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Debates, plans and interventions to overcome the 1931 banking crisis in Romania and Bulgaria¹

Debatten, Pläne und Interventionen zur Überwindung der Bankenkrise von 1931 in Rumänien und Bulgarien

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Abstract

In summer 1931, the Austro-German banking crisis propagated in Romania and Bulgaria. In the Romanian case, the management of the crisis confronted three types of protagonists - politics, bankers and central bankers - and positions about the relevant attitude to adopt, in to avoid or not the Marmorosch Blank Bank bankruptcy. In Bulgaria, the management of the crisis was more consensual. The intervention of the Bulgarian National Bank allowed to refund the more important banks, while other 34 were declared bankrupt and smaller ones silently disappear. One of the largest banks in Bulgaria, Credit Bank, has been rescued. Archive documents, reports of participants and comments from contemporaries, emphasize the different conceptions of the function of lender of last resort by the different

¹ The authors would like to acknowledge Hans-Michael Trautwein whose comments and remarks have helped to improve the quality of this text. They are also indebted to Valentin Fuscan and to the participants of the Conference *International Lending of Last Resort in Historical and Theoretical Perspectives*, Schlaues Haus Oldenburg, 16-17 September 2021 for their comments, remarks, and suggestions.

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protagonists in front of this systemic crisis.

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1 Introduction

The role of Lender of Last Resort initially defended by Thornton then Bagehot was not presented during long decades as something natural, safe and efficient. It was however a practice of quite all Central Banks, alone, and sometimes cooperatively.⁴ The defense of the principle was probably difficult during the inter-war period due to its incompatibility with both real-billist and quantitative approaches, the first being dominant especially in US until early-1920s' and the other gaining influence after the diffusion of Fisher and Pigou views from this time. The pro-cyclical real-billist doctrine was promoting accommodation (on a real bills' basis) during booms, but restrictive attitudes during crises, while the strict quantity approach was *in se* less against counter-cyclical measures but was also mined by the idea that an excess of credit is the cause and not the remedy to banking crises.

Over time, both with the revival of Thornton and Bagehot writings and with the observation of Central Banks attitudes during the last 50 years banking crises, the condition of Central Banks interventions were detailed and discussed, according the nature of the crises, the microeconomic form of the illiquidity of individual banks, and more recently the systemic nature of banks in difficulty or the risk of contagion of the crisis. The opinion of specialists then ranks from a restrictive vision (accommodation only when the recipient is strictly facing liquidity problems, no macroeconomic or systemic considerations) to a elaborated conception of the role of the Central Banks in situation of crisis. Given the international transmission of financial crisis, the distinction between liquidity and solvency should not be relevant at the macroeconomic level: only the systemic criteria would finally matter at the global level, which pleads for the implementation of some international equivalent to Central Banks for dealing with International banking crises.

In the early 1990s, Bordo⁵ and Black⁶ presented the restrictive/orthodox view, which explains the natural exposition of banks to liquidity crisis but also insists on the necessity to maintain a relatively high discount rate for the provided liquidity. In defense of a more accommodative attitude, Charles Goodhart advocates assistance to insolvent banks, both since the distinction is not always clear and because of the risk of propagation of crises.⁷ In between, more elaborated approaches invite to distinguish financial systems with rather liquid or illiquid assets in the

⁴ The episode of the first rescue of the Barings in 1890 is an example of such international cooperation of Central Banks in the objective to avoid a bank failure and a systemic crisis.

⁵ M. D. Bordo, The lender of last resort: alternative views and historical experience, in: FRB Richmond Economic Review 76 (1), 1990, pp. 18-29.

⁶ R. Black. In support of price stability, in: FRB Richmond Economic Review 76 (1), 1990, pp. 3-6.

⁷ C. A. Goodhart, Why do banks need a central bank? In: Oxford Economic Papers 39 (1), 1987, pp. 75-89.

balance sheets of the banks. In the first case, the assistance should be given freely and without limitations, but it should be discretionary in the second case.⁸ Literature also discusses the nature and quality of the assets to be accepted in counterpart of liquidity⁹ or explains that open market practices must be promoted when possible instead of discount windows.¹⁰

The banking crises we study in this paper occur at a time when these discussions have not yet been fueled. The 1931 banking crisis in Central Europe was the not the first inter-war crisis in Europe, but the previous ones, in Austria, Hungary or Germany were directly linked to the post-war situation and were for the most sovereign crises, even when they appear as for the most monetary crises. The 1931 crisis is a crisis of the private sector. The general context is well known: fragility of the financial sector in a region reshaped by the war, the differed effect of the US Great Depression and overall its effect on agriculture, little experience and background of Central Banks learning their new responsibilities and frequently advised by foreign experts, division of Europe between winners and losers with the unsolved question of war reparations payments. Romania and Bulgaria are two Balkan countries, but with different histories, cultures, and especially they were on two different sides during the war. The crisis could not be exactly the same in both countries and the solution exactly identical in both cases. We present crises and solutions in the rest of the paper, and try to understand in which way both countries implicitly debated and explicitly applied or not the Lender in Last Resort principles.

The Section 2 presents the economic background of the crisis in both countries. Section 3 presents an gives and account of the crisis in Romania and the measures adopted by the authorities to rescue the banks and the financial sector. Section 4 draws the parallel in the case of Bulgaria. The final section synthesizes the way each government and central bank adapted the lender of last resort principle to the situation of the country.

2 The 1931 general context in Balkan countries

2.1 The contagious Austrian crisis

The Austrian crisis of 1931 is generally considered to be the main European replica of the American crash of 1929. Austria was a country weakened by the defeat of 1918. A mission of the League of Nations had to be assigned to it in the immediate post-war period to solve a problem of hyperinflation. But the 1920s proved to be better. Economic activity had picked up and the Credit-Anstalt had become the major bank that could finance most of the growth in Austria and even in its close neighbors and former dependencies. But from late 1929, the contagion from Wall Street crash gradually slowed activity in Europe. The bank's liquidity was affected everywhere.

⁸ F. Fecht/M. Tyrell, Optimal lender of last resort policy in different financial systems. in: Monetary Policy, Financial Crises, and the Macroeconomy, 2017, pp. 27-57. Springer.

⁹ V. Bignon/C. Jobst, Economic crises and the eligibility for the lender of last resort: Evidence from 19th century France (Working Paper Series 2027, European Central Bank, 2017).

¹⁰ G. G. Kaufman, Lender of last resort: A contemporary perspective, in: Journal of Financial Services Research 5 (2), 1991, pp. 95-110.

The Credit-Anstalt was more exposed than the average given its dynamism and its risk level. Between May 8th and 11th, the bank was forced to suspend payments and then declared bankruptcy. A huge literature has been devoted to elucidating the causes of this sudden and rather unexpected crash¹¹.

The German banking system was the first to be affected, but the countries of the Danubian basin were not spared. The contagion severely affected Hungary. "Even though Austria had a larger economy than Hungary did, it had fewer bankruptcies and liquidations, and their number did not increase during the period."¹² The contagion took a double form. On the one hand, the slowdown in activity multiplied the number of defaults, which ultimately affected the liquidity and solvency of banks. On the other hand, the multiplication of bank-runs deprived institutions of their remaining liquidity and turned them to illiquid partners, and finally to Central Banks, to honor their commitments and avoid bankruptcy. This sequence is typically the one that affected Romania, with specificities linked to its political context and to the structure of its banking system.

