</td>
<td></td>
</tr>
<tr>
<td>XVIII.</td>
<td><strong>THE ERA OF NAPOLEON.</strong></td>
<td>203</td>
</tr>
<tr>
<td></td>
<td>(In the sign of Mars—The pound note—The Assignats—The continental bankruptcies.)</td>
<td></td>
</tr>
<tr>
<td>XIX.</td>
<td><strong>THE LIBERAL RÉGIME.</strong></td>
<td>211</td>
</tr>
<tr>
<td></td>
<td>(The period of the Census—Parliaments—The wars after 1848—The growth of loans and conversions—The new loan market—The debt of the German States—England—The French indemnity and the third Republique—The gold standard restored.)</td>
<td></td>
</tr>
<tr>
<td>XX.</td>
<td><strong>THE WORLD WAR.</strong></td>
<td>226</td>
</tr>
<tr>
<td></td>
<td>(Inflation—Money and prices—The principles underlying the financing of the war—Settling-up—Deflation crises.)</td>
<td></td>
</tr>
<tr>
<td>XXI.</td>
<td><strong>UNSETTLED PROBLEMS.</strong></td>
<td>240</td>
</tr>
<tr>
<td></td>
<td>(The reparations—The Dawes plan—The new gold mark—The new Austria—Inter-Allied debt—Russia—The Successor-States.)</td>
<td></td>
</tr>
</tbody>
</table>
viii CONTENTS

APPENDIX

ENGLAND. 265
(The war—The armistice.)

THE UNITED STATES. 272
(The inheritance from the civil war—The twentieth century.)

FRANCE. 276
(Loans not taxation—Towards the abyss.)

THE GERMAN EMPIRE. 283
(1870–1914—The policy of inflation—The dissolution—The fate of the mark.)

DENMARK'S NATIONAL DEBT FOR 300 YEARS. 296
(1660–1800—The bankruptcy—The resurrection of the national credit—The armed neutrality—Appendix.)
PART I

DESCRIPTION

CHAPTER I

HOW TO MEET A BUDGET DEFICIT

The State’s Expenditure.—In order to carry out its functions a State needs not only personal services (officials) but also tangible property such as fixed capital (invested in buildings, fortifications, ships, and factories), raw materials and commodities for consumption (e.g. for the work-houses). In the age of Natural Economy the State took property and services directly and in kind from the working community; sometimes in the form of payment of a licence, for the privilege to carry on a certain business or professional activity, or as a tax on land, or often as revenue from public domains. Nowadays under our economic system, where money is the means of exchange, only few traces of the former system remain, such as compulsory military service, the duty of clearing public thoroughfares of snow and, in war-time, the obligation of delivering certain quantities of grain to the State. To-day the State uses indirect methods, raising money from its citizens by means of taxation and making use of this money to purchase the goods and services that it needs. Thus the State has an income and expenses and consequently also economic rights and obligations. These are taken care of through the particular medium of the Treasury, a kind of juristic person which differs from every other juristic individuality such as limited companies, in that the Treasury is one of the manifestations of the State backed by the State’s sovereign authority.

A State’s expenditure depends on what functions that State undertakes, and on how, and with what economy, these functions are carried out. In contrast to both private and other legal individuals expenditure is the primary and income the secondary consideration for the Treasury. How much the State
can collect through taxation depends on the income of its citizens and also on the functions it assumes. On the one hand a tax of 10 per cent. on an average income of one thousand dollars will leave the tax-payer less for his own consumption than a tax of 20 per cent. on an income of two thousand dollars, prices being the same. On the other hand, the individual will be able to contribute more if the State gives him more; if the State grants old-age pensions it can increase taxes by the amount of the life insurance premium, or again if the Norwegian government provides consumers with free electricity from its waterfalls, the tax could and should be considerably increased, because the State cannot supply its benefits gratis. Finally, the burden of taxation varies according to the manner in which the tax is assessed; a tax on income can absorb a greater average percentage of the total revenue of the population than the consumption taxes (such as "la gabelle" or salt tax) in vogue in France under the absolute monarchy, which in their effect approached to poll taxes. For these three reasons, the attitude of such writers as Falbe-Hansen and Leroy-Beaulieu is purely arbitrary when they assert that the State must never take more than 10 to 12 per cent. of the total income of its citizens: according to circumstances such a percentage may represent too much or too little. There is naturally a limit to the amount of taxes that can be levied, not only as regards what the population is able to bear (in this connection it may be pointed out that many taxes imposed by absolute monarchies have proved that a too burdensome or badly adjusted taxation destroys a country's productivity) but also as regards the will to contribute, since a citizen who considers a tax too burdensome and unjust will resort to tax evasion, an act which is not always equally immoral. When one speaks of the natural maximum limit of taxation, this applies to a policy covering a long period; the burden of taxation for any one particular year must not normally approach so near to the limit as to leave no margin for unforeseen developments. A debate regarding "Retrenchment"—such as the one now taking place in most countries—always seems hypocritical; the Conservatives attack the Social Welfare schemes, the left wing the expenditure for military purposes, in spite of the fact that the criticism ought by rights to be aimed at quite a different
thing, viz. that the State’s functions are not exercised according to the economic principle of achieving one’s purpose at the smallest sacrifice; it is not against what the State does but against the way in which it does it that criticism should be levelled.

