The gold standard, deflation and fascism in Polanyi's *Great Transformation*. A multidisciplinary analysis

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Introduction

In 1944 Karl Polanyi published a work that would become a milestone in 20th-century social science, *The Great Transformation*. He was among the first to explain the economic and political catastrophe of the inter-war period as the final stage of a long-term process that reigned in Western Europe (and the United States) in the wake of the Napoleonic wars, market liberalism. Polanyi considered those 'one hundred years' to be a coherent period covering the rise and fall of 19th-century civilization.

Polanyi characterized the 19th-century civilization that was destined to die with the Great Depression of the 20th century by four institutions: the balance-of-power system, the gold standard, the self-regulating market and the liberal state. Of these institutions, Polanyi asserts that the gold standard was the only one to survive both the Long Depression (previously known as the Great Depression) of 1873-1886 and the Great War. However, its ultimate failure delivered the death blow for market liberalism and, in some places, also swept liberal democracy away with it. The final part of Polanyi's book gives a historical account of this process.

However, early on in the book, Polanyi warns us that he is not conducting historical research: «what we are searching for is not a convincing sequence of outstanding events, but an explanation of their trend in terms of human institutions»[1]. This statement should be understood as a declaration of intent; Polanyi's analysis was not limited to a single subject, such as history or economics, and he made this very clear by saying «we shall encroach upon the field of several disciplines in the pursuit of a single aim»[2].

This paper focuses on the causal chain Polanyi established in his work, which links the gold standard with deflation and the failure of democracy during the inter-war period. It examines to what extent the three-step causal connection was accurate, or not. In quite a similar way to Polanyi, we have searched for answers in several disciplines, in particular, economic and sociological history. First, we present Polanyi's thesis on the crisis of liberalism in the 1920s and 1930s. We then study the different parts of his causal link, highlighting the possible effect of deflation on the rise of fascism in Europe. We use some reference works in economic history and sociology concerning the inter-war period to evaluate Polanyi's thesis, in addition to statistics reflecting the dynamics of price movements in the inter-war years, which also allow us to present evidence of a rupture with the laissez-faire economy in Europe, which Karl Polanyi seems to have overlooked.

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[1] K. POLANYI, *The Great Transformation. The Political and Economic Origins of Our Time*, Boston, Beacon Press, 2001 [1957], p. 4.
[2] *Ibidem*.

The gold standard, deflation and the failure of liberalism in The Great Transformation

Between the First World War and the Second World War, everything referred to by Polanyi as 'the energies of history' were brought into play in Europe. Although the war of 1914 had brought the 19th-century world to an end, there were many who were convinced that only by reproducing the same pre-war liberal system (based on the self-regulating market economy) could the continent regain peace and prosperity. However, many of the conditions that had made the system work in the 19th century were absent after the war on a continent where universal suffrage tended to be the rule and not the exception. The result was a weak economic equilibrium surrounded by dangerous non-democratic alternatives, from communism in the Soviet Union to fascism in Italy. The Great Depression broke that equilibrium by eroding the liberal model, both economic and political. Democracies with a long liberal tradition (Britain and the United States) could survive, whereas other countries embraced radical solutions as an alternative to free markets. Consequently, the 1930s marked the end of the liberal model and ushered in the 'great transformation' expressed in the title, which Polanyi himself summarized as Britain's withdrawal from the gold standard, the five-year plans in the USSR, the New Deal in the United States, and Nazism in Germany. In his opinion, some of these ruptures with the principles of the liberal economic model (in particular, naturally, Nazism) led to the outbreak of World War II.

What did Polanyi believe to be the main cause of the failure of the self-regulating market economy during the first post-war? From the very beginning the author gives us a clear indication: the gold standard; in fact, he says that «its fall was the proximate cause of the catastrophe»[3]. The beginning of the second chapter of his book reinforces this idea by pointing out the «breakdown of the international gold standard' as the factor behind both 'the disintegration of world economy which started at the turn of the century and the transformation of a whole civilization in the thirties»[4]. Polanyi explains the former through the narrow link between the international monetary network (gold standard) and the new international order that emerged in the wake of the Napoleonic Wars and lasted until 1914, known as the Pax Britannica. Since the gold standard was crucial for the European political equilibrium through free trade, a landmark of the traditional (liberal) world economy, as soon as gold was used for the purposes of protectionism and colonial expansion, a perversion of the model that Polanyi first attributes to Germany, the Hundred Years' Peace was bound to end.

The latter process, the so-called great transformation, conveys the fundamental explanation of Polanyi's thesis. In the two decades that followed World War I, the failed attempt to restore the international monetary system was unable to make the balance of power among nations work for peace. In the 1920s there was an «almost universal conviction that only the reestablishment of the pre-1914 system … could restore peace and prosperity»[5]. And this implied the reconstruction of the gold standard model as the best way to promote free trade among nations. In short, the impossibility of doing so led to the political and economic transformation of the 1930s. Again, the role of gold standard was a key element in the outcome. Polanyi already describes the sequence of facts in his second chapter. Tied to an informal compromise with the League of Nations and the dominant financial centres (Wall Street and the City of London), nations worldwide made

[3] *Ivi*, p. 3.
[4] *Ivi*, p. 21.
[5] *Ivi*, p. 23.

an effort to keep their currency stable, but this became an impossible task without a free trade policy. Finally, when the gold standard collapsed, so did the institutions devoted to promoting a world of stable currencies. Polanyi mentions the League of Nations and the international haute finance[6]. In the end, the economic crisis affected the liberal political system by turning democracies into totalitarian dictatorships, where the free market was replaced by the role of authoritarian states.

These ideas are further developed in the last chapters of the book. Chapter 16 contains a detailed dissertation by Polanyi on the relationship between the gold standard and central banks. In the 19th century (and even as far as 1914), the priority given to the gold standard and free trade over the needs of domestic economies meant that many countries resorted to deflation in order to avoid depreciation of their currencies. According to Polanyi, deflation was not a huge problem in terms of income and unemployment thanks to the supply of internal credit by independent central banks. Nonetheless, the aim of promoting exports to prevent withdrawals of gold reserves implied a restrictive monetary policy with the recurring result of the liquidation of the least efficient firms and growing unemployment. Polanyi's conclusion regarding the whole situation stresses the negative effects over the positive ones: «again and again a complete disorganization of business and consequent mass unemployment, is the most powerful of all the indictments of the gold standard»[7].

The gold standard in the 19th century represented the difficulties of separating economics from politics, the «outstanding characteristic of market society» in Polanyi's words[8]. The concept of money as a commodity, a mere means of exchange, predominated for over a century, but in the early 20th century the concept of money as purchasing power began to gain ground, particularly after the breakdown of the gold standard system in 1914. The belief held in the twenties that the gold standard was the «precondition of a return to stability and prosperity»[9], i.e. to a pre-war world, allowed central bankers to impose their deflationary measures in order to keep exchange rates stable. When the crisis came in 1929, the chaos in world trade changed the priority from foreign stability to internal stability. In the end this change implied that monetary policy in the hands of central banks was increasingly becoming a political issue. While levels of deflation were quite low (2-3 per cent), there was no need to manage the currency, and money as a commodity along with the automatic adjustment mechanism of the gold standard remained undisputed. But when prices fell by ten per cent or even more, threatening people's purchasing power, central banks were forced to implement policies that involved monetary intervention against the principles of the gold standard. Polanyi considers this issue (the managing of the national currency) to be the centre of the conflict between economic classes in the thirties, and certainly one of the basic causes «in the growth of the antidemocratic movement»[10].

