Central banking independence, historical narratives and the Bank deutscher Länder, 1948-1957

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Introduction

There was no West German consensus for central banking independence when the Federal Republic of Germany was established in 1949. Far from it, the issue was a controversial one. It often sparked heated public debates. This paper is a tale of two cities. It examines how the Frankfurt-based Bank deutscher Länder defended its central banking independence from the Bonn government in the public sphere.\(^1\) In particular, the paper examines how historical narratives of Germany’s two inflationary episodes were used by the central bank in the media amid efforts to influence the debate surrounding the upcoming Bundesbank Law. The law was a crucial piece of legislation that would determine the future structure and institutions of the Bank deutscher Länder’s successor: the Deutsche Bundesbank. The paper concludes by stressing that central banking independence was not defended by success in the field of economics alone. It was guarded in the public sphere, too.

The troubled legacy of central banking independence

Central banking independence is lauded in present-day Germany. But this was not the case at the foundation of the Federal Republic. In the late 1940s, Germans looked back on three turbulent decades of monetary history. The country had experienced two inflations and one deflation within a single generation. The first inflation occurred in 1922-3, when a hyperinflation induced by government spending devastated the Weimar Republic. The second inflation was a different creature. It occurred during and after the Third Reich and Second World War. It was a ‘repressed’ inflation, characterised by price controls, empty shelves and a flourishing black market. Both inflationary episodes ended with the same result: Germany’s currency had become worthless as a means of exchange. Germany’s deflation, which marked the twilight years of the Weimar Republic, had devastating consequences. The deflation aggravated mass unemployment, helping to radicalise an electorate that was becoming increasingly disillusioned with democracy. Mass unemployment turned the National Socialists from a fringe party into an electoral force.\(^2\)

Throughout this all stood Germany’s central bank, the inter-war Reichsbank. The Reichsbank was independent of government instruction from 1922 until 1937, legally speaking. These dates are important. It means the inter-war Reichsbank was independent at the height of the hyperinflation and the depths of deflation. The origins of the Reichsbank’s central banking independence were not German; rather, they were foreign. The Reichsbank was made independent in May 1922 at the behest of the Allied powers, who made it a key condition should Germany receive a moratorium on its reparations burden – the enormous sum of money imposed on the country following its

\(^1\) For the sake of clarity, the public sphere is defined as an array of media platforms which served to foster public debate: that is, regional and national newspapers, journals, radio and television.

defeat in the First World War. In the late 1920s, under the leadership of Hjalmar Schacht, the independent Reichsbank became a controversial political actor. And during the Great Depression, too, it pursued restrictive monetary policies that helped worsen economic conditions. Taken as a whole, the inter-war record of central banking independence was a troubled one.

The Bank deutscher Länder: a ‘child of the occupation’

The Bank deutscher Länder, established in 1948, was a by-product of its time. It was founded over a year before the establishment of the Federal Republic. Germany’s territory was divided among the four Allied military powers – America, Britain, France and the Soviet Union – following its defeat in the war. Each authority administered its own ‘zone’. By 1948, America, France and Britain had joined their zones to form a western bloc. The creation of the Bank deutscher Länder was ultimately a compromise stemming from American and British negotiations. German opinions were not heeded. As such, the new central bank was seen as a ‘child of the occupation’, a product of military law.

The Bank deutscher Länder was set up to help oversee the currency reform of 1948, which introduced the deutschmark. It was a federal institution, with its key decision-making body, the central bank council, comprised primarily of men appointed by the various state governments. The Allied powers maintained a veto over the central bank council’s decisions. But the Allies decided that the Bank deutscher Länder should itself be independent from German political authorities. It was the second time that the impetus for central banking independence came from abroad.

Adenauer: reclaiming sovereignty

The Bank deutscher Länder was seen as a provisional institution. A foreign creature operating on occupation law, it did not fit into the vision of a new republic. The West German state sought to reclaim sovereignty in areas of political and economic importance following its creation. Its constitution, the Basic Law, stated that the German parliament was to pass legislation establishing a federal bank, or Bundesbank, to replace the functions of the Bank deutscher Länder. In 1949 it was assumed by many politicians, including the chancellor Konrad Adenauer, that it was only a matter of time before the central bank was placed under the government’s thumb. As the economic historian Volker Hentschel notes, ‘Politicians of all parties were of the view that the complete independence of the Bank deutscher Länder was a mistake of occupation policy in need of correcting’. Even Ludwig Erhard, the new economics minister, acknowledged the primacy of the state in the formation of economy policy. Where politicians differed was over the extent to which the federal government should be able to influence monetary policy.

