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Gold rush
The political economy of gold standard adoption in the Kingdom of Yugoslavia

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Abstract:

This paper provides a political economy perspective on gold standard adoption in the Kingdom of Yugoslavia which joined the monetary system in midst of the Great Depression in June 1931. The analysis proceeds in three stages. First, the high relative costs faced by a peripheral country like Yugoslavia for maintaining a gold standard, stemming from a fluctuating balance-of-payments and lacking institutional structures, are analysed. Against this background, the economic and political reasons why policy elites nevertheless endeavoured to adopt the gold standard are examined by looking at debates in Yugoslavia's central bank, correspondence between governmental institutions and various economic newspapers. Subsequently, the paper analyses how the convictions of policy-makers were formed by looking at pressures exerted by foreign lenders such as the Bank for International Settlements and the state of economic knowledge in the country, as well as the ideological and cultural convictions of policy-makers. The third part analyses interest group pressures in bringing about the the gold standard, revealing that Serbian economic elites played a crucial role for its adoption while policy makers from Croatian regions, as well as lower layers of the Yugoslavian society opposed the monetary system and the deflationary policies it required.

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1 Introduction

The gold exchange standard has been viewed as a major contributing factor to the spread of the Great Depression because it required contractionary monetary policy to retain gold and foreign exchange reserves. From this perspective, the decision of governments across Europe to implement and maintain this monetary system in the interwar period has often been presented as primarily "ideological" and hardly rationalisable in hindsight. For example, in his seminal work *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*, Eichengreen presents a "belief, based more on assumption than analysis", as an important reason why major European powers restored the gold standard after the Genoa Conference of 1922.[1] However, a growing number of contributions argues that the decision to maintain a gold standard is explainable through individual economic benefits such as price stability or cheaper foreign borrowing instead of ideological commitments. For example, Bordo and Rockoff identify improved conditions for foreign borrowing as a primary rationale for gold standard adoption.[2] However, by strongly focusing on the importance of individual economic factors, analyses do not sufficiently capture the importance of political and cultural rationales for gold standard adoption which were often crucial motivations for policy-makers. Furthermore, analyses often omit the distributional effects of the gold standard and how different societal layers viewed and influenced its implementation. Even studies which prove more complete in the respects above, such as Straumann's analysis of gold standard adoption in peripheral European countries, do not focus on the scarcely studied gold standard adoption on the South-Eastern European periphery.[3]

Building on the shortcomings of previous literature, this paper provides an example for a more complete political economy perspective on gold standard adoption, taking the peripheral Kingdom of Yugoslavia as a subject of analysis which existed under different forms of government between 1918 and 1941.[4] Yugoslavia's adoption of the gold standard on 28th June 1931 formed the end of a decade-long struggle of authorities in the Kingdom of Serbia, and later the Kingdom of Yugoslavia, to join the world's prevalent monetary system by stabilising the Serbian, and later Yugoslavian, dinar at a fixed value compared to gold. The Kingdom of Serbia had already pegged the dinar to the French franc in 1873 and started following the rules of the Latin Monetary Union

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1 B. Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939* (Oxford, 1996), p. 100.

2 M.D. Bordo and H. Rockoff. 'The Gold Standard as a Good Housekeeping Seal of Approval', *The Journal of Economic History* 56/2 (1996), pp. 389-428.

3 T. Straumann, *Fixed Ideas of Money: Small States and Exchange Rate Regimes in Twentieth-century Europe* (Cambridge, 2010).

4 The name of the Kingdom changed with its regimes. While it was established as the *Kingdom of Serbs, Croats and Slovenes* in 1918, the name was changed to *Kingdom of Yugoslavia* by King Alexander in 1929 which is also the name it had in the year of gold standard adoption 1931.

to coin the dinar in 1878 without being able to join the treaty.[5] An attempt to move from bimetallism to a gold standard in 1878 was unsuccessful because the convertibility of gold had to be suspended due to gold shortages. After the First World War, the dinar was maintained as the official currency of the new Kingdom of Yugoslavia, and the country's authorities, many of whom had served in the Kingdom of Serbia, attempted to stabilise the dinar soon after the country's formation in 1918. Already in 1920, an official cover ratio was introduced which meant that the amount of bank notes was not to surpass the triple value of the central bank's gold and foreign exchange reserves.[6] Capital controls required exporters to deposit one-third of their export earnings at the National Bank of the Kingdom of Yugoslavia (NBKY). This created foreign exchange reserves worth 216 million dinars in 1925 and allowed for stabilising the value of 100 dinars at 9.12 Swiss francs through foreign currency market operations.[7]

However, government authorities aimed to go further and legally stabilise the dinar, i.e. introduce the gold standard, which required extensive foreign borrowing for the acquisition of reserves and for settling a loan the government had at the NBKY. Hence, an international loan was taken up on 8th May 1931 from a French banking consortium. It amounted to 1.025 billion French francs in gold at a 7% interest rate and had a 40-year repayment period. After several statutory changes in the NBKY, the value of one dinar was fixed at 26.5 milligrams of pure gold on 11th May 1931. Furthermore, a legal cover ratio, i.e. the amount of gold and foreign currency compared to all money in circulation, was set to 35%.[8] However, the gold standard could only be sustained for 101 days after 28th June 1931. The fall of the Kreditanstalt in May 1931, the Hoover Moratorium which cancelled German reparation payments in July 1931, and the British departure from the gold standard in September 1931, led to uncertainties in the Yugoslavian economy. As deposits fled from commercial banks and gold and foreign exchange reserves plummeted in the NBKY, capital controls were reintroduced on 7th October 1931 and the gold standard was effectively abandoned. Two further international loans for the purposes of foreign exchange acquisition taken up from the Bank for u International Settlements (BIS) in Basel and the Banque de France in July and October 1931 respectively, could not prevent this outcome. The "rush" to adopt the gold standard and the persistence to maintain it appear as curious policy decisions against the background of the Great Depression and give rise to the impression that it was indeed a policy-decision fuelled by belief rather than sound economic judgement, just as Eichengreen recognised it for major European economies.

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[5] J. Lampe and M. Jackson, *Balkan Economic History, 1550-1950: From Imperial Borderlands to Developing Nations* (Bloomington, 1982), p 205.

[6] D. Gnjatovic, 'The Experience of Exchange Rate Regimes in Southeastern Europe in a Historical and Comparative Perspective', *Second Conference of South-Eastern European Monetary History Network Working Papers* (2007), p. 332.

[7] *Ibid.*, p. 307.

[8] *Ibid.*, p. 336.

To evaluate the motivations of policy-makers, I conducted a thorough analysis of the political economy of gold standard adoption in the Kingdom of Yugoslavia and analysed a variety of sources, such as governmental documents, correspondence between the Finance Ministry of Yugoslavia and the NBKY, minutes of meetings at the NBKY in 1930 and 1931, correspondence between the NBKY and the Bank of England, the Banque de France and the BIS, as well as articles published in economic and public newspapers. I consulted these sources in the Archive of the National Bank of Serbia, the Archives of Yugoslavia, the Serbian National Library in Belgrade, and the BIS Archive in Basel. Official documents and correspondence allow for understanding the views of policy elites, and how these were formed. Articles written in three prominent conservative economic newspapers *Bankarstvo, Privredni Pregled* and *Narodno Blagostanje,* often reflected their views as well because numerous policy-makers contributed to them. Furthermore, elaborations by prominent economists like Slavko Sećerov or Dr. Velimir Bajkić, the latter of whom participated at the Paris Peace Conference in 1919 and edited his own newspapers *Narodno Blagostanje*, allow for interpreting the state of economic knowledge in Yugoslavia.[9] Popular newspapers such as *Vreme* and *Politika*, as well as letters written to government authorities and pamphlets, help to understand the views of different societal layers on the gold standard. It should be noted that newspapers were also partially influenced by governmental institutions and should therefore be evaluated with caution. For instance, *Vreme* received direct advances from the NBKY as I argue in section 6.

My analysis led me to two conclusions. First, analysing rationales by policy elites for justifying gold standard adoption, and how their policy decision was framed, reveals that it can only be explained through an interplay of economic, political, and cultural influences, as well as interest group pressures, rather than by ungrounded beliefs in the viability of this monetary system, or any other monocausal influence. Second, identifying that the policies which gold standard implementation required affected agricultural workers negatively and were disapproved of in Croatian regions makes the Yugoslavian gold standard a mirror of and contributing factor to the larger political struggles between classes and regions which were characteristic for interwar Yugoslavia.

Section 2 maps out the gold standard in theory, while section 3 provides an overview of the literature on economic and political rationales of gold standard adoption. Section 4 proceeds with the difficulties Yugoslavian authorities faced in adopting the gold standard, both in terms of the costs for maintaining the cover ratio, as well as for required institutional innovations. Against the background of these difficulties, section 5 asks which of the rationales identified in section 3 were used by Yugoslavian policy elites to justify their decision (section 5.1), inferring that a pronounced desire for foreign borrowing and capital inflows was the main economic rationale.

[9] M. Obradović and I. Poljak, 'The Man with five Lives', *Monopolist* (2015).

Section 5.2 then explains how their decision was framed by pressures exerted by foreign lenders (section 5.2.1), and the present economic knowledge (section 5.2.2). Section 6 focuses on political rationales for gold standard adoption. It reviews claims by policy-makers calling for gold standard adoption to signal Yugoslavia's prestige and join the international community and explains them by referring to an internationalist political ideology present among Yugoslavian policy elites, as well as a longstanding wish for cultural integration with "the West". Section 7 then moves from the views of the elites depicted in previous sections to another political economy perspective, namely the views and influences of different interest groups across societal layers and regions on gold standard implementation. This shows that predominantly Serbian economic elites favoured the adoption of the gold standard and influenced policy-making in the NBKY in favour of it while agricultural workers and Croatian policy-makers were resisting the deflationary policies it necessitated. Section 8 summarises the findings and provides an outlook.

2 Perspectives on the Gold Standard

The currency regime which forms the centre of this analysis is the gold standard, an exchange rate regime in which the values of multiple currencies were fixed at a certain weight of gold which stabilised the exchange rates between nations partaking in the system.[10] According to Eichengreen, the gold standard was characterised by three features:

(i) the convertibility between money and gold at a fixed official price,
(ii) the freedom of private market agents to import or export gold,
(iii) the institutionalisation of a set of rules relating the quantity of money in circulation to the gold stock.[11]

An important qualification of (i) is that different systems of the gold standard are distinguished according to whether money was only convertible into gold, or foreign exchange as well. This is the distinction between the "classical gold standard" on the one hand, and the "gold exchange standard" on the other hand. Under the gold exchange standard, whose adoption in the Kingdom of Yugoslavia is the central concern of this paper, currency was convertible into gold or foreign exchange.[12]

From a theoretical perspective, if not necessarily in practice, the gold standard was characterised by a specific mechanism for restoring the international balance-of-payments through international gold and capital flows and internal price changes. According to Hume's *price-specie-flow* mechanism, a country experiencing gold outflows due to a negative balance-of-payments also experienced a reduction in the money supply. This in turn put downward pressure on the domestic price level and increased foreign demand for domestic goods, which then led to gold inflows. The reverse process held for countries running balance-of-payments surpluses.[13] In essence, Hume applies the quantity theory of money and the law of one price to explain how the system equilibrates itself, assuming that an increased money supply causes inflation and that arbitrage will lead to price equalisation.[14] However, Hume's analysis has since been modified and it was recognised that the system was not necessarily self-equilibrating. Whale for example argued in 1937 that increases in

[10] P. Clavin, *The Great Depression in Europe, 1929-1939* (New York, 2000), p. 40.
[11] B. Eichengreen, *The Gold Standard in Theory and History* (London, 1985), pp. 3-4.
[12] R. Mundell, 'The Global Adjustment System', in Baldassarri, M./McCallum, J./Mundell, R. (eds.), *Global Disequilibrium in the World Economy* (Basingstoke, 1992), p. 411.
[13] D. Hume, 'Of the Balance of Trade'; in: Hume, D., *Essays and Treatises on Several Subjects. Vol. IV* (London, 1754)., pp. 69-88.
[14] Mundell, 'The Global Adjustment System', p. 411.

money demand played a crucial role in the gold standard system as they raised interest rates and thus directed gold flows.[15]

To explain how the gold standard worked in practice, Kindleberger famously argued that the classical gold standard was maintained by the Bank of England which acted as a lender of last resort for countries running balance-of-payments deficits against its own economic interest.[16] Eichengreen disagrees with this contention by presenting historical evidence suggesting that British capital markets did not increase foreign lending when economic activity decreased, and that the Bank of England did not usually forgo its own profits in order to act as a lender of last resort.[17] Instead, it was the system's credibility and cooperation between central banks that made the gold standard work smoothly before the First World War. Market participants believed that central banks would do anything necessary to maintain the system. If a currency threatened to weaken due to gold outflows, market participants anticipated that the central bank would increase discount rates in order to attract gold inflows. This anticipation of capital gains led investors to direct their funds from abroad to this country, thereby offsetting the gold losses. Hence, the psychology of market participants worked to equilibrate the system.[18]

From a policy-perspective, adopting a gold standard implied giving up an independent monetary policy. According to the "impossible trinity" of monetary policy, a country can only choose two options between international capital mobility, fixed exchange rates and an independent monetary policy. The gold standard required international capital mobility as international gold flows were needed to equilibrate international balances-of-payment. Furthermore, exchange rates were fixed between countries under the gold standard. This implied the necessity to forgo an independent monetary policy and central banks had to work on preserving the cover ratio by setting discount rates appropriately.[19] J.M. Keynes called the subordination of monetary policy adherence to the "rules of the gold standard game".[20] Hallwood and MacDonald argue that the pressure to adhere to the "rules of the game" was especially strong for peripheral economies as only core countries could afford to violate them and maintain an independent monetary policy because their currency pegs would nevertheless be perceived as credible.[21]

Viewed from a historical perspective, the gold standard was certainly the most wide-spread monetary regime among major economies in the 19th century. In the second half of the century,

15 P. Whale. 'Working of the Pre-War Gold Standard', *Economica*, 18 (1937), p. 36.
16 C. Kindleberger, *The World in Depression, 1929-1939* (Harmondsworth, 1987), pp. 27-28.
17 Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*, p. 30.
18 *Ibid.*, p. 5.
19 R. Mundell, 'Capital Mobility and Stabilization Policy under Fixed and Flexible Exchange Rates', *Canadian Journal of Economics and Political Science*, 29 (1963), p. 475.
20 J. Keynes, *The Economic Consequences of Mr. Churchill* (London, 1925), p. 220.
21 C. Hallwood et al., 'Credibility and fundamentals: Were the Classical and Interwar Gold Standards Well-Behaved Target Zones?', in T. Bayoumi et al. (eds.), *Modern Perspectives on the Gold Standard* (Cambridge, 1996).

most countries adopted a gold bullion standard. Britain was the only country to already adopt it in 1821, while it was Germany in 1871 which initiated a row of gold standard adoptions leading to the "high summer of the international gold standard" between 1870 and 1914.[22] After its victory in the Franco-Prussian War, the country had accumulated gold reserves which allowed for fixing the value of one German mark at 0.3982 ounces of gold.[23] The governments of Holland, Denmark, Norway and Sweden reacted to German gold purchases which initiated a fall in silver prices by suspending silver convertibility and adopting the gold standard.[24] Mundell argues that this was the case because the decrease in silver prices made silver-backed currencies inflationary.[25] While virtually all major economies soon adopted the gold standard, smaller economies on the South-Eastern European periphery were mostly left out of the system. Yugoslavia, Bulgaria and Romania endeavoured to move from a bimetallic- to a gold-standard because many Balkan state budgets were mortgaged to the repayment of loans which were repayable in gold denominations. However, these states struggled with accumulating sufficient gold reserves. Only Romania succeeded in doing so thanks to the country's long-standing access to European capital markets.[26] The classical gold standard unravelled at the onset of the First World War as European governments suspended the convertibility of money into gold in order to prevent gold outflows. Russia and Germany suspended specie payments immediately after the war erupted.[27] Britain prohibited the export of gold coin and bullion later, namely in 1920, thereby making its currency inconvertible.[28] However, already during the war, the re-establishment of the gold standard was planned. The British Treasury and the Ministry of Reconstruction appointed a committee on currency and foreign exchange under the chairmanship of Lord Cunliffe.[29] The committee reported already in 1918 that the restoration of the gold standard was imperative for the postwar period, even though Britain had lost its pivotal role in the gold standard system as gold reserves had accumulated in the US during the First World War.[30] This opinion was echoed internationally as governments gathered at the Genoa Conference of 1922 in the absence of the United States to establish guidelines for a successful post-war economy. The gold exchange standard was established by allowing central banks to maintain convertibility both with gold and foreign exchange.[31] The interwar gold standard would work less successfully than its prewar predecessor. In the heated political climate of the

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[22] W. Scammell, 'The Working of the Gold Standard', *Yorkshire Bulletin of Economic and Social Research* 17/1 (1965), p. 32.
[23] Mundell, 'The Global Adjustment System', p. 360.
[24] B. J. Eichengreen, *Hegemonic Stability Theories of the International Monetary System* (London, 1987), p. 16.
[25] Mundell, 'The Global Adjustment System', p. 365.
[26] Lampe and Jackson, *Balkan Economic History, 1550-1950: From Imperial Borderlands to Developing Nations*, pp. 212-213.
[27] Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression*, pp. 67-70.
[28] *Ibid.*
[29] D. Moggridge, *The Return to Gold 1925: The Formulation of Economic Policy and Its Critics* (Cambridge, 1969), p. 12.
[30] P. Temin, *Lessons from the Great Depression* (London: 1989), p. 13.
[31] Clavin, *The Great Depression in Europe, 1929-1939*, p. 48.

interwar period, the credibility on markets which equilibrated international gold flows was upset because market participants did not assume that central banks would adhere to the "rules of the game" and adjust discount rates to equilibrate international gold flows, but rather serve national interests.[32] Nevertheless, the gold standard once again developed into the world's prevalent monetary system. Britain adopted the gold standard in 1925 at its prewar parity of 1 pound equalling 4.86 US dollars after a protracted debate between the Treasury and the Cunliffe Committee about when to take the politically difficult, deflationary measures for introducing it. Australia, New Zealand, Hungary and South Africa followed in the same year. France went on gold in 1928 at a strongly devalued rate (14.5% of its prewar parity) which led to a balance-of-payments surplus and substantial accumulations of gold reserves.[33] Together with the so-called "gold-bloc" nations Belgium, Holland, Switzerland, Italy and Poland, France also remained on the gold standard until 1936, unlike most other European countries which left it amid the Great Depression in 1931.[34] Countries on the South-Eastern European periphery generally adopted the gold standard later, such as Bulgaria in 1927, Greece in 1928, or Yugoslavia in 1931, and were amongst the first to abandon it during the Great Depression.

The main question this paper asks is why governments, and the Yugoslavian government in particular, endeavoured to adopt the gold standard. While idiosyncrasies were involved in the gold standard adoption of every European country, economic historians have identified common economic and political rationales. These are reviewed in the following section. The applicability of these rationales and difficulties of gold standard adoption will then be assessed at the example of Yugoslavia in subsequent sections.

[32] Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*, p. 10.
[33] W. Garside, *Capitalism in crisis: International responses to the Great Depression* (London, 1993), p. 11.
[34] Clavin, *The Great Depression in Europe, 1929-1939*, pp. 135-136.

3 Comparative Political Economy of Gold Standard Adoption

Since understanding the process of gold standard adoption involves both elements from economics and political history, a political economy analysis suggests itself as the appropriate method of analysis of this monetary system. Thereby, problems of economic relations are evaluated considering the full policy-making perspective, incorporating economic and political considerations, and interest group pressures.[35] Furthermore, it proves useful to review the analyses of different countries in order to identify similarities in rationales for adoption and place the case of Yugoslavia within a broader international context.

3.1 Economic Rationales for Gold Standard Adoption

In this sub-section, I review three economic benefits for gold standard adoption which were recognised as essential by economic historians before evaluating their viability in peripheral countries by referring to empirical studies. I also review how each of these rationales was employed by governments and interest groups to justify gold standard adoption in the two gold standard periods which provides a useful starting point for analysing the Yugoslavian which is analysed subsequently.

(i) Price stability,
(ii) International borrowing and capital inflows,
(iii) International trade.

Price stability

A gold standard ensures price stability because it constrains a country's monetary policy independence. If a central bank adhered to the "rules of the game", it could not arbitrarily increase the monetary base and thereby raise the inflation rate. Already in the 19th century, proponents of the so-called "Currency-School", including Samuel Jones-Loyd, Robert Torrens and George Norman, argued that price stability was guaranteed by the institutionalisation of gold convertibility as it constrained central bank activity and reduced it to one rule.[36] The view persisted in some form until today as rules for monetary policy are viewed as an effective means for influencing market expectations and controlling price levels.[37]

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[35] B. Cohen, *Organizing the World's Money: The Political Economy of International Monetary Relations* (New York, 1977), pp. 7-8.
[36] A. Arnon, *Monetary Theory and Policy from Hume and Smith to Wicksell: Money, Credit, and the Economy* (Cambridge, 2011), pp. 187-188.
[37] F. Kydland and E. Prescott, 'Rules rather than discretion: The inconsistency of optimal plans', *Journal of Political Economy*, 85 (1977), pp. 473-490.