In Polanyi's view, what happened in the monetary field during the Great Depression took with it all that was left of the world of the self-regulating market. Britain's withdrawal from the gold standard in 1931, followed by the United States two years later, marked the end of an era: «final failure of the gold standard was the final failure of market

[6] *Ivi*, p. 29.
[7] *Ivi*, p. 204.
[8] *Ibidem*.
[9] *Ivi*, p. 208.
[10] *Ivi*, p. 207.

economy»[11]. And its place was taken by «forces of charismatic leadership and autarkist isolationism»[12], not only in economics but also in politics. Those two facts (the end of market economy, and its replacement by authoritarian solutions) were very closely connected. Part three of The Great Transformation goes deeper into these topics.

Being part of the international monetary system known as the gold standard usually meant that internal wages and prices could not rise steadily without damaging exports. In the first decade after World War I, a thick line separated groups who demanded 'treasury inflation' (Polanyi identifies trade unions and 'labour' parties, allied with the labour movement) from those who opposed any intervention of that kind from central bankers (middle-class and conservative parties). Similarly, employers and employees were on opposing sides with regard to budget and public expenditure. But interventionism was not merely a matter of right and left-wing politics. Polanyi explains that situation experienced by Britain and Germany in 1931, Belgium and France in 1926, and Austria in 1923 was similar: labour parties losing elections after sacrificing the budget for the benefit of the currency. Taking Britain in 1931 and Léon Blum's unsuccessful French 'New Deal' of 1936 as examples, Polanyi concludes that the effects on popular policies of defending the currency under gold standard rules was crippling. Except for the United States, whose economy was not dependent on foreign trade, and Britain, whose large share of world trade enabled it to shift «the burden of the gold standard largely to other shoulders»[13], other countries (Germany, France, Belgium and Austria) were tied to the gold value of their currencies, which strongly restricted any trade union influence on wages.

Polanyi blames the League of Nations and specially the Gold Delegation of the Financial Committee in Geneva for expanding a deflationist policy in the world of the first post-war or inter-war period. More or less in line with the same idea he develops in his criticism of the free market in Victorian England, Polanyi sees the aim of restoring currency stability and free exchange as taking priority over free markets and free governments, «the two pillars of liberal capitalism»[14]. Thus, the 'deflationary governments' were forced by Geneva to take any measure that was needed to stabilize the currency, even though this went against the liberal ideal of non-intervention in the markets. In 1932, when exchange rate stability proved to be a chimera, the Report of the Gold Delegation, Polanyi notes, abandoned its obsession with deflation. Free markets were never achieved, but at the expense of free governments. In the end, the liberalism represented by all the defenders of the gold standard facilitated the rise of fascism. Polanyi's conclusion leaves little doubt: «The stubbornness with which economic liberals, for a critical decade, had, in the service of deflationary policies, supported authoritarian interventionism, merely resulted in a decisive weakening of the democratic forces which might otherwise have averted the fascist catastrophe»[15].

In Polanyi's mind the process that brought fascists to power was a consequence of the collapse of the market system between the wars as much as it was the result of the triumph of socialism in Russia. Labour parties in continental Europe were inspired by this to turn their desire to reform capitalism into a more revolutionary approach. When those parties gained parliamentary weight in the twenties, capitalists begun to fear for their property rights. Polanyi points out that while socialism was seen by workers as the natural solution

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[11] *Ivi*, p. 209.
[12] *Ibidem*.
[13] *Ivi*, p. 238.
[14] *Ivi*, p. 241.
[15] *Ivi*, p. 242.

for the subordination of markets to the political community, for the economic system it meant:

> a radical departure from the immediate past, insofar as with the attempt to make private money gains the general incentive to productive activities, and does not acknowledge the right of private individuals to dispose of the main instruments of production[16].

The inevitable clash of interests between classes (employers versus employees) took a dramatic twist when the latter used democracy to intervene in business in what Polanyi saw as 'warfare against the industrial system' (2001: 244), while the former encouraged the population to blame their freely elected governments for the economic crisis. In a context of widespread fear, fascists emerged all over Europe (from Finland to Spain) with easy solutions to complex problems.

Chapter 20 asserts that there was a necessary link between the failure of liberal capitalism and the rise of fascism in Europe. In fact, Polanyi discredits any other interpretation:

> The appearance of such a movement […] should never have been ascribed to local causes, national mentalities, or historical backgrounds as was so consistently done by contemporaries. Fascism had as little to do with the Great War as with the Versailles Treaty, with Junker militarism as with the Italian temperament.

Therefore, the success of fascism in the thirties, illustrated by the case of Germany in 1932, was a product of an objective situation (the «institutional deadlock» of free market societies) and had little to do even with the strength of the movement itself. In Roaring Twenties Europe, nationalism and counterrevolution served fascism on its road to power, especially in the defeated countries of the Great War. Nevertheless, Polanyi regards the connection with those post-war tendencies as accidental, a «case of symbiosis between movements of independent origin»[17]. The only factor that determined the political strength of fascism was the difference in the economic situation before and after 1929. While the market system functioned, whether with difficulties (1917–1923) or without them (1924–1929), fascists had to wait for their opportunity, but when the Great Depression hit the liberal system so brutally, that opportunity was turned into a reality in only a few short years.

Unsurprisingly, when Polanyi lists the events that evidenced the temporary restoration of market capitalism between 1924 and 1929, the last (but not least) is once more the gold standard ruling the world «from Moscow to Lisbon»[18]. In that sense, the monetary system seemed to be the anchor of the entire international economy in the twenties, and the crack in Wall Street was the storm that swept it away. Barely four years later, with the gold standard «put out of action by its Anglo-Saxon creators»[19], world trade and capital flows collapsed, foreign debts were repudiated, and many economic turbulences became political and military issues:

> A Wall Street slump grew to huge dimensions and was followed by Great Britain's

[16] *Ibidem*.
[17] *Ivi*, p. 250.
[18] *Ivi*, p. 252.
[19] *Ibidem*.

> decision to go off gold and, another two years later, by a similar move on the part of the United States. Concurrently, the Disarmament Conference ceased to meet, and, in 1933, Germany left the League of Nations[20].

Polanyi's reasoning is even taken a step further when he describes Germany under the Nazis as the paradigmatic example of the great transformation caused by the failure of liberal capitalism. Germany broke free from the economic international system to the same extent that it repudiated any political commitment or obligation with other nations. Unhindered by the sacrifice imposed by orthodox economics, the Nazis could fulfil their plans through autarchy, whereas Great Britain hindered economic recovery and rearmament due to its blind faith in «the principles of stable exchanges and sound currency»[21]. Even more, Polanyi says that Britain's approval of Czechoslovakia handing over its gold reserves to Germany in 1938 (after the Munich Agreement*)* was not a sign of appeasement but of «homage to the spirit of the gold standard, which continued to govern the outlook of the leading men of the City of London on strategic as well as on political matters»[22]. Halifax and Chamberlain believed that peace depended on the restoration of world trade through some new version of the gold standard system. Polanyi's opinion on this subject is conclusive: «England's military unpreparedness was mainly the result of her adherence to gold standard economics»[23].

Having presented Polanyi's thesis, our goal in the next chapters is to evaluate it through two core questions. The first is the role of the gold standard during the inter-war period. To what extent was it a determining factor in the crisis of the market system? The second question arises directly from the previous one: was fascism a result of the malfunctioning of the gold standard model? Other collateral questions taken from Polanyi's statements inevitably appear during the course of our research. For example, did deflation cause greater social and economic distress than that caused by inflation in Europe? Or, can we explain the rise of fascism purely in terms of the economic situation, disregarding other factors, as Polanyi suggests? In order to answer these questions, we present statistical evidence and, more importantly, we review important literature concerning three issues: the gold standard after 1914, the economic situation in Europe during the 1920s, and the roots of fascism. Economic history, political history and sociology will provide enough clues to enable us to combine these three aspects and provide an answer to our questions.

The gold standard in the inter-war period

As we have observed, Polanyi attributes to the gold standard a crucial role in the Great Depression and, as a consequence, the failure of the self-regulating market system. In this assertion, he shared the explanation given by John Maynard Keynes to the crisis in the early thirties, though their interpretation differed in some details, as we will mention later[24].