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4 Müller (1973), pp. 44-51.
11 Ludwig Erhard to Fritz Schäffer, 12 Oct. 1950, Bundesarchiv Koblenz [BAK], B102/5706.
The fight for central banking independence, 1949-51

Supporters of central banking independence pointed to the lessons of the Weimar Republic’s abysmal hyperinflation. Opponents, on the other hand, stressed the independent Reichsbank’s dismal record during the Great Depression. At the dawn of the new republic, it remained to be seen which side would triumph. The Bank deutscher Länder, for its part, did not stand in the corner of this public discussion. Rather, it stepped into the fray. And it used lessons taken from Germany’s monetary history to support its efforts.

The Bank deutscher Länder was led in this respect by Wilhelm Vocke, chairman of the directorate, the body which ran the central bank’s day-to-day operations. A former Reichsbanker – he entered the monetary authority in 1918 and left in 1939 – Vocke was an avid supporter of central banking independence. His very first speech before the entire central bank council stressed the need for its defence. Following its establishment, West Germany was in desperate need of capital to help rebuild its shattered infrastructure; Vocke argued that to remove the central bank’s independence vis-à-vis the Bonn government was to enable the government to embark on reckless spending programmes, endangering the currency.

An internal central bank taskforce was set up to monitor the political debate surrounding the Bundesbank Law. In September 1949 the central bank began to lobby the federal government behind the scenes for the maintenance of the central bank’s independence. Such efforts were unlikely to succeed, as one internal Bank deutscher Länder report lamented. This fear was confirmed when the finance minister, Fritz Schäffer, proposed the first draft of the Bundesbank Law to the federal cabinet in March 1950. Schäffer was an opponent of central banking independence. His draft proposed the establishment of an arbitration committee, comprised of government and central bank officials, to oversee disputes between Bonn and Frankfurt concerning monetary policy. The second draft, which appeared later that month, strengthened the government’s grip, giving Bonn an effective veto on central banking decisions. In 1950 Schäffer grounded his arguments with reference to the independent Reichsbank’s controversial actions during the Great Depression.

The Bank deutscher Länder efforts at persuading the government behind the scenes had failed. The monetary authority fired back with a counter-draft of the Bundesbank Law, and explicitly stressed the need for central banking independence ‘in light of two inflations triggered by the state occurring within a single generation’. By now the central bank also took to the public sphere. The Bank deutscher Länder’s communication channel was surprisingly centralised. Interaction with the media was controlled by Vocke’s directorate. The central bank began a campaign via the media to win public opinion over to the benefits of central banking independence. The Bank deutscher Länder’s press chief during the 1950s treated ‘public opinion’ and ‘the press’ as synonymous terms. Initially, the central bank pursued this campaign behind the

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12 Central bank council minutes, 1 Jun. 1948, Deutsche Bundesbank Historisches Archiv [DBHA], B330/2/3.
13 Central bank council minutes, 30-31 Aug. 1949, DBHA, B330/17/1.
16 ‘Begründung – Entwurf. Gesetz über die Währungs- und Notenbank des Bundes (Bundesbankgesetz)’, Nov. 1950, BAK, B102/5648 II.
17 Central bank council minutes, 31 Mar. and 4-5 April, 1950, DBHA, B330/25/1.
18 Wilhelm Vocke to all Bank deutscher Länder departments, 2 Aug. 1948, DBHA, B330/3356.
scenes. The monetary authority was helped in this respect by Volkmar Muthesius, whose publication *Die Zeitschrift für das gesamte Kreditwesen* the central bank helped finance.20 An established journalist, Muthesius used his network of contacts to organise a number of confidential meetings with leading newspapers on behalf of the central bank.21 These meetings took place in Frankfurt, Munich, Hamburg and Stuttgart. In the Frankfurt meeting, which a Bank deutscher Länder official also attended, the need for central banking independence was stressed to the general agreement of the journalists present; this need for independence was grounded in light of Germany’s history of inflations.22 It was agreed that the central bank’s cause be supported by the newspapers in question. Muthesius also organised a number of pro-central banking independence articles to be published in newspapers around Germany.

The Bank deutscher Länder also took to the public sphere directly. Vocke was cautious, however. He timed his interventions at moments when he felt there was little choice but to act.23 ‘[L]et me state a fact’, Vocke said before an audience of bankers on 12 May 1950. ‘An independent central bank, one free from politics, is the best guarantee of the currency, especially here in Germany, where the currency stands or falls with the central bank and its management … The time when you have to destroy the independence of the central bank is when you wish, as Hitler did, to start an inflation. No sensible person wants to do that now’.24 Other central bank speeches in support of independence followed.