2.2 The banking system and its environment in Romania

2.2.1 The banking system in Romania in 1931

The enlarged size of the country¹³ and the need to find appropriate sources of funding motivated the emergence of new banking institutions and resized older ones. This development was

¹¹ See C. P. Kindleberger, *The world in depression, 1929-1939*. University of California Press, Berkeley, and Los Angeles, 1984; A. Teichova/P. Cottrell, *Industrial structures in west and east central Europe during the interwar period*, in: *International business and Central Europe, 1918-1939*, 1983, pp. 31-55; P. L. Cottrell, *Mushrooms and dinosaurs: Sieghart and the Bodencreditanstalt during the 1920s*, in: *Universal banking in the twentieth century, finance, industry and the state in North and Central Europe*, 1994, pp. 155-177; A. Schubert, *The credit-anstalt crisis of 1931*. Cambridge: Cambridge University Press, 1991. pp. 205, tables, graphs, in: *Austrian History Yearbook 26*, pp. 292-294; and F. Macher, *The causes of the Austrian crisis of 1931*, in: *The Economic History Society*, 2015, pp. 145-150 for a classification of the theses.

¹² F. Macher, *The causes*, p. 9.

¹³ Romania emerged in 1859 with the unification of the principalities of Wallachia (the South of contemporaneous Romania, with Bucharest and Craiova as main cities) and Moldavia (a region further west than the current Republic of Moldova, located between the Eastern Carpathians and the Dniester River), followed in 1877 by the proclamation of independence from the Ottoman Empire. Romania became a Kingdom in 1881. From this period, politics, followed by intellectuals, developed the idea of integrating other neighboring regions with a majority or strong minorities of Romanian speakers. The First World War, during which Romania made opportunistic alliance choices, led to the gain of important territories. Transylvania extended by Banat in the South and Maramures in the North was won over Hungary. It was a huge territory west of the Carpathians with a strong Hungarian-speaking and a significant German-speaking communities. Bessarabia corresponds approximatively to the contemporaneous Republic of Moldova: this territory, momentarily under the domination of Russia from 1912 but with a majority of Romanian speaking people, declared its sovereignty as the Moldavian Democratic Republic in 1917, then voted in 1918 its union with Romania. The small Bukovina was historically populated by Romanian and Ukrainian populations of equal importance with two German and Polish minorities, the latter two contributing to the choice of an integration to Romania in 1918. Last, in 1913, the Treaty of Bucharest which ended the Second Balkan War had unaccountably assigned the South Dubroja to Romania, a region where only 2% of people were at this time Roman speakers while 48% were Bulgarian (the rest was for the most a huge minority of Turkish speakers, but also Roma and Tatars).

encouraged by successive governments, even when the new financial entities were the fruit of foreign investment. "In reality, the banks have been kneecapped first and foremost by their own fault, by the credit inflation they indulged in after the war, along with monetary inflation, because of the policy of unlimited investment policy which they pursued indiscriminately, the fault of megalomania of their leaders."¹⁴

Marmorosch Blank Bank was the biggest and one of the oldest Romanian banks in the early 1930s. It resulted from the merger in the late 1800s of two institutions respectively created by Iacob Marmorosch and Mauriciu Blank during the end of the Ottoman domination on Balkans.¹⁵ During the 1920s, it exercised the leadership over the Romanian banks, with 25 branches in Romania and 4 abroad (Paris, Istanbul, Vienna and New York). It was also connected with many foreign banks (German, Hungarian or French in particular) and, following the German model, it took various participations in local industrial companies.

The *Banca Generala a Tarii Romanesti*, the *Banca Chrissoveloni*, the *Banca Bertkovici*, the *Banca de Credit Român*, the *Banca Commercială Română*, and the *Banca Commercială Italiană și Română* were other big banks among a population which increased every years until 1930. Their capital stocks were quite always internationalized and diversified, the connexions with Paris, London, Vienna or Milan being the more important.¹⁶ Bucharest was frequently chosen for the headquarters but all the country and especially the cities of average dimension hosted branches and sometimes headquarters of small banks.

2.2.2 The French mission (1929-1933)

The post-war depreciation of the *leu* and the inability of successive governments to conduct a rigorous and appropriate policy-mix led the Romanian government to look for an international stabilization loan in the late 1920s. After discussions with the Bank of England and the League of Nations, an agreement was finally reached with *Banque de France*. A stabilization loan (also labeled the 7% external loan) was provided to the Romanian authorities with the contribution of New-York financial place, with a soft commitment on its use controlled by a French mission. Charles Rist, previous Deputy Governor of *Banque de France*, then Roger Auboin, were delegated as advisors, and as part of a small French team were influential on National Bank of Romania (NBR) decisions, but not really on successive government's financial choices and orientations.¹⁷

One of the main advice was to restore the convertibility of the leu at a depreciated level

¹⁴ C. Argetoianu, *Memorii*. Vol. 9. Machiavelli, 1997. București, p. 268.

¹⁵ I. Vorovenci, *The Evolution and Collapse of the Marmorosch-Blank Bank*, in: *Business Excellence and Management* 5 (3), 2015, pp. 40-46.

¹⁶ P. Marguerat, *Les investissements français dans le bassin danubien durant l'entre-deux-guerres : pour une nouvelle interprétation*, in : *Revue historique* (1). 2004, pp. 121-162.

¹⁷ K. Mouré, *French money doctors, central banks, and politics in the 1920s*, in: *Money Doctors*, Routledge. 2005, pp. 154-181, and D. Torre/E. Tosi, *Charles Rist and the French missions in Romania 1929-1933. Why the 'Money Doctors' failed?* In *Economic and Financial stability in Southeast Europe in a historical and comparative perspective* (Conference proceedings of the 4th meeting of the South-Eastern European Monetary History Network). 2009, pp. 91-106.

when compared to the prewar one, as it had been the case for the French franc *de facto* in 1926 and *de jure* in 1928. Its application was followed by a first months restoration of the NBR's exchange reserves, and by an increase of trust in Romanian monetary authorities. The mission encountered more difficulties on the financial side, as successive governments were unwilling or unable to acquire the financial autonomy that would allow them to finance increasing expenditures through receipts and taxation. The prospect of a new 'development loan' promised for 1931 kept the tensions at a reasonable level but, from 1932, the relationships between Romanian administration and the French mission eventually deteriorated: the default of the Romanian State and the return of the *leu* to inconvertibility, finally occurred in 1933.¹⁸

The financial events of summer 1931 occurred just after the payment of the second loan (the development loan) at a time when trust had not yet really disappeared between the two parties. As the facts will make clearer, the main disagreements took place in 1931 summer between the members of the government, dominated at that time by the authority of a newly installed king, and the economists - Romanian and French - in charge of the central bank.

2.3 The banking system and its environment in Bulgaria

In contrast to Romania, Bulgaria was a defeated country in two consecutive wars (the Second Balkan War and the First World War). As a result, in addition to the deprivations from the military conflicts, including territorial losses, Bulgaria suffered serious financial and economic burdens (mainly reparations), respectively results of the treaties of Bucharest (1913) and Neuilly (1919). Industrialization progressed slowly and Bulgaria remained an agrarian country (about 75-80% of the population).

Bulgaria was politically and economically dependent on the Great Powers, much of the country's foreign debt was 'political' with a weak economic efficiency. Capacities to issue domestic debt were extremely limited. The constraints of public finance and monetary system were set from abroad. A Reparations Commission was set up under the League of Nations. In addition to reparations payments, the servicing of pre-war debts was controlled (under the Bondholders Committee). Control was exercised through representatives of these structures in the central bank (Bulgarian National Bank/BNB) and the Ministry of Finance.¹⁹

As in most countries after the war, Bulgaria experienced inflation, depreciation of the lev, and growing public and payment deficits.²⁰ Between 1924 and 1928, the stabilization of the *lev*,

¹⁸ D. Torre/E. Tosi, Ibid.