Specialists in monetary issues at the time of the Great Depression confirm a great

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[20] *Ibidem*.
[21] *Ivi*, p. 253.
[22] *Ivi*, p. 254.
[23] *Ibidem*.
[24] Cfr. G. BECCHIO, *Karl Polanyi fra Marx, Keynes e Hayek: visione e analisi*, in «Studi e Note di Economia», 2, 2006, pp. 141-154.

consensus among economists in considering the gold standard «a key element – if not the key element – in the collapse of the world economy» during the thirties. In any event, some clarifications are required. It was not a matter of the monetary system causing the crisis, but rather of helping it to convert an «unexceptional downturn … into the Great Depression»[25]. Why were wrong policies continued when it was clear that they were aggravating the contraction? Their argument is that the gold standard was the ideological pillar of central bankers and politicians in Europe and the United States, precisely one of Polanyi's main ideas back in the 1940s: the commitment of the dominant classes to what he called the «obsolete market mentality» (interestingly enough, Barry Eichengreen and Peter Temin use the same word: mentality) was materialized through the gold standard, so that even when the boat was sinking they stuck to it[26]. Ironically, Polanyi is an absent reference in their paper[27].

From a different perspective, agreement with Polanyi's thought lies in a causal link between the economic slump of 1929-1933 and the failure of the gold standard. On the contrary, it denies the responsibility of the gold-backed monetary system for the Great Depression[28]. More interestingly, this perspective reveals a crucial issue: by no means was gold standard the same mechanism that operated prior to 1914. First of all, few countries returned to the pre-war (coin) gold standard. Second, the «servomechanisms» that were supposed to adjust internal economies to the necessities of a stable currency were rarely implemented during the inter-war period. Central banks, under important political pressures, decided not to follow the «rules of the game» of insulating domestic economies from gold inflows, by sterilizing the monetary effects on internal credit, prices and wages. Indeed, the post-1914 gold standard «depended upon the financiers, central bankers and politicians [who] … only imperfectly understood the system they operated»[29].

A classic work in economic history on the economy of the inter-war period by Derek Aldcroft seems to be in line with Drummond's conclusions[30]. In Aldcroft's view, the post-war economic environment had changed so much that it became an impossible task «to recreate a viable gold standard in the 1920s». Consequently, he regards the monetary system reconstructed in the twenties «was but a pale reflection of the old». The wrong stabilization process ended up with undervalued or overvalued parities in the majority of countries, a starting problem with no subsequent solution, given that everybody was

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[25] B. EICHENGREEN, P. TEMIN, *The Gold Standard and the Great Depression*, in «Contemporary European History», 9, 2, 2000, p. 195.

[26] This is not the only idea in the paper to recall those of *The Great Transformation*. In fact, the main differences between the two are apparently found in the terms they use to describe this 'mentality'. While Polanyi insists on calling it liberal(ism), Eichengreen and Temin only use the word liberal on one occasion (when referring to Sir Herbert Samuel of the Royal Commission on the (British) Coal Industry). Rather, they refer to those elites supporting the gold standard the term coined by Keynes the «investing class». And the recurrent "self-regulating" market that was behind the gold standard mentality in Polanyi becomes the «self-correcting powers» in the world economy between the two wars.

[27] Fifteen years later, in his book about the similarities between the Great Depression and the Great Recession, Eichengreen did mention Karl Polanyi among the scholars whose lessons of the Great Depression had some influence on the decisions taken in 2007-08. B. EICHENGREEN, *Hall of mirrors*, Oxford, Oxford University Press, 2015, p. 378.

[28] I.M. DRUMMOND, *The gold standard and the international monetary system, 1900-1939*, Basingstoke, Macmillan Education, 1987.

[29] *Ivi*, p. 56.

[30] D. ALDCROFT, *From Versailles to Wall Street, 1919-1929,* Oakland, University of California Press, 1981[1977].

reluctant to adjust them later on. The main reason was that «few countries were prepared to sacrifice the stability of their domestic economies for external equilibrium»[31]. On this particular issue, Aldcroft agrees with Polanyi that the fear of unemployment was a basic factor behind the priority given to domestic monetary objectives over the stabilization of exchange rates.

These relevant changes had already been noticed by Polanyi in his book, although certain difficulties arise when following his argument. Naturally, he was aware of the interventionism displayed by central banks in the inter-war period, but such interference with the servomechanisms of the system did not seem to concern him at all. On the contrary, he saw management of the currency by central banks through the mechanism of supplying credit as «part of the rules of the game under which the gold standard was supposed to function»[32]. Therefore, Polanyi sees practically no differences before and after 1914, ignoring that the post-war international monetary system was commonly called the «gold bullion standard» for good reason[33]. As a consequence, this position allows him to regard the return to gold in the 1920s as perfectly compatible with the self-regulating market system, extending the pre-war model of the gold standard as far as 1930. Nevertheless, it is doubtful whether the international monetary system after 1914 could replace the 19th-century world of the self-regulating market. While the Great War had resulted in a rupture with the gold standard system as it had functioned previously, the 1920s could not be seen as a return to 1913, mainly because the world, and Europe specifically, had so many unresolved problems (inflation, weak budgets, territorial arrangements and political instability, among others) to pretend that nothing had changed[34].

Another discrepancy arises with periodization. While Polanyi seems to concentrate on the effects of monetary intervention in the 1930s, Aldcroft sees that it was already chronic in the 1920s, even in the United States when, in 1928–1929, the Federal Reserve «favoured domestic over external objectives»[35]. Polanyi's reasoning is that with deflation levels at around three per cent, there was no need to manipulate the currency to stay in gold. But huge deflation soon demanded a degree of intervention from central banks that was far from the ideal of self-regulation; in fact, «monetary policy was thereby drawn into the sphere of politics»[36]. According to Polanyi, that situation took place only after the shock of 1929, showing that bankers were not sufficiently qualified to stabilize their national currencies under the combination of dire straits and gold standard rules. In turn, it opened up a decade in which internal conflicts between economic classes forced politicians to leave the gold standard. He saw Britain's relinquishment in September 1931 as «the final failure of market economy»[37].

Last but not least, it is interesting to evaluate Polanyi's conclusions about the negative consequences of whether to pursue an orthodox monetary policy. For Polanyi there was little doubt that deflation was the evil. In reference to the *Gold Delegation of the League of Nations* (Geneva), an institution he says to have put 'deflationary governments' in power, Polanyi asserts:

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[31] *Ivi*, pp. 167-168, and 172.
[32] K. POLANYI, *op. cit.*, p. 206.
[33] I.M. DRUMMOND, *op. cit.*, p. 34.
[34] *Ivi*, p. 31.
[35] D. ALDCROFT, *op. cit.*, p. 179.
[36] K. POLANYI, *op. cit.*, p. 207.
[37] *Ivi*, p. 209.

> In 1932 the Report of the Gold Delegation of the League of Nations declared that with the return of the exchange uncertainty the main monetary achievement of the past decade had been eliminated. What the report did not say was that in the course of these vain deflationary efforts free markets had not been restored though free governments *had* been sacrificed[38].

On the other hand, inflation was only a spectre that served the liberals' purpose of imposing the gold standard and deflationist policies. Polanyi recalls first how «hundreds of millions of people had been afflicted by the scourge of inflation»[39] in the 1920s; later in the book he points out how that «charge of inflationism became an effective argument against democratic legislatures»[40].

Interestingly, his position regarding inflation was not the same in the 1930s. In a text written in 1932 for the Austrian economic and political magazine Der Österreichische Volkswirt, he claimed that several left-wing governments in Europe (Britain, Belgium, France and even Germany) were removed from power due to currency mismatches that caused inflation[41]. In his 1930s' interpretation of the Great Depression, Polanyi stressed the major role inflation played in the crisis, whereas Keynes thought the same role to be «surprisingly modest». Moreover, Polanyi was critical of Keynes' solutions to the crisis involving inflationary policies[42]. Ten years later, Polanyi seemed to see things differently, and he considered inflation the main enemy economic liberals found in their pursuit of restoring a self-regulating economy.