A State’s revenue as estimated in a Budget will often prove to be insufficient; a Budget deficit may result from: (1) the fact that revenues and expenditures are not always contemporaneous; (2) the fact that the incomes and expenditures of a State’s business enterprises often fall in different periods; expenses, which should really be charged to several years, occur in one single financial year; (3) unforeseen expenditure which occurs once and for all, as, for example, damage done by floods or fire, sudden increase in coal prices, etc.; (4) extraordinary expenditures arising from the investments in new construction of the State’s interest yielding capital (e.g. railways); (5) expansion of State enterprises which are useful but do not return interest; and (6) war. To these must be added that (7) the ordinary revenues may partly fail (the consumption of spirits and tobacco may decrease, imports may diminish, the amount of trade turnover which determines the revenue from stamp-duties may decrease, just as the State’s enterprises may show decreased revenues owing, for example, to lesser patronage of the railways and telegraphs, and a period of depression will greatly diminish the revenue from income-taxes). The extraordinary expenditure resulting from capital investments counts heavily nowadays because it is not only in private industry that our methods of production require large amounts of fixed capital—or in other words that the disbursements involved by production in an ever-increasing degree consist of interest and amortisation—but also in the State’s enterprises (including railways, public health, education and defence). Fixed capital expenditure (the expansion and replacement of fixed capital), however, occurs by jerks. This fact in particular—the increasing importance of fixed capital in the activities of the State and the influence of the economic cycles which cause strong fluctuations in both revenues and expenditures—from time to time bring about a deficit in the State accounts not to be covered by the estimated revenues.

The State’s Assets.—A private individual will in case of a deficit draw upon his capital. But the State’s capital is invested; (1) in
hospitals, schools, prisons, fortifications, and other public buildings, and in loans to local government bodies and special institutions; these are necessary for the functions of the State, and moreover are not realisable assets; (2) in economic enterprises such as means of transport, lands and mines; these properties can be sold, but rarely without great losses; since the State’s motives in investing capital in such ways are not only to obtain a return but to benefit the Community, that is to say, that the advantage of public ownership goes partly beyond the question of their remunerativeness; these assets are consequently not such as can be realised merely with a view to covering a deficit unless there are political reasons for such a sale; (3) the State may for various special Reserve Funds purchase and hold shares and bonds, which may be sold when the market price is favourable on the supposition, however, that such assets should be replaced in following years if the Reserve Funds thus depleted continue to have a valid “raison d’être”.

Some years ago the Danish Conservative Party contended that the Government Reserve Fund contained too many Danish securities which would prove hard to realise in case the country got into war, and recommended the purchase of foreign securities; the statement was in itself correct, but the World War and the neutrality of Denmark upset the underlying premises; (4) finally the State may have deposits in banks or hold cash funds. If the latter be paper money, it may just as well defer putting the printing press in motion till it actually needs the money, unless technical reasons make it necessary. When Dr. Miquel became Minister of Finance in Germany, he made an estimate of the quantity of Government bonds and paper money which would be needed in case of war. The Government Printing Office replied that it would take some years to produce the necessary quantity and he consequently had the printing works enlarged. If on the other hand the State holdings consist of precious metals it may of course, in case of need, hand over the metal to the bank of issue, which in turn issues notes to, e.g., three times the value of the metal; but this is inflation, which may for that matter just as well be created without gold cover. The 120 millions hoarded in the Julius Tower at Spandau and gold pieces hoarded in a stocking produce the same effect; so long as they are kept out of circulation they will reduce the
possible medium of exchange and bring about a lower level of prices than would otherwise be the case; and when they pass into circulation from the tower or the stocking they cause a moderate inflation such as we experienced during the first months of the World War, when the gold from State Depositories, from general circulation, and from stockings found its way into the banks of issue.