¹⁹ A significant restructuring of all these debts was implemented in 1925 (see H. Prost, *La liquidation financière de la guerre en Bulgarie*. Marcel Girard. Paris. 1925, and N. Stoyanov, *Reparations and Inter-Union Debts*. Bulgarian State Debts. Ed. Glushkov, Sofia. 1925).

²⁰ G. T. Danailov, *Les effets de la guerre en Bulgarie*, Volume 1. Les Presses Universitaires de France; New Haven: Yale University Press. 1932. See also J. Petkof, *Prix, circulation et change en Bulgarie de 1890 à 1924*. Jouve & Cie Editeurs, Paris. 1965, A. Focarile, *Bulgaria d'oggi nei suoi aspetti sociali, economici, commerciali e finanziari*. 1929, J.-P. Koszul, *Les efforts de restauration financière de la Bulgarie (1922-1931)*. Félix Alcan, Paris. 1932, D. V. Molloy, *La crise mondiale et la Banque nationale de Bulgarie (Etude de Documentation Economique)*. Ph. D. thesis, Paris. 1934,

legally formalized in 1928, took place with the help of the two loans (the Refugee Loan of 1926 and the Stabilization Loan of 1928), under the auspices of League of Nations. The gold-exchange standard recommended by the Genoa Conference was adopted. Bulgarian stabilization, due to balance of payments and debt constraints, was carried out in a regime of strict exchange controls and a monopoly of the Central Bank over the foreign exchange market.²¹

The stabilisation of the lev was accompanied by a profound change in the BNB legal and institutional framework. BNB became a pure bank of issue and a bank of banks (Law of October 1928). The Bank was freed from all kinds of commercial industrial and mortgage lending, its operations concentrated mainly on short-term credit (maturity 3 months), on discounting and rediscounting commercial papers, pledging gold, etc. The 1928 Act abolished the possibility of commodity credit, as well as the opening of current accounts with two signatures. Illustratively, if in 1926 the discount portfolio in the balance sheet of the BNB was about 43%, in 1928 it already exceeded 60% (in 1939 it became 100%). Interaction with the state was limited and strictly regulated.²²

Experts under the Financial Committee of the League of Nations supervised compliance with the new monetary regime. After a debate on 'deflation vs. devaluation' and about the exchange rate level to adopt, Bulgaria finally opted for the devaluation as the exchange rate is set at 92 leva for 1 gram of pure gold, or taking into account the commission, it makes 139 leva for 1 dollar (according to the gold content of the dollar). This represents a 27-fold devaluation of the gold parity of the lev before the war. Technically, the currency reform in Bulgaria was largely inspired by the reform in France.²³

The banking system was growing rapidly, consisting of numerous financial institutions, which was in clear contradiction with the weak economic development of the country. It was built in the form of a pyramid, at the top of which stands the BNB. The other two large state-owned banks are the Bulgarian Agricultural Bank (which inherited the agricultural funds/*zemedelski kasi*) that had a dominant position and financed the agricultural credit cooperatives (around 1400), and the agricultural sector as a whole. Interestingly, the Bulgarian Agricultural Bank played the role of a

N. Nenovsky/G. Pavanelli/K. Dimitrova, Exchange control in Italy and Bulgaria in the interwar period: History and perspectives, in/ *Economic Alternatives* 1, 2017, pp. 5-33, *N. Nenovsky*, Theoretical debates in Bulgaria during the great depression, confronting Sombart, Marx, and Keynes, in: *Oeconomia. History, Methodology, Philosophy*, 2012. pp. 67-101, and *T. Marinova*, La Bulgarie et la grande guerre (1912-1919) - quelques questions en discussion parmi les économistes bulgares de l'époque, in : *Revue d'histoire de la pensée économique* (10), 2020, pp. 287-315.

²¹ *N. Nenovsky/G. Pavanelli/K. Dimitrova*, Exchange control.

²² *BNB*, Jubilee Collection of the Bulgarian National Bank 1897-1929. State Printing House, Sofia. 1929, *A. Hristoforov*, A Course in Bulgarian Banking. Part I Historical Development. edition of the "General Fund for the Support of Students and Higher Educational Institutions in Bulgaria, Sofia. 1946, and *A. Hristoforov*, Central banks in modern conjunctural theories. Yearbook of High School of financial and administrative science, Sofia, 5. 1946, pp. 1-72. For more information on the banking system in these years, see *N. Nenovsky/T. Marinova*, The first steps of the lender of last resort in Bulgaria. History and debate during the Great Depression. *Economic Thought*, 2022, 67(1): 7-28 (in Bulgarian).

²³ *N. Nenovsky/D. Pavanelli/K. Dimitrova*, Exchange control.

mini central bank, and a mini LOLR with respect to credit cooperatives. The other state-owned bank Bulgarians Central Cooperative Bank was primarily focused on craft credit and performed similar mini LOLR functions.

The next portion was the cooperative banks operating in the field of crafts (*popolyarni banki*) (they were over 200 banks), which specialize in credit to artisans and independents. The private banking sector (about 160 banks) was grouped: by (1) a few large joint-stock foreign banks and branches of the leading Western banks, mainly concentrated in Sofia (specializing in lending to large industry and financing foreign trade), there were Credit Bank, Bulgarian German Bank, Balkan Bank, etc.; (2) two large Bulgarian banks (Bulgarian Commercial Bank and Girdap); and (3) a hundred small Bulgarian banks, scattered all over the country. To these credit institutions may be added the Postal Savings Bank. All banks maintained certain unregulated liquid amounts with the BNB, through which they settle their mutual accounts.

Between 1925 and especially after the legal stabilization in 1928, there was a strong inflow of foreign capital, which strengthened the BNB's reserves and created conditions for uncontrolled credit expansion. This occurred both through the two loans concentrated in the BNB and through the inflow of short-term private capital within foreign banks (deposits of parent banks in their branches in Bulgaria). The fixed exchange rate as well as higher interest rates in the country were the main drivers. Credit growth intensified in 1928-1929, and outpaced strongly that of deposits. The foreign exchange reserves of the BNB began to melt. Almost half of this growth was accounted for by private foreign banks. Commodity credit (for which there are no statistics) was growing particularly strongly.²⁴ In this state of credit euphoria and lack of regulation, the first blows of the crisis fell on the Bulgarian economy at the end of 1929.

3 The banking crisis of summer 1931 in Romania

Two phases can be distinguished in the Romanian 1931 crisis. The first wave affected all banks without distinction. The ingredients were the same as in Austria (slowdown of the activity, multiplication of defaults, rapid depreciation of real assets previously considered risk-free) but the massive withdrawals of liquidity - by big or small depositors - were often decisive in the massive demands for liquidity addressed by the banks to the Central Bank to prevent default and bankruptcy. After this first phase of the crisis to which answered a cautious but reasonable management of the NBR, the second wave was specifically linked to the treatment of the Marmorosch's situation. During this phase, the motives behind the Romanian state's decisions are highly questionable, while the central bankers seem to have lost sight of the systemic nature of the crisis in order to apply a solution which now appears as microeconomically sound but probably too severe to promote a rapid recovery.

3.1 The first phases of the crisis

²⁴ D. Yordanov, The supervision of private banks in Bulgaria and its influence on their activity, in: Journal of the Bulgarian Economic Society 42 (1-2). 1943, pp. 23-43.