What was more damaging during the inter-war period, deflation or inflation? Deflation hit several countries in the twenties, especially in the process of macro-economic stabilization prior to their return to gold standard: Sweden between 1920 and 1922 ('severe'), Norway and Denmark between 1925 and 1928 ('sharp') and Britain until 1925 ('intermittent'), all the result of an overvalued currency. The Scandinavian countries, particularly Sweden, were able to adjust their economies to the requirements of external stability, but in any event, devaluation was always preferred to further internal deflation. Britain, through the management of interest rates by the Bank of England, was a paradigmatic case in this respect[43].

Would all these nations have performed better if they had implemented a monetary policy independent from the restrictions imposed by the gold standard? Polanyi tends to suggest they would have, as we have seen previously. Aldcroft admits that deflation prevented these economies from realizing their «full growth potential». Nonetheless, he considered an even worse alternative. Thus, the German hyperinflation of the early twenties left the figures for real income, production and exports so far below pre-war levels that they could not, he states «be matched by any of the countries which carried out a deflationary policy». Between 1919 and 1923, years of «turmoil, poverty, starvation and tension» conditioned the lives of Germans in such a way that it made the country dependent on borrowing abroad heavily by the late twenties. And despite the flight of foreign capital from Germany that accompanied the slump of late 1929, the government

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[38] *Ivi*, p. 242.
[39] *Ivi*, p. 148.
[40] *Ivi*, p. 235.
[41] K. POLANYI, *Wirtschaft un Demokratie*, in «Der Österreichische Volkswirt», 13-14, 1932, pp. 301-303.
[42] G. BECCHIO, *op.cit.*, pp. 144-145.
[43] D. ALDCROFT, *op. cit.*, p. 52.

rejected any expansionary policy because of the long shadow of inflation[44].

Given that Polanyi's logical sequence began with the return to gold after the war and ended with the coming of fascists to power, the German case is, by no means, irrelevant, and it is somewhat controversial. After the destruction of the pre-war German currency and the creation of a new one (Retenmark), Germany was forced to restore the pre-war parity as part of the American financial assistance provided in 1924 (Dawes Plan). The harsh memory of hyperinflation (and the aim of bolstering confidence in German reparations payments) forced successive governments to tie the future of the nation to the gold standard as a safeguard against economic chaos. In this respect the economic historian Theo Balderston asserted that world financial markets drew a connection between the indiscipline of German fiscal politics and the gold standard regime, leaving the Reichsbank no room to finance the deficit. This in turn reinforced the government policy of expenditure cuts and tax increases from 1930 under the threat of Reich bankruptcy[45]. But in the turmoil of the Great Depression, deflation «provoked hunger marches and mass demonstrations» in the streets. Eichengreen and Temin detail how the government struggled to maintain the parity of the German currency in 1931 by reducing all prices by decree, half a year after having abandoned gold. Even the Socialists opposed monetary expansion at the time. All these policies led Germany to economic contraction, which for these authors would help the Nazis (who were against gold standard) to rise[46]. This argument would give credit to Polanyi's thesis.

Nonetheless, Germany was not the only country to turn to an authoritarian political system from 1920 to 1935. In his Notes on Sources in relation to Chapter 2, Polanyi lists the countries from Central and Eastern Europe in which a one-party government was established during the inter-war period: Estonia and Lithuania in 1926, Yugoslavia in 1929, Austria, Bulgaria and Germany in 1933, and Latvia in 1934. Obviously, fascist Italy in southern Europe should be included in this list, and Portugal's Estado Novo could also be added[47]. Here a question arises: given Polanyi's direct link between gold standard and the rise of fascism, was the impact of deflation harder on those countries which finally embraced authoritarianism?

The statistics compiled by the League of Nations in their Statistical Yearbooks allow us to study the changes in the retail price index (cost of living) in many countries throughout the 1921–1932 period. Table 1 shows the annual increase in retail prices in several European countries and the United States between 1921 and 1932. A classification has been made on the basis of the percentage of years with deflation, from highest to lowest, separate from the United States figures.

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[44] *Ivi*, p. 144.

[45] T. BALDERSTON, *Economics and politics in the Weimar Republic*, Cambridge, Cambridge University Press, 2002, p. 97.

[46] B. EICHENGREEN, P. TEMIN, *op. cit.*, pp. 202-205.

[47] The Falange Española fascist movement emerged in Spain under the wings of Italian fascism, but it had very little political support in the 1930s. Although they did have some relevance after the end of the Spanish Civil War, this was less than four months before the start of the Second World War.

Table 1. Evolution of annual cost of living in retail prices in Europe and USA, 1921–1932 (index numbers, 1914:100).

	1921	1922	1923	1924	1925	1926	1927	1928	1929	1930	1931	1932	% Years deflation
Norway	-7.7	-16.6	-5,6	9,6	1,7	-15,2	-9,7	-7,0	-4,0	-3,0	-5	-2.6	83,3
UK	-9.2	-19	-4.9	0.6	0.6	-2.3	-2.3	-1.2	-1.2	-3.7	-7	-2.7	83,3
Sweden	-8.2	-19.8	-10.1	1.7	1.7	-2.3	-1.2	0.6	-1.2	-2.9	-3.6	-1.9	83,3
Denmark	-11.1	-13.8	3	4.9	-2.3	-12.8	-3.8	-1.1	-1.1	-4.6	-6.1	0,0	75,0
Holand	-8.6	-9.9	-4.4	1.7	1.1	-6.1	0	0.6	-0.6	-4.2	-6.2	-6.6	66,7
Lithuania				23.6	11	-6.6	0	-2.8	-2.2	-14.2	-8.7	-16.2	66,7
Hungary					-6	-6.4	8.8	5.4	0	-9.4	-4.7	-3	62,5
Switzerland	-10.7	-18	0	3	-0.6	-3.6	-1.2	0.6	0	-1.9	-5.1	-8	58,3
Italy	22.4	-7.4	-1.4	6.7	15.9	7	-10.1	-9.9	2.8	-2.8	-8.5	-3.5	58,3
Finland		-2.7	0.7	2	3.6	-2.4	2	2.2	-0.6	-7.8	-8	-1.3	54,5
Estonia		7.1	12.1	-7.8	13.8	-0.9	-0.9	6.7	4.5	-11.1	-3.8	-6	54,5
Spain	-0.5	-4.2	-2.2	4	2.7	-1.1	1.1	-6.9	2.8	3.3	4.8	-4.6	50,0
Latvia		4.1	3.9	35	0.9	-1.8	-3.7	6.8	7.3	-14.4	-2	-7.1	45,5
Bulgaria	3.3	36.5	-5.4	14.4	6.4	-4.2	-3.4	4.4	2.9	-13.1	-18.5	0.8	41,7
Poland			21.2	101.6	15	21.9	-35.4	0	0.9	-6.9	-9.3	-8.2	40,0
Czechoslovakia					0.4	4.2	-1.1	4.3	0.1	-0.5	0.3	-4.4	37,5
Germany	17.4	331.4	-30.2		9.4	0.7	5	2.7	1.3	-4.5	-7.5	-11	36,4
Belgium		-7	17.2	17.4	6.3	21.3	23	2.5	5.8	3.6	-10.5	-9.8	27,3
Romania		30.9	46.4	19.4	8.9	9.3	8.5	2.8	7.1	-0.9	-28.6	-16.4	27,3
France			12.8	10.5	8.4	26.3	1.8	1	7.1	4.5	-2.1	-7.6	20,0
Austria	95.1	2544.4		17.3	9.1	7.3	2.9	1.9	2.8	0	-4.5	1.9	9,1
USA	-24.6	-7.2	2.8	0	7.5	2.5	-3.7	-0.6	1.9	-6.4	-17.7	-15.7	58,3

Source: League of Nations, Statistical Yearbooks, 1922-1933, own elaboration.