Estimates of the price stability for the gold standard eras yield differing results. Mundell argues that under the classical gold standard, the price level depended on the price of gold which was stable over time. According to the Kondratieff index, the gold price was the same in 1815 as it was in 1857, which stabilised the price level over long time horizons.[38] However, this did not imply the absence of inflationary or deflationary trends. Inflation would occur steadily if gold production exceeded demand which was equal to a growth in the money supply. For example, gold discoveries in California between 1847 and 1851 made world gold production rise from 1.76 million ounces in 1841-50 to 6.45 million ounces in 1851-60. The price index rose from 101 in 1849 to 143 in 1857 in the UK.[39] Between 1873 and 1896, gold production stabilised, but as the population and income continued to grow (i.e. the demand for golf-backed money remained high), deflation ensued between 1873 and 1896.[40] Given that the gold standard led to inflationary and deflationary swings, Bordo et al. estimate that a policy of inflation targeting by setting a broad price index would have led to higher price level stability during the classical gold standard.[41]

However, in the early interwar period the gold standard was a central factor in restoring price stability throughout Europe. According to Sargent, the unravelling of the gold standard in the First World War allowed for inflationary debt monetisation which led to hyperinflation in various European countries.[42] The polar example for this practice was Germany where debt monetisation conducted for paying war reparations made money in circulation double from 1921 to 1922.[43] The price level increased to a degree that on 29th October 1923, an one-kilogram-loaf of bread cost 5.5 billion marks.[44] Many other countries were experiencing extreme levels of inflation due to debt monetisation, among them Austria, Hungary, Poland and Czechoslovakia. While the reasons for debt monetisation differed between them, the measures for stabilising the price level were similar. In essence, they comprised tax reforms, central bank independence from governmental interference and currency pegs. The latter two measures were integral parts of the "rules of the gold stanadard game" which leads back to Sargent's observation that the absence of the gold standard enabled economically detrimental inflation in the first place. However, later in the interwar period, the gold standard became associated with price instability and heavy deflation. During the First World War, the US had turned into a net creditor to Europe and US gold reserves had risen, while gold scarcity ensued in Europe. This was the main reason for the recommendation

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[38] Mundell, 'The Global Adjustment System', p. 354.
[39] *Ibid.*, p. 354.
[40] *Ibid.*, pp. 360-361.
[41] M.D. Bordo et al., *Gold, Fiat Money, and Price Stability* (Cambridge, 2003), p. 26.
[42] T. Sargent, *The Ends of Four Big Inflations*, in R.E. Hall (ed.), Inflation: Causes and Effects (Chicago, 1983), p. 50.
[43] C. Bresciani-Turroni, *The Economics of Inflation: A Study of Currency Depreciation in Post-war Germany* (London, 1937), p. 33.
[44] S.B. Webb, S.B, *Hyperinflation and Stabilization in Weimar Germany* (Oxford, 1989), p. 3.

to hold foreign exchange in addition to gold as reserves during the Genoa Conference of 1922.[45] During the Great Depression, central banks saw their scarce gold and foreign exchange reserves decrease due to market uncertainties which required discount rate increases. According to Eichengreen, this is how the gold standard caused deflation and made the effects of the Great Depression spread globally as real economic activity was stifled through higher discount rates which made borrowing expensive.[46] Bernanke and James estimate that deflation in gold standard countries amounted to 13% per year on average in 1930 and 1931, and while most countries going off gold in 1931 had stable price levels by 1933, deflation continued in gold standard countries until 1936 when the gold exchange standard unravelled.[47]

Altogether, there is no clear conclusion on the potential of the gold standard to secure price stability for either of the gold standard periods. Importantly, however, many governments and commercial interest groups believed in this potential. Mundell argues that in the classical gold standard period, the movement to gold in many countries was induced by the fear of creditor classes of inflation.[48] In the interwar period, the dangers of inflation and the potential of currency pegs to restore stability were made obvious by the mid-1920s. Using a sample of 24 countries, Wandschneider argues that the experience of hyperinflation is significantly correlated with a longer maintenance of the gold standard in the interwar period, which indicates that governments believed in the ability of the gold standard to prevent hyperinflation.[49] An instance for this is the French government under Poincaré which favoured a gold standard mainly in order to avoid inflation.[50] On the European periphery, there additional inflationary pressures arose from the establishment of new currencies. For example, Bulgaria's price level in 1923 was 30 times the prewar level.[51] Feinstein et al. argue that the main reason why Bulgaria, Poland, Romania and Yugoslavia maintained the gold standard was that there was a deep prevailing fear of inflation in the minds of politicians and the public. They quote the Polish economist Lipinski who called the preservation of the currency value a sacrosanct principle of popular belief.[52] While a concern for price stability was not the primary factor for Yugoslavian gold standard adoption as I argue in section 5, these examples illustrate how widespread the belief in this economic benefit was throughout Europe.

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[45] Mundell, 'The Global Adjustment System', p. 369.
[46] Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*, p. 262.
[47] B. Bernanke and H. James (1990). *The Gold Standard, Deflation, and Financial Crisis in the Great Depression: An International Comparison* (Cambridge, 1990), p. 15.
[48] Mundell, 'The Global Adjustment System', p. 365.
[49] K. Wandschneider, 'The stability of the interwar gold standard: Did politics matter?', *Journal of Economic History*, 68/1 (2008), pp. 152.
[50] K. Mouré, *The Gold Standard Illusion: France, the Bank of France and the International Gold Standard, 1914-1939* (Oxford, 2002), p. 189.
[51] L. Berov, 'Budgetary Policy, Money Supply and Banking in Bulgaria between the Wars', in C. Feinstein et al., *Banking, Currency, and Finance in Europe Between the Wars* (Oxford, 1995), pp. 374-375.
[52] C. Feinstein et al., *Banking, Currency, and Finance in Europe Between the Wars* (Oxford, 1995), p. 23.

International borrowing and capital inflows

A major economic benefit stemming from adopting a fixed exchange-rate system like the gold standard is the increase in capital flows between countries partaking in the system. Bordo and Rockoff argue that this was the case because the gold standard was perceived as a "good housekeeping seal of approval" by international lenders. It created a commitment device for monetary and fiscal policies and decreased the incentive to deviate from announced inflation targets with discretionary monetary policy, or to default on public debt.[53] Next to increasing policy commitments, the gold standard led to institutional reforms conducive to policy credibility such as central bank independence which provided an additional assurance to lenders that central banks would refrain from debt monetisation.[54]

Using data on interest rates in a sample of nine countries from 1870 to 1914, Bordo and Rockoff find that countries with a strong commitment to the gold standard benefited from lower interest rates on international markets. For example, Australia was able to borrow at only 1% above the risk-free rate on the London market. However, already a de facto commitment to stable exchange rates without legal convertibility was enough to lower borrowing costs. Italy, despite its inconsistency in maintaining the classical gold standard, paid only marginally higher interests rates.[55] In terms of capital flows, there is agreement in the literature that they increased substantially in the second half of the 19th century.[56] Bordo and Meissner find that these capital inflows enabled substantially higher national incomes during the classical gold standard era.[57] For the interwar period, Feinstein et al. argue that capital flowed to European borrowers on a massive scale if countries stabilised their currencies. Gross inward flows between the 17 principal European borrowing countries amounted to approximately 10 billion USD between 1924 and 1930. Most of these funds flowed to Germany (7 billion USD) which borrowed to service reparation payments while other notable borrowers included Austria, Italy, Romania, Poland, Greece and Hungary.[58]

However, some have questioned the claim that borrowing costs were lowered through the gold standard. Obstfeld and Taylor argue that during the classical gold standard, borrowing costs were on average 30 basis points lower for countries on the gold standard, but that there was no such effect in the interwar period.[59] Alquist and Chabot deny even that, finding that borrowing costs in the 19th century were not substantially lower in gold standard countries after controlling

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53 Bordo and Rockoff. 'The Gold Standard as a Good Housekeeping Seal of Approval', pp. 391-392.
54 J. Kirshner, *Monetary Orders: Ambiguous Economics, Ubiquitous Politics* (Ithaca, 2003), p. 25.
55 Bordo and Rockoff, 'The Gold Standard as a Good Housekeeping Seal of Approval', p. 414.
56 C. Meissner, 'Capital Flows, Credit Booms, and Financial Crises in the Classical Gold Standard Era', *NBER Working Paper Series* (2013), p. 3.
57 M.D. Bordo and C.M. Meissner, 'Foreign Capital, Financial Crises and Incomes in the First Era of Globalization', *European Review of Economic History* 15/1 (2011), pp. 61-63.
58 Feinstein et al., *Banking, Currency, and Finance in Europe Between the Wars*, pp. 31-32.
59 M. Obstfeld and A. Taylor, 'Sovereign Risk, Credibility and the Gold Standard: 1870–1913 versus 1925–31*', *Economic Journal* 113.487 (2003), pp. 241-275.

for US risk factors.[60] In terms of the South-Eastern European periphery, Lampe and Jackson argue that countries on (bi-)metallic standards in the region did not experience lower borrowing costs. Serbia and Bulgaria were able to place government bonds at similar rates as Romania which was on the gold standard, namely at around 5.5%.[61] Stiglitz even argues that capital inflows into peripheral economies led to financial instabilities.[62] Feinstein et al. see this view confirmed for the interwar period when an end of the foreign borrowing boom was a significant factor for initiating the Great Depression in Hungary and Poland.[63]

However, there is little doubt that many governments and interest groups firmly believed in the ability of the gold standard to ease access to cheap loans and ensure capital inflows. Mitchener et al. provide the example of Japan which joined the gold standard in 1897 with the desire to borrow on international markets.[64] Peripheral countries especially hoped to foster economic stability and development in this way. For instance, despite the view that capital inflows can generate instability, Austro-Hungarian gold standard supporters in the government argued in 1887 that having to rely solely on internal borrowing during crises created instability.[65] In the interwar period, especially South-Eastern European governments sought to adopt the gold standard to secure capital inflows, and many did so successfully. Hungary, for example secured 127 million USD of foreign investment after legal stabilisation between 1929 and 1931 while in Bulgaria the figure amounted to 27 million.[66] In Yugoslavia, a wish for foreign borrowing will be identified as the main economic rationale for joining the gold standard in section 5.

International Trade

The fixed exchange rates between gold standard countries had the potential of increasing international trade because the exchange rate risk from international purchases was removed. This stabilised the domestic currency prices of foreign goods. Furthermore, fixed exchange rates implied an elimination of the risk for competitive currency devaluation to create a competitive advantage for certain goods. This in turn simplified international trade deals and made governments refrain from the imposition of trade barriers.[67] However, the empirical evidence for the potential of the gold standard to facilitate trade is mixed. Using a gravity model of trade, Lopez-Cordova and

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[60] R. Alquist and B. Chabot, 'Did Gold-standard Adherence Reduce Sovereign Capital Costs?' *Journal of Monetary Economics* 58.3 (2011), pp. 262-272.
[61] Lampe and Jackson, *Balkan Economic History, 1550-1950: From Imperial Borderlands to Developing Nations*, p. 232.
[62] J. Stiglitz, 'Capital Market Liberalization and Exchange Rate Regimes: Risk without Reward', *Annals of the American Academy of Political and Social Science* 579 (2002), pp. 219-248.
[63] Feinstein et al., *Banking, Currency, and Finance in Europe Between the Wars*, p. 36.
[64] K.J. Mitchener, et al. 'Why Did Countries Adopt the Gold Standard? Lessons from Japan', *The Journal of Economic History* 70.1 (2010), p. 27.
[65] F. Perl., 'Zur Frage der Valutaregulirung in Oesterreich-Ungarn', *Verlagsmagazin* (Zurich, 1887), p. 64.
[66] Clavin, *The Great Depression in Europe, 1929-1939*, p. 179.
[67] *Ibid.*, p. 42.

Meissner estimate that gold standard countries traded up to 30% more with each other than with countries outside of the monetary system. Furthermore, without the classical gold standard global trade would have been lower by 20% between 1880 and 1910.[68] However, using currency premium data for 21 countries, Mitchener and Weidenmier estimate that between 1870 and 1913, joining the gold standard did not eliminate the foreign exchange risk premium in emerging markets, which is the market's anticipated excess return to holding foreign currency. Especially on the South-eastern periphery it remained constantly high, namely 384, 232 and 241 basis points for Bulgaria, Greece and Romania respectively five years after adoption, while it decreased for "core countries".[69] This indicates that the Balkan region remained risky in terms of exchange rate fluctuations even after the countries legally stabilised their currencies. This effect occurred because the currency pegs were not perceived as credible internationally, and makes it questionable whether benefits from trade could be realised.

In terms of the views of policy-makers and commercial interest groups, Frieden argues that interest groups favouring commercial integration tend to support fixed exchange systems to stabilise currency values.[70] Yeager argues that in Hungary, export and import competing interests switched in favour of the gold standard around 1880 to 1890 when it became clear that the gulden would not be pegged to the mark at an overvalued rate which had the danger of hampering exports.[71] This indicates that interest groups involved in trade had a general interest in currency stabilisation. In the interwar period, a major reason why Poland remained on the gold standard (and in the gold bloc with France until mid-1936) was that the country had a trade relationship with France.[72] South-Eastern European countries became increasingly sensitive to trade with gold bloc countries like France since the dissolution of the Austro-Hungarian empire which formed part of their reason to adopt it.[73] Hence, trade was a major positive economic externality which governments wanted to realise through gold standard adoption.

Altogether, the three economic benefits which have been identified in pertinent literature as rationales why governments chose to join the gold standard have been explained. However, the reasons for adoption were not always motivated by economic concerns. The following sub-section reviews political rationales.

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[68] J.E. Lopez-Cordova and C.M. Meissner, 'Exchange-Rate Regimes and International Trade: Evidence from the Classical Gold Standard Era', *American Economic Review* 93.1 (2003), p. 344.
[69] K.J. Mitchener and M.D. Weidenmier, 'Was the Classical Gold Standard Credible on the Periphery? Evidence from Currency Risk', *The Journal of Economic History* 75.2 (2015), p. 489.
[70] J. A. Frieden, *Currency Politics: The Political Economy of Exchange Rate Policy* (Princeton, 2018), p. 19.
[71] L.B. Yeager, 'The Image of the Gold Standard', in M.D. Bordo and A.J. Schwartz, *A Retrospective on the Classical Gold Standard, 1821-1931* (Chicago, 1984), p. 655.
[72] N. Wolf, Nikolaus, 'Scylla and Charybdis: The European Economy and Poland's Adherence to Gold, 1928-1936', *IDEAS Working Paper Series* (2007), p. 3.
[73] Clavin, *The Great Depression in Europe, 1929-1939*, p. 179.

3.2 Political Rationales for Gold Standard Adoption

In the words of Kirshner, monetary phenomena are "always and everywhere political", and the gold standard seems to be a good example for that view.[74] Schumpeter argues that noneconomic reasons were often decisive for gold standard adoption.[75] One explanation of a political motivation for gold standard adoption are considerations of *prestige*. According to Schumpeter, the gold standard symbolised honour and decency. It implied an on-a-par position with other members of the gold bloc in terms of monetary matters.[76] There are several examples for gold standard adoptions which were driven by such considerations. Yeager argues that since exchange rate fluctuations in Austria-Hungary were not extreme by present-day standards, and there was no price inflation, economic reasons were not of primary importance for gold standard adoption in 1892. Instead, considerations of prestige were clearly at play. For example, influential Austrian economist Carl Menger argued that being on gold meant being among the most advanced nations in the world.[77] Von Laue argues that in Russia, the gold standard had become a matter of respectability for the Tsarist government.[78] Discussions of the imperial free economic society in St. Petersburg between March and April 1896 show that advocacy of the gold standard was not part of conventional wisdom in Russia which is why the state had to implement it against public opinion and the press through autocratic decrees.[79] For the interwar period, Moggridge argues that Churchill's decision to legally stabilise the pound at an overvalued rate in 1925 was partially driven by a wish for restoring the British role as the world's financial centre.[80] James and O'Rourke argue that Mussolini pegged the Italian lira at an overvalued rate for nationalist reasons.[81] Kindleberger ascribes it to Mussolini's pride in the lira that he determined the currency to be overvalued by 25-30% under the gold standard.[82] According to Straumann, the precise levels at which countries went back on the gold standard mattered for prestige-related reasons in Scandinavia. For example, in Denmark and Norway which returned to the gold standard in 1927 and 1928 at prewar parity respectively, the failure to do so earlier was depicted as dishonest and a national disgrace given that their neighbour Sweden had stabilised at prewar parity already in 1925.[83]

However, while these explanations identify a prestige-driven motivation for gold standard adoption, they do not capture the underlying political motivations to employ "prestige signalling"

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[74] Kirshner, *Monetary Orders: Ambiguous Economics, Ubiquitous*, p. 3.
[75] J.A. Schumpeter, *History of Economic Analysis* (London, 1954), p. 738.
[76] *Ibid.*
[77] Yeager, 'The Image of the Gold Standard', pp. 653-657.
[78] T. v. Laue, *Sergei Witte and the Industrialization of Russia* (New York: 1963), p. 139.
[79] G. v. Schulze-Gavernitz, *Volkswirtschaftliche Studien aus Russland* (Leipzig, 1899), pp. 461-462.
[80] Moggridge, *The Return to Gold 1925: The Formulation of Economic Policy and Its Critics*, p. 66.
[81] H. James, Harold and K.H. O'Rourke, *Italy and the First Age of Globalization, 1861-1940* (Rome, 2011), p. 15.
[82] Kindleberger, *The World in Depression, 1929-1939*, p. 250.
[83] Straumann, *Fixed Ideas of Money: Small States and Exchange Rate Regimes in Twentieth-century Europe*, p. 81.

as a means for a political objective. For example, prestige signalling can be used for internal political purposes such as pleasing electorates. Noteworthy in this respect is the election of William McKinley as US president in 1896 whose main campaign promise was to suspend the convertibility of silver and introduce a gold standard in the United States.[84] Furthermore, prestige signalling can be used for external political purposes in the realm of international relations. Sharing the same monetary system as the advanced nations of the world asserted an equal footing in terms of financial affairs. Especially newly founded countries could use this assertion of an equal footing for the purposes of nation building. The example of Japan's Meiji government is striking in this respect. Between 1868 and 1912, the Meiji government worked tirelessly on acquiring all ingredients of a modern state.[85] According to Michener et al., part of the reason Japanese Finance Minister Matsukata was favouring the adoption of the gold standard in the late 19th century was that it would increase the standing of Japan internationally, and that it would be consistent with the national goals of modernising Japan's economy and military.[86] Apart from putting countries on the same footing economically, adherence to the gold standard could also signal a cultural attachment to other countries in the monetary system. According to Gnjatovic, this motivation for gold standard adoption proved especially important on the Balkans in the interwar period, a region which had only recently been liberated from Turkish occupation and strove for economic proximity to Western European countries in the interest of strengthening its cultural ties with them. As I argue in section 6, both the internal and the external "prestige signalling", will play crucial roles in the adoption of the Yugoslavian gold standard.

The rest of the paper explores the case of the 1931 gold standard adoption in Yugoslavia. The purpose of section 4 is to illustrate the hardships policy-makers faced in adopting the gold standard. Sections 5 to 7 then analyse how policy elites and commercial interest groups justified the decision against this background, searching for parallels with rationales of governments mentioned in this section.

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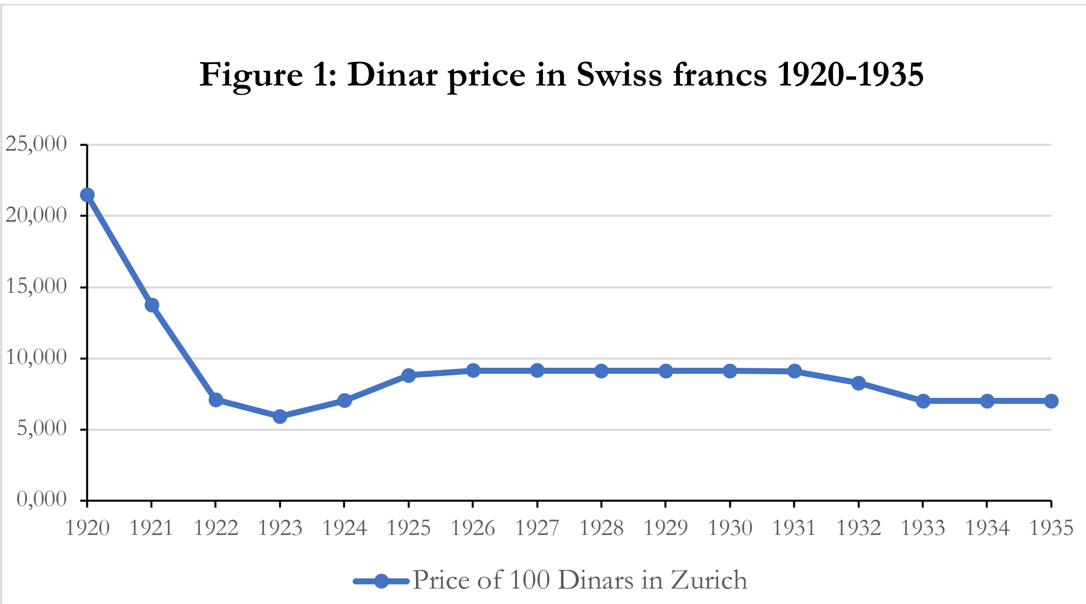
84 *Encyclopedia Britannica*, 'United States Presidential Election of 1896' (2019).
85 A. Iriye, Akira, 'Japan's Drive to Great-Power Status', *The Cambridge History of Japan* (Cambridge, 1989), p. 729.
86 Mitchener, et al. 'Why Did Countries Adopt the Gold Standard? Lessons from Japan', p. 8.

4 The Yugoslavian Gold Standard – Difficulties of Implementation

4.1 Sustaining the Cover Ratio

Eichengreen and Flandreau argue that the accumulation of gold and foreign exchange for sustaining cover ratios was prohibitively expensive for small economies in times of high bullion prices.[87] This made countries resort to foreign borrowing in order to build up cover ratios. That was also the case in interwar Yugoslavia. Figure 1 shows the exchange rate of the Yugoslavian dinar compared to the Swiss franc which was used as a reference point by Yugoslavian policy-makers in the interwar years. It shows that after a period of debt monetisation which led to exchange rate depreciation, the dinar was de facto stabilised at 9.12 francs equalling 100 dinars in 1925, meaning that this currency-peg was maintained without gold convertibility. Already this de facto stabilisation required foreign exchange reserves for foreign market operations to maintain the currency value. The legal cover ratio introduced with the gold standard in 1931 required a further increase in foreign exchange and gold reserves.