In May and early June 1931, the crisis diffused rapidly from Austria to Hungary, but also Romania, which was economically linked with both countries. The Central Bank and the government initially limited to observe the propagation of this crisis.

First the banks of Transylvania were concerned, but rapidly the contagion propagated everywhere in the country. "The wind started to blow harder at the end of June. who fell was the *Banca Generale*. Stuck in Creangă's hands after the war and nationalized under the liberals, the unfortunate institution fell under the tutelage of nice people but who had no idea about the bank, either of economy [...] The *Banca Generale*, however, had stakes in good business (as the Bank Bessarabia, for example)".²⁵

The 'old Romanian provinces' were not spared and the main banks of Bucharest ended up to be concerned by liquidity and sometimes solvency problems: after the *Banca Generale*, the *Banca Chrissoveloni*, the *Banca de Credit Român*, the *Banca Commercială Română* among other. On June 30, a real 'run' occurred at the *Banca de Scont*, to which 157 million rediscounts had to be granted by the NBR in one day.²⁶

The extent of the crisis can be observed in the evolution of the requests for rediscount, in the evolution of the capital of the banks and in the number of banks itself during the period (see Tables 1 and 2).

Table 1: Papers rediscounted by the NBR during the crisis.²⁷

	Papers presented for discount	Discounted papers	Proportion of accepted papers
April	1635	1169	71
May	1538	1192	78
June	2287	1564	68
July	4465	2612	58
August	4302	2838	66
September	3099	2366	76
October	5589	4447	80
November	3367	2277	68
December	2862	2228	78

²⁵ C. Argetoianu, *Memorii*. p. 273.

²⁶ C. Rist, *La Banque de France 1926-1929*. Papiers Charles Rist, Archives de la Banque de France. 24/2. Bolgert to Moret, July 6th, p. 3.

²⁷ Source: V. Slavescu, *La situation Economique de la Roumanie et sa capacité de paiement*. 1934, p. 47.

Table 2: The Romanian banking system before and after the crisis.²⁸

Year	Number of banks	Total amount of capital
1927	1.054	8.319
1928	1.122	10.000
1929	1.097	11.181
1930	1.102	11.627
1931	1.037	11.879
1932	953	10.587
1933	893	9.992

3.2 Iorga-Argetoianu position

The Iorga-Argetoianu administration in charge during the crisis was also the only one not directly dominated by the two main Romanian parties during the period. It was the result of an attempt of King Carol to take the lead of the situation, or “to break the barriers of traditional Governments”²⁹ from Spring 1931. His first choice was to ask Nicolae Titulescu, then Romanian delegate in London, to head the new government. Titulescu negotiated with the main political leaders but failed to obtain a consensus. The King then chose the charismatic historian Nicolae Iorga to substitute him: Iorga was free from any close link with the main political parties, he had been the francophile defender of irredentism and Romanian nationalism, previously in sympathy with left wing positions, but now closer to the ‘third way’ agrarian options. His profile made him the ideal leader for a consensual government. Constantin Argetoianu was in charge of Finance. He had also been a member of the Board of Directors of the Marmorosch³⁰ whose main leaders he knew well.

It is difficult to know what Iorga thought about the crisis and how best to deal with it. Few things have remained of him on this episode, although he was a so prolific writer before and after. Clearly, he delegated to Argetoianu the economic and financial decisions, when the King did not take them directly. Argetoianu was a cautious man, one of the only interwar Romanian politicians to escape both fascist executions and slow death in communist prisons. At the end of his life, he wrote in Romanian 11 volumes of memoirs. One of them is partly devoted to the crisis of 1931. This text is a precious record of the intertwining of political and business life in the interwar Romania. It however offers few precision of the objective of Iorga administration when it decides to approve the actions of the NBR to defend attacked banks. Argetoianu considers overall important to justify his proactive attitude in the defense of the Marmorosch from July. He then writes: “What I did for Blank Bank, I would have done for any other; I did it for *Banca Bercovici*,

²⁸ Source: Arnaldo Mauri/Claudia Gabriella Baicu, Il sistema bancario romeno fra le due guerre, Working Paper 2010-03, Università degli Studi, Milano, 2010.

²⁹ M. Ilie, King Carol II's Political View-from the “Governing over the Political Parties” Formula to the Authoritarian Regime, in: Revista de Stiinte Politice (62). 2019.

³⁰ C. Argetoianu, Memorii. pp. 270-271.

for *Banca Chrissoveloni*, for the Bank of Moldova".³¹ However, the situation of these three banks was not identical. Didn't Argetoiani see it?

3.3 Auboin as a cautious lender of last resort

The French position was consensual until the Blank crash. Besides, this attitude was recognized and appreciated by the government. "I had during the hardest moments, the loyal, disinterested and intelligent cooperation of the *Conseiller Technique* Roger Auboin, without whom would not been removed many of the obstacles we encountered along the way."³² In his correspondence with Clément Moret, then Governor of the Bank of France, or with Charles Rist, Auboin mentions for the first time the local consequences of the financial crisis on June 19th. He describes the first effects of the financial crisis in Central Europe. He comments deposit withdrawals in Bucovina: the situation is reflected in a loss of £525,850 since the beginning of June, compared to a strengthening of £32,000 in May³³. In this same letter, he relates an arrangement associating "a group of big Romanian banks with the BNR" to rescue the *Banca Generale*.³⁴ He also refers to the case of the *Chrissoveloni bank*. Also in big difficulty, the bank asked for a discount of 100 million lei against an industrial paper that has been properly immobilized, because it is asked for an immediate reimbursement of 100 million. The opinion of Auboin seems this time rather negative "It is quite impossible that we immobilize ourselves again to give this bank sums destined to amounts intended to ask us for foreign currency"³⁵ and in spite of Auboin's apparent serenity, we understand that two of the biggest Romanian banks are already affected, that one has been helped (rescued?) by the National Bank, while the case of the other is still under discussion.

Barely 10 days later, in a letter of June 29th addressed again to Rist³⁶, the tone changes. This time it is a long list of defaults that Auboin announces to his reader. The case of the *Banca de Credit* seems the less serious. The *Banca Generale* that Auboin considered saved 10 days earlier, is now declared bankrupt. "The *Banca Generale* has requested a preventive concordat. It has long since lost all its capital, all its reserves and 100 or 200 million beyond that and claimed to maintain itself with the help of the National Bank. We have only admitted a help of the other banks in the form of a mortgage on the building of the *Generale*, but the events have obliged to unmask a bankruptcy really acquired for a long time."³⁷ Auboin also mentions the *Banca de Scont*, in the same situation than the *Banca Generale*. Auboin continues on the case of the *Banca Chrissoveloni* about which he expresses reservations. He discusses the conditions of an help of the NBR to *Chrissoveloni* mentioning two risks: (i) to fund foreign partners who would withdraw their participation, (ii) to take as sincere falsified accounting documents. Auboin sounds like a Central Banker when he writes to summarize the situation: "In short, my impression is that one should

³¹ Ibid. p. 281.

³² Ibid. p. 286.

³³ C. Rist, La Banque de France 24/2. Auboin to Rist. June 19th.

³⁴ Ibid.

³⁵ Ibid, p.3.

³⁶ Ibid, Auboin to Rist, June 29th.