If we match Polanyi's list with the table, only two Baltic countries, Lithuania and Estonia, experienced deflation for more than half the analysed period. In all the other cases, price increases prevailed in the years of the period. That said, it could be argued for the sake of Polanyi's thesis that severe deflation impacted those countries in the early thirties, but it is also true that many of them (Austria, Germany, Latvia) abandoned the gold standard in 1931. The one country that did retain the gold standard until 1934 was the one to show the highest percentage of years with deflation among the countries with a one-party regime, Italy. However, deflation in Italy was a product of fascism, (Mussolini's commitment to the gold standard and an overvalued currency in the mid-twenties) and not the other way around[48]. Nevertheless, Polanyi sees no contradiction between this fact and his thesis, though his justification may sound unconvincing.

> The antidemocratic philosophy of fascism was already born, but was not as yet a political factor. Trotsky gave a voluminous report on the situation in Italy on the eve of the Second Congress of the Comintern in 1920, but did not even mention fascism, although *fasci* had been in existence for some time. It took another ten years or more before Italian fascism, long since established in the government of the country, developed anything in the nature of a distinctive social system[49].

In short, Italian fascism did not really develop into a recognizably fascist regime until the 1930s, which helps Polanyi sustain his logical sequence of gold standard-deflation-fascism. However, on reading Aldcroft's explanation, we find the implication to be the

[48] The so called *quota novanta* meant a revaluation of the Lira, following «the Anglo-American-sponsored international capitalism of the gold-exchange standard. [...] as a tragic caricature of that system» (Charles S. MAIER, *Recasting Bourgeois Europe: Stabilization in France, Germany, and Italy in the decade after World War I*, Revised Edition, Princeton, Princeton University Press, 2015, p. 577).

[49] K. POLANYI, *The Great Transformation*, cit., p. 251.

contrary. Citing the article *The 1927 Revaluation of the Lira: a Study in Political Economy* by J.S. Cohen, Aldcroft argues that Mussolini was able to enforce a deflationary adjustment policy (which involved an increase of unemployment) in the late twenties with more freedom «than his counterparts in the pre-war parity countries' because he had all the political authority of a one-party regime»[50]. In other words, his reasoning is that deflation did not pave the way for fascism, but rather that fascism paved the way for deflation.

The results of the table raise other question with respect to the gold standard-deflation-fascism causal link. Why did some countries with serious deflation problems both in the twenties and thirties manage to avoid authoritarian solutions? The Scandinavian countries (Sweden, in particular) offer us a very interesting point with regard to Polanyi's thesis, but we will deal with this later. For the moment, we can start with the two classic examples of the steady decrease in prices associated with loyalty to the gold standard, Britain and the United States. With the exception of Norway, both nations actually recorded the highest average fall in retail prices between 1921 and 1932 of all the countries in Table 1 (5.1 in the United States and 4.5 in the United Kingdom).

Eichengreen and Temin focus their analysis on the effects of the gold standard mentality once the Great Depression became a reality in four cases, those of France, Germany, Britain and the United States. We have already discussed the German case, while France was late to deflation as it remained in the gold standard system (leading the creation of the so-called 'gold bloc') until 1936. Polanyi's model seems to fit quite well in the light of Eichengreen and Temin's description of the events in Britain and the United States, surrounding the commitment of those countries' governments to gold standard-imposed deflation levels which, in the context of a harsh crisis, were no longer accepted by workers and unions, and with serious political consequences[51]. Why did they not follow the German political path? Polanyi has one answer for both cases.

The two prototypical liberal countries were able to save their democracies from collapsing along with the self-regulating markets in the 1930s, not mainly because they were «masters not servants of the currency»[52], but rather because both abandoned the gold standard in time. According to Polanyi, the United States and Britain shared this common factor. A second answer gives a particular explanation to the limited success of fascism in Britain (and France): «its antipatriotism»[53]. Unfortunately, as Polanyi does not go into detail in this matter, we have to concentrate on the shared factor.

The United States was able to both reject laissez-faire and avoid any temptation authoritarianism might have at the same time through the New Deal, which was implemented in the same year the country went off the gold standard (1933). However, things were much more complicated in Britain. Polanyi stresses that leaving the gold standard in 1931 did not mean dispelling its mentality. We have already noted his conviction that Britain followed a policy of stable exchanges and sound currency that would prevent the nation from quickly rearming. Eichengreen and Temin delimit this gold mentality inertia to 1932 when the Bank of England was still reluctant to reduce interest rates under the fear of fostering inflation[54]. At any rate, Drummond says that «Britain

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[50] D. ALDCROFT, *op. cit.*, p. 152.
[51] B. EICHENGREEN, P. TEMIN, *op. cit.*, pp. 192-193, 202.
[52] K. POLANYI, *The Great Transformation*, cit., p. 242.
[53] *Ivi*, p. 250.
[54] B. EICHENGREEN, P. TEMIN, *op. cit.*, p. 203.

soon discovered that a floating currency had its advantages»[55]. Consequently, by the summer of 1932 Britain had circumscribed its commitment to stable exchange rates to the Empire, while the pound would float for the rest of the world, leaving the Bank of England free to implement an inflationary policy. In the end, Britain's gold standard mentality seemed to have lasted barely one year.

Precisely, 1932 saw the peak of the biggest problem encountered by Britain in the entire inter-war period, unemployment. After 1921 the unemployment rate was never below 10 per cent of the working population, and it would exceed 20 per cent in 1931 and 1932. It was not until 1934 that unemployment began to decrease steadily, but the crisis had left deep wounds in the labour market. Long-term unemployment, which was around five per cent in 1929, reached twenty-two per cent between 1933 and 1937. In turn, this economic instability would also affect the political scene. The Labour Party government fell after barely two years in power, deeply affected by the sterling crisis of the summer of 1931. A National Government was formed comprising members of the Labour, Conservative and Liberal parties, with strong opposition from unions and the Labour party itself, which went so far as to expel the First Labour Party prime minister, Ramsay McDonald.

In such economic and political circumstances, it is not surprising that Brenton Priestley, in his analysis of the failure of fascism in inter-war Britain, writes:

> The British political climate was as opportune as it would ever be for a Fascist party to seize power; people were searching for leaders who stood for national interests and who had the power to remedy the ailing economy and political system[56].

In October 1932 Oswald Mosley, a high-profile figure in Britain after the Great War[57], founded the British Union of Fascists (BUF), influenced by what he had seen in Italy earlier that year. Initially a more left-wing politician, he embraced fascism convinced that the corporate state he saw in Italy would be the best way to bring prosperity and order back to Britain.

The BUF was an authoritarian and nationalistic movement. This seems to give little credit to Polanyi's claim that British fascism had little importance owing to its anti-patriotism. In fact, the nationalist approach was a dominant factor in the short-lived success of the Blackshirts. In June 1934 the BUF reached 50,000 members, when only a year and a half before there were 10,000. According to Priestley, the movement's downfall was due to a combination of a legislative offensive by the National Government and the party's espousal of anti-Semitic views. Nevertheless, he points out, that anti-Semitism was just an attempt to draw attention when it was realized that fascism was

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[55] I.M. DRUMMOND, *op. cit.*, 49.