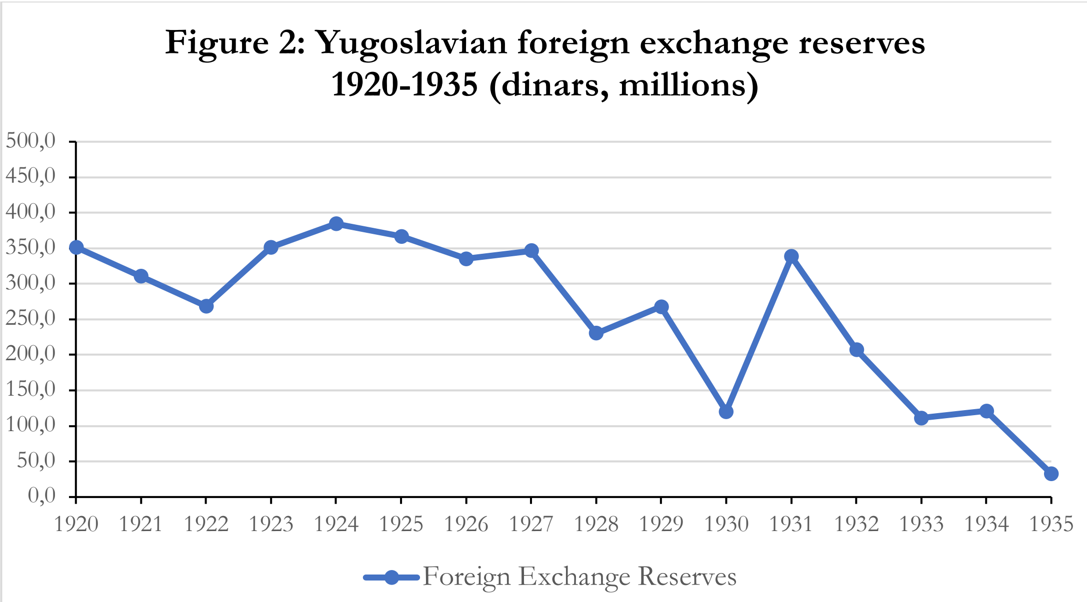


Source: Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II, (Athens/Sofia/Bucharest/Vienna, 2014).

Gold reserves were persistently low relative to money in circulation. Their dinar value at constant prices fluctuated between 64.2 million dinars and 98.6 million dinars between 1920 and 1930. Establishing a sufficient cover ratio for the gold standard required acquisitions of gold reserves which made the dinar value of gold reserves jump from 99.6 to 1540.5 million dinars from

[87] B.J. Eichengreen and M. Flandreau, *The Geography of the Gold Standard* (London, 1994), p. 6.

May to June 1931, the month of gold standard adoption.[88] Furthermore, foreign exchange reserves, the other component of the cover ratio, were heavily fluctuating which is illustrated by Figure 2. It also illustrates that in the period when gold standard adoption started being planned, namely after 1925, reserves were overall falling until 1931 when a 1.025-billion-franc French stabilisation loan allowed for acquiring foreign exchange reserves, which indicates unfavourable conditions for gold standard adoption in the years before the loan.



Source: Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II, (Athens/Sofia/Bucharest/Vienna, 2014).

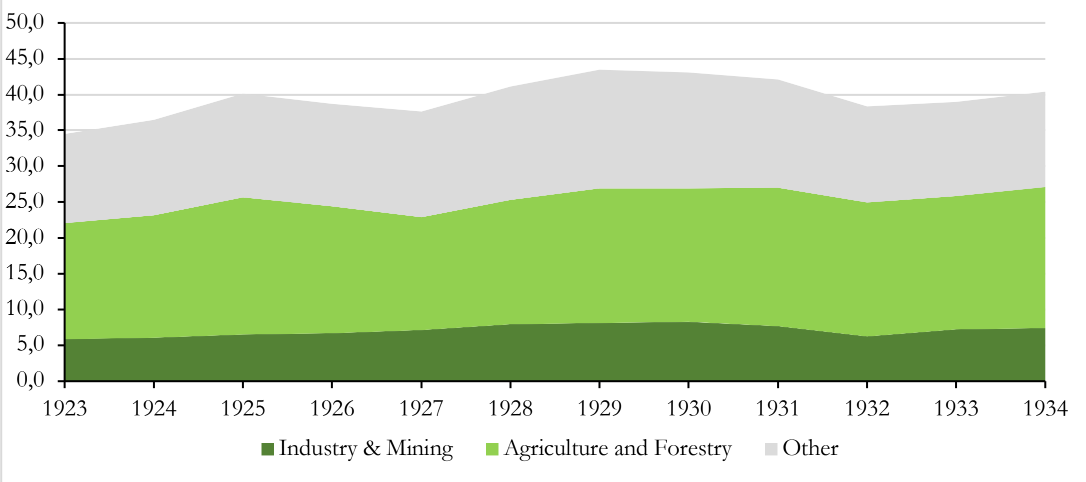
What the graph does not show is to which extent foreign exchange reserves fluctuated within the years. A government report titled "Proof that the stock of foreign exchange reserves varies and can fall below 100 million" reveals that the minimum cover ratio for 1926 amounted to 17.59% in July, while the maximum was reached in December at 26.72%. In 1927, the ratio was 20.33% in May and 34.89% in June.[89] Hence, foreign exchange fluctuations of up to 15% within one year were not unusual for Yugoslavia in the 1920s and they continued after dinar stabilisation. Once the dinar was adopted on 28th June 1931, the cover ratio fell from 41.10% to below 38% within a month, which was already close to the legally required cover ratio of 35%.[90]

The country's reserves fluctuated for three reasons. The first reason was a fluctuating balance-of-payments. Interwar Yugoslavia was an agrarian country. Figure 3 illustrates that

[88] Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II, (Athens/Sofia/Bucharest/Vienna, 2014).
[89] 'Proof that the stock of foreign exchange reserves varies and could fall below 100 million', 29th August 1931, National Bank of Serbia Archives [hereafter: NBS], ANB-1/I-58-1.
[90] Minutes of the 13th GAC meeting, 13th July 1931, NBS, ANB-1/II-30-2.

agriculture contributed decisively more to national income than industry and other income sources such as state monopolies in the interwar period. Furthermore, 78.87% of the labour force was employed in agriculture, forestry and fishing while peasant estates were mostly below 5 hectares in size.[91] Vojvodina which lies in Northern Serbia today was the most fertile part of the country. Many peasants from different parts of the Kingdom had populated this region thanks to the government's policy of distributing land to peasants who had fought in the First World War.[92] Immediately after the war, industry only accounted for 9.6% of national income.[93] In later years, the share of industry grew to 20%. However, as Figure 3 shows, industrial growth remained stagnant over the years. Industrial centres were located in the North West of the Kingdom, predominantly in Slovenia, Croatia and Vojvodina, as well as in Belgrade. Predominant industries were the food industry, the electrical and the wood industry.

Figure 3: Yugoslavian national income at constant prices 1923-1934 (dinars, billions)

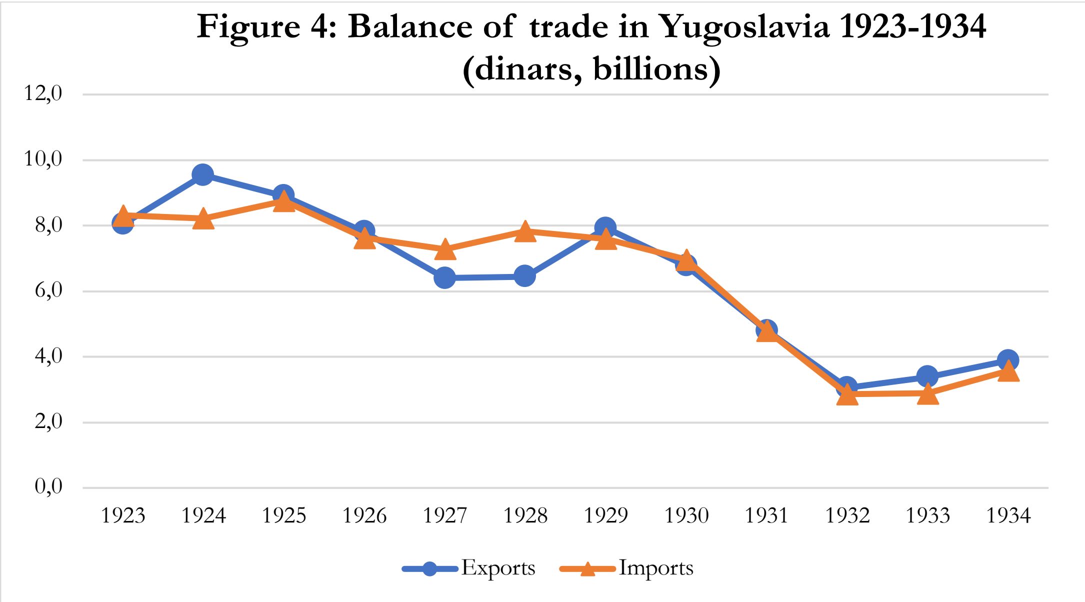


Source: Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II, (Athens/Sofia/Bucharest/Vienna, 2014).

Altogether, the agrarian structure of Yugoslavia's economy was also reflected in the country's trade. According to Nikolić, trade only contributed to GDP between 12 and 13% in the interwar period which was significantly lower than in most other advanced European economies.[94] Exports were mainly to Italy, Austria and Germany. France, which had extensively cooperated with Yugoslavia on financial affairs, was less cooperative in terms of trade and even cancelled the Serbian-French Trade Treaty from 1907.[95] Major export goods to Yugoslavia's trade partners

[91] I.M. Becić, *Finansijska Politika Kraljevine SHS: 1918-1923* (Belgrade, 2003), pp. 17-18.
[92] *Ibid.,* p. 18.
[93] *Ibid.*
[94] G. Nikolić, *Kurs dinara i devizna politika Kraljevine Jugoslavije 1918-1941* (Belgrade, 2003), p. 66.
[95] Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923* (Belgrade, 2003), pp. 219-220.

included wheat, flour, cattle, meat, wood, dried fruits, as well as raw materials like copper, while most industrial goods had to be imported.[96] The effect of export goods mainly being foodstuff was that exports were seasonal, which led to foreign exchange fluctuations within the years. Furthermore, the balance of trade over the years (Figure 4) indicates that no foreign exchange-generating trade surpluses were achieved in the Yugoslavian agrarian economy on average.



Source: Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II, (Athens/Sofia/Bucharest/Vienna, 2014).

The second reason for foreign exchange reserve fluctuations was internal governmental borrowing. By borrowing up to 600 million dinars per year from the NBKY as was permitted in the new bank statutes (explained in section 4), the government could initiate a growth in the monetary base and a fall in the cover ratio. This was met with disapproval by the NBKY. In May 1931, NBKY Governor Bajloni (1928-1934) described government expenses as a great worry because if the government took full advantage of its seasonal loan, this alone would make the cover ratio fall from 41% to 37% after legal stabilisation.[97] Member of the General Administrative Council of the NBKY (GAC) Radović also called upon the government to refrain from taking up loans and interfering with the work of the NBKY.[98] Furthermore, the government was directly using foreign exchange reserves for purchases abroad. In a strongly confidential letter from the NBKY to the Finance Ministry from December 1929, the bank urged the government to refrain from purchases abroad given the small stock of foreign exchange reserves.[99]

[96] D. Gnjatovic, *Stari Državni Dugovi* (Belgrade, 1991), p. 153.
[97] 'Minutes of the 16th GAC meeting', 29th May 1931, NBS, ANB-1/II-30-2.
[98] 'Minutes of the 18th GAC meeting', 2nd June 1931, NBS, ANB-1/II-30-2.
[99] 'Strongly confidential letter from the NBKY to the Finance Ministry', 13th December 1929, NBS, ANB-1/II-30-2.

The third reason for foreign exchange fluctuations was the economic shock of the Great Depression. According to the newspapers *Privredni Pregled*, the effects of the global economic crisis began to be felt in the second half of 1930.[100] As an agrarian country, Yugoslavia was particularly affected due to internationally declining prices of agricultural products which lowered the prices of its exports. Internally, the index for Yugoslavian agricultural prices fell from 138 in March 1929 to 73 in March 1931 (base month: December 1926).[101] *Narodno Blagostanje* noted a decrease in exports by 62% in January 1931 compared to January 1930.[102] Overall, the Great Depression led to a fall in export earnings during the crucial phase of dinar stabilisation between 1929 and 1932 from 7.9 billion to 3 billion dinars.[103] This in turn lowered foreign exchange incomes. *Privredni Pregled* wrote that the means for maintaining the stability of the dinar, and that is the stock of foreign exchange, decreased by two thirds towards the end of the 1930s.[104] Next to a deteriorating economic climate, three particular shocks led to diminishing foreign exchange reserves. The first shock was the bankruptcy of the Austrian bank *Kreditanstalt* on 11th May 1931, ironically the day when the final legal amendments for the Yugoslavian gold standard were passed. NBKY Governor Bajloni estimated that the uncertainties caused by this event alone led to an outflow of 350 million dinars.[105] The second shock was the Hoover moratorium which was announced on 20th July 1931 and cancelled German annuities in marks worth 450 million dinars which were a substantial foreign exchange income for Yugoslavia. Finally, the third shock was the abandonment of the gold standard by the United Kingdom on 21st September 1931 which increased uncertainties in global capital markets and contributed to a 500-million-dinar foreign exchange outflow according to Bajloni.[106] After the near halving of foreign exchange reserves between August and October 1931, the Finance Ministry re-introduced exchange controls on 7th October 1931.[107] Exporters were required to deposit the entire value of exported goods in foreign exchange at an authorised bank within 3 months of obtaining them. Foreign currency for imports could only be obtained with a permit from the NBKY. Foreign borrowing had to be permitted by the Finance Ministry.[108] A NBKY report blamed a combination of factors leading to decreasing foreign exchange reserves,

[100] 'Prices are falling because there are insufficient means', *Privredni Pregled* (22nd February 1931).
[101] Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II'.
[102] 'Conjuncture', *Narodno Blagostanje* (7th March 1931).
[103] Gnjatović, 'The Experience of Exchange Rate Regimes in Southeastern Europe in a Historical and Comparative Perspective', p. 339.
[104] 'Prices are falling because there are insufficient means', *Privredni Pregled* (22nd February 1931).
[105] Letter from NBKY to the Finance Ministry, 15th January 1932, NBS, ANB-1/I-58-1.
[106] *Ibid.*.
[107] 'Minutes of the 6th GAC meeting', 5th October 1931, NBS, ANB-1/II-30-2.
[108] 'Events and Problems', *Narodno Blagostanje* (10th October 1931).

including the agrarian nature of the economy, the Hoover Moratorium, and the abandonment of the gold standard by the UK, as reasons why Yugoslavia went off gold.[109]

Implications of the Inability of maintaining the Cover Ratio

The difficulty of securing stable gold and foreign exchange reserves had costly implications for Yugoslavia. To establish the legal cover ratio of 35% in gold and foreign exchange, these had to be generated through foreign loans and deflationary policies. Already for the de facto stabilisation of the dinar, Yugoslavia borrowed abroad. As the NBKY remarked in a letter to Finance Minister Stojadinović (1922-1924, 1924-1926, 1932-1935) in August 1926, the significant fall in foreign exchange reserves required taking up a 1-million-USD-loan abroad.[110] Concerning legal stabilisation, Yugoslavia sought support from the Bank of England for a six-million-pound-stabilisation-loan already in 1926.[111] As mentioned before, legal stabilisation was eventually achieved through a 1.025-billion-Franc-loan from a French banking consortium. With the cover ratio falling to 38% after legal stabilisation, the bank borrowed 3 million USD from the BIS in Basel for the acquisition of foreign currency.[112] GAC member Radović criticised that loans were always necessary since it was clear that the Yugoslavian economy was never able to sustain the gold standard without foreign aid, by which he insinuated that the gold standard actually increased the country's need for foreign borrowing to sustain the cover ratio, while it should have facilitated capital inflows for investments.[113] Hence, the legal stability of the dinar was inherently connected to foreign borrowing.

Apart from international borrowing, deflationary policies for the purpose of currency stabilisation were conducted for years in Yugoslavia. According to Gnjatović, these began in 1922 when the NBKY stopped buying up government debt and restricted credit provision. In 1923 and 1924, no loans were granted to banks. However, this policy was abandoned in 1925 out of fear that the rising exchange rate would paralyse the economy.[114] Probably the most consequential deflationary policies occurred in 1931, the year of dinar stabilisation. A 1930 NBKY report remarks that while credit elasticity was an important component of monetary policy, an extension of credits constituted a risk to monetary stability and should be refrained from. Once the gold standard was adopted, foreign currency would flow into the country and this would enable an increase in credit provision.[115] Hence, the position of the NBKY was that deflationary policies were necessary in the

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109 'Yearly overview of the NBKY', 17th February 1932, NBS, ANB-1/II-30.2., p. 17.
110 Letter from the NBS to Finance Minister Stojadinović, 12th August 1926, NBS, ANB-1/I-58-2.
111 'Letter to the Bank of England', 1926, NBS, ANB-1/I-58-2.
112 Toniolo, *Central Bank Cooperation at the Bank for International Settlements, 1930-1973* (Cambridge, 2005), p. 99.
113 'Minutes of the 5th GAC meeting', 5th September 1931, NBS, ANB-1/II-30.2.
114 Gnjatović, 'The Experience of Exchange Rate Regimes in Southeastern Europe in a Historical and Comparative Perspective', p. 332.
115 'Determination of the stock of foreign Exchange', 25th November 1930, NBS, ANB-1/I-90-17.

short-term, but could be suspended after gold standard adoption. Minutes of discussions in a GAC meeting reveal that in May 1931, the need for drastic credit restriction was recognised. Outstanding Lombard loans reached their yearly minimum of 153 million dinars on 25th May.[116] On 31st July, the Governor announced that the bank terminated granting loans backed by government bonds to local companies.[117] Since it was recognised that these measures were insufficient for preserving the cover ratio, the bank decided on 29th June to increase the discount rate from 5.5 to 6.5%, and the Lombard rate from 8 to 9%.[118] This constituted a shift in bank policies for the sake of maintaining the gold standard as the discount rate had not been changed at all in the previous decade. Furthermore, in September the bank demanded an immediate repayment of 20% of all credits granted to monetary institutions.[119] On 8th August, the bank terminated all unused credits in its credit contingent. Given that none of the adopted measures could prevent the cover ratio from falling, some shareholders proposed extreme measures. Dr. Marković proposed "selling state-owned mines, factories, forest-related enterprises, industrial and agrarian enterprises for acquiring gold and foreign exchange".[120] This illustrates how far some bank representatives would go to preserve the gold standard.

Altogether, due to the apparent inability of retaining reserves, the government and the NBKY had to take various economically and politically difficult measures to stabilise the dinar. The deflationary policies by the NBKY in 1931 fit well into Eichengreen's argument that the gold standard served as a catalyst for the Great Depression by requiring increases in interest rates and credit restrictions.[121] Another difficulty involved in the gold standard was the implementation of institutional innovations it required such as central bank independence.

4.2 Establishing Central Bank Independence

Bordo and James argue that financially underdeveloped systems of peripheral countries needed to undergo institutional reform for gold standard adoption.[122] This included changing bank mandates and establishing an independent central bank with a full control over the monetary base. In Yugoslavia, the NBKY had been founded by recommendation of the Council of Ministers on 2nd January 1920 by transforming the National Bank of the Kingdom of Serbia which in turn had been founded in 1883, into the new central bank for the entirety of the Kingdom. Extending the

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116 'Minutes of the 11th shareholder meeting', 17th February 1932, NBS, ANB-1/II-30-2.
117 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30-2.
118 *Ibid.*
119 'Minutes of the 5th GAC meeting', 5th September 1931, NBS, ANB-1/II-30-2.
120 'Minutes of the supplemental shareholder meeting', 12th July 1931, NBS, ANB-1/II-30-2.
121 Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*, p. 262.
122 M. Bordo and H. James, 'The Trade-offs between Macroeconomics, Political Economy and International Relations', *Financial History Review* 26/3 (2019), p. 249.

scope of Serbian institutions to the entirety of the Kingdom was a frequent policy pattern in the Kingdom because policy-makers were faced with finding appropriate institutions for five different legal environments in a short timeframe. Another example for that are Serbian governmental accountancy laws which were extended to the entirety of the Kingdom.[123] Just as its predecessor, the NBKY was a joint-stock company and had a capital of 180 million dinars divided into 60,000 shares with a nominal value of 3,000 dinars.[124] The General Administrative Council (GAC) was constituted of the governor and 24 elected members who were bank shareholders. The main responsibilities of the GAC included fixing the official discount rate, formulating bank regulations and appointing members of the Executive Council.[125]

A new bank mandate and changes in bank statutes were necessary in order to enshrine the functioning of the gold standard into law and make the NBKY independent from governmental influence.[126] The final law on money was only passed by the government on 11th May 1931, shortly before legal stabilisation on 28th June. This law laid out the precise functioning of the Yugoslavian gold standard, such as the legal obligation of the NBKY to convert money into gold. Furthermore, article 5 required the bank to maintain a cover ratio of 35% in gold and foreign exchange reserves.[127] Thereby, the law assigned the primary mandate for securing dinar stability to the NBKY. Central bank independence was institutionalised in a contract between the government and the NBKY, as well as new bank statutes, which were approved on 14th June 1931, meaning two weeks before legal stabilisation.[128] Article 20 of the new statutes prohibited the bank from making arbitrary direct transfers to the government.[129] Previous laws according to which the government was entitled to loans from the bank were repealed and the government's right for receiving loans limited to a 600-million-dinar seasonal loan on which it had to pay interest. The bank was thus prohibited from indefinitely increasing the monetary base on demand from the government.[130] The statutes also ensured bank independence in personnel management. State employees or MPs were excluded from entering the GAC and from becoming bank governors.[131] The primary responsibility of the Governor was to make sure that bank statutes are being respected and the Finance Minister only had the right to interfere should the Governor fail in this duty.[132] The Governor in turn was chosen by the Finance Ministry after five candidates were proposed by the GAC. These institutional

123 B. Kršev, *Finansijska Politika Jugoslavije 1918-1941* (Novi Sad, 2007), p. 43.
124 'Minutes of the supplemental shareholder meeting", 14th June 1931, NBS, ANB-1/II-30.2.
125 'The Statutes of the National Bank of Yugoslavia', 14th October 1930, BIS, Ref. No. CH-000583-8.
126 Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923*, p. 211.
127 'Official Part', *Službene Novine* (11th May 1931).
128 'Minutes of the 11th shareholder meeting', 8th March 1931, NBS, ANB-1/II-30-2.
129 'The Statutes of the National Bank of Yugoslavia', 14th October 1930, Bank for International Settlements Archive [hereafter: BIS], Ref. No. CH-000583-8.
130 'A Letter to Shareholders', 21st June 1931, NBS, ANB-1/I-58-1.
131 'Determination of the stock of foreign exchange', 25th November 1930, NBS, File ANB-1/I-90-17.
132 Letter from the NBKY to the Finance Ministry, 29st August 1930, NBS, ANB-1/I-58-1.

innovations provided suitable conditions for the effective operation of the gold standard as the monetary base was placed in the hands of the central bank which was thereby able to concern itself effectively with the maintenance of the cover ratio, i.e. to adhere to the "rules of the gold standard game" without interference.