³⁷ Ibid, p. 3.

be careful not to commit oneself unnecessarily to banks whose liquidation one should hope for, but if necessary act vigorously if there is a danger for the few main banks and that, in this case, I should not hesitate to ask for temporary help from Basel; all this being accompanied, of course, by an effort to amortize, save on overheads, etc."³⁸ However, Auboin was only the head of the French mission to the NBR and not its governor. Mihail Manoilescu has been the head of the NBR for some months. We will see what influence he had on the subsequent events. From the end of June, however, we can think that Auboin's assurance reflects a convergence of views between his own analysis and that of Manoilescu. No doubt about it: Auboin obtained Manoilescu's agreement on the application of his discretionary choices regarding the rescue of banks in difficulty. Under the attitude of the Manoilescu-Auboin team, there is a tendency to distinguish temporary liquidity problems from more serious solvency problems, to refund the first and not the second.

From June 30th, Auboin corresponds with Pierre Quesnay, now the first director of the young Bank of International Settlements, to inform him of the situation and prepare a possible demand of this institution, if the situation compromises the situation of the Central Bank. He clarifies once again the Manoilescu-Auboin doctrine. "The National Bank, in agreement with me, has adopted the following attitude: a very prudent policy with regard to the banks whose difficulties stem from management failures, but energetic and rapid support for the main banks threatened by the simultaneous withdrawal of deposits, the aid to the banks being naturally subordinated to a close monitoring of their real situation."³⁹ The events that followed would destabilize both the NBR and Auboin's cautious but healthy attitude.

3.4 The Marmorosch crash

The Marmorosch bank was led by Aristide Blank, the son of Mauriciu Blank, a complex personality who maintained close links with various political protagonists of the period, with a decisive influence of this network on the course and outcome of the 1931 crisis. In particular, after supporting some of Iorga initiatives in the mid 1920s, Blank chose to promote the come-back of King Carol "with whom he still had a friendship from the period of his Parisian exile (1927-1930)."⁴⁰ It is likely that the King's eagerness to save Blank's bank at any cost in the summer of 1931 was prompted by these earlier ties between the banker and the sovereign. This eagerness would only have been a sign of appreciation if Blank's management had been above reproach, which was not the case. Argetoianu⁴¹ and other ulterior commentators, previous collaborators to the bank, revealed later that Blank defrauded associates such as Ion G. Duca⁴² and George II of Greece. But that is not all. An impressive list of the bank's fraudulent operations were for

³⁸ Ibid, p. 4.

³⁹ Ibid, Auboin to Quesnay, July 9th.

⁴⁰ C. Secașiu, Biografia lui Aristide Blank (ii), in: Realitatea Evraică, 2018, pp. 1322-1323. See also the Wikipedia article devoted to Aristide Blank in Romanian language.

⁴¹ C. Argetoianu, Memorii. pp. 270-272.

⁴² who will be Romania Prime Minister in 1933 and will be killed as many other democrats of this period, by members of the Iron Guard in 1938.

instance revealed in the parliamentary discussions by Florin Zaharia, Deputy of Iasi.⁴³

While for the majority of banks the crisis was a liquidity crisis, caused by the bank run due to the loss of confidence following the Austrian crisis, or the search for liquidity by partners in Austria or Hungary, the Marmorosch crisis was a real solvency crisis. During the crash, the bank only exhibited overpriced guarantees: “a plot of land (Bordei) owned by the bank was overvalued by about leu 200 million, while its stake in Banca Industrială was overrated by leu 1,590 million.”⁴⁴ This situation was quickly identified as such by the most astute observers, including the current central banker and the most sagacious members of the French mission. This was the beginning of the second phase of the Romanian crisis, during which the partners who were working together to save the system clashed over the means of doing so, and in particular over the conditions for rescuing the banks in difficulty.

Auboin and Manoilescu, previously ready to accommodate all situation of temporary illiquidity, were now opposed to intervene in the case of Blank. In a letter addressed to Manoilescu and intended to list what it is possible or not to do in favor of the Marmorosch, Auboin writes that “the National Bank may not exceed the framework provided for in the draft agreement, nor may it make any advance not covered by a riskless and realizable asset.”⁴⁵

3.5 The attitude of King Carol II

As previously noted, “King Carol II was [...] a close friend of Aristide Blank.”⁴⁶ This proximity, added to the ambiguous attitude of Argetoianu, himself previously member of the Blank’s board, motivated a series of specific initiatives to the rescue of Marmorosch bank, quite all unjustified by the situation of the bank. Argetoianu then proposed (but probably as a result of an idea from King Carol) to merge the banks of the syndicate created by the NBR to rescue banks in difficulty. When the project failed, he then proposed a takeover of the state over Marmorosch Blank.

This extreme defense of a bank that was not above suspicion, generated immediate or delayed reprobation. In a letter of September 24th, commenting on much earlier events, Bolgert handwrote: “On August 12, we [probably Manoilescu, Auboin and Bolgert, and possibly Argetoianu] had taken the decision to drop Blank. The king received Arget. Monoil.(sic) and Auboin. On their way out, they informed the members of the NBR Committee, who were very surprised, that the intervention would continue. Only one man could have opposed it without any risk: the one who had been brought from abroad so that he was protected from any political influence.”⁴⁷

⁴³ F. Zaharia, *Politica Bancară a Guvernului în Fata Parlamentului*. București, 1932.

⁴⁴ E Blejan/B Costache/A Aloman. *The National Bank of Romania during the Great Depression*. National Bank of Romania, Bucharest, 2010, p. 20. Given the crisis and deflation, it is nevertheless difficult to consider the whole overvaluation as a sign of deliberate concealment.

⁴⁵ C. Rist, *La Banque de France 24/2*. Auboin to Moanoilescu. August 6th, p. 4.

⁴⁶ E Blejan/B Costache/A Aloman. *The National Bank*, p. 20.

⁴⁷ C. Rist, *La Banque de France 24/2*. Bolgert to Moret. September 4th, p. 1.

Another member of the mission completed the account of the royal initiatives. It is Henri Guitard, whose positions can be compared to those of Bolgert. In a letter to Lacour-Gayet⁴⁸ dated September 2th, he wrote: "Recently, we learned that the defender of the interests of the NBR and the State at the Blank Bank will be Mr. Burillianu, former Governor of the NBR, of a notorious financial incompetence, having ties with Blank, and who seems to be willing to support Blank, in order to return to the King's favour."⁴⁹

3.6 Bolgert inflexibility

The French mission was directed by Auboin, although by delegation from Charles Rist. It also included several collaborators, located at the NBR or at the Ministry of Finance. Among them, Jean Bolgert had without doubt the strongest personality. The tonality of his letters, addressed to Moret or Rist, contrasts with the more diplomatic style of Charles Auboin, whose measured positions he did not share. His first intervention is from July 6th. He already points out at this date the abnormal swelling of the Bank's assets, generated by the increase of the rediscount activity. Concerning the crash of the *Banca Generale*, he explains that "the Bank refused to waste its resources on a bank whose recovery seemed impossible. [But] the fall of the *Generale* has nonetheless awakened the public's distrust."⁵⁰ He relates the interventions of the NBR in favor of the *Banca Românească* explaining that given NBR balance sheet and the decrease of reserves in external currency, it would not be possible to go further."⁵¹

In a letter to Manoilescu on September 11th, Bolgert detailed the delays in the operation to form a syndicate of the main banks in Bucharest to rescue Blank. He has serious doubts about the process chosen and the course of the operation to rescue the bank.⁵² In a subsequent letter on October 8th, Bolgert provides a chronology of the actions taken by the state to save Blank and also outlines his own perception of this limitless rescue. He ends up this letter writing: "Technically, any solution that does not correspond to the *de facto* liquidation of Blank Bank and the ousting of its 'animator' is doomed to failure."⁵³ Referring to the king's abusive protections of the Marmorosch management, Bolgert also writes: "We are heading for a real regime crisis [which will actually come much later]. Morally, I do not wish to be associated any longer with this malpractice, and to accept, by my presence, any responsibility in a policy of which I have always disapproved."⁵⁴

3.7 Manoilescu position and dismissal

Since January 1927 Dimitrie Burillianu, who was more a lawyer than an economist, was Governor of the NBR. His relations with the French mission had never been excellent but they deteriorated

⁴⁸ then Director of the Research Department at *Banque de France*

⁴⁹ C. Rist, La Banque de France 24/2. Guitard to Lacour-Gayet. September 2nd, p. 3.