[56] B. PRIESTLEY, *Oswald Mosley and the British Union of Fascists*: *Destined to failure*?, 2000, www.brentonpriestley.com

[57] A young MP in the 1920s, his 1925 book *Revolution by Reason* denied the sacrosanct relationship between extra purchasing power (through credit to the consumers) and inflation, at least in the severe situation of unemployment Britain was experiencing. In other words, Mosley was advocating a managed currency just as the country was about to return to the discipline imposed by the gold standard. Everybody ignored it. Five years later, as a member of the Labour government, he made several proposals concerning unemployment, including the so-called 'Mosley Memorandum'. He proposed high tariffs, nationalization of industries and a plan of public works. Once more, he was ignored, and he resigned his ministerial position and left the Labour Party to form one of his own.

increasingly losing its appeal as the threat of economic chaos and Communism receded[58]. Finally, liberal democracy proved to have a more solid basis in Britain than on the Continent

After all, if Britain was able to evade the peril of an authoritarian solution, it was due more to political and social factors, while economic (or monetary) issues seemed to play a secondary role. Polanyi himself expressed this idea in the early thirties. In an article for the previously mentioned Der Österreichische Volkswirt magazine, he talks about the philosophical ligation of democracy in the Anglo-Saxon countries, due to their Puritan background, a political culture those European countries which turned into dictatorships lacked[59].

At this point it is pertinent to ask to what extent fascism in inter-war Europe was the product of economic factors. Once again, history and sociology have already provided us with some answers.

Failure of economic liberalism, crisis and the rise of fascism

As we have previously expounded, Polanyi establishes a direct link between the failure of economic liberalism and the fall of several democracies in inter-war Europe. And though Polanyi frequently uses the word 'authoritarian' to describe the anti-democratic governments that spread all over Europe after the First World War, the last two chapters of the book (20 and 21) make no mistake about what he was referring to by this: fascism. Fascists were able to rule all across Europe because they emerged as 'an alternative solution of the problem of industrial society' (2001: 252), i.e. the ruinous condition of the free market system after the crash of 1929.

What do historians have to say about this particular issue, the economic factor behind fascism? To begin with, some answers can be found in the book by Michael Mann, *Fascists* (2004), because the author explicitly enquires into this subject. In particular, he revises different theories that have explained fascism through the economic factor. One set of those theories concentrates on the effect of the Great Depression. Thus, Mann studies whether the authoritarian coups d'état were preceded by a strong recession. He admits that this could be the case in many of the countries Polanyi mentioned in his end notes: Austria, Bulgaria, Estonia, Germany and Lithuania. Even 1919-1922 Italy could fit into those theories. Nevertheless, he points out that there is a different regional pattern between the north of Europe on the one hand, and the centre, east and south of the Continent on the other: all suffered from the crisis, but only in the second group was democracy replaced by authoritarian (and fascist) governments. Given that it is not possible to explain those differences based on economic factors alone, he concludes that economic difficulties were never decisive in the rise of the fascists[60].

If we accept this description, the emphasis on a conflict between economic classes worsened by the crisis would place Polanyi among the group Mann calls the «theorists of the capitalist class»[61]. For them, as well as for Polanyi, the fear of a socialist revolution by unions and labour parties would have made capitalists prone to authoritarian solutions. When people on the political right felt that both private property and social order may

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[58] B. PRIESTLEY, *op. cit.*
[59] K. POLANYI, *Wirtschaft un Demokratie*, cit.
[60] M. MANN, *Fascists*, Cambridge, Cambridge University Press, 2004, p. 58.
[61] *Ivi*, p. 59.

have been threatened, nationalism, statism and militarism were the ideologies they found to defend those principles. In so far as fascism sustained all those ideologies, the capitalist and conservative classes would have given their support to anti-democratic groups.

Nonetheless, Mann notes that «the most ambitious type of economic explanation could be only a partial, not a total, explanation» of fascism[62]. His thesis makes reference to four interconnected crises in the inter-war period: military, economic, political and ideological. Without these crises and the Great War that caused them, fascism would never have become a mass movement, he claims. In line with the idea expressed by Polanyi in the thirties, the way countries responded to the crises (including high inflation in the 1920s and the Great Depression in the 1930s, both capable of destabilizing governments) was different in those with a liberal democratic tradition compared to the «dual» states («half liberal democratic, half authoritarian»). In the first group of countries (north and west of Europe), crises prompted populist parties to search for solutions within the rules of democracy, while in the second group (in the centre, east and south of the Continent), the conservatives used the authoritarian half of the state, the army and the police, as a way of popular repression, «reducing or overturning the power of the state's parliamentary half». Fascism would eventually take advantage of the willingness of «authoritarian rightists» to explore more radical solutions in a context of growing nationalism and paramilitarism[63].

In contrast with Polanyi, Mann does not think of fascism as a product of the failure of liberalism, but rather «a product of a sudden, half-baked attempt at liberalization amid social crises»[64]. Since the defects of liberalism and the Great Depression, he states, affected the whole continent, it would not be correct to link them with fascism, given that half of Europe was able to avoid that authoritarian solution. Obviously, Mann understands liberalism more from a political perspective, and it is true that the crisis was unable to bring down institutionalized liberal systems. By the same token, he says that those liberal democracies that did survive had been able to develop economic strategies (the New Deal in the United States, social democracy in Scandinavia, splitting the Labour Party in Britain) to protect capitalism in the way, he notes, proposed by Keynes[65]. Therefore, it could be said that wherever liberal democracy rode out the crisis in the 1930s, it was through the abandonment of liberal economy, and thus giving credit to Polanyi's thesis.

Another reference work on this subject, *Liberalism, Fascism or Social Democracy* by Gregory M. Luebbert, supports Polanyi's view regarding the clash between politics and economics. The failure of liberalism prior to the victory of fascism did not necessarily mean the end of representative democracy, as long as it fulfilled the labour movements' demand that politics were to replace markets in the handling of the economy. Certain countries (France, Britain and Switzerland) presented an alliance between the liberal bourgeoisie and the workers' movement before 1914 that prevented the latter from defying the liberal order in the inter-war period. Other countries failed to develop such alliances as a result of the inability of liberalism to gather enough support from the bourgeoisie. Those countries finally turned into social democracies or fascist dictatorships[66].

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[62] *Ivi*, p. 64.
[63] *Ivi*, pp. 358-359.
[64] *Ivi*, pp. 354-355.
[65] *Ivi*, p. 196.
[66] G.M. LUEBBERT, *Liberalism, Fascism, or Social Democracy. Social Classes and the Political Origins of Regimes in Interwar Europe*, Oxford, Oxford University Press, 1991, p. 234.

Contrary to Polanyi's opinion, Luebbert sees no causal link between economic crisis and the rise of fascism from the perspective of compared history. Neither high inflation nor deflation offer explanations applicable to all the cases, he says. Rather, the causes of fascism would lie in the political field, as those described above[67]. However, it may be that the link between recession and fascism still worked for individual examples, which is why mention must be made of the main European fascist countries highlighted by Polanyi (Italy, Germany and Austria).

The inter-war years in Italy were characterized by economic difficulties and social turmoil. The historian Vera Zamagni accounts for all these problems in the so called *Biennio Rosso* or 'two red years' (1919-1920). Controls on foodstuffs imposed during the war, including rationing, lasted until the middle of 1921. The middle classes saw their income diminished due to high inflation, while unemployment grew steadily until 1921. At the same time, class conflict gained intensity through popular revolts (1919), strikes (1919-1920 especially) and factory occupations (1920). Nevertheless, Zamagni does not necessary link these events with Mussolini's rise to power. Instead, she believes the main reason to be «the inability of political parties to form a stable government»[68].

The American historian Charles S. Maier, in his work on interwar stabilization in Europe, states that historians have «perhaps overstressed the relative distress of the lower middle class in Italy […] especially […] the recession of late 1920 and 1921 […] seem less agonizing a social problem in Italy than in Germany from 1919 to 1933»[69]. Citing Italian commentators on fascism such as Missiroli or Renzo De Felice, Maier regards wartime inflation a relevant factor in the understand of why impoverished urban middle classes embraced fascism. In any event, he concludes that the victory of fascists was the product of «a socio-political continuum between town and countryside» in some particular Italian regions, where political instability and the incapacity of liberalism eased the way for Mussolini's black shirts[70].