The establishment of central bank independence in Yugoslavia followed the example of other European countries. For example, Bulgaria's central bank assigned its bank the primary responsibility of note issuance in 1928 while advances to the state were limited to 400 million leva.[133] As mentioned above, in Yugoslavia this figure amounted to 600 million dinars. In fact, Yugoslavian policy-makers explicitly analysed how central bank independence was institutionalised in other peripheral countries and drew implications for Yugoslavia, which is an insight into the institutional learning of a peripheral country like Yugoslavia. For example, in a letter to the Finance Ministry, the NBKY Governor wrote that "a new law has to be introduced that limits governmental institutions from holding more than 10% of the bank shares as it is the case in Romania and Greece".[134] The bank would furthermore contemplate the example of Poland where the government was allowed to hold one-third of bank shares, but had no voting rights in the governing council.[135] The aforementioned way of the Governor being chosen by the Finance Ministry was inspired by how this process was conducted at the Banque de France according to *Privredni Pregled*.[136] However, the establishment of central bank independence in Yugoslavia was still distinctive. Next to its remarkably late institutionalisation, it seems as if it was specifically introduced for the gold standard. A newspaper article from *Privredni Pregled* argued that the institutional innovations such as limiting governmental profits at the NBKY or increasing the influence of the bank on the economy were sacrifices the government made specifically for the purpose of legal stabilisation.[137] This is also confirmed by the linkage of the issues of the new bank statutes and gold standard adoption in the NBKY. In many other European countries, however, central bank independence was established to prevent governments from arbitrarily taking up loans after the great inflations of the early 1920. For example, the League of Nations specifically pressured for the establishment of central bank independence for granting loans to Austria and Hungary in order to prevent another hyperinflation.[138] According to Wandschneider, this was also the main rationale for central bank independence in Poland and Czechoslovakia. Hence, Bordo's view of the gold standard being a catalyst for institutional innovations seems to be particularly accurate for Yugoslavia. Another governmental policy which had to be completed specifically for the gold standard, and which

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[133] Berov, 'Budgetary Policy, Money Supply and Banking in Bulgaria between the Wars', p. 388.
[134] 'Letter from the NBKY to the Finance Ministry', 29th August 1930, NBS, ANB-1/I-58-1.
[135] *Ibid.*
[136] 'Reforms in the National Bank', *Privredni Pregled* (21st June 1931).
[137] *Ibid.*.
[138] Wandschneider, *Central Bank Independence and Policy Performance: Central-East Europe* (2003)*, 1919–1939*, p. 50.

sparked an uproar among Yugoslavian intellectuals and the public, was the repayment of the governmental loan to the NBKY.

4.3 Repaying the Government's Loan

The changes in the statutes of the NBKY alone were not sufficient for giving it full control over the monetary base. Prior to 1931, the monetary base of Yugoslavia was divided into two parts. Of the approximately 6 billion dinars in circulation, only 2 billion were backed by gold reserves worth one-third of their value which was required by the 1922 bank statutes. The other 4 billion were issued in the early 1920s for the purposes of debt monetisation and were backed by a loan the government had taken up at the NBKY for this purpose. This meant that a part of the monetary base was dependent on the maintenance of a governmental liability. *Privredni Pregled* wrote that this led to a situation where the money in circulation was not fully managed by the NBKY.[139] Hence, prior to legal stabilisation, the notes backed by the governmental loan needed either to be pulled out of circulation, which would have led to a deflation of 400-500% according to economic journalist Vojnik-Hajduk, or the governmental loan could be repaid and the liability replaced with gold and foreign exchange reserves stored in the NBKY.[140] The second alternative was chosen.

In the moment of stabilisation, the French stabilisation loan was used for repaying the governmental loan by 2.2 billion dinars through a direct money transfer to the NBKY (1.4 billion dinars) and a contribution to the cover ratio (770 million dinars). Furthermore, future governmental dividends achieved through bank shares (50 million) were to be transferred to the NBKY.[141] The contribution to the cover ratio proved sufficient for creating a cover ratio of 41.10% of the value of all notes in circulation in the moment of stabilisation on 28th June 1931, 27.63% of which was in gold.[142] Repaying the loan through taxation was rejected because "completing the stabilisation and leaving the economy behind would be psychologically bad", as it says in a letter from the NBKY to the Finance Ministry, which indicates that it would put a strain on public finances.[143] One could also argue that this was hardly possible as the Yugoslavian taxation system was heterogeneous and inefficient.[144] Interestingly, this implies that the French stabilisation loan connects the two issues of establishing a sufficient cover ratio (section 4.1) and making the central bank and the monetary base completely independent from governmental influence through loan repayment (section 4.2).

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139 'The Legal Stabilisation of the Dinar', *Privredni Pregled* (29th July 1930).
140 J. Vojnik-Hajduk, 'The value of the Dinar, its stabilisation and the National Bank', *Bankarstvo* (December 1930).
141 'Minutes of the regular shareholder meeting', 17th February 1932, NBS, ANB-1/II-30.2.
142 *Ibid.*
143 Letter from the NBKY to the Finance Ministry, 29th August 1930, NBS, ANB-1/I-58-1.
144 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 43.

While the repayment of governmental loans preceded gold standard adoption in both Belgium and Italy, the Yugoslavian case is striking due to the uproar it sparked among Yugoslavia's intellectuals and the public. Policy-makers and government officials viewed the repayment of the loan as a crucial component of gold standard adoption, such as NBKY Director Novaković who asserted this already in 1926.[145] However, several economists and economic journalists, as well as parts of the public, viewed it as a means for the enrichment of shareholders, and the use of foreign borrowing for repaying the loan as unjustified. Economic journalist Đorđević wrote in *Bankarstvo* that since the bank did not produce the loan to the government by giving out assets, but by issuing unbacked paper notes, there was no duty for repayment.[146] Milosavljević wrote in *Bankarstvo* that this opinion was reflected in parts of the public who deemed it unjustified to repay the bank for issuing unbacked paper money.[147] Other journalists accepted loan repayment but opposed borrowing abroad for this purpose. Plavšić argued in *Riječ* that the governmental loan should be repaid through taxation and that the foreign loan should instead be used for domestic lending.[148] The issue also sparked responses in favour of repayment. Jelić denounced opponents of repayment as "charlatans" who underestimate the duty the government incurred on itself by excessively borrowing from the bank in the early 1920s in the economic newspapers *Bankarstvo*.[149] An article in the newspapers *Pravda* criticised the main opponent of loan repayment economist Dr. Topalović for inflicting harm on the international image of Yugoslavia by insinuating that the country was a "bankrupt nation" unable to repay the loan.[150] Altogether, the heated debate among economists and the public surrounding governmental loan repayment was a crucial component of gold standard adoption in Yugoslavia. The prominent Yugoslavian economist Šećerov argued in September 1930 that it was so widespread that the entire public debate surrounding the gold standard was reduced to the question of whether the governmental loan should be repaid or not.[151]

4.4 Awareness of the Difficulties of Gold Standard Adoption

The three previous sub-sections have shown that the stability of the dinar could not be maintained without foreign loans and deflationary policies against the unfavourable economic background (section 4.1), that institutional innovations were required to implement the gold standard (section 4.2), and that some policies it required, such as the repayment of the

[145] 'Report of the NBKY Director about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.
[146] V. Đorđević, 'The Legal Stabilisation of the Dinar', *Bankarstvo* (December 1930).
[147] K. Mirosavljević, 'The National Economy and Monetary Stabilisation', *Bankarstvo* (December 1930).
[148] D. Plavšić, 'The Governmental Loan at the National Bank', *Riječ* (16th August 1930), NBS, ANB-1/I-58-1.
[149] M. Jelić, 'Legal Stabilisation and the Governmental Loan', *Bankarstvo* (September 1930).
[150] 'Defeatism at its worst', *Pravda* (1930), ANB-1/I-58-1.
[151] S. Šećerov, 'The value of the Dinar and the Repayment of the Loan to the National Bank', *Bankarstvo* (September 1930).

governmental loan, required foreign borrowing and sparked opposition in Yugoslavian intellectual circles and the public (section 4.3). It appears that the latter two difficulties were of little concern to Yugoslavian policy-makers. The implementation of central bank independence for the gold standard, even if rash, was viewed as a positive by-product. A NBKY report on the gold standard argued that replicating the processes of central bank independence completed in other countries allowed the NBKY to take its due place among the important European central banks.[152] The NBKY responded to the uproar that was sparked concerning loan repayment in 1930 by issuing reports arguing that the bank would not profit from the preconditions involved in legal stabilisation such as loan repayment or the planned gradual increases in the bank capital because shareholder dividends could be limited by increasing the number of outstanding shares. Instead, the public as a whole would profit from this repayment because the legal stabilisation would allow everyone to obtain gold in exchange for notes.[153] Hence, policy-makers did not perceive these obstacles as threats to the gold standard.

However, the economic realities of the Yugoslavian economy which made legal stabilisation difficult (section 4.1) could hardly be overlooked and numerous economic journalists pointed out that Yugoslavia was not in the position to maintain a gold standard. Đorđević warned in *Bankarstvo* that "the factual stability is conditioned by the balance of the state budget. It is necessary to have a favourable capital and current account that does not allow for gold outflows".[154] Popović argued in *Bankarstvo* that not every country could introduce the gold standard. This required an active trade balance and economic stability. He concluded that Yugoslavia would have to raise its level of economic development before legal stabilisation, for example by cultivating unused lands.[155] Hence, there was doubt among economic journalists about whether Yugoslavia could maintain a gold standard. Policy-makers in the NBKY were aware of looming difficulties stemming from the country's inability of retaining foreign exchange reserves as well. A NBKY report concluded that the central question surrounding dinar stabilisation was whether the state of the economy allowed for maintaining a stabilised dinar. Exchange reserve fluctuations were closely monitored at meetings of the GAC and in a letter to the Finance Ministry, the NBKY concluded that the country's agrarian nature would lead to strong fluctuations of foreign exchange reserves. Therefore, the legal cover ratio in Yugoslavia would need to be especially high.[156] Furthermore, NBKY officials were aware that achieving a legal stabilisation by relying on extensive foreign borrowing was unsustainable in the early years of the discussions surrounding legal stabilisation. In 1926, NBKY

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152 'Determination of the stock of foreign exchange', 25th November 1930, NBS, ANB-1/I-90-17.
153 'Proof that there is no possibility for an increase in bank profits', 1930, NBS, ANB-1/I 58-2.
154 Đorđević, 'The Legal Stabilisation of the Dinar'.
155 M. Popović, 'The Solution of our Monetary Problem, *Bankarstvo* (December 1930), p. 557.
156 Letter from the NBKY to the Finance Ministry, 29th August 1930, NBS, ANB-1/I-112-2.

Director Novaković noted to be unsure whether the benefits from dinar stabilisation outweighed the burdens which it created for the government.[157] In 1929, the NBKY clearly distanced itself from an "artificial" legal stabilisation through borrowing as this excerpt from a bank report shows:

> "Taking up a loan abroad for legal stabilisation would be a flawed policy […]. Such a loan would be dead capital. It would not stabilise our reserves. If the preconditions for the legal stabilisation of the dinar are met in our country, no foreign loan is necessary, and if these preconditions are not met, there is no way how such a loan could secure such a stabilisation."[158]

Against this background, it seems curious that the NBKY recommended the Finance Ministry to stabilise with a loan from abroad in August 1930.[159] What seems furthermore ironic against the background of a sustained inability to retain foreign exchange, is that the Yugoslavian government, and the Finance Ministry in particular, insisted on legal stabilisation without capital controls which had previously served as a protective mechanism. These had been in place since 30th March 1919 and exporters were required to deposit one-third of foreign exchange earnings in the agency in exchange for dinars.[160] NBKY Governor Bajloni criticised the ministry in the retrospect for this demand by pointing out that the NBKY had always had the view "that the free trade of foreign exchange should not be allowed after legal stabilisation".[161] Apart from the NBKY, economic journalist Eropkin criticised the abolishment of capital controls in the newspapers *Bankarstvo*, writing that it was a grave mistake to abolish capital controls as the five-year-long factual stabilisation of the dinar was enabled exclusively by this policy.[162] Furthermore, the Zagreb stock exchange stated officially that "in the interest of the monetary reform, it will be necessary to maintain exchange controls in the near future, meaning that all transactions are concentrated in domestic stock exchanges".[163] The board of the Zagreb stock exchange was constituted of the representatives of banks, as well as industrial and trade enterprises.[164] The article therefore shows that there were forces among the economic elites that viewed abolishing capital controls critically. Hence, it seems sensible to ask which rationales made NBKY representatives and the Yugoslavian government eagerly pursue an "artificial legal stabilisation" through foreign loans and without capital controls which could only last for 101 days. Subsequent sections examine the economic and political rationales behind their determination, as well as interest group pressures.

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157 'Report by NBKY Director Novaković about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.
158 'Legal Stabilisation of the Dinar', NBS, 1929, ANB-1/I-58-1.
159 Letter from the NBKY to the Finance Ministry, 29th August 1930, NBS, ANB-1/I-112-2.
160 Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923*, p. 144.
161 Letter from the NBKY governor to the Finance Ministry, 15th January 1932, NBS, ANB-1/I-58-2.
162 A. Eropkin, 'The Stabilisation of Yugoslavian Money', *Bankarstvo* (September 1930).
163 'Election of the new leadership of the National Bank', *Privredni Pregled* (12th July 1931).
164 Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923*, p. 181.

5 Economic Rationale for the Yugoslavian Gold Standard

As mentioned in section 3.1, the three major economic reasons for gold standard adoption which were recognised by governments throughout Europe were price stability, foreign borrowing and trade. This section aims to extract the primary economic rationale policy elites used for justifying the gold standard over the years in Yugoslavia, looking at the views of the Finance Ministry and the NBKY, the two institutions which were mainly determining Yugoslavian economic policy, especially after parliamentary powers were seized in 1929.

5.1 The Economic Rationale of Policy Elites

The Finance Ministry

The Finance Ministry took a straightforward approach to stabilise the dinar throughout the interwar period. The ministry under Stojadinović who was a member of the conservative Serbian Radical National Party, was responsible for initiating *de facto* dinar stabilisation in the mid-1920s. According to the Finance Ministry, a concern for dinar stability as the sole duty of the NBKY. This is exemplified in a letter from the ministry to NBKY Governor Bajloni, which described the maintenance of the cover ratio as the bank's "most holy duty towards the national economy", and that "[t]he concern for our money is the first and most important task of the bank as a money-issuing institution".[165] In a letter from the NBKY to the Finance Ministry from 16th September 1925, the bank criticised the ministry (then under Milan Stojadinović) for accumulating foreign currency with the intention of stabilising the dinar without a mandate:

> "[…] [W]e found that contracts no. 8238 and 40646 between the Finance Minister and the NBKY determine the way for conducting foreign exchange purchases. However, the ministry went beyond the scope of these contracts and purchased foreign exchange […] not only to obtain means for payments in foreign currencies for its obligations, but it broadened the scope of the contracts to its monetary policy with the goal of stabilising the dinar. […] [T]his action by the Finance Minister, however it may be justified in industrial circles, has no permission in the law of the national bank."[166]

This passage indicates that the Finance Ministry was the institution pushing ahead with dinar stabilisation already in 1925 against the banking laws. However, on 10th October 1925, the scope of the contracts mentioned in the quote above was extended by the Council of Ministers and foreign exchange purchases for monetary stabilisation were permitted.[167] Finance Minister

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[165] Letter from Finance Minister Đorđević to NBKY governor Bajloni, 9th January 1932, NBS, ANB-1/I-58-1.
[166] 'Measures for the Protection of the Dinar', 16th September 1925, NBS, ANB-1/I 58-2, Doc. No. 99424.
[167] 'Reply to Finance Minister Stojadinović', 10th October 1925, NBS, ANB-1/I-58-2, Doc. No. 23110.

Stojadinović also demanded to place the responsibility for foreign exchange transactions in the hands of the NBKY, thereby transferring more autonomy over the monetary base to the bank.[168] On 3rd November 1925, the NBKY approved the suggestions by the Finance Ministry, adding that the institutional changes proposed by the Finance Minister should be enshrined into national bank law. Hence, it appears that the efforts for stabilising the dinar by the Finance Ministry under Stojadinović were the main initiators of early legal innovations for gold standard adoption mentioned in the previous section, and set out a trajectory which was later pursued by Finance Minister Švrljuga (1929-1931).[169] In terms of legal stabilisation, it was also the Finance Ministry which took decisive steps for implementing the gold standard without capital controls against the warnings of bank officials and the Zagreb stock exchange as mentioned in the previous section. Finance Minister Stojadinović had a clear idea why he was propagating gold standard adoption, as expressed in an article in the Chicago Tribune quoted below which was re-printed in *Privredni Pregled* in July 1930.

> "The legal stabilisation of the dinar opens new perspectives for the advantageous development of our future economic and financial life. [...] The natural resources of Yugoslavia are almost infinite, but for exploiting them capital is needed which cannot be found within the country."[170]

He adds that from any possible viewpoint, the country was ready for legal stabilisation, especially because the economy had adjusted to the de facto stabilisation and had a favourable cover ratio of 48.49% at that point in time.[171] His view that capital has to flow into the country to activate the resources which would then lead to economic development is characterstic of pre-WWI Serbian and Yugoslavian governments. Soon after the liberation from the Ottoman empire in 1878, the Serbian government extended its international borrowing for the purposes of economic development. Among the loans which the government took up was a 33-million-franc-loan from *Société Générale* in 1881 which was partially used for railway construction. A 10-million-franc-loan from *Wiener Bank Verein* in 1888 was used for buying up the tobacco monopoly. A 150-million-franc-loan from France in 1909 was again used for railway construction.[172] All these loans were later inherited by the Kingdom of Yugoslavia. The new Kingdom took up 3 major international loans, including a 100-million-USD-loan for railway construction from the private US bank *Blair & Co* for which the government did not ask parliament for permission.[173] Against this

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168 Letter from Finance Minister Stojadinović to the Council of Ministers, 6th October 1926, NBS, ANB-1/I-58-2, Doc. No 23110.
169 Letter from the NBKY to the Finance Ministry, 3rd November 1925, NBS, ANB-1/I-58-1, Doc. No. 117339.
170 M. Stojadinović, 'The Legal Stabilisation of the Dinar', *Privredni Pregled* (July 1930).
171 *Ibid.*
172 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 152.
173 *Ibid.,* p. 178-179.

background, it does not seem surprising that the government, and hence the Finance Ministry, were mainly motivated to adopt the gold standard to facilitate foreign borrowing. Another example is a letter written by the Secretary of Foreign Affairs to the foreign mission of Yugoslavia in Washington D.C. which explains why the Hoover moratorium was harmful for Yugoslavia:

> "We have managed to legally stabilise our national currency under the biggest hardships, […]. [The moratorium] would leave us no option but to lift our hands from the stabilisation of our national currency and from any hope of securing foreign credit, and to accept nothing else than going into bankruptcy".[174]

This quote illustrates the fear of an inability to secure foreign loans should the gold standard be abandoned which was present in the Yugoslavian government. GAC member Šumanović summarised an in his view excessive governmental concern for ensuring foreign borrowing through gold standard adoption in 1931 by claiming that "[s]ince our liberation, we have not had a government which did not from its beginning until its end work on obtaining a loan abroad."[175]

The National Bank

In the early years after the First World War, Yugoslavia was experiencing a period of high inflation which went hand-in-hand with a strong depreciation of the dinar. Compared to pound sterling, the value of the dinar fell from 51.4 dinars equalling 1 pound in June 1919 to 477.3 dinars equalling 1 pound in January 1923.[176] This was mentioned in NBKY reports as one of the reasons why the dinar should be stabilised. In fact, the bank named as the rationale for authorising the Finance Minister to buy foreign currency for the purpose of de facto stabilisation (which it first criticised him for as mentioned in the previous sub-section) that "strong fluctuations in the exchange rate undoubtedly have detrimental effects on our economy".[177] Hence, the bank stressed the benefit of price stability of a de facto stabilisation. In terms of legal stabilisation, a bank report from 1929 showed an ambivalent view on stabilisation by stressing the difficulties of the deflationary policies it required. It held that "[o]ur dinar went through a difficult inflation crisis and we have all felt on our own bodies and our property how difficult it was and with which difficulties the subsequent calming of our monetary situation was connected".[178] The report further says that "the same perturbations which follow inflation are also an effect of deflation, just in the other direction. But for money, its value is not important. It is only important that its determined value

174 P. Krejić and M. Todorović (eds.), *Jugoslovensko-Američki odnosi* (Belgrade, 2015), p. 149.
175 'Report by the Executive Council for October', 28th October 1931, NBS, ANB-1/II-30-2.
176 Bank of Greece et al., 'South-Eastern European Monetary and Economic Statistics from the Nineteenth Century to World War II'.
177 'Measures for the Protection of the Dinar', 6th September 1925, NBS, ANB-1/I 58-2, Doc. No. 99424.
178 'Legal Stabilisation of the Dinar', 1929, NBS, ANB-1/I-58-1.

is lasting, meaning that it is fixed to the value of gold".[179] Hence, the report acknowledged the difficulties of stabilisation, but stressed the importance of price stability. However, stability of the currency value was not viewed as a goal in itself:

> "currency has, apart from having stable purchasing power within the country, to have some form of backing […], which stabilises it whatever the domestic purchasing power of the currency […], and this freedom is given to the currency only by a backing to gold […]. Only if a country has this good, i.e. a currency backed by gold, […] it can always hope to receive international loans."[180]

The final sentence shows that foreign borrowing was viewed as the "end goal" of legal stabilisation. Furthermore, a bank report which details the height of the cover ratio in 1930 argued that the Yugoslavian economy was stagnating, but that the stagnation would be followed by an acceleration in performance once the dinar is stabilised.[181] Hence, similarly to the Finance Ministry, it was the position of the NBKY that the gold standard would facilitate capital inflows which would enable economic development.