⁵⁰ Ibid, Bolgert to Moret, July 6th, p. 3.

⁵¹ Ibid, pp. 4-5.

⁵² Ibid, Bolgert to Manoilescu, Sept. 11th.

⁵³ Ibid, Bolgert to Moret, Oct. 8th, p. 1.

⁵⁴ Ibid., p. 2.

during the winter of 1931. At that moment, the second part of the French mission was negotiated between the French and Romanian authorities. In return for obtaining the benefit of the development loan, the Romanian authorities (at that time represented by the Prime Minister Iuliu Maniu and the Minister of Finance Mihai Popovici) approved the extension of the mission until 1933, under the authority of Charles Auboin. Burillianu was opposed to it and made it known: the crisis ended with his replacement in March by Constantin Angelescu.⁵⁵ Constantin Angelescu was not an economist but doctor in Medecine. He had been member of the Liberal Party, and participated to various Liberal governments during the 1920s, in particular as a specialist of education policy. His name is proposed by the King but in complete agreement with Argetoianu. "But only 3 months after his appointment, the Constitutional Court of Romania decid[ed] to invalidate the royal decree which removed Dimitrie Burillianu from his position as governor of the of the National Bank of Romania."⁵⁶ Angelescu was dismissed, Burillianu was no longer a candidate (the banking crisis had already started and the place was no longer very attractive considering the personality of the King). The King (probably with the agreement of Iorga) but without/against the advice of Argetoianu chose Mihail Manoilescu.

As many Romanian nationalists, Mihail Manoilescu was at this moment considered as close to the King: as Blank, he contributed to his come-back from the late 1920s. But Moanoilescu was an economist. He was already known for his attempts to justify protectionist practices in certain phases of economic development. His refutation of the Ricardian principle of comparative advantages would later make his reputation, especially in developing countries, where he was considered as an advocate of protected industrial development.⁵⁷ He was currently serving as minister of industry in the Iorga government when the King chose him to head the National Bank. Manoilescu had probably the most interesting personality of the Romanian politicians of that period. He had the mental strength and the decision making capacity to stand up to the King but also to other strong personalities within the French mission. He also had the economic competence that the other holders of decisional functions during the period did not have.

But Manoilescu did not have only friends, both among the agrarians and among the liberals. For Argetoianu, it was for sure a bad choice. "I didn't trust Manoilescu, I had swallowed him at the formation of the Ministry because the King had imposed him on us. I expected him to make us one every day. If I had to take it from home and to install it at the National Bank, I would never have consented."⁵⁸ Finally Argetoianu was convinced that Manoilescu, more than Auboin, was responsible of the negative attitude of Central Bank in the Blank bank crash, and that he did so for personal reasons: "I'm not talking about Manoilescu, who passionately hated Aristide, sabotaged as much as he could and delayed the National Bank's action."⁵⁹

⁵⁵ See for this episode *I. Racianu*, L'indépendance de la Banque nationale de Roumanie en question : le gouverneur Burillianu et la mission de la Banque de France au début des années trente, in: *Histoire, Economie, Société*, 30(4). 2011, pp. 19–28.

⁵⁶ *Ibid*, p. 28.

⁵⁷ See N. Nenovsky/D. Torre, Productivity-based protectionism: a Marxian reconstruction of Mihail Manoilescu's theory, in: *Journal of Economic Issues* 49 (3), 2015, pp. 772-786, and N. Nenovsky/D. Torre, Manoilescu's approach of losses of trade: a Ricardian interpretation, in: *Economic Alternatives* (1), 2018, pp. 49-54.

⁵⁸ C. Argetoianu, *Memorii*. p. 279.

⁵⁹ *Ibid*. p. 283.

The story is probably less Manichean. In interaction with Auboin but on his own initiative, Manoilescu “insisted on the creation of a syndicate comprising *Banca Marmorosch Blank*, *Banca Româneasca*, *Banca de Credit a României*, *Banca Moldova* and *Banca Chrissoveloni*. The purpose of this association was to provide ailing banks with the required commercial paper to obtain liquidity via rediscounting with the NBR.”⁶⁰ However this initiative was at the beginning of his problems with politics. When the King and Argetoinau proposed a takeover of the bank by the state he refused this arrangement in the name of financial orthodoxy and given the unclear situation of the bank. The inflexibility of Manoilescu led to his dismissal from the NBR and to the come-back of Constantin Angelescu who renounced after 5 months to keep the position of Central Banker. As the historians of NBR now note it, “looking beyond the drama of small depositors this episode ended with a renewed breach of central bank independence in relation to the state.”⁶¹

4 The banking crisis of summer 1931 in Bulgaria

In Bulgaria, the origin of the crisis is twofold. Initially, it is an agricultural crisis. It only became a banking crisis when the financial crisis that had started in Austria spread to Germany.

4.1 The agrarian crisis and the waves of the banking crisis

In the autumn of 1929, the first consequences of the Great Depression reached Bulgaria. Its first effect was a fall in the prices of agricultural commodities (grain, tobacco, rose, etc.). This movement was combined with strong distortions of relative prices. In the period 1929-1932, for example, while the prices of agricultural products fell by around 60 %, those of industrial products fell by only 30 % (in some commodity items prices even rose) (Table 3).

Table 3: Wholesale price indices in gold leva (base 1914 = 100).⁶²

	Foods, plant origin	Food, animal origin	Textile	Fuels	Building materials	Miscellaneous	Total index
1929	155	134	155	108	104	124	131
1930	98	103	121	98	96	128	106
1931	74	79	89	92	87	94	84
1932	68	68	82	90	83	81	76
1933	59	59	81	89	89	79	71

Source: Mollof, *La crise mondiale*, p. 146.

Falling prices automatically lead to debt deflation *à la Fisher* (debt and tax burdens rise in real

⁶⁰ *E Blejan/B Costache/A Aloman*. The National Bank, p. 19.

⁶¹ *Ibid*, p. 21.

⁶² Source : *D. V. Mollof*, *La crise mondiale et la Banque nationale de Bulgarie* (Etude de Documentation Economique). Ph. D. thesis, Paris. 1934.

terms), which hits peasant incomes hard. At the same volumes of production, their monetary income was reduced by more than twice over the same period. Non-performing loans in the banks (see protested bills, Table 3) started piling up rapidly, the liquidity reserves of banks in the BNB melted.

Table 3: Protested bills, insolvencies (bankruptcies) and moratoriums.⁶³

	Protested bills (number)	Underwritten bills (million leva)	Insolvencies (number)	Moratoriums (number)
1928	200 000	1 432	95	153
1929	250 000	2 213	107	211
1931	350 000	over 3 000	224	619

Source: Hristoforov, A Course, p. 163. See the data in Molloy, *La crise mondiale*, p. 137; and K. Kossev, *The Banking Sector and the Great Depression in Bulgaria*, Bulgarian National Bank, DP/68, 2008.