In his chapter devoted to Italian fascism (the 'Pristine Fascists'), Michael Mann also refers to the economic factor. For him: «the economic problem was less one of recession than of the postwar class conflict»[71]. Class confrontation in Italy after the Great War involved not only employers versus employees but also rural landowners versus peasants. The fascists presented themselves as the solution to overcoming class conflicts, through nation-statism, attracting the favour of capitalists. Mann reflects on the reason for Italian capitalists rejecting Giolitti's reforms and embracing fascism, and he sees other causes besides economic ones. Thus, Mussolini took advantage of the Italian political crisis by flying the flag of nationalism and statism to attract the economic elites. In the end, he concludes that fascism in Italy was a product of the First World War, with one of its best representations being the paramilitary militancy in the *fasci di combattimento* of many young men demobilized after the war[72].

Luebbert's interpretation is in line with those made by Zamagni, Maier, and Mann. His view was that the economic factor played no part in the rise of Mussolini. In fact, he points out that Italian output grew at eleven per cent between 1919 and 1923. The failure

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[67] *Ivi*, p. 307.
[68] V. ZAMAGNI, *Industrial wages and workers' protest in Italy during the "bienio rosso": (1919-1920)*, in «The journal of European economic history», 20, 1, 1991, pp. 137-153.
[69] C.S. MAIER, *op .cit.*, p. 313.
[70] *Ivi*, p. 305.
[71] M. MANN, *op. cit.*, p. 99.
[72] *Ivi*, p. 95.

of liberalism in Italy was clearly a political issue. The American author revises all the political changes Italy experienced in the decade prior to the *Marcia su Roma* in October 1922. The failure to achieve liberal stabilization through political alliances gave room to Mussolini's radical solution, which had little support in the elections of 1919 and 1921. He notes that the inability of the successive governments to restore order in the cities and in the countryside helped Mussolini to come to power[73].

Therefore, it seems that the economic distress was not a determining factor in Italy. On the contrary, some scholars have observed a strong relationship between the Depression and the rise of Nazism in Germany. In particular, William Brustein supports this thesis in his book *The Logic of Evil*. If under three per cent of the electorate voted for the Nazis in 1928, and they were able to become the largest party in the 1932 elections with 37 per cent of the vote, the difference was the economic crisis. Many Germans perceived the Nazis to offer much better solutions to overcome the effects of the Great Depression than the other political options did[74].

Michael Mann discusses Brustein's conclusion, among his other economic arguments. Mann studies Nazi support (and militancy) by the economic classes, and finds that 'economic success thus helps to explain Nazism more than does deprivation'. In this regard, he notes that the Nazis became the major party of the radical right even before the Depression hit the German economy. Nonetheless, he agrees with other scholars in that «if there had been no Great Depression, there would have been no Nazi regime», because the economic crisis marked the end of the Weimar democracy. Consequently, «the core truth of economic explanations of Nazism», as Mann himself concludes, would be that Nazism was there before the 1930s crisis, but the crisis was a necessary determinant that brought it to power. He saw this as necessary but not sufficient, because «Germany was not in chaos», and economic recession was nothing that a democracy could not handle. This is why Mann concludes there were «other causes besides economic crisis» to consider, in particular the political weakness of the Weimar regime[75]. Once again, the failure of liberalism would have been more a political than an economic issue.

Charles S. Maier interpretation seems to be in line with Mann. Maier considers economic distress in the 1920s, inflation in particular, as a factor that first eroded rents and then radicalized the middle class in Germany. But he adds that it is also true that other groups (such as farmers) supported the Nazis when their debts had been liquidated as early as in 1923. Finally, in the context of deflation during the early 1930s, mass unemployment and the perceived inability of democratic political leaders to overcome it proved to be decisive for the end of Weimar's democracy. Nevertheless, he also stresses that the corporatist organization of German society was key to bringing together different economic groups under the same radical right-wing political response[76]. Here too, political causes interact with economic causes to explain the victory of fascism in Germany.

Economic history has also reviewed the debate over the impact of the economic downturn on Hitler's political success. Balderston deals with the possible link between Brüning's policy of deflation and Nazism. Labelled the 'hunger chancellor', Heinrich Brüning was the head of the German government from 30 March 1930 to 30 May 1932,

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[73] G.M. LUEBBERT, *op. cit*., pp. 284, 301.
[74] W. BRUSTEIN, *The logic of evil. The Social Origins of the Nazi Party, 1925-1933*, London, Yale University Press, 1988.
[75] M. MANN, *op. cit*., p. 201.
[76] C.S. MAIER, *op. cit*., pp. 363, 591.

a period in which the country saw unemployment rise to 6 million. His deflationist policy is believed by many to have caused misery, therefore creating a propitious atmosphere for the Nazis, a belief Polanyi had supported[77].

In any event, Balderston adds some political nuances: for example, when the chancellor dissolved the Reichstag and called the election (September 1930) in which the Nazis gained 105 seats, Hindenburg had his share of the blame by appointing Brüning so as not to depend on the Social Democratic Party (SPD) to pass his decrees. What is more, the SPD tolerated many of the measures implemented by Brüning's restrictive policy, and there was no support at the time for reflation in the Reichstag. The author points out that the problem was more political: the Brüning government was not seen by the German people as putting crisis management ahead of a balanced budget and reparations payments, which played into the hands of the Nazis and their anti-system strategy[78].

The economic review by Balderston offers us an interesting conclusion: the Nazi vote showed high sensitivity to the crisis. However, the Nazis came to power as the economic context was improving. June 1932 marked the end of reparations for Germany, and Von Papen's public works scheme achieved recovery in employment by the end of 1932. In this sense, the final elections of March 1933 did not respond well to that sensitivity to crisis[79]. But that was obviously after the Reichstag fire.

Finally, we have already seen Luebbert's contrary opinion on the rise of fascism as a consequence of the dynamics of the economy. This naturally includes the Great Depression. In particular, he states that the economic crisis cannot explain the success of Nazism. However, what for him is a key element, the support given by the rural bourgeoisie to Hitler, he considers to be somewhat economically motivated. He asserts that the Nazi Party was nothing more than a group of fanatics with no social roots until neither socialists nor liberals were able to solve agrarian misery. Deflation depleted agrarian revenues in the 1930s and led the landowners to advise their party (the *Zentrumspartei* or Centrists) to support the Nazis[80]. Again, an unstable economy somehow helped the Nazis.

While there is doubt as to whether the economic situation was crucial for Nazis on their road to power, it seems to have played a determining role in Austria. Michael Mann states that economic recession and fascism correlate quite well in inter-war Austria. What is more, «economic crisis was a major factor in the collapse of the republic and especially in the Nazi seizure of power». For many Austrians, integration with Germany was the best way to fight unemployment, as the Nazis had successfully done in their neighbouring country. The Great Depression had actually hit harder and lasted longer in Austria, but it is also true that Hitler's blockade of the Austrian economy had contributed to this situation[81].

Nonetheless, Mann makes some observations on the economic factor. German nationalism already existed when the economy begun to worsen in Austria, and mass unemployment did not turn many Austrians towards Nazi militancy. Given that the paramilitary variable was as important there as in Germany or Italy, the author concludes that other factors, apart from the economy, have to be considered to explain the Austrian

[77] T. BALDERSTON, *op. cit*., pp. 90-91.
[78] *Ivi*, pp. 91-93.
[79] *Ivi*, p. 99.
[80] G.M. LUEBBERT, *op. cit*., p. 284.
[81] M. MANN, *op. cit*., p. 222.

case, particularly that of being an «ethnic German» country[82].