It is insightful to analyse whether the justifications of the gold standard provided by bank officials changed towards the Great Depression and after it was adopted, and when the faith of many GAC members in the benefits of this monetary system faded. Interestingly, right before adoption, namely in the period between January and May 1931, there was a conscpicuous absence of discussions relating to legal stabilisation in GAC meetings. This could be attributable to the view held in Yugoslavian economic circles that monetary matters should be discussed as little as possible in order to prevent speculation. According to Nikolić, the theory on the influence of expectations on economic fluctuations by Albert Aftalion was especially prominent among Yugoslavian policy-makers.[182] An example for the fear of discussing monetary matters in the NBKY is the discussion relating to the effects of the Hoover moratorium from July 1931. Only in October 1931 did GAC members engage in an open discussion about it, even though it was already announced in July. Đunderski argued that it was awful to hear the word moratorium mentioned. Savčić added that discussing the moratorium spread mistrust. Jovanović even refused to say the word moratorium out of fear of the speculation while Marković argued that it was a mistake to mention the word during GAC meetings, and that it should have been deleted in minutes of earlier meetings.[183] Hence, the fear of speculation could explain the absence of discussions relating to the gold standard right

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[179] 'Legal Stabilisation of the Dinar', 1929, NBS, ANB-1/I-58-1.
[180] *Ibid.*
[181] 'Determination of the stock of foreign exchange which the bank needs for the foundation of the circulation', 25th November 1930, NBS, ANB-1/I-90-17.
[182] Nikolić, *Kurs dinara i devizna politika Kraljevine Jugoslavije 1918-1941*, p. 117.
[183] 'Report by the Executive Council for October', 28th October 1931, NBS, ANB-1/II-30-2.

before its adoption. However, after it was adopted the problems of the gold standard could no longer be omitted, and heated discussions were sparked in the GAC.

Recognising the additional strain the deflationary policies inflicted on the Yugoslavian economy, GAC members Marković and Šumanović demanded a legal intervention into the banking laws specifying the functioning of the gold standard. Already in May 1931, Marković demanded a lowering of the cover ratio from 35% to 25%.[184] Similarly, Šumanović maintained in October 1931 that without a lowering of the legal cover ratio, the economic crisis could not be overcome. Mihajlović added that higher discount rates had detrimental effects on the economy. The two were joined by 11 other members of the GAC in criticising the 1% increase of the discount rate.[185] The replies by Governor Bajloni and other GAC members to these criticisms remained consistent throughout 1931. Just as the rationales provided for gold standard adoption in general, they were connected to foreign borrowing. Referring to the loans Yugoslavia had accumulated until 1931, GAC member Kulmer argued in July 1931 that "previous speakers have talked about the catastrophe of credit restrictions, but the real catastrophe would come upon us if the dinar value falls", adding that the deflationary policies would therefore be acceptable.[186] The reason he and other members such as Berković gave is that Yugoslavia was "a debtor country and for that reason the value of our currency ought not go downhill".[187] The view that the gold standard had to be maintained for the repayment of foreign loans was reflected in economic newspapers such as *Narodno Blagostanje* which wrote that Yugoslavian loans were denominated in dollars and francs, and a fall in the dinar would require using a bigger amount of the domestic production to pay for the same loans in gold.[188] This increased pressure on Yugoslavian authorities to preserve the value of the dinar which could have deteriorated with the abandonment of the gold standard.

However, the reason which appears to be most central for the maintenance of the gold standard was the concern for *further* loans from abroad. NBKY Governor Bajloni argued against the proposed legal interventions as follows:

> "The Executive Committee has given itself the task to maintain the status quo at any price […]. If we change what has been achieved until now, we could not hope to receive any more loans from abroad. Abroad, the situation has improved and other countries will not abandon us."[189]

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184 'Minutes of the 16th GAC meeting', 29th May 1931, NBS, ANB-1/II-30.2.
185 'Report by the Executive Council for October', 28th October 1931, NBS, ANB-1/II-30-2.
186 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.
187 'Minutes of the 6th GAC meeting', 5th October 1931, NBS, ANB-1/II-30.2.
188 'Events and Problems', *Narodno Blagostanje* (21st February 1931).
189 'Minutes of the 5th GAC meeting', 5th September 1931, NBS, ANB-1/II-30.2.

This passage reflects the Governor's belief in receiving further loans if the gold standard is maintained. In a GAC meeting in July members of the Executive Council also communicated that new loans were expected to follow after stabilisation.[190] However, many GAC members did not believe this anymore. Berković noted that "[o]ther countries cannot give us more means, because they are protecting their own interests".[191] Jelačin Jr. argued that the NBKY "ought not to be fearful of how other countries will react in response to a lowering of the cover ratio as they have never provided Yugoslavia with sufficient means anyways".[192] Šumanović argued that he deeply believes that no credits can be obtained abroad as "these are political loans. They can only be obtained from political allies".[193] Apparently, he questioned the political leverage Yugoslavia had internationally for receiving loans. However, despite their opposition, GAC members still agreed to the deflationary policies for maintaining the gold standard unanimously, such as in June 1931 when the discount rate was increased from 5.5 to 6.5%.[194] Furthermore, Governor Bajloni who was a stern defender of maintaining the gold standard was re-elected as bank Governor in July 1931.[195] Finally, even the sternest critic of the deflationary policies Šumanović accepted to support them if the belief in foreign credit enabled by the gold standard, which is what the Governor assured, was strong.[196] Therefore, it seems like there was a shared conviction within the bank just as in the Finance Ministry, that the gold standard should be maintained to secure borrowing and capital inflows, which will then stimulate the economy. This is also confirmed by views depicted in economic newspapers such as *Privredni Pregled* which identified the wish to attract foreign capital as the main intention behind legal stabilisation.[197] Hence, the borrowing motive, which is one of ther three economic rationales generally recognised in the literature on gold standard adoption, was the primary economic rationale for justifying the Yugoslavian gold standard.

In terms of the other two economic rationales explained in section 3, price stability and trade, I argue that the *de facto* stabilisation of the dinar was viewed as a measure for ensuring price stability in both the Finance Ministry and the NBKY, and Stojadinović was depicted as the politician who achieved this stabilisation. However, concerning legal stabilisation, the borrowing motive was of primary importance. Increased trade was seldom linked to the issue of legal stabilisation. As mentioned in section 4, the share of trade in GDP was low (12-13% on average in the 1920s). Improved trade might have been viewed as a long-term objective once the economy

[190] 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.
[191] 'Report by the Executive Council for October', 28th October 1931, NBS, ANB-1/II-30.2.
[192] *Ibid.*
[193] 'Report by the Executive Council for October', 28th October 1931, NBS, ANB-1/II-30.2.
[194] 'Minutes of the 21st GAC meeting', 27th June 1931, NBS, ANB-1/II-30-2.
[195] 'Minutes of the 13th GAC meeting", 13th July 1931, NBS, ANB-1/II-30.2.
[196] 'Minutes of the 5th GAC meeting', 5th September 1931, NBS, ANB-1/II-30.2.
[197] 'Election of a new Leadership in the National Bank', *Privredni Pregled* (12th July 1931).

had developed in response to the capital inflows rather than a direct effect of legal stabilisation, which could explain the absence of a connection between the issues of trade and legal stabilisation.

5.2 Explaining the Positions of Policy Elites

As the previous section shows, the economic rationale for gold standard adoption was broadly aligned among Yugoslavia's economic elites and focused on international borrowing and capital inflows which would then lead to economic development. This section goes beyond the identification of the economic rationale used by policy-makers and asks how this it was formed, focusing on external and internal factors. The external factors refer to how foreign lenders exerted an ideological and economic influence on Yugoslavian policy elites which contributed to the formation of their idea that foreign borrowing necessitated gold standard adoption. Subsequently, internal factors will refer to the state of economic knowledge present in Yugoslavia which made policy elites ignorant towards the disadvantages of the gold standard and made them excessively focus on its alleged benefits.

5.2.1 External Factors: The Influence of Foreign Banks

In a letter to shareholders, the NBKY wrote how the Yugoslavian government was trying to obtain international loans, but how "the first condition for a loan was that a legal stabilisation of the dinar is introduced just like in practically all European countries".[198] Equally, GAC member Marković argued that gold standard adoption was required by Yugoslavia's international financial relations: "The move onto gold is not demanded by us, but comes from abroad."[199] The newspapers *Privredni Pregled* added in 1930 that a mere de facto stabilisation was insufficient because international financiers would only respect a currency pegged to gold.[200] This indicates that there was a substantial pressure for gold standard adoption in order to borrow internationally. In the phase when gold standard adoption started seriously being considered from 1926 onwards, the efforts for obtaining international loans were focused on the UK, France and Switzerland where the Yugoslavian authorities mainly cooperated with the Bank of England, the Banque de France and the Bank for International Settlements in Basel. The interactions between Yugoslavian policy-makers and these three institutions will hence be examined in this respect. This will show that not only were loans conditioned on gold standard adoption, but that international lenders conveyed a gold standard ideology to Yugoslavian policy-makers, presenting it as something any advanced country should strive for.

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198 'Letter to Shareholders', NBS, ANB-1/I-58-1.
199 J. Marković, Legal Stabilisation of our Money', *Bankarstvo* (October 1930), p. 435.
200 'In the wake of significant events in the National Bank', *Privredni Pregled* (17th August 1930).

Interaction with the Bank of England

In 1926, NBKY Director Novaković travelled to London and Paris to apply for loans at the Bank of England and the Banque de France, as well as to seek advice on legal stabilisation. Upon his return, he received a letter from Governor of the Bank of England Norman in which the latter recommended principles for central bank operation:

> It appears to me that our principal concern as central banks of emission has to be stabilisation in the widest sense of the word, and that for your country, stabilisation in the first place means a monetary *de jure* stabilisation. If you desire collaboration and advice from the Bank of England for the end of elaborating and managing such a program which, earlier or later, must be adopted, I am ready to give you my personal assurance that we will be quick to help you in the general interest."[201]

Apparently, Norman directly called on the NBKY to adopt the gold standard, presenting it as a necessity, and a benefit to the international community. The letter continues as follows:

> "It is clear that your country is in the first place an agrarian one which leads to fluctuations of the exchange rate. This endangers the stability of the dinar. If an arrangement is found for your debts, the Bank of England would be willing to discuss a loan commencing on 1st March 1927 for the purpose of currency stabilisation […]."[202]

Hence, next to reiterating the necessity of legal stabilisation, the Bank of England provided the prospect of a loan in case the Yugoslavian government implements it. Norman also mentioned that given the government loan at the NBKY, Yugoslavia would necessarily have to borrow internationally to adopt the gold standard, as it was eventually done. Later in the letter, a consultation is offered to the NBKY on how to prepare for legal stabilisation technically, and by influencing public opinion. However, as the quote above shows, any support by the Bank of England was conditioned on the repayment of previous debts. A report by NBKY Director Novaković shows that a further condition was that reserves were to be stored in London.[203]

What were the views of Yugoslavian officials on this cooperation? NBKY Director Novaković reported that by lending for gold standard adoption as it had done in Austria, Hungary and Belgium, the Bank of England was trying to establish the position of London as the world's principal financial market.[204] Furthermore, there was a view among Yugoslavian policy elites that

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[201] Letter from the Bank of England to the NBKY governor, 3rd December 1926, NBS, ANB-1/I-58-1.
[202] *Ibid.*
[203] 'Report of NBKY Director Novaković about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.
[204] *Ibid.*

the Bank of England was ideologically motivated. Economist Bajkić wrote about an Anglo-Saxon free capital market ideology which led British and US authorities to categorise countries into first- and second-class ones depending on whether they had legally stabilised their currencies. This Anglo-Saxon ideology would incentivise them to give out international stabilisation loans.[205] Similarly, Director Novaković reported that there was an agreement between the Bank of England and the Federal Reserve that international cooperation between central banks should be increased in order to help them with adopting the gold standard.[206] However, Yugoslavian policy-makers were willing to accept this ideology, as well as most of the conditions set by the Bank of England in exchange for loans. Novaković recognised that "a loan would be approved only if the NBKY and the government declare their intention to complete a programme for currency stabilisation without further delays", but that it was demanded in the House of Commons that all previous loans (especially private loans taken up by Yugoslavian merchants in Britain) were regulated.[207] In a calculation of the costs for adopting the gold standard from 1926, the NBKY incorporated the settlement of Yugoslavian loans to England which amounted to 150 million dinars (the total costs of adoption were estimated to 1.5 billion dinars).[208] This indicates a willingness to repay old debts. In 1926, Novaković described the demanded exclusive cooperation on loans with the Bank of England as possible, but in terms of depositing reserves exclusively in London, Yugoslavian authorities were reluctant, stating towards the Bank of England that they planned on storing bank deposits internationally.[209] Presumably this is why the cooperation between the NBKY and the Bank of England deteriorated. In a 1928 GAC meeting, it is reported that the Bank of England rejected almost all suggestions made by the NBKY and the Finance Minister in terms of agreeing on further cooperation, which eventually terminated at least in terms of the stabilisation loan.[210] Nevertheless, the Bank of England had played a decisive role in the early years of the debates surrounding the gold standard conveying that it would have to be adopted in order to receive loans, and because it was something any country and central bank should strive for.

Interaction with the Banque de France

France had longstanding financial links in the Balkans. Lampe argues that while foreign banks avoided setting up branches in the region throughout the 19th century, several large banks opened branches in Bucharest and Sofia with French support after 1905. Major Paris houses began

[205] V. Bajkić, 'Concerning Legal Stabilisation', *Narodno Blagostanje* (13th September 1930).
[206] 'Report of NBKY Director Novaković about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.
[207] *Ibid.*
[208] 'Letter Draft which should be sent to the Bank of England', 1926, NBS, ANB-1/I-58-1.
[209] 'Report of NBKY Director Novaković about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.
[210] 'Minutes of the 19th GAC meeting', 5th July 1928, NBS, ANB-1/I-58-1.

handling the majority of post-1900 bond issues for Balkan states and underwrote 461 million francs borrowed by Bulgaria and 312 million by Serbia between 1902 and 1912.[211] Yugoslavia's first international loan was concluded in France in 1919 and was used for the purpose of backing the bank notes in circulation with gold reserves.[212] This loan together with further French loans inherited from Serbia resulted in an indebtedness to France which created a peculiar pressure to adopt the gold standard. Once France went on the gold standard, its international debtors were demanded to repay loans in gold. Yugoslavia was directly pressured and sued by French lenders in that respect. The Permanent International Court of Justice in The Hague ruled on 12th July 1929 that the substantial Yugoslavian debts owed to French lenders ought to be repaid to 55% in gold starting from 1st April 1930 while the share of gold should gradually increase until the loans are completely repaid in gold.[213] Having a gold-pegged currency which was stable compared to the Franc would allow Yugoslavia to have stable conditions for loan repayments in real terms which put pressure on policy-makers to adopt the gold standard.

However, next to this indirect pressure, French policy-makers were also more direct in their demands on Yugoslavia. It appears that in 1931, France was only willing to lend to Yugoslavia for the purposes of gold standard adoption. The most important loan granted for this purpose was the 1.025-billion-franc stabilisation loan in May 1931, for which the negotiations had already begun in 1926, meaning before France had adopted the gold standard itself as the report by Director Novaković shows.[214] Importantly, one fourth of the stabilisation loan was used for investing into public works which meant that in exchange for implementing the gold standard, the Yugoslavian government could invest into economic development.[215] The Banque de France also proved willing to support Yugoslavia in the maintenance of the gold standard, for example by providing two-thirds of a 3-million-USD-loan provided by the BIS in July 1931 which was used for the acquisition of foreign exchange. Yugoslavia also received another loan in October 1931 directly from the Banque de France for the purpose of reserve acquisition which NBKY Governor Bajloni viewed as a sign of French amicability towards Yugoslavia:

> "He had the impression that we would immediately receive help, and we received it to the amount of 285,000,000 dinars. Similar aid would be provided in the future and the Governor believes that the Banque de France will not abandon us."[216]

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211 Lampe and Jackson, *Balkan Economic History, 1550-1950: From Imperial Borderlands to Developing Nations*, pp. 225-227.
212 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 165.
213 Gnjatović, 'The Experience of Exchange Rate Regimes in Southeastern Europe in a Historical and Comparative Perspective', p. 342.
214 'Report of NBKY Director Novaković about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.
215 'Explanations of the new Loan', *Narodno Blagostanje* (16th May 1931).
216 'Minutes of the 6th GAC meeting', 5th October 1931, NBS, ANB-1/II-30.2.

Interestingly, while the Banque de France was willing to grant loans for preserving gold convertibility in Yugoslavia, it rejected a smaller loan solely for public works which the Governor applied for at the same occasion in October 1931. This indicates that French authorities had an interest in the maintenance of the Yugoslavian gold standard in particular.[217] Altogether, it appears that France was willing to continuously extend loans to Yugoslavia which were either conditioned on gold standard adoption (such as the stabilisation loan), or connected to the maintenance of the gold standard (such as the two loans from 1931), without demanding that previous loans are repaid before stabilisation loans are concluded in France.[218]

Next to conditioning loans on adopting and maintaining the gold standard, there are also indications for an "ideological pressure" for gold standard adoption just as the Bank of England exerted it. The newspapers *Privredni Pregled* quoted the Vice-Governor of the Banque de France Furnier, who had fought together with Serbian soldiers at the National Front in the First World War, during a speech at a bank opening in Belgrade where he praised improvements in public finances (presumably after the Yugoslavian tax reform):

> "But you know that the results, however important they might be, remain incomplete as long as stability does not become law, as long as a law does not determine the final value of your money and until the convertibility of your bank notes into gold is not secured."[219]

This position appears similar to the one authorities of the Bank of England voiced towards the NBKY. The implementation of the gold standard was presented as a logical step in the work of central banks and as the next crucial step in the economic development of a country in general.

Which motives were recognised behind the willingness of the Banque de France to channel public and private funds towards Yugoslavia for maintaining the gold standard? One could point out the country's concern for the repayment of its gold-denominated loans. However, the French actions were also viewed as serving two political goals. According to Killen, France wanted to preserve the economic and territorial arrangements arrived at after the World War, and especially the solution for German reparation settlements for which the government sought allies in the Balkans.[220] This view was echoed in Yugoslavian newspapers. In an article titled "French Gold on the Balkans" in *Privredni Pregled*, the author argued that with its lending practices, France was trying to build a new Middle Europe as French bankers would require political guarantees before giving out loans. The main goal of France was to isolate Germany economically, and thus politically. The

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[217] 'Minutes of the 6th GAC meeting', 5th October 1931, NBS, ANB-1/II-30.2.
[218] 'The Stabilisation Loan', *Vreme* (9th May 1931).
[219] 'Institution for Note Issuance', *Privredni Pregled* (2nd February 1930).
[220] L. Killen, *Testing the Peripheries: US-Yugoslav Economic Relations in the Interwar Years*, (New York, 1994), p. 125.

article also maintained that the resignation of Finance Minister Schober in Austria was enforced by France in order to prevent an Austro-German customs union by threatening to cancel a loan they had announced, which in the end was not granted at all.[221] Another article argued that in order to borrow in France, countries had to subordinate their policies to the French dictate. The resignation of Count Bethlen in Hungary was also presented as being enforced by France in order to isolate Germany by withholding loans.[222]

The second political objective of French lending practices connected to the gold standard was the containment of British power on the Balkans. According to Mouré, the Governor of the Banque de France Moreau was angered about negotiations for a stabilisation loan between the Bank of England and the NBKY in 1928 as France had a longstanding diplomatic influence in the region and saw its political influence at stake.[223] In fact, this is already reflected in 1926 during a visit of NBKY Director Novaković to Paris where the NBKY is warned from entering exclusive arrangements for a stabilisation loan with the Bank of England:

> "The Banque de France said that arrangements should not only be realised with the Bank of England, but also the Federal Reserve and the Banque de France. Moreau even suggested to be the intermediary between the NBKY and the Fed so we receive the same lending conditions as the Banque de France would."[224]

Apparently, there was a fear of growing British influence in Yugoslavia through the support with gold standard adoption. This view was adopted in the NBKY as well. As mentioned above, GAC member Šumanović argued that the loans given out during the Great Depression were purely politically motivated. Altogether, the Banque de France exerted both a direct pressure (as exemplified by the conditioning of loans on maintaining the gold standard), as well as an ideological pressure (as exemplified by the speech of Vice-Governor Furnier) on Yugoslavia to adopt the gold standard, while it seems plausible to assume a political motivation behind these practices to some extent.