This was the first wave of the banking crisis, which started at the end of 1929 and lasted through 1930. There was an outflow of capital, mainly from foreign banks, and a withdrawal of deposits. The above dynamics are illustrated in Table 4.

Table 4: Deposits, own funds, and placements of all domestic and foreign banks (million BGN).⁶⁴

	Own Resources (1)	Deposits and foreign funds (2)	All (3) = (1) + (2)	Placements (claims)	Number of banks
1929	1157	6959	8116	8442	135
1930	1247	5888	7135	7412	138
1931	1376	4464	5840	6510	131
1932	1343	3918	5261	5361	128
1933	1256	3293	4549	4406	119

Source: M. Rusenov (Ed.), *History of the Financial and Credit System in Bulgaria*. Vol. 2: From Liberation to 9 September 1944, Varna 1983, p. 728.

The BNB started to lose its foreign exchange reserves and raises its discount rate from 9% to 10%. The latter provoked a new deflationary spiral. The BNB's discounting volumes grew rapidly. The BNB helped mainly the big banks, and less often the small ones, which went into insolvency and stopped payments.

The debt problems in the agricultural sector and the difficulties in the banking system triggered the state's response and it made a number of institutional and regulatory innovations aimed at

⁶³ Source: A. Hristoforov, *A Course*, p. 163. See the data in D. V. Molloy, *La crise mondiale*, p. 137, and K. Kossev, *The Banking Sector and the Great Depression in Bulgaria*, Bulgarian National Bank, DP/68. 2008.

⁶⁴ Source: M. Rusenov, (ed.) (1983). *History of the financial and credit system in Bulgaria*. Vol. 2 From Liberation to 9 September 1944, Georgi Bakalov Publishing, Varna, p. 728.

creating rules in credit and a financial safety net. The main act was related to the 'Deposit Protection Act (*Zakon za zashtita na vlogovete*)', and the accompanying creation of the Bankers' Council (*Bankerski savet*) under the Ministry of Finance (Law from January 12th, 1931). The Bankers' Council proposed regulatory frameworks for banking registration, capital, liquidity and operations of banks, provisions for bad loans, balance sheets statistics, etc. Of particular interest for monetary policy was the introduction of a compulsory percentage of liquidity reserves in accounts with the BNB on savings deposits and on the total amount of deposits attracted.⁶⁵ The liquidity of individual banks and the banking system as a whole, its measurement and control, became central to the new framework of banking supervision. In his report for the Bulgarian Economic Society, Dimitar Yordanov provides at this occasion a definition of liquidity:

"The safety of bank capital, whether own or foreign, is directly dependent on the liquidity of bank placements. Therefore, the most important issue that we will consider next is the question of liquidity. Liquidity must be understood as the ability of an undertaking to meet its payment obligations. Liquidity can also be referred to as willingness to pay. Liquidity is the ratio between payment obligations and the assets available to cover them, calculated at a given date."⁶⁶

Yordanov also presents its specific measurement grouping assets by liquidity and liabilities by degree of maturity, according to the practice of the German school of bank accounting and business administration and in particular of Wilhelm Kalveram.⁶⁷

The second wave of the banking crisis, accompanied by a currency crisis (i.e., taking the form of a 'twin crisis) came in the summer and fall of 1931. It was provoked by the onset of the banking turbulences in Austria and Germany, itself the result of the devaluation of the British pound. There was a powerful new push of short-term capital flight by foreign banks. For Bulgaria, of particular relevance was the German banking panic, which was reflected as an attack on Credit Bank (*Kreditna banka*) on July 14th, a day after the attack on the headquarters of the shareholder Deutsche Bank. Between July 14th and 19th, the largest foreign bank (like Marmorosch in Romania) was subjected to a run on deposits. Most small Bulgarian banks started to lose capital and went bankrupt (BNB helped only some of them by discounting their securities). BNB was also starting to take a big hit, its profits shrinking by 38%.

As an end point, the BNB's reserves, despite the introduction of a foreign currency monopoly (*de facto* suspension of convertibility while preserving the exchange rate level), melted rapidly and

⁶⁵ see D. Yordanov, The supervision of private banks in Bulgaria and its influence on their activity, in: Journal of the Bulgarian Economic Society 42 (1-2), 1943, pp. 23-43.

⁶⁶ Ibid, p. 40.

⁶⁷ Primarily, W. Kalveram, Goldmarkbilanzierung und Kapitalleitung, Berlin-Wien, 1925, Organisation und Technik des bankmäßigen Kontokorrentgeschäfts, Stuttgart: Poeschel, 1933, and Bankbetriebslehre, Berlin, Spaeth & Linde, 1939. It should be noted that the German School of Accounting was leading in Bulgaria, see G. Georgiev, Nature and goals of the annual balance sheet in terms of balance theories, in: Yearbook of the Higher School of Commerce, Varna, Vol. 15, 1943, pp. 1-164.

the BNB was actively seeking refinancing from abroad. From October 1931, centralisation of the foreign exchange market at the BNB and a de facto suspension of convertibility was reintroduced. The country quickly took the path of clearing and compensation agreements, and entered the orbit of Germany's *Lebensraum* living space.

As a final, a third wave of banking crisis corresponds to the problems in the banks in 1933-1934. These were largely provoked internally, by political populism and legal interference of the state. These interventions consisted mainly in the two laws passed in March-April 1932, the one 'for the relief of debtors', and the second 'to protect the farmer-holder'. The two laws were typical measures that provoked moral hazard and adverse-selection, and generally undermined the 'debtor's payment morale'. As a final result, and despite the warnings of most economists and BNB experts, the populist decisions were having a knock-on effect on the behavior of depositors and bank customers who withdrew deposits and suspended servicing of their debts expecting new relief. The BNB was called in again to discount and rediscount large volumes of paper, and to seek refinancing abroad.

The state was moving towards new institutional solutions such as the creation of the Sinking Fund (*Pogasitelna Kasa*), and accelerated bank mergers and consolidation. These several institutional solutions to the banking crisis could be seen as specific LOLR forms and as steps in building a comprehensive safety net (LOLR, deposit insurance and bank regulation).⁶⁸

4.2 Sinking Fund and bank consolidation

Despite the fact that they were implemented late after the beginning of the crisis, the sinking fund and the operations of banking consolidation were organized or/and encouraged by the BNB.

The Sinking Fund was created in August 1934: it issued 2, 10, 15 and 20 year 3% bonds against the "convertible mass/volume" of canceled debt. Those assets were backed by claims from the Government and partly from the peasants. The total amount of relief is on average about 30% of the total debt, and this varies according to the three categories of debtors. The main burden was shifted to the budget; the state has to make its regular contributions to the sinking fund. In turn, against the forgiven liabilities, Sinking Fund bonds appear in the banks' assets (for example, in 1938 Sinking Fund bonds represented 1/4 of the banking system's balance sheet). According to A. Hristoforov in the same year the two state banks (Bulgarian Agricultural Bank and Bulgarians Central Cooperative Bank) concentrated about 36% of bonds. The remaining 21% were held by popular banks and 7% by private banks.⁶⁹ Later the Sinking Fund bonds can be discounted at the BNB in case of liquidity problems. It is the possibility of this indirect way of refinancing banks during a liquidity crisis that gives us motive to consider the creation of the Sinking Fund as a kind of substitute for the traditional LOLR. Despite this possibility (discounting at BNB, that was rarely used), banks' lending was shrinking sharply.

⁶⁸ For more details on BNB's Lender of Last Resort activities and debates among the Bulgarian economists, see N. Nenovsky/T. Marinova, *The first steps*.