The emergence of the Korean War and West Germany’s first balance of payments crisis in late 1950 heightened the public debate. But the dispute itself came to a sudden halt with the surprise Allied decision in March 1951 to return monetary sovereignty back to the German state. It was expected that the German state come up with legislation quickly to allow this to happen. But there was still no consensus concerning the Bundesbank Law. As such, a temporary piece of legislation, the Transition Law, was passed in mid-1951. The Transition Law removed the Allied veto and the Bank deutscher Länder remained effectively independent from German control.

**The fight for central banking independence, 1956-7**

The Bank deutscher Länder began to enjoy an increased public profile as time went on. The central bank gradually shed its image in the West German media as a product of Allied occupation law. Instead, it began to be seen as a German institution. In part, this was due to the fact that it now operated under West German law. However, the legitimacy of the monetary authority’s structure and institutions was also buoyed in light of strong economic growth and the deutschmark’s ascension to one of the most trusted currencies on the continent.

Overall Frankfurt enjoyed good relations with Bonn during the period 1952 to mid-1955. This was not to last, however. Inflationary forces began to assert themselves and the central bank felt compelled to increase the interest rate on several occasions to ward off the threat. This earned the anger of the chancellor. In an unprecedented speech in May 1956, Adenauer launched a public attack on the central bank’s independence. ‘The central bank council, gentlemen, is completely sovereign from the federal

24 Wilhelm Vocke, ‘Sound money for savers’ speech, 12 May 1950, Deutsche Bundesbank Pressearchiv [DBPA], no. 1242, pp. 5-6.
government. It is of course accountable to itself, but here we have an institution that is responsible to no one, not even parliament, not even a government’. The discount rate hike, Adenauer famously said, was like a ‘guillotine’ falling down on the West German people.\(^{25}\)

It was one of Adenauer’s few political mistakes. Public opinion had shifted markedly towards the central bank: the Bank deutscher Länder had the strong support of the mainstream press. News articles and commentary pieces flowed in support of the monetary authority’s policy.\(^{26}\) Der Spiegel depicted Vocke on the front page with the title ‘chancellor of the deutschmark’.\(^{27}\) The central bank’s triumph emerged at the expense of the chancellor’s standing. Adenauer damaged the solidarity of his cabinet just a year before the next election. Vocke, too, emerged from the ‘guillotine’ affair stronger and more confident. Speaking before an audience in Hamburg, Vocke discussed the indispensability of central banking independence for the economy’s health:

[T]he remembrance of the experiences which the German nation has passed through in the currency field has been terrible and is still alive in our memories. If it is desired to produce a new bank law, then such a law must have only one aim, viz. the preservation of what we have achieved in the currency field, the reinforcement and maintenance of confidence in the currency and of confidence in the central bank.\(^{28}\)

Shortly after the affair, Vocke was interviewed by the tabloid newspaper Bild Zeitung, another indication of his popularity, and a collection of Vocke’s speeches was released in the months following the clash with Adenauer by a publishing house linked to Muthesius.\(^{29}\)

The chancellor backed down; but he continued his efforts to limit the monetary authority’s independence behind the scenes. Adenauer was now an isolated figure, however. Key figures in his government, such as Erhard, as well as the media, were against the idea of a government veto on central banking policy. A compromise was reached. The Bundesbank Law was eventually passed in July 1957. The legislation stated that the central bank was independent of government instruction, but that it was to support the general economic policy of the government. Bonn increased its influence via a different route, too: the government could now appoint the central bank’s directorate. Nevertheless, a sizeable degree of independence remained.

**Conclusion**

The Bank deutscher Länder, ‘a child of the occupation’, helped to defend its independence vis-à-vis Bonn by means of a press policy that aimed to win the support of the West German people. Historical narratives of Germany’s two inflations played a crucial role in this endeavour. And they did so despite the mixed record of inter-war central banking independence. Today historians and journalists often remark on the German aversion to inflation, an attitude frequently attributed to the so-called ‘national trauma’ of the Weimar hyperinflation.\(^{30}\) The lessons of the hyperinflation, too, were

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\(^{29}\) ‘Er hält die Mark an der Kette’, Bild Zeitung, 4 Jun. 1956; Vocke (1956).

often used to justify the Bundesbank’s independence. This paper has demonstrated that there was no West German consensus for central banking independence in the early post-war years, however. By contrast, it was the subject of public debate. Historical narratives of 1922-3 and the second inflation entered the public discussion primarily due to a clash of interests between Frankfurt and Bonn. These narratives remained thereafter because an increasingly powerful institution, the Bundesbank, had a strong interest in propounding them. The memory of the hyperinflation has survived so well in Germany in part because it proved to be a useful one. This paper, then, provides a clue as to why the Weimar inflation is remembered to this day in Germany, while other ‘traumas’ of Weimar, such as mass unemployment, are largely forgotten.

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