Interaction with the Bank for International Settlements

The BIS in Basel was founded through an agreement between the governors of the central banks of Belgium, France, Germany, Italy, Japan, Switzerland and the UK on 27th February 1930 in Rome. The primary initial purpose of the BIS was to commercialise German reparation

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221 'French Gold on the Balkans', *Privredni Pregled* (6th December 1931).
222 'What does France want?', *Privredni Pregled* (4th October 1931).
223 Mouré, *The Gold Standard Illusion: France, the Bank of France and the International Gold Standard, 1914-1939*, p. 167.
224 'Report of NBKY Director Novaković about his trip to London and Paris', 20th December 1926, NBS, ANB-1/I-58-1.

payments, i.e. issue German debt as long-term bonds, as was laid out in the Young Plan from June 1929.[225] Further functions included fostering cooperation between central banks and providing them with credit, accepting deposits, and carrying out currency and gold operations on their behalf.[226] The bank also aimed at ensuring a stable system for international payments which meant restoring the gold standard.[227] In the words of Toniolo, "the gold standard was embedded in the very DNA of the BIS".[228] The BIS board reportedly viewed it as the best available monetary mechanism for enabling the free flow of international financing.[229] Hence, any bank which applied for membership at the BIS by acquiring its shares had to operate with a national currency pegged to gold. This put pressure on governments to pursue gold standard adoption. For example, *Privredni Pregled* presents the legal stabilisation of the Czechoslovak crown as purely motivated by a wish to join the BIS.[230] The BIS also actively supported central banks in gold standard adoption and conditioned the provision of loans on the maintenance of the gold standard. When the Spanish government wanted to legally stabilise the peseta, the government approached the BIS for advice and a loan.[231] The President of the BIS McGarrah and General Manager Quesnay informed the Spanish delegation that a loan would only be approved once Spain had adopted the gold standard. The BIS also conditioned a 2-million-pound advance on Spain depositing 1 million pounds worth of gold in London which was criticised as an unacceptable interference with the country's national economic policies by Spain.[232] Interference into internal economic policies by the BIS would also be characteristic of its connection to the Yugoslavian government and the NBKY.

Yugoslavia showed an interest in becoming a member of the BIS already before it was founded. While the conferences surrounding the foundation of the BIS were being held in 1930, an article in *Privredni Pregled* presented the BIS as a significant new factor in global banking and the biggest financial institution in history.[233] Membership in the BIS was viewed as a measure for increasing the country's influence on global financial affairs, as later expressed by Governor Bajloni:

> "The National Bank will assume an active role in the work of the BIS. Our voice will be heard when global financial and economic questions are being debated."[234]

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[225] Toniolo, *Central Bank Cooperation at the Bank for International Settlements, 1930-1973*, p. 32-35.
[226] *Ibid.,* pp. 24-27.
[227] *Ibid.*, p. 3.
[228] *Ibid.*, p. 131.
[229] *Ibid.*, p. 135.
[230] 'The Czechoslovak Monetary Reform', *Privredni Pregled* (24th August 1930).
[231] C.E.V. Borio and G. Toniolo, 'One Hundred and Thirty Years of Central Bank Cooperation: A BIS Perspective', *IDEAS Working Paper Series* (2006), p. 10.
[232] Toniolo, *Central Bank Cooperation at the Bank for International Settlements, 1930-1973*, p. 80.
[233] 'The Bank for International Settlements', *Privredni Pregled* (16th March 1930).
[234] 'Monthly Chronicles', *Bankarstvo* (June 1931).

While section 6 examines the reasons for the Yugoslavian belief in internationalism, the quote illustrates that Yugoslavian authorities had an interest in joining the BIS, which in itself was a contributing factor for adopting the gold standard as the BIS made it clear in a letter from BIS directors Huelse and Van Zeeland that relations would only be established with markets in which the national currency was pegged to gold.[235] In June 1930, the BIS board authorised the NBKY to subscribe to a maximum of 4,000 shares. The transaction was "to have effect as soon as they have satisfied the President that an adequate currency stabilisation plan has been brought into effect".[236] According to Yugoslavian economist Bajkić, during a visit to Belgrade in September 1930, General Manager of the BIS Quesnay "acknowledged the participation in the BIS of our bank", but added that the transaction of BIS shares would only be finalised after legal stabilisation.[237] Hence, the BIS conveyed the view to Yugoslavian authorities that Yugoslavia was a BIS member early on, but conditioned the formal acceptance to legal stabilisation which can be interpreted as a pressure on Yugoslavian policy elites to adopt the gold standard.

The BIS also pressured for the maintenance of the gold standard through deflationary policies once it was implemented in exchange for loans. As soon as Yugoslavia officially became a BIS member by joining the gold standard in June 1931, it turned to the BIS with the request for a loan. Against the background of the cancellation of German reparation payments, BIS representative Bolgert recommended granting a 3-million-USD-loan to Yugoslavia specifically for the maintenance of the gold standard after visiting Belgrade.[238] Due to its moderate size, the loan was only a temporary solution for sustaining the cover ratio. However, organising even this small loan proved difficult against the background of economic recession in Europe. Correspondences between the BIS board and central banks show that the latter were reluctant to participate in the Yugoslavian loan. For example, the National Bank of Czechoslovakia offered 500,000 dollars regretting not to be in a position under present conditions to raise participation given that foreign exchange reserves were decreasing.[239] Banque de France Governor Moreau complained to the BIS that the Banque de France was not mentioned in official documents about the Yugoslavian loan, but attributed it to the fact that the BIS was unable to find any other lenders which prevented the finalisation of the loan.[240] Furthermore, the BIS was faced with outrage from previous lenders to

[235] Letter from Directors Huelse and Van Zeeland to the NBKY, 11th August 1930, BIS, ABIS-CH-000583-8-A.BISA.2.10.

[236] 'Extract from the first meeting of the Board of Directors', 16th June 1930,BIS, ABIS-CH-000583-8-A.BISA.6.11.a.

[237] V. Bajkic, 'Concerning Legal Stabilisation', *Narodno Blagostanje* (13th September 1930).

[238] Toniolo, *Central Bank Cooperation at the Bank for International Settlements, 1930-1973*, p. 99.

[239] Letter from the National Bank of Czechoslovakia to the BIS Governor, August 1931, BIS, ABIS-CH-000583-8-A.BISA.6.35.

[240] Letter from Governor Moreau to BIS President McGarrah, 10th August 1931, BIS, ABIS-CH-000583-8-A.BISA.6.35.

Yugoslavia. The Permanent Commission for the Interests of German Foreign Bond Holders wrote to the Governing Council of the BIS that it should refrain from granting a loan before Yugoslavia repaid its German loans.[241] The Union des Financières de Genève and the Swiss National Bank issued the same complaint to the BIS.[242] Eventually, on 30th July 1931, it succeeded with the support of the Banque de France which provided 2 million USD, while 1 million was provided by the BIS. This credit allowed for raising the Yugoslavian cover ratio above the legally required minimum of 35% to 37.8% and shortly preserved the gold standard.[243]

However, next to credits only being granted for the maintenance of the gold standard, the BIS worked out a well-defined set of policies which it wanted to see implemented in Yugoslavia to ensure it. This is exemplified by a BIS report which recommended central banks to help Yugoslavia cope with the difficulties caused by the economic crisis, "[b]ut only if the NBKY makes efforts to justify this intervention."[244] According to a BIS report on the Yugoslavian monetary situation, the biggest threat to the Yugoslavian gold standard were not foreign exchange outflows, but internal credit demands and potential cancellations of foreign loans to Yugoslavia.[245] In two BIS reports from July and August 1931, the BIS suggested policies divided into internal and external ones, in order to address the identified problems. The first internal policy suggestion focused on credit restrictions. As a first measure for restricting credits, the BIS proposed an increase of discount rates, arguing that the raise from 6.5% to 7.5% in July 1931 was insufficient. The second policy suggestion pertained to Lombard credits granted directly to firms by the NBKY. The BIS criticised that while 2.3 billion dinars of credits were approved, only 1.3 billion were utilised in July 1931.[246] This was interpreted as an excess credits provision, and not as an indication of credit conditions being too unfavourable for credit institutes and commercial enterprises to apply for them. The BIS suggested a reduction of interior credits (both Lombard loans and rediscounts to the banking system) by 20% (or 270 million dinars) until the end of 1931. It was argued that this rapid restriction would make credit applicants more prudent.[247] The report also noted that the NBKY seemed receptive to this proposition. Indeed, the NBKY accepted this policy:

> The BIS insists that we take the necessary measures for reducing our credit provision, so that at the end of the year the amount of credits is 20% lower than the credits which are used up today."[248]

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241 Letter from the Permanent Commission for the Interests of German Foreign Bond Holders to the Governing Council of the BIS, 3rd July 1930, BIS, ABIS-CH-000583-8-A.BISA.6.11.a.
242 'Stabilisation of the Yugoslavian Currency', 10th July 1930, BIS, ABIS-CH-000583-8-A.BISA.6.11.a.
243 Toniolo, *Central Bank Cooperation at the Bank for International Settlements, 1930-1973*, p. 99.
244 'Report on Yugoslavia', 31st July 1931, BIS, ABIS-CH-000583-8 A.BISA.3.2.w.
245 *Ibid.*, p. 7.
246 'Report on Yugoslavia', 1st August 1931, BIS, ABIS-CH-000583-8 A.BISA.6.11.a., p. 10.
247 *Ibid.*, p. 12
248 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.

In a telephone conversation from 1st August 1931 between NBKY Governor Bajloni and BIS Assistant Manager Royot, the former confirmed that the demanded credit restrictions were approved by the GAC and would be implemented. The NBKY would register an increased demand for credits which it refused in order to adhere to the conditions set out by the BIS. Bajloni even demanded an increase of the BIS loan to 5 million USD given that foreign exchange reserves were again diminishing.[249] Apparently, the BIS was monitoring whether the NBKY was implementing the demanded policies. However, the BIS did not only demand deflationary policies from the NBKY, but also the Yugoslavian government, asking it to refrain from borrowing at the NBKY:

> "The state is allowed to receive 600 million of seasonal loans [from the NBKY]. It should be pointed out to the Finance Minister that this should be limited."[250]

The BIS also suggested the government to further exploit monopoly rents from Yugoslavia's Tobacco monopoly which generated two-thirds of the overall monopoly income.[251] In terms of external policies, the BIS set the condition that the Yugoslavian government had to apply for further international loans for the acquisition of foreign exchange reserves. This was done and a further 300,000-franc-loan was obtained in France.[252]

These were only some policies which the BIS demanded the NBKY to implement in exchange for a loan and which were broadly targeted at sustaining the Yugoslavian gold standard, but they already illustrate the substantial interference in Yugoslavian economic policies it exerted, just as it previously had done in Spain. In fact, the deflationary policies for sustaining the gold standard which aggravated the effects of the Great Depression in Yugoslavia (section 4.1) were to large parts implemented because the BIS demanded them for the sustainance of the gold standard. It had leverage for exerting pressure on Yugoslavia for implementing them because the loan it granted had to be renewed every three months by the BIS board. It was decided only in February 1934 that the renewal of the loan was to be granted merely at the discretion of the BIS President.[253]

A striking feature of BIS conditionality for short-term loans is its resemblance to the conditionality of League of Nations long-term loans from the early 1920s. According to Flores and Decorzant, the League of Nations demanded a reorientation of economic policies prior to granting a credit and monitored the implementation of the demanded conditions after granting them,

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[249] Minutes of telephone conversation between NBKY Governor Bajloni and BIS Assistant Manager Royot, 1st August 1931, BIS, ABIS-CH-000583-8 A.BISA.3.2.w.
[250] 'On the Monetary Situation of Yugoslavia', 18th July 1931, BIS, ABIS-CH-000583-8 A.BISA.3.2.w.
[251] Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923*, p. 107.
[252] 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.
[253] 'Resolution No. 470', 12th February 1934, BIS, CH-000583-8 A.BISA.6.35.

thereby limiting the sovereignty of countries.[254] Once the gold exchange standard was widespread, fixed exchange clauses entered loan contracts between the League of Nations and borrowers, just as it was done by the BIS.[255] The BIS conditionality also resembles the conditionality of IMF loans, which according to Flores and Decorzant was inspired by League of Nations. The IMF often recommended establishing a fixed exchange rate system (such as in its stand-by-arrangement with Chile in 1958). The variable to be controlled by governments as specified in IMF stand-by-arrangements after 1963 was "net domestic credit of central banks to the banking system", covering both central bank loans and rediscounts to the banking system, just as it was the case with BIS conditionality.[256] While stand-by-arrangements limited private and public borrowing, central banks were encouraged to borrow abroad. For example, in Argentina the central bank was encouraged to apply for credits worth 900 million USD internationally in 1976 and 1977 while limits were demanded for other international borrowing, which resembles the demand by the BIS that the NBKY should apply for public loans abroad.[257] Hence, BIS lending practices in Yugoslavia were similar to requirements demanded by international lending institutions before and after the Second World War.

The conditionality applied by the BIS was met with resistance in Yugoslavia, which adds credibility to the view that the conditions were largely implemented on demand by the BIS. In a letter to BIS President McGarrah from 1st August 1931, NBKY Governor Bajloni noted that while his bank did everything possible to implement the demanded policies for maintaining the gold standard, the NBKY would also have to consider the vital interests of the Yugoslavian economy.[258] In another letter, he was even more explicit, stating that he repeatedly pointed out to the BIS board that the NBKY cannot only "account for the monetary situation, but also protect[s] the vital interests of our national economy", which is striking given that the NBKY did not have a mandate for improving the performance of the real economy.[259] The 10% discount rate which the BIS demanded was met with stern resistance in Belgrade:

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[254] J.H. Flores and Y. Decorzant, 'Going Multilateral? Financial Markets' Access and the League of Nations Loans, 1923–8', *Economic History Review* 69.2 (2016), p. 657.
[255] *Ibid.*, p. 658.
[256] S. Marshall et al., 'IMF Conditionality: The Experiences of Argentina, Brazil, and Chile', in: J. Williamson, *IMF Conditionality* (Washington, 1983), p. 280.
[257] *Ibid.*, p. 287.
[258] Letter from NBKY Governor Bajloni to BIS President McGarrah, 1st August 1931, BIS, ABIS-CH-000583-8 A.BISA.6.35.
[259] Letter from NBKY Governor Bajloni to BIS President Fraser, 6th November 1931, BIS, ABIS-CH-000583-8 A.BISA.6.35.

> "The conditions the BIS demanded were hard, which is why the negotations took so long. At first, it was demanded that we increase our official discount rate again, which we had raised twice in the last weeks, namely to 10%, just like Austria. This demand was abandoned thanks to our stern insistence."[260]

NBKY representatives resisted as strongly because they feared that interior markets would become too unstable which would result in fire-sales of dinars if the discount rate was increased again.[261] GAC members Radović and Berković argued that Yugoslavia's international creditors would not understand that the theory demanding interest rate increases in large economies, was not applicable for small economies where raises had disproportionally large effects on the economy.[262] In fact, the demanded tightening of credits was temporarily suspended in October 1931. The BIS accepted this under the premise that the NBKY was under severe pressure from domestic commercial banks whose existence was threatened by these policies.[263] GAC member Milanović argued that the credit restrictions were demanded at a time when these were urgently needed in the economy.[264] Due to the strict conditions demanded for maintaining the gold standard in exchange for loans, the BIS was also increasingly viewed critically in Yugoslavian economic circles. Economist Bajkić described the BIS as infiltrated by an exaggerated Anglo-Saxon free-market ideology which placed excessive importance on the maintenance of the gold standard. He argued that because the BIS exerted substantial pressure on Yugoslavia to legally stabilise, the country should try to borrow privately in the USA instead of approaching the BIS.[265]

To sum up, just as the Bank of England and the Banque de France, the BIS exerted pressures on Yugoslavia for gold standard adoption. The initial pressure was exerted by offering membership under the condition of gold standard adoption. Once Yugoslavia became a member, a loan was granted in exchange for deflationary policies necessary for maintaining the gold standard. While the motivations of all three institutions were viewed critically in Yugoslavia, authorities were willing to overlook them in favour of receiving loans. This sub-section has shown that the "rush" to adopt the gold standard to gain better access to international loans (section 5.1), even if better borrowing conditions were unlikely to be realised as argued in section 3.1, was partially justified given the demands and recommendations of foreign lenders. More generally, this shows that for a peripheral economy like Yugoslavia, external influences constrain the set of policy-choices which explains decisions that at first glance seem incomprehensible. Therefore, a realist

[260] 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.
[261] 'Report on Yugoslavia', 1st August 1931, BIS, ABIS-CH-000583-8 A.BISA.6.11.a.
[262] 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.
[263] 'Renewal of credit to the NBKY', 12th October 1931, BIS, CH-000583-8 A.BISA.6.35.
[264] 'Minutes of the 4th GAC meeting', 31st July 1931, NBS, ANB-1/II-30.2.
[265] V. Bajkić, 'Concerning Legal Stabilisation', *Narodno Blagostanje* (13th September 1930).

perspective on gold standard adoption as a strategic interplay of institutions with different interests and different bargaining powers, proves valid in the Yugoslavian case.[266] However, while this explains why policy-makers saw a particular economic upside of the gold standard, it remains curious why they were ignorant towards the economic downsides, such as the advantages of a flexible exchange rate system, or the detrimental effect of deflationary policies. This ignorance can be explained by referring to the state of economic knowledge in Yugoslavia.

5.2.2 Internal factors: The State of Economic Knowledge

Straumann argues that the flawed macroeconomic models of policy makers played a central role in gold standard adoption in small European economies.[267] For example, Belgian, Dutch and Swiss policy-makers questioned the benefits of flexible exchange rates and argued that devaluation would only deteriorate their situation.[268] Deflation was furthermore viewed as an appropriate way for mitigating economic distortions.[269] In some countries, these beliefs were so strong that policy-makers failed to see the economic benefits of devaluation experienced by countries, for example after the United Kingdom left the gold standard in September 1931.

Yugoslavian policy elites exhibited similar economic misjudgements and used flawed macroeconomic economic models from today's perspective as described by Straumann. Firstly, the judgement on the ability to maintain a gold standard against the economic background depicted in section 4 was flawed. Secondly, there was a widespread belief that the deflationary policies which were necessary for the maintenance of the gold standard were appropriate for mitigating the economic crisis. GAC member Radović explained that such policies had a beneficial effect during economic crises because they limited peoples' spending on luxury items abroad and improved the current account.[270] Thirdly, among bank officials, there was a lack of understanding how changes in the discount rate are transmitted to the real economy. In 1932, the NBKY Governor wrote to the Finance Ministry that "it remains to be seen what the banks will do with the discount rate if we raise it […]. The raises for smaller bank clients are insignificant."[271] Against this stands the contention from a newspaper article in *Privredni Pregled*, which reported that after a temporary lowering of the discount rate in 1930, private rates directly followed suit and eased the performance of the national economy.[272] As I argue in section 7, there was also a widespread view in the population that interest rates for small bank clients rose substantially with the discount rate. Finally,

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[266] Frieden, *Currency Politics: The Political Economy of Exchange Rate Policy*, p. 15.
[267] Straumann, *Fixed Ideas of Money: Small States and Exchange Rate Regimes in Twentieth-century Europe*, p. 10.
[268] *Ibid.*, p. 61.
[269] *Ibid.*
[270] 'Minutes of the 5th GAC meeting', 5th September 1931, NBS, ANB-1/II-30.2.
[271] Letter from NBKY governor Bajloni to the Finance Ministry, 15th January 1932, NBS, ANB-1/1-58-1.
[272] 'Our Banks in the Wake of 1931', *Privredni Pregled* (4th January 1931).

the fourth misjudgement relates to the ignorance of Yugoslavian policy makers towards the benefits of a flexible currency, which had to be forgone with the adoption of the gold standard as explained using the impossible trinity in section 2. In his 1925 essay *The Economic Consequences of Mr. Churchill*, Keynes provided an elaboration why the gold standard was inferior to a system of flexible exchange rates. He argued that the high value at which the pound was pegged to gold encouraged imports and harmed export industries which led to unemployment and neutralised the positive effects of the gold standard.[273] The credit restrictions required by the "rules of the game" were another source of unemployment because they deprived employers of the possibility to hire workers.[274] In his 1931 essay *The End of the Gold Standard*, Keynes analysed the positive effects of the British abandonment of the gold standard. He argued that if sterling depreciates by 25%, this would restrict imports just as a tariff, while it fostered exports.[275] It would therefore be no wonder that Englishmen "rejoice at the breaking of our gold fetters".[276] Keynes's views were widely rejected in Yugoslavia. Velimir Bajkić, one of the country's most prominent economists, elaborated on them in the newspapers *Narodno Blagostanje*, which he owned and edited. Against the alleged benefits of devaluation, he argued the following:

> Keynes is wrong if he believes that prices will rise for countries abroad while domestic prices stay the same. […] [T]he depreciation of the currency means a lowering of the purchasing power, it means that prices jump. Only as long as prices don't adjust an export premium exists, but this process is fast."[277]

Hence, he argued that prices would adjust too fast through higher foreign demand for a benefit from currency devaluation to materialise. Bajkić further maintained that it was too difficult to construct a reliable price index which could be targeted under flexible exchange rates.[278] In November 1931, Bajkić's newspapers *Narodno Blagostanje* wrote that Keynes was proven wrong by the increase in the value of imports in the UK from 68.3 million pounds in September to to 80.7 million in October.[279] Furthermore, UK prices would have risen by 10-20%.[280] Other newspapers echoed the disbelief in Keynes's theory. *Privredni Pregled* wrote that the British decision to abandon the gold standard and lower the cover ratio constituted an epochal reform in the global gold standard system. The article concluded that this move would simply cause inflation because the

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273 J.M. Keynes, *The Economic Consequences of Mr. Churchill* (London, 1925), p. 15.
274 *Ibid.*, p. 18.
275 J.M. Keynes, 'The End of the Gold Standard', in: *Essays in Persuasion* (London, 2010), p. 245.
276 *Ibid.*
277 V. Bajkic, 'What England loses by leaving the Gold Standard', *Narodno Blagostanje* (10th October 1931).
278 *Ibid.*
279 'Events and Problems', *Narodno Blagostanje* (November 1931).
280 Bajkić, 'What England loses by leaving the Gold Standard'.