As regards bank deposits it is practical for the State to have such under circumstances not too abnormal; in case of extraordinarily large disbursements it is convenient for the Finance Minister to be able to draw on his deposits, but from an economic viewpoint the situation is not different from what it would be if the State drew on the bank without having a deposit, because the money which is deposited in a bank is with the exception of the necessary cash reserve—e.g. 4 per cent. —lent to the public; when the State draws on its credit balance the Bank must, in the same way as when it only grants the State credit accommodation, either avoid granting another loan to private clients or ask one of its debtors to pay up; in both cases the effect on the business community is the same. From the administrative point of view, the State ought to maintain certain bank deposits, amounting to e.g. a three months’ need, and it is then reasonable to cover deficits occurring by utilizing such deposits, but they can never be very large. Bank deposits are convenient for the State Treasury, but immaterial from a national-economic point of view.

Extraordinary Taxation.—Even as a government, in drawing upon the State’s accumulations, covers current expenditures by means of funds accumulated (past taxation), so it may also cover a deficit by means of extraordinary i.e. current taxation, or by levies on future incomes, anticipated taxation, that is to say in reality by loans.

If an existing tax is increased to an appreciable degree, e.g. by 50 per cent. the old axiom applies that a difference in quantity often produces a change in quality in the same way as “too much” makes an efficient medicine a deadly poison. (1) The regulations for each tax must be broad and general, in disregard of individual cases, such as family obligations, dwellings, health, age, the time during which the tax-payer has been in possession of his wealth, etc.; in proportion as the tax increases, the
inevitable injustice to the individual ceases to be negligible and becomes vital; the remedy is to introduce into the taxation law more exceptions and special regulations, which in turn make the administrative machinery very expensive and inquisitorial in character, and which again afford new tempting loopholes for the evader. Every high tax violates, so to speak, Adam Smith’s famous rules of taxation. (2) Every tax has *incidences*, that is to say attendant circumstances which affect the national economy, provide an unintended protection, favour or prevent the sale of certain goods or shift the productive forces; a high tax renders these by-effects more violent and more damaging. (3) A tax levied once and for all, whether it be an increase of an old or an altogether new tax is fortuitous in its effects, because it is a matter of chance whether I happen to be this year in such a position as makes me a tax-payer; a tax on real property would not have affected me last year if I had bought my property this year; this year I may perhaps have to buy new furniture or a new motor car, and I am then hit by an extra tax on luxuries which those will escape who will not have to make their purchases till next year; an increase in the income-tax falls on the man who this year, and not last year, got the opportunity of his life to make money; it is only in the case of the tax on capital that this fortuitousness is eliminated, though here again the market value of securities (such as corporation shares) and real capital (such as factories) change from time to time. (4) The effect of a rigid taxation levied once and for all is very disturbing; it may compel me to modify my consumption, to leave my house, to let or sell it, to realize personal possession at a loss, so that my sacrifice will be greater than the State's gain; in so far as the tax falls on raw materials or complementary materials or, on the whole, on production at any stage, I am compelled to modify my production in some manner to incur too heavy losses, unless I am in a position to *substitute* a cheaper raw material for a more costly one, or a more expedient method of production for the one hitherto employed. (5) Every tax is subject to "the Law of Decreasing Return": it is a matter of experience that the doubling of a tax does not yield double the return. (6) Finally, it often happens that a new tax and sometimes an increased old one cannot be administered by the existing official machinery, and such an increase of taxation is often viewed by the Public
with disapproval; every law, including laws imposing taxation, must not only be based on the fiat of the legislative body, but must also have the tacit consent of the public; and an extra tax is not supported by the force of habit, i.e. by the fact that the tax-payer is accustomed to it, which can render bearable a customary though unjust tax. There are times when the public cannot pay, viz.: when supplementary taxation coincides with a crisis with its attendant depreciation of securities.

Whereas, within a margin of 20 to 30 per cent. of the total taxation, a supplementary tax contribution, spread over the whole system of taxation, can be justified, powerful reasons will under normal conditions militate against an increase over and above that margin; it may therefore become necessary for the State to borrow, and the State Debts will then become a normal part of public finance administration in the capitalistic community; it will only be in exceptional cases that a State has no debts as, for example, the U.S.A., whose debts in 1835 amounted to only 37,000 dollars, or after the end of a victorious war where the defeated party really pays the stipulated indemnity (as was the case with Germany after the war of 1870–71).

A last possibility which may be said to be included in the preceding one, is a falsification of the currency, a subject which will be treated elsewhere. But both borrowing and depreciation of the currency are such great evils that, in many cases extra taxation is to be preferred.