According to Luebbert, the influence of Germany was decisive in the failure of Austrian parliamentary system. Thus, liberalism failed in Austria both during the late part of the empire and in the 1930s as the result of the country's international situation. On the contrary, he sees no link between the Great Depression and fascism in Austria. His point is that the economic downturn was as bad as it was in Germany, but in terms of electorate (he takes the local and regional elections of 1932 as his example) the Nazis had only minimum support, and in spite of extreme inflation in the 1920s and harsh recession, Austria only became a fascist nation after the *Anschluss* of 1938[83]. Here an important difference between Mann and Luebbert should be noted: the latter considered the philo-fascist Dollfuss regime of (1932–1934) a traditional dictatorship.

In summary, the link between economic distress and the rise of fascism in the 1930s was not the general rule in Europe. In reference to the main countries, it did not occur that way in Italy; it presented objections in Germany; while Austria seems to be the case with the best fit to that causal link. In any event, Polanyi's general consideration that market liberalism was followed in the 1930s by interventionist governments everywhere (whether authoritarian or not) is a fact that leads us to one final and important thought.

The overlooked Scandinavian model of social democracy in the 1930s

The deflation/inflation table shows that among the most highly ranked of the countries that suffered from deflation during the inter-war years were the Scandinavian countries of Norway, Sweden and Denmark. It is worth noting here that Sweden was one of the few countries (along with the United States, the Netherlands and some Latin American countries) to restore the gold standard in its full pre-1914 version. Swedish income and output felt twice as much in 1920-1922 than it did in the aftermath of the 1929 crash. Unemployment throughout the decade averaged 14.2 per cent in Sweden and 16.8 per cent in Norway. Apart from Germany, the countries that experienced the most severe strike activity in inter-war Europe were Norway and Sweden. Thus, it comes as no surprise that real wages grew above industrial output and real GDP in the Scandinavian countries. Those three elements (high unemployment, intense strike activity and quick real wages increase) were a challenge for Sweden and Norway's democracies as much as they were in Germany and Austria. In this regard, Luebbert's conclusion seems to be in line with Polanyi's proposition about the failure of liberalism. That failure did not prevent democracy from succeeding[84]. The basic condition was that politics had to substitute markets, exactly the point that Polanyi highlights in his book. And this is what happened through social democracy.

Following Polanyi's argumentation, the Social Democrats in Norway and Sweden achieved their economic goals through monetary expansion even more than they could through fiscal policy. Shortly after leaving the gold standard (1931, the same year that Britain left) social democracy broke with orthodoxy, issuing millions of crowns into their economies. Along with a fiscal policy of public works funded through higher taxes on the urban bourgeoisie, the Social Democrats created expectations of economic recovery in the 1930s. After the Social Democrats came to power in 1932, social democracy was

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[82] *Ivi*, p. 224.
[83] G.M. LUEBBERT, *op. cit.*, p. 265.
[84] *Ivi*, pp. 138-139.

consolidated in Sweden after the 1936 elections, and the Saltsjöbaden Pact of 1938 imposed a full employment programme on Swedish capitalists. The role of the state was to promote economic growth and centralized collective bargaining, and in return, private control was guaranteed for capital markets, firms and property[85]. Like fascism, those measures meant a break with economic liberalism, but unlike fascism, social democracy survived the war and the model, expanded to all the Nordic countries, reached its maturity in the 1950s.

Margaret Weir and Theda Skocpol studied Sweden's 'new deal', comparing it with the cases of Britain and the United States as a kind of Keynesian response to the Great Depression. They regarded Sweden as the world's first ever full-employment welfare state. Like Luebbert, these sociologists and political scientists find the root of the 'social democracy recovery strategy' in 1920s Sweden. The long tradition of a centralized state eased the way for public intervention and spending, even for the Liberals before 1932. It allowed the Social Democrats to finance extensive public works without having to trigger inflation and promote exports. At the same time, the role of Swedish economists (the so-called Stockholm School) in influencing recovery policies with state-sponsored reforms would have been even greater than that of Keynes in Britain. Ironically enough, Sweden was where «the earliest and fullest "Keynesian" policy successes» were achieved[86].

After all, what these authors are stressing could be summarized in this way: while fascism in Europe and the New Deal in the United States have attracted attention as paradigmatic examples of the rupture with laissez-faire economics in the 1930s, there was another response that was equally (if not more) successful and was destined to last a long time. Why did Polanyi overlook the Scandinavian (particularly the Swedish) case as a major example of his own thesis? No plausible explanation seems to justify why Polanyi did not write a single line about Sweden or Norway in the 1930s. And this neglect does not only apply to his most popular work. In his 1947 essay, *Our Obsolete Market Mentality*, Polanyi named several countries in which liberalism was being discarded. Among them were American New Dealers, European fascists and British Social-Democrats (sic), but no reference is made to the Scandinavian experience[87].

Conclusions

The Great Transformation was Karl Polanyi's chief intellectual achievement. His historical account of the difficult times Europe (and the United States) experienced between the two world wars had the virtue of being understood in a broader perspective, the rise and fall of market liberalism. Polanyi was also a pioneer in blaming the gold standard mentality for the persistence of the Great Depression into the 1930s. As we have seen, economic historians who have studied the gold standard and the Great Depression would also stress this link many decades later.

However, Polanyi's desire to sustain his thesis that the Great Depression marked the end of one hundred years of market economy, made him picture the gold standard as something that ceased to exist after the Great War: the last bastion of market liberalism.

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[85] *Ivi*, pp. 269-70.

[86] M. WEIR, T. SKOCPOL, *State Structures and the Possibilities for "Keynesian" Responses to the Great Depression in Sweden, Britain, and the United States*, in P.B. EVANS, D. RUESCHEMEYER, T. SKOCPOL (a cura di), *Bringing the State back in*, Cambridge, Cambridge University Press, 1985, pp. 107-164.

[87] K. POLANYI, *Our Obsolete Market Mentality*, in «Commentary», 3, 1947, p. 116.

The gold standard was never the same after 1914, and though it was only in the 1930s when the system collapsed, the essence of an economic device independent of political intervention (represented by servomechanisms), was already a thing of the past in 1919.

The second part of his thesis, that the end of market liberalism also brought down liberal democracy in many European countries is more debatable. The gold standard-deflation-authoritarian regime link does not seem to have operated that way, and Polanyi himself may have changed his initial emphasis from inflation to deflation. Of the three paradigmatic fascists regimes of the thirties, Nazism does not seem to be the direct result of economic crisis, although it certainly helped Hitler in his bid for power; fascism in Italy had no connection with that link; only Austria seemed to present economic reasons for the rise of fascist solutions, but it is also true that its condition as Germany's neighbour had much to do with it. In any event, historical sociology understands the rise of fascism in Europe through more complex mechanisms, and explains the continuity/fall of liberal democracy more in terms of the political agreements (liberal parties, workers) that were respectively present and absent prior to 1914.

Finally, some countries did share membership of the gold standard, harsh deflation in the 1920s and the final implementation of an economic response to the crisis that was even further from laissez-faire than it was from the New Deal: Scandinavian social democracy. Polanyi neglected to mention the cases of Sweden and Norway in his historical account, and we have no clue as to why he did so. Perhaps he saw social democracy as a rebuttal of his main thesis, as seen in his statement: 'Inevitably, society took measures to protect itself, but whatever measures it took impaired the self-regulation of the market, disorganized industrial life and thus endangered society in yet another way' (2001: 4). On the contrary, what social democracy did was to protect business from the recession and promote industry in their countries. And its success marked the path many western countries would take after the Second World War.

By the time *The Great Transformation* was reissued as a paperback in 1957, the developed world experienced the rise of mixed economies everywhere. The so-called Golden Age of Capitalism was also known as the Age of Keynes, three decades of market intervention, welfare states and economic growth under the international monetary system created in Bretton Woods. There would be no sign of self-regulating markets until 1980, and no sign of fascism in Europe. But apparently, all those realities were not strong enough to make Polanyi reconsider some of his ideas, as if he were still writing in the first half of the 1940s.