Bank of England would now increase credit provision while this should only be done if production rises.[281] Apparently, the article dismisses the central causality from Keynesian economics that economic performance improves with credit provision. From this perspective, the British decision was viewed as incomprehensible. For example, on 4th October *Privredni Pregled* wrote that "it is curious that this measure which is usually presented as almost unnormal is being received with so much excitement in England".[282] The decision itself was generally viewed as either involuntary or irrational. Economic journalists cited Britain's passive trade balance, the maldistribution of global gold reserves, socialist pressures in Britain, the British mistake to lend to Germany which experienced a banking crisis, and a widespread misunderstanding of the quantity theory of money among British bankers, as reasons why the gold standard was abandoned. It was assumed that the move was only temporary and limited to six months.[283] In fact, *Narodno Blagostanje* soon discussed at which exchange rate the UK would re-adopt the gold standard.[284] Altogether, the prevalent theories in economic circles in Yugoslavia did not speak in favour of flexible exchange rates, and thus corroborated the belief in the gold standard. This is probably also the reason why the abandonment of the gold standard in Britain and other countries was not viewed as a reason to question the Yugoslavian gold standard. In a review of 1931, the NBKY depicted the British abandonment as an unfortunate event that destroyed the faith of depositors and required an urgent reaction by the NBKY.[285] The maintenance of the gold standard itself was not questioned. Economic journalists similarly viewed abandonments in other countries as unfortunate events without drawing conclusions about the viability of the gold standard itself. The case of Japan was traced back to a passive trade balance and fears from cheap British imports in Japanese industry.[286] The adoption of the silver standard in Mexico was viewed as the effect of an attack on the gold standard by the USA and France.[287] Hence, while during the period of gold standard adoption, the decisions of other countries served as bases for institutional innovations as was explained in section 4, this way of institutional learning was abandoned while other countries were going off gold.

Altogether, the from today's perspective deficient economic knowledge of policy-makers which manifested itself in misassessments in terms of the ability to sustain the gold standard, the view that deflationary policies can mitigate economic crises, and the ignorance about the benefits of flexible exchange rates, contributed its part to the adoption of the gold standard. This meant that just as Straumann identified it for various other periperhal European economies, Yugoslavian

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281 'England adopts an elastic system of gold coverage', *Privredni Pregled* (16th August 1931).
282 'The future level of stabilisation of the British pound', *Privredni Pregled* (4th October 1931).
283 'Optimism returns', *Privredni Pregled* (27th September 1931).
284 'The falisified Gold Standard or the Revenge of healthy Money', *Narodno Blagostanje* (24th October 1931).
285 'Minutes of the shareholder meeting', 17th February 1932, NBS, ANB-1/II-30.2.
286'The Abandonment of the Gold Standard in Japan', *Narodno Blagostanje* (19th December 1931).
287 'Bimetallism and the Economic Crisis', *Privredni Pregled* (2nd August 1931).

policy-makers underestimated the opportunity costs involved in this monetary system, and rather focused on the benefits it promised such as improved opportunities for foreign borrowing, which were indicated to them by foreign lenders. Moving from economic to polical motivations, the next section examines reasons for gold standard adoption that go beyond economic rationales.

6 Political Rationale for the Yugoslavian Gold Standard

6.1 Prestige and the Yugoslavian Gold Standard

As explained in section 3.2, in Italy Mussolini viewed a gold standard with a currency pegged to gold at a high exchange rate as indicating his country's superiority.[288] This view was also widely held in Yugoslavia. Economist Bajkić presented the interwar gold standard as a success which prewar Serbia could not achieve.[289] This view was also adopted in *Privredni Pregled* to express the superiority of Yugoslavia:

> "With the law on money from the 11th we are getting a gold value that we have never had in its true sence before, that neither prewar Serbia nor Austria-Hungary had, and that even today Czechoslovakia and Italy do not have. And therefore, caution becomes an even holier duty. What we have today, we have to preserve at any cost."[290]

The article furthermore argued that Italy still maintained capital controls, making the Yugoslavian gold standard superior. Hence, a gold standard without capital controls was viewed as worth preserving for the sake of signalling prestige. This could explain why the Finance Ministry insisted on abandoning capital controls after legal stabilisation while the economic preconditions for this were not given, as was explained in section 4. Popular newspapers such as *Politika* or *Vreme* joined into the prestige rhetoric. The newspapers *Politika* presented the gold standard as something neither former Serbia, nor Austria-Hungary had.[291] Hence, especially the reference to prewar Serbia which failed to move from a bimetallic standard to a gold standard before the First World War was remembered in Yugoslavia. Similarly, economist Bajkić described the law mandating gold convertibility from 1878 as "dead words" because insufficient gold reserves prevented convertibility and silver money was introduced in 1885 which drove gold money out of circulation.[292]

Recalling the argument from section 3.2 that prestige signalling can be used for specific political purposes, it appears that the Yugoslavian government was in need of signalling fast economic successes to legitimise itself in 1931. Yugoslavia had experienced a political polarisation towards the end of the 1920s. Especially the pronounced political centralisation and the dominance of Serbian elites resulted in a sustained dissatisfaction in other regions of the Kingdom. Parliament increasingly witnessed insulting debates, with the Croatian Peasants' Party taking the strongest

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[288] James and O'Rourke, *Italy and the First Age of Globalization, 1861-1940*, p. 15.
[289] V. Bajkić 'Yugoslavia adopted the Golden Money', *Narodno Blagostanje* (16th May 1931).
[290] 'The Use of the Loan', *Privredni Pregled* (24th May 1931).
[291] Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 272.
[292] Bajkić, 'Yugoslavia adopted the Golden Money'.

opposition against the government. After a shooting of five members of the latter on 20th June 1928 by members of the Serbian Radical Party in the *Skupština* in Belgrade, King Alexander accused all parties of deteriorating the political climate. He dissolved the parliament, introduced the absolutist "6th January Dictatorship", and changed the official name of the Kingdom from *Kingdom of Serbs, Croats and Slovenes* to *Kingdom of Yugoslavia*.[293] According to Nikolić, the gold standard was needed as an economic success to justify this move.[294] It appears that the gold standard was indeed presented as a success of the King's government in public newspapers. An article in *Vreme* presented legal stabilisation as "one of the key programs for the economic prosperity of our country which the parliamentary government tried to achieve, but failed to."[295] Securing a stabilisation loan was "a big success of today's government".[296] The author further maintained that the political situation had improved since the King had completely taken over the government both internally and towards other countries. In this respect, the stabilisation loan was "the best approval which our regime could have received".[297] Interestingly, the newspapers *Vreme* were a direct beneficiary of the NBKY. Credit records from 3rd January 1931 (three months before the article was published) show that it received a 500,000-dinar-loan directly from the NBKY.[298] While this is no proof of a direct exertion of pressure, at least it shows that the latter depended on support by governmental institutions. It seems likely that it would express views which cohere to what the government wanted to hear at this time.

6.2 Yugoslavian Internationalism

Reviewing statements by members of policy elites reveals a particular sense of *internationalism* involved in statements relating to gold standard adoption. A letter to shareholders from the NBKY argued that the legal stabilisation has to be completed so that the bank joins the international circle of central banks and so it can cooperate on stabilising the economic conditions in the world.[299] Similarly, GAC member Radović expressed that gold standard adoption was necessary to join the circle of European banks of emission.[300] GAC member Marković argued that the gold standard was demanded by both political and economic affairs, and was a duty towards the international community:

293 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 39.
294 Nikolić, *Kurs dinara i devizna politika Kraljevine Jugoslavije 1918-1941*, p. 108.
295 'The Stabilisation Loan', *Vreme* (9th May 1931).
296 *Ibid.*
297 *Ibid.*
298 'Minutes of the 1st shareholder meeting', 3rd January 1931, NBS, ANB-1/II-30.2.
299 'Letter to Shareholders', NBS, ANB-1/I-58-1.
300 'Minutes of the supplemental shareholder meeting", 14 June 1931, NBS, ANB-1/II-30.2.

> "If the entirety of Europe is calcalculating in gold, can we be an exception? There is no way we could. We have to switch to gold. […] Legal stabilisation is not the fulfillment of a duty towards the country, but towards the international community."[301]

It would furthermore in the long run "open the necessary paths towards the international community".[302] An article in *Privredni Pregled* summarised the "internationalist" position of the NBKY:

> "Our bank is one of the biggest advocates of international cooperation between note-issuing banks and it will gladly contribute to expanding cooperation to the best of all nations, especially once the dinar is legally stabilised."[303]

The internationalism present in the NBKY was also adopted by economic journalists. *Privredni Pregled* noted that Yugoslavia is about to integrate politically, economically and financially with other countries. While the economists criticising the excessive foreign borrowing for legal stabilisation and the questionable economic benefit of going on gold were correct, "they forget that we cannot live isolated".[304] Adjusting to the global monetary system was necessary even if it required substantial sacrifices.[305] A 1931 article in *Privredni Pregled* argued that this sacrifice would have to be made to establish a connection with the rest of the world.[306] Apparently, the integration into the international community was at times viewed as an even stronger motive for adopting the gold standard than economic benefits. What were the motives of policy elites to exhibit a pronouned wish for integration into the international community through the gold standard?

One possible explanation is to affirm the nationhood of the Yugoslavian state in the international community. The Kingdom of Yugoslavia had only been founded in 1918 through the Declaration of Corfu. Serbian and Croatian politicians involved in state formation in the *Yugoslavian Committee* had been trying to signal the unity of Yugoslavia as a state for years, both internally and externally. The committee, whose members went on to be leading politicians in Yugoslavia, lobbied internationally for support of the foundation of a Yugoslavian state.[307] But also internally in the national discourse, they symbolically placed the Yugoslavian state within the international community to achieve acceptance for the state among the South-Slavic people.[308] A common

301 Marković, 'The legal stabilisation of our money'.
302 *Ibid.*
303 'Prices are falling', *Privredni Pregled* (22nd February 1931).
304 'In the Wake of significant Events in the National Bank', *Privredni Pregled* (17th August 1930).
305 *Ibid.*
306 'Election of the new Leadership of the National Bank', *Privredni Pregled* (12th July 1931).
307 C. Robinson, 'Yugoslavism in the Early 20th Century', in: D. Djokić and J. Ker-Lindsay, *New Perspectives on Yugoslavia: Key Issues and Controversies* (London, 2010), p. 11.
308 Robinson, 'Yugoslavism in the Early 20th Century', p. 24.

currency which functioned on the same basis as the currencies of the most developed nations at the time had the potential of fulfilling the same purpose for Yugoslavia and signify that the country was united and thereby further establish Yugoslavia's position as a sovereign state both towards the international community, and the population.

Another possible explanation for internationalism could be the wish to signal a cultural attachment to European gold core countries. Morys argues that among peripheral economies, adherence to a common monetary system with gold bloc countries was viewed as a way of bringing these regions "closer to Europe".[309] Nenovsky argues that since the 19th century, the elites and the population in Balkan countries strove to be a part of Europe or come closer to its economic and cultural development. He identifies this as the reason why Balkan policy-makers followed and copied European institutions such as monetary systems in the 19th century for which the adherence of the Kingdom of Serbia to the rules of the Latin Monetary Union is an example.[310] The interwar gold standard can be seen as an example for this. With the foundation of Yugoslavia, policy-makers sought a cultural foundation for the state. An article in the Croatian newspapers *Riječ* from August 1930 argued that there was no cultural continuity within Yugoslavia: "Yugoslavia is there, but there is no Yugoslavian mindset."[311] At the same time, it argued that "Brits, Westerners, we will never be."[312] Instead, Yugoslavia was a "rusty copy of Europe", an imitation.[313] While the author's expression is polemic, Yugoslavia has indeed numerously been depicted as a state with an ununified culture, and social and ideological antagonisms among its people.[314] Moreover, having just been liberated from Ottoman occupation after the Balkan Wars 1912-1913 which had brought with it a heavily opposed culture, Yugoslavian authorities under primarily Serbian leadership turned to the West for cultural integration, which the author from *Riječ* viewed as cultural imitation. The policies of the Yugoslavian government indeed exhibited an attachment to the West in various policy areas, such as migration policies, where the controversial Treaty of Nettuno allowed Italian nationals to settle in the region of former Dalmatia without a special permit.[315] In financial policy circles, a large part of policy-makers was educated in Western Europe, indicating a Western cultural influence on policy-circles. For example, finance ministers Momčilo Ninčić (1918-1919), Vojislav Veljković (1919-1920), Kosta Kumanudi (1921-1922) held PhDs in Law from the University of Paris, Velizar Janković (1920-1920) held a PhD in economics from Berlin.[316] Finance Minister Milan

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309 M. Morys, 'Financial Supervision to Fight Fiscal Dominance? The Gold Standard in Greece and South-East Europe between Economic and Political Objectives and Fiscal Reality, 1841-1939', *IDEAS Working Paper Series* (2016), p. 9.
310 N. Nenovsky et al. 'The Latin Monetary Union and the Balkans', *Revue de la régulation*, 22/2 (2017), p. 2.
311 'The Yugoslavian Cultural Problem', *Riječ* (16th August 1930).
312 *Ibid.*
313 *Ibid.*
314 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 24.
315 J. Rothschild, *East Central Europe between the Two World Wars* (Seattle, 1974), p. 227.
316 Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923*, p. 25.

Stojadinović, who introduced the *de facto* stability of the dinar and initiated legal stabilisation, was educated in Belgrade, Munich, Potsdam, Paris and London.[317] Hence, there are indications to believe that cultural attachments played an underlying role in the Yugoslavian "rush" on the gold standard as well. Economic journalist Đorđević wrote in *Bankarstvo* that once the value of the dinar was legally stabilised, the people would be more powerful and Yugoslavia's culture would have a strong footing.[318] An article in the newspapers *Privredni Pregled* asserted that the first condition of the progress of the Yugoslavian people was dinar stabilisation.[319] Hence, the question of dinar stabilisation was tied to cultural development in the public discourse. It implied a development towards the nations which were the propagators of the gold standard. Furthermore, within Yugoslavian policy-circles the looming failure of the gold standard and the termination of loans from Europe to Yugoslavia was perceived as an abandonment by the West. NBKY Governor Bajloni argued that "the cancellation of credits [...] abroad is not in the spirit of a tendency towards international cooperation on the economic field."[320] Finance Minister Stojadinović was reportedly disillusioned with both his philosophy of monetary stability, and with Yugoslavia's dependence on Western Europe after the Great Depression.[321]

Altogether, Yugoslavia's politics played an important role in gold standard adoption next to the economic factors involved in the decision. The prestige involved in introducing the gold standard was employed by King Alexander for justifying the authoritarian policies of his government similar to Mussolini in Italy who aimed to adopt the gold standard for signaling the prestige of Italy's economy. Furthermore, there was a strong desire of integration into the international community through gold standard adoption among Yugoslavia's policy elites which could have been motivated by a wish to signal Yugoslavia's sovereignty internally and externally, and the wish to culturally ingegrate with the West. With this section, a detailed view on the roles of domestic and international policy elites on gold standard adoption has been provided. The next section examines the views of different societal layers on the gold standard, and how they influenced its implementation.

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317 A. Fogelquist and B. Krekić, *Politics and Economic Policy in Yugoslavia, 1918-1929* (1990), p. 213.
318 V. Đorđević, 'The Legal Stabilisation of the Dinar', *Bankarstvo* (December 1930), p. 540.
319 'Reforms in the National Bank', *Privredni Pregled* (21st June 1931).
320 'Minutes of the 19th GAC meeting', 18th June 1931, NBS, ANB-1/II-30.2.
321 Lampe and Jackson, *Balkan Economic History, 1550-1950: From Imperial Borderlands to Developing Nations*, p. 468.

7 Interest Group Pressures and Distributional Effects

7.1 Influential Economic Elites and neglected Agricultural Workers

Policy elites and newspapers presented the gold standard as something that would benefit all classes everywhere in Yugslavia by facilitating economic development through capital inflows and creating stable wages. Economist Bajkić wrote that it was important for capitalists that the value of domestic money is fixed abroad.[322] At the same time, economic journalist Mešić wrote in *Bankarstvo* that the stability of the dinar was an existential question for workers: "[t]he monetary question is one of the first and most important foundations of a forthcoming and development of any nation, of any national and especially of farmers […]. Our peasant, our tradesman, our salesman and worker would know his material standing."[323] Hence, he presented the stability of wages as a decisive benefit for "lower classes". This was echoed in an article in *Privredni Pregled* which argued that the gold standard and the resulting price stability would mostly benefit the standard of living of working classes.[324] Economic journalist Blagojević warned of the worrying effects inflation could have on "lower classes". He presented the growth in prices as "the best means for propagating revolutionary socialism", and as "the economic reason for communism."[325] Apparently, a legally stabilised currency was viewed as keeping the "lower classes" in check. In the NBKY, a similar view was voiced by Governor Bajloni who warned of the "dreadful consequences" of an unstable value of money on the political stability of a country because the value of private assets could be wiped out.[326] Altogether, according to policy-makers and economic journals, the coming of the gold standard was greeted by all societal layers with an "undivided satisfaction in the population", as expressed by *Privredni Pregled*.[327] However, these views fail to disentangle the winners and losers of the deflationary policies and the high exchange rate the gold standard required. Clavin calls the process "politically distressing and socially divisive".[328] Generally, large business corporations have been viewed as better equipped to cope with the economic environment caused by measures for introducing gold parity, including high interest and expensive credits. Given that Yugoslavia introduced substantial deflationary policies, and that three-quarters of the population of approximately 12 million (1921) consisted of farmers, one should expect to see more polarisation surrounding gold standard adoption than indicated by the articles mentioned above.[329]

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322 Bajkić, 'Concerning Legal Stabilisation'.
323 A. Mešić, 'Before the Solution of the Monetary Question in Yugoslavia', *Bankarstvo* (December 1930).
324 'Falling prices and gold reserves', *Privredni Pregled* (23th November 1930).
325 D. Blagojević, 'The Stabilisation of the Value of Money', *Bankarstvo* (January 1931).
326 Letter from NBKY governor Bajloni to the Finance Ministry, 15th January 1932, NBS, ANB-1/1-58-1.
327 'The Law on Money of the Kingdom of Yugoslavia', *Privredni Pregled* (17th May 1931).
328 Clavin, *The Great Depression in Europe, 1929-1939*, p. 59.
329 Kršev, *Finansijska Politika Jugoslavije 1918-194*, p. 26

The deflationary policies involved in the gold standard were not beneficial for commercial banks and industrial corporations as both directly depended on expensive credits granted by the NBKY. In fact, some banks have noted difficulties in obtaining loans from the NBKY already in 1930.[330] However, banks stood to significantly benefit from the increased international transactions enabled by the gold standard. Similarly, industrial interest groups hoped to benefit from foreign loans after gold standard adoption. However, Killen argues that exporters were put at disadvantage due to the overvaluation of the dinar after its legal stabilisation.[331] Minutes of a GAC meeting from 1928 reveal that the chamber of industry in Novi Sad demanded more credits for industry from the NBKY than the bank was willing to grant.[332] However, the policies of the NBKY catered to the interests of the exporting sector even while the deflationary policies were being introduced. The bank planned to restrict credits granted to industrial exporters less than credits for importing industries as these would generate incomes in foreign currency. GAC member Matejić argued that the bank gave preferential treatment to exporters in its credit restrictions as these were bringing in foreign exchange reserves.[333] GAC member Petković applauded this idea arguing that exporters should receive an ever-increasing share of the approved loans, given the service they did for Yugoslavia.[334] He was referring to the foreign currency generated by exporters. Eventually, the exporting industry did receive more credits than the import industry in 1931, namely 125 million dinars compared to 113 million. Additionally, 600 million dinars were granted to other industrial corporations whose division into importers and exporters is not clear.[335] Hence, while there are indications that the disadvantages of the gold standard were at least partially contained for exporting industries, it is certain that there were forces within the NBKY lobbying for their interests.

Accordingly, the views expressed by economic elites on gold standard adoption were positive. *Privredni Pregled* wrote that the gold dinar had always been demanded by industrialists because it would allow them to base their calculations on a secure basis.[336] *Bankarstvo* captured the views of 21 industrialists, representatives of industrial interests, and banks on the stabilisation loan and the gold standard from acorss the Kingdom.[337] The President of the Division for Trade and Industry in Zagreb Vranić noted that especially industrial circles would approve of the stabilisation loan and that it was an enormous international acknowledgment of the Yugoslavian economy. The President of the Chamber of Commerce, Exchange and Industry Jeličanin also viewed commercial

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330 'Our Banks on the Doorstep of 1930', *Privredni Pregled* (5th January 1930).
331 Killen, *Testing the Peripheries: US-Yugoslav Economic Relations in the Interwar Years*, p. 124.
332 Minutes of the 19th GAC meeting, 5th July 1928, NBS, ANB-1/I-58-1.
333 'Minutes oft he 16th GAC meeting', 29th May 1931, NBS, ANB-1/II-30-2.
334 *Ibid.*
335 'Minutes of the 11th shareholder meeting', 8th March 1931, NBS, ANB-1/II-30.2.
336 'The completion of a 40-million-dollar stabilisation loan', *Privredni Pregled* (16th April 1931).
337 'Monthly Chronicles', *Bankarstvo* (June 1931).

circles as the main proponents of stabilisation. The President of the Trade Division in Sarajevo approved of the loan as it would ease the waiting for better times. The President of the Division of Trade and Industry in Novi Sad Mirosavljević argued that the stabilisation loan restored the belief in the Yugoslavian economy in one swoop. The President of the Union of Industrialists and Agriculturalists in Dunavska Banovina Đunderski described it as one of the most significant moments in Yugoslavia's economic life. The Secretary of the National Union of Industrialists in Zagreb Bauer hoped for the activation of the economy through the stabilisation loan and describes it as a success of the King's government. The President of the Organisation of Monetary Institutions Ristić argued that the belief in the dinar will be improved and that capital will flow into Yugoslavia. The President of Monetary Institutions in Zagreb Slokar described the stabilisation loan as a step of extraordinary importance while Sidarević, the Director of the "Jadransko-Podunavska Banka" argued that legal stabilisation would be of great use to businesses. Finally, the Director of the Yugoslavian Banking Society Weinberger also viewed it as a proof of the belief in the Yugoslavian economy from abroad. Altogether, while some political bias should be allowed for in the selection of views to be published by the newspapers, the considerable number of views of prominent representatives of industrial interests and bank representatives on gold standard adoption indicates a positive view on the gold standard in this societal layer.

However, not only were the views of economic elites on gold standard adoption positive, but they played a crucial role in bringing it about due to their representation in the NBKY. Only NBKY shareholders were allowed to be elected into the GAC which made monetary policy decisions and elected the Governor. The shares of the NBKY were owned to 20% by privileged state-owned banks ("Državna Hipotekarna Banka" and "Poštanska Štedionica"), to 30% by private monetary institutions, to 42% by small businessmen and private persons, and to 8% by large-scale industrialists.[338] It is expectable that agricultural workers were rare, if not non-existent among shareholders. Shareholder Marinković summed it up by saying that the NBKY consists of "representatives of private capital in the service of public interests".[339] In fact, at least three of the representatives of industrial interests cited as applauding the adoption of the gold standard above, namely Vranić, Jeličanin and Berković, were also GAC members and directly co-responsible for introducing the gold standard which they viewed as a major benefit to industry in Yugoslavia. Hence, commercial and financial interest groups had the power to directly influence policy-making while this was not the case for the country's labouring class at a time when democracy was suspended.

[338] Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 194.
[339] 'Minutes of the supplemental shareholder meeting', 14 June 1931, NBS, ANB-1/II-30.2.

Agrictulture had historically received substantially fewer loans than industry from the NBKY. Between 1923 and 1929, it received only 1% of direct loans while industry received 30%.[340] When the preferential treatment of exporting industrialists was being discussed in the NBKY in 1931, the needs of agricultural workers who made up the majority of the population featured less prominently in the debate. Instead, the 1931 credit restrictions for sustaining the cover ratio proved especially hurtful to agriculture. Bajloni noted that seasonal credits should be restricted first for the preservation of the cover ratio in May 1931 on which agricultural businesses relied most.[341] Furthermore, the increases of the discount rate to 7.5% and the Lombard rate to 9% in July 1931 for preventing foreign exchange reserves from diminishing resulted in higher rates on private markets of up to 13.5% according to *Privredni Pregled*, and the high rates affected agricultural businesses and their workers disproportionally as the rates charged to them tended to be even higher than that.[342] This was especially problematic because the agricultural sector was hit hardest during the Great Depression by the falling prices for agricultural produce globally.

Accordingly, the views of "lower layers" of the Yugoslavian society which did not have the possibility to influcence policy-making by the NBKY diverged substantially to the ones of economic elites. The Secretary of the Central Organisation of Labour Unions criticised the repayment of the governmental loan at the central bank through foreign borrowing which allowed for adopting the gold standard. Repaying the bank in gold worth 4 billion dinars for issuing paper money would be wealth of the people given to shareholders. Furthermore, if the gold standard was established, this ought not to be done without capital controls in order not to "burden the masses", by which he referred to the accompanying credit restrictions.[343] However, there were also more specific views by agricultural workers themselves. A letter from by agricultural worker Toth Mikloš from Senta in Northern Serbia, written to King Alexander of Yugoslavia in January 1931 reveals the plight infringed upon agricultural workers by the high interest rates:

> "[C]apitalists and banks are giving out loans at 8-14% to those who can obtain one, so neither the capitalists nor the banks care that people are being ruined. The bank is raising interest rates with which it helps the destruction of the economy. […] Your Honour, if the interest rate fell to 3-4%, a happy improvement would obtain in the economic crisis. The economic crisis would terminate because a good saying says that one should not accumulate money, but work, which in the case of an interest of 3-4% is possible, but not if it amounts to 8-14%. […] 15-20% of the population are thriving under today's high interest rates while they are

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340 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 198.
341 'Minutes of the 16th GAC meeting', 29th May 1931, NBS, ANB-1/II-30.2.
342 'The Governor of the National Bank on the State of the Country', *Privredni Pregled* (11th October 1931).
343 Z. Topalovic, 'The Dinar Question', *Bankarstvo* (November 1930).

> destroying 80-85% of the population. […] I most humbly ask your Highness to lower interest rates which the entire population is wishfully awaiting […]. I live among the people and work, I feel and know that my demand is in the name of a million people […].[344]

This letter is a remarkable illustration of the backlash against the deflationary policies, and hence the gold standard, by agricultural workers. Propaganda pamphlets, supposedly from the region of today's Croatia, hint to a public movement against the interest rate increases which were necessary for sustaining the gold standard:

> "People! Whose fault is this evil? […] For many months, banks have cut our people off from loans. […] Bank directors claim that the banks would not have any money. We are asking them where they put the money of the people who have placed all their suffering on savings accounts. They are only paying out 5% interest for deposits while they are charging 20%. […] A peasant told me that he could not obtain a loan because the banks have no money. […] Banks and only banks are the problem."[345]

While there is no indication as to the size of the popular uprising, this pamphlet indicates the presence of organised resistance against deflationary policies. Altogether, the view propagated by policy elites that gold standard adoption was a class-concensus seems inaccurate. Instead, agricultural workers who were affected by the policies it necessitated opposed it while they could not organise any effective political opposition. However, a few members of policy elites fought for their interests when the deflationary policies were being established, most notably a shareholder of the NBKY named Stamenković. He was a Social Democrat who had previously attracted attention by criticising that the NBKY was mainly in private ownership.[346] In March 1931, i.e. before gold standard adoption, he urged other shareholders "to devote attention to our agricultural workers which constitute 90% of our workers."[347] The credits granted to them by the NBKY were "simply insufficient".[348] In June, Stamenković deemed it questionable whether conditions in Yugoslavia would improve after legal stabilisation given that prices were low internationally. He maintained to be against the stabilisation plan given that agricultural workers would lose their access to cheap capital under the gold standard.[349] He furthermore tried to shout down the Governor when the latter aimed to table the debate and was the only shareholder voting against the stabilisation plan.

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344 Letter from Toth Miklos to King Alexander of Yugoslavia, 28th January 1931, Archives of Yugoslavia [hereafter: AY], 74-86-455.
345 V. Maletić, 'The Theft of Banks and Savings Houses', AY, 74-86-458.
346 Fogelquist and Krekić, *Politics and Economic Policy in Yugoslavia, 1918-1929*, p. 98.
347 'Minutes of the 11th shareholder meeting', 8th March 1931, NBS, ANB-1/II-30.2.
348 *Ibid.*
349 'Minutes of the supplemental shareholder Meeting', 14th June 1931, NBS, ANB-1/II-30.2.

Stamenković continued to criticise the work of the NBKY, loudly protesting against the increase in the discount rate and credit restrictions in June 1931. Once again, he was the only shareholder who voted against passing on the proposals to the GAC for implementation.[350] Some GAC members criticised the deflationary policies, and recognised the plight inflicted on the population as well. GAC member Kulmer presented farmers as the backbone of the Yugoslavian economy, arguing that in earlier economic crises, the continuous repayment of loans by farmers helped to save Yugoslavian banks.[351] However, GAC members voted univocally in favour of the deflationary policies as argued previously. Only several years later, namely in 1935, did NBKY Governor acknowledge in an official letter to the BIS, that lowering the discount from 6.5% to 5% had a "happy effect on the situation of the labouring classes".[352] What prevented their interests from being considered earlier was that unlike industrial interests, farmers could hardly organise any effective political opposition against the policy elites at the time when the deflationary policies were introduced because democracy was suspended and economic policies were decided between the Finance Ministry and the NBKY, the latter of which was heavily infiltrated by the interests of the country's economic elites. This hints at a possible incompatibility of the gold standard with democracy in Yugoslavia.

7.2 The Yugoslavian Gold Standard: A Serbian Project?

The NBKY was not only to large parts in the hands of private capitalists, but the owners were also mostly Serbian which led to a regional polarisation surrounding the deflationary policies required to maintain the gold standard. As mentioned in section 4, the NBKY was founded by extending the scope of the National Bank of the Kingdom of Serbia. Serbian shareholders were granted the right to buy one NBKY share in exchange for 3 shares of the National Bank of Serbia which allowed them to hold at least half of the NBKY shares.[353] In 1931, a report by the Yugoslavian government about the NBKY noted that of the 60,000 outstanding shares, 50,000 were in the hands of shareholders from Serbian regions.[354] Hence, the inequality in the distribution of shares among Yugoslavian regions increased over the years. This meant that crucial policy-decisions including gold standard implementation were primarily influenced by Serbs. Dr. Ivo Belin, a Croatian economist who held a PhD from the University of Frankfurt and was the

[350] 'Minutes of the supplemental shareholder Meeting', 14th June 1931, NBS, ANB-1/II-30.2.
[351] 'Minutes of the 10th GAC meeting', 21st December 1931, NBS, ANB-1/II-30.2.
[352] Letter from NBKY Governor Bajloni to the BIS Director General, 6th February 1935, BIS, ABIS-CH-000583-8-A.BISA.3.2.w-(3).
[353] Bečić, *Finansijska Politika Kraljevine SHS: 1918-1923*, p. 210.
[354] 'How to solve the Question concerning the National Bank', 1931, AY, 74-86-21.

Secretary of the Zagreb Stock Exchange, openly criticised this state of affairs.[355] In a report on the NBKY he noted that of the 24 members in the GAC, 18 were from Belgrade and other Serbian parts while only 2 were from Zagreb. Other regions of Yugoslavia had only one representative each. This meant that while the non-Serbian parts constituted 60% of the population, their representation in the bank was only 25%.[356] According to Belin, the effect of this unfair distribution of shares was that the deflationary policies which were used to stabilise the dinar throughout the 1920s were disproportionally applied to the detriment of the Croatian part of Yugoslavia. According to him this unfairness was even embedded in the statutes of the NBKY, no. 61 of which restricted the duty of credit provision to the Serbian GAC members. Belin noted that while there was a total decrease in the value of bills discounted to banks from 1,885,848 in 1922 to 1,585,419 in 1929, the bills discounted in the Serbian region did not decrease, but remained stable (741,000 in 1929 compared to 739,000 in 1922).[357] Furthermore, 90.8% of the Lombard loans granted by the NBKY went to Serbian regions in 1930.[358] In 1929, of the 3,840 credit holders, 2,672 were in Serbian regions and only 174 in Croatian which led Belin to conclude that "[w]hile in Belgrade even the smallest craftsman enjoys a credit of the National Bank, in the non-Serbian parts, not even the biggest firms can obtain one".[359] In 1931, the Yugoslavian government viewed the preferential treatment of the Serbian region in terms of credit provision as justified given that Serbia was destroyed most in the First World War and given that the "Serbian economy was in a more primitive state than others". Even establishing a public bank with the sole purpose of granting credits to former Serbia was discussed.[360] Belin argued that this view was only justified in the first years following the war. He demanded "radical reforms" in the bank and a gradual lowering of the discount rate which would increase the access to credits throughout Yugoslavia. [361] Belin's demands were in line with what other Croatian officials demanded. Finance Minister Švrljuga, who was Croatian, resigned over disputes about the regime not satisfying Croatian economic interests.[362] Before assuming office, he claimed in a newspaper article that he was especially unsatisfied with the credit policies of the NBKY.[363] In 1928, the Union of Croatian Entrepreneurs issued a statement condemning the "ruthless financial exploitation and economic neglect of Croatia [and] especially protest[ed] against the credit policies".[364] It is no surprise that when the deflationary

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355 V. Stipetić, 'Nepoznata studija Iva Belina o sanaciji novčarstva iz 1933', in: *Anali Zavoda za povijesne znanosti Hrvatske akademije znanosti i umjetnosti u Dubrovniku* (2001), p. 462.
356 I. Belin, 'The Credit Policies of the National Bank', 1930, AY-74-86-1.
357 *Ibid.*
358 *Ibid.*
359 *Ibid.*
360 'How to solve the question concerning the National Bank', 1931, AY, 74-86-21.
361 Belin, 'The Credit Policies of the National Bank'.
362 Fogelquist and Krekić, *Politics and Economic Policy in Yugoslavia, 1918-1929*, p. 153.
363 Belin, 'The Credit Policies of the National Bank'.
364 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 107.

policies were deepened in 1931 to maintain the gold standard, criticism from Croatia continued. The Zagreb Chamber of Commerce sent a letter to NBKY Governor Bajloni demanding that the entire remaining stabilisation loan should be used for conducting an expansionary monetary policy in October 1931, which was not implemented by the NBKY.[365] One should also recall from section 4 that the Zagreb Stock Exchange which Belin presided over was explicitly against introducing legal stabilisation without capital controls.

However, the claims made by Ivo Belin have to be viewed critically. While his data about the distribution of loans by the NBKY seems to largely cohere to the recent analysis of Kršev, there is no evidence about a systematic exclusion of non-Serbian interest within the NBKY.[366] For example, two vice-governors of the NBKY in 1931, Meljko Čingrija and Miroslav Kulmer, were Croatian.[367] In 1936, Belin himself would become the Vice-Governor of the NBKY for five years.[368] However, independently from their accuracy, the claims of Croatian policy-makers reflect that in their view there was an unfairness of the government's deflationary policies towards the non-Serbian parts of Yugoslavia, and that the gold standard as it was implemented was perceived as a "Serbian project". Recalling the political tensions between Croatian and Serbian parties which were based on Croatian claims that Serbian elites exerted too much political influence over non-Serbian parts, which eventually led to a suspension of democracy by King Alexander as described in section 6, it appears that the economic issue of gold standard adoption and the deflationary policies it required were a mirror, and to some extent propagators, of political tensions characteristic for interwar Yugoslavia. The same can be said about the social divisiveness of the gold standard described in section 7.1. The burden caused by the deflationary policies for the "lower classes" in Yugoslavia together with the numerous failed attempts of the Yugoslavian government to improve the living situation of its agricultural workers fed into an elitist narrative of Yugoslavia's government. It is not far-fetched to claim that this sentiment contributed to the popularity of the Yugoslav Partisans which were founded in 1941 and whose influence determined the fate of Yugoslavian politics for the decades to come.

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365 Letter from the Chamber of Commerce in Zagreb to the NBKY governor, 27th October 1931, AY, 74-86-86.
366 Kršev, *Finansijska Politika Jugoslavije 1918-1941*, p. 199.
367 'Election of the new Leadership of the National Bank', *Privredni Pregled* (12th July 1931).
368 Stipetić, 'Nepoznata studija Iva Belina o sanaciji novčarstva iz 1933', p. 462.

8 Conclusion

Drawing on a variety of primary sources, this paper has provided a detailed political economy analysis of the the difficulties, the economic and political rationales and their formation, as well as the societal and regional implications, of the Yugoslavian gold standard. After sections 2 and 3 defined the gold standard and reviewed arguments in existing literature about rationales for gold standard adoption, section 4 analysed the difficulties of gold standard adoption in Yugoslavia, referring to the unsuited economic realities for sustaining the cover ratio (section 4.1), necessary institutional innovations (section 4.2), how the repayment of the government loan for making the monetary base independent from governmental influence sparked a backlash from economists and the public (section 4.3), and how these obstacles were recognised but accepted by policy elites (section 4.4). Section 5 then explored existing rationales given by policy elites, identifying a pronounced wish for international borrowing and capital inflows as the primary economic motive for gold standard adoption. However, the decision to adopt it and implement deflationary policies for its maintenance was realised under various pressures from foreign public and international banks including the Bank of England, the Banque de France and the BIS (section 5.2.1), and buttressed by the prevalent economic theory used by policy elites which made them ignorant towards the benefits of flexible exchange rate regimes (section 5.2.2). In terms of political rationales, gold standard adoption was used by the government to signal the prestige of the economy during the 6th January dictatorship, as well as to signal a wish for integration with gold core countries, and the Western culture in particular (section 6). Section 7 abstracted from the interplay of Yugoslavian and international elites and focused on the views and influences of different layers of the Yugoslavian society, revealing a strong influence of Serbian economic elites who were co-determining NBKY policies while agricultural workers were left out, as an important factor for bringing about the gold standard (section 7.1). This also revealed the monetary system as a contributing factor to the dissatisfaction of agricultural workers, and to the regional political divide between Serbian and Croatian policy-makers (section 7.2).

This paper complements existing literature on Yugoslavian gold standard adoption and opens up paths for further research. It extended the scope of previous analyses by not only extracting the motives of policy-makers for gold standard adoption, but also showed how these were formed taking into consideration various internal and external factors. This showed that gold standard adoption can only be explained through an interplay of various influences, including improved opportunities for international borrowing, pressures from foreign institutions, political aspirations by the government, cultural attachments to "the West", economic theory used by policy-makers and interest group pressures. I argue that disentangling these factors has to some degree made the decision of Yugoslavian policy-makers understandable despite the difficulties it involved as explained in section 4. Dismissing it as merely an "ideological" attachment to the benefits of an outdated monetary system, which Eichengreen argues made policy-makers from European "core countries" re-establish the gold standard after the 1922 Genoa Conference, would not do justice to the complexities involved in the position of Yugoslavian policy-makers.[369] As I illustrated in sections 4 and 5, the path set out by governments and institutions from core countries was at times viewed critically by NBKY representatives and among economic journalists, but peripheral countries like Yugoslavia had little leeway to deviate from this path due to the reality of an inferior economic and political position in the international community. Further research on the influence of economic dependencies and direct pressures on gold standard adoption in peripheral European countries is a fruitful research path for understanding the policy-perspective of these countries in the interwar period. For example, other peripheral economies like Czechoslovakia cooperated with the BIS on legal stabilisation and provide possibilities for further analyses. Next to explaining gold standard adoption in Yugoslavia, this paper extended previous literature by placing it within the country's larger societal and regional divides. The detrimental effect of high interest rates on agricultural workers and the particularly restrictive credit policies in Croatian regions made gold standard adoption contribute to already existing divisions between classes and regions in a highly unstable society. Beyond these two main conclusions, this paper illustrated various smaller aspects of gold standard adoption which were peculiar for Yugoslavia. These include the institutional learning of policy-makers by analysing institutions in other countries, how the gold standard was a catalyst for Yugoslavian central bank independence, the public backlash involved in the repayment of the government loan at the NBKY, and the nature of BIS conditionality demanded from Yugoslavia.

Reflecting on the use of this paper for understanding the policy-perspective of peripheral countries on the Balkans throughout history, one should remark that the "rush" for gold standard adoption is only one instance of how economic, political and cultural dependence on core countries created a regional policy-pattern focused on monetary integration. As mentioned in the introduction, the Kingdom of Serbia, whose currency was later adopted in Yugoslavia, pegged the dinar to the French franc in 1873. The Kingdom also followed the rules of the Latin Monetary Union and strove to legally stabilise the dinar in 1878 unsuccessfully. After the Second World War and the creation of the Socialist Federal Republic of Yugoslavia, the dinar was fixed to the US dollar at 50.06 dinars per dollar from 1945 until 1973, when a manged float system was adoped.[370] After several currency reforms, the dinar was pegged again to the German mark in 1989 to facilitate

[369] Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939*, p. 100.
[370] B. Stojanović, 'Exchange rate regimes of the Dinar 1945-1990', Second Conference of South-Eastern European Monetary History Network (2007), p. 234.

trade with Germany and remained so with temporary suspensions until 2006.[371] After the dissolution of Yugoslavia, the dinar continued to exist in the Republic of Serbia which has become a candidate for EU membership in 2012. Since 2015, the dinar has been on a hypothetical peg at around 120 dinars per Euro.[372] This has sparked discussions as to whether the country is ready for a legal currency peg to the Euro to ease market integration.[373] This shows that for some peripheral economies like formerly Yugoslavia and Serbia today, currency pegs have remained early steps towards deeper economic integration, and that such policy decisions are informed by a fundamental dependence on countries and international organisations which have the means to promise economic exchange and development, as well as provide a lead-culture which peripheral countries strive to integrate with. It is this dependence that has created a regional, historically consistent policy-pattern for monetary integration which stretches temporarily before the gold standard and far beyond.

371 Stojanović, 'Exchange rate regimes of the Dinar 1945-1990', p. 234.
372 Bloomberg, 'EUR-RSD Exchange Rate' (2020).
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