⁶⁹ A. Hristoforov, *A Course*, p. 186.

One of those proposing the Sinking Fund was the economist Slavtcho Zagorov (1898-1970).⁷⁰ He also promoted concrete financial engineering, seeing clearly the problems of moral hazard resulting from debtor forgiveness laws. Another important economist, Ilia Palazov (1888-1964), was also critical of the debtors' laws previously proposed by government and establishing a moratorium for 30% of the debts contracted by the farmers before 1931, while he supported the Sinking Fund. According to I. Palazov, debts cannot be calculated (especially commodity credit), and besides, "the time will soon come when the government will bail out the banks and depositors with reverse laws."⁷¹ Kiril Nedelchev, the author of numerous studies on monetary topics and foreign trade of Bulgaria⁷² shared the same views.

Other economists supported debtor laws but were skeptical about the need for a Sinking Fund. For example, Nikola Kamenarov⁷³ believes that the Sinking Fund blocks huge amounts of 'dead' capital, and that a radical reduction of the discount rate of the BNB and of interest rates in general is needed to make them correspond to the profitability of economic activity. He also considers that this is the only way to unblock lending. Marxists economists were also active and provided interesting analyses. Specific manifestations of the financial crisis, for example the state of the banking sector⁷⁴, or the structure of debtors⁷⁵, are examined through the prism of Marxist analysis and a number of Lenin's premises. Terziev makes an original statistical analysis of the structure of debtors at a time of discussion on debt simplification (1931/1933) and compares the different models of reform proposed by Dimitar Mishaykov, Petko Stoyanov, or Slavtcho Zagorov. According to Terziev, only the poor debtors should and could be saved.

The second form of the LOLR substitute is the decision for a large-scale consolidation of the surviving and rescued Bulgarian banks. Thus, as early as 1930, 12 small Bulgarian joint-stock banks were merged into the United Bulgarian Bank (*Saedineni Balgarski Banki*), and later in 1934 it itself merged with 7 other joint-stock banks to form the Bulgarian Credit Bank (*Banka Balgarski Kredit*). These were practically bankrupt banks that could not be saved by BNB after being placed under special supervision (among them were mostly small and medium-sized banks in Sofia, including 'Sofia Bank'⁷⁶). The state had almost half of the capital of the Bulgarian Credit Bank (50 out of 120 million BGN), and the BNB immediately opened a loan of 100 million *leva* to it against a guarantee. The new bank was systematically supported by the BNB, and this gives us reason to believe that this consolidation is a form of LOLR measure. For many years to come, the Bulgarian Credit Bank would dominate the country's banking landscape (e.g. in 1935 it accounted for 80% of the capital,

⁷⁰ S. Zagorov, Assistance to distressed debtor farmers and strengthening of credit in Bulgaria, in: Journal of the Bulgarian Economic Society 32 (1), 1933, pp. 1-9.

⁷¹ I. Palazov, The problem of debtors' relief, in: Journal of the Bulgarian Economic Society 31 (4), 1932, pp. 205-224.

⁷² Collected in K. Nedelchev, Problems of Bulgarian Economy, 1941.

⁷³ N. Kamenarov, The impact of low prices on farms and their debts, in: Economic Thought 3 (2), 1933, pp. 23-489, and N. Kamenarov, Deepening the crisis, in: Economic Thought 4 (3), 1934, pp. 147-159.

⁷⁴ N. Kovachev, Banking capital in Bulgaria, in: Zvezda, 1931-1932, pp. 722-731.

⁷⁵ V. Terziev, Debts and debtors, in: Zvezda, 1931-1932, pp. 947-954.

⁷⁶ L. Berov (ed.), Bulgarian National Bank at 120 years (1879-1998). Draft. BNB Ed., Sofia, 1999, p. 98.

deposits and reserves of all joint stock banks).⁷⁷

Mergers continued at various levels. In 1934, the two large state-owned banks, Bulgarian Agricultural Bank and Bulgarians Central Cooperative Bank merged to form Bulgarian Agricultural and Cooperative Bank. Similar processes occurred among foreign banks in the country; these generally followed the mergers and takeovers of parent banks abroad. In their case, it started as early as 1929, when Credit Bank (*Kreditna banka*) (whose main shareholders are Disconto-Gesellschaft and Norddeutsche Bank), specialized in foreign trade and industrial contacts, merged with the Bulgarian branch of Deutsche Bank. As a consequence of this consolidation movement, the architecture of the banking system simplified dramatically, and in general as a result of several waves of banking crises and BNB regulatory measures, and its banking volumes and total lending reduced considerably.

4.3 The traditional discounting and rediscounting policy

Turning specifically to the classic LOLR function, during the three waves of the banking crisis the BNB actively discounted various types of commercial and sovereign papers. Decisions on which banks to lend liquidity to, and against what collateral, were made discreetly by the BNB Board and the Discount Committee (which included the two deputy-governors, the President of the Sofia Chamber of Commerce and Industry, the Governor of the BAB and the Head of the Budget Department of the Ministry of Finance). In this respect, there is a many of documents and files which testify to professionalism and objectivity, with no trace of political pressure or affiliation (see the debates at the meetings, BNB, 2004). In fact, compliance with the rules of the LOLR became particularly rigorous after the bankruptcy of the Bucklow Brothers Company (*Bratya Baklovi*) in September 1929.

Table 5 : Structure of the BNB's assets (in millions and %).⁷⁸

⁷⁷ M. Rusenov (ed.), A Course in Bulgarian Banking. Part I Historical Development, Vol. 2 From Liberation to 9 September 1944. Georgi Bakalov Publishing, Varna. 1983, p. 633.

⁷⁸ Source N. T. Kirklisiiskii, Findings on the credit activity of banking institutions with a view to their impact on the more important branches of the Bulgarian national economy, in: Yearbook. Varna University of Economics. Varna, I (1): 1941, 1; 3; 5; pp. 7-135; pp. 137-182.

	Banks and bankers		Trade		Industry		Miscellaneous	
	Million leva.	%	Million leva	%	Million leva	%	Million leva	%
1926	130,5	14,7	330,4	39	342	40	79,1	6,3
1927	332,5	34,1	265,5	27,2	315,4	32,3	62,4	6,4
1928	446,4	34,6	368,6	28,6	417,5	32,4	56	4,4
1929	787,8	55,4	276,6	19,4	301,5	21,2	57,1	4
1930	316,8	50,1	124,7	19,7	149,6	23,7	40,7	6,5
1931	383,9	66,4	98,6	17,1	78,2	13,4	17,8	3,1
1932	263,3	61,7	84,6	19,8	63,7	14,9	15,3	3,6
1933	351,5	74,4	62,8	13,3	47,5	10,1	10,5	2,2
1934	250	67	59,7	16	36,8	9,9	26,5	7,1
1935	552,2	85,3	42,9	7	38,2	6,2	8,5	1,5
1936	398,1	78,8	47,11	9,3	53,5	10,6	6,3	1,3
1937	835,9	83,5	100,2	10	45,3	4,5	19,7	2

Source N.T. Kirklisiiskii, Findings on the Credit Activity of Banking Institutions with a View to their Impact on the more important Branches of the Bulgarian national Economy, in: Varna University of Economics Yearbook, I/1, Varna 1941, pp. 7-135; pp. 137-182.

Generally speaking, it can be argued that the BNB and the Bankers' Council respected the principles of Bagehot. They knew them not mainly theoretically, but also by observing the Western Central Banks policy. Only illiquid (but solvent) institutions were refinanced, BNB lent liquidity only against quality collateral (priced by the market) and this was done at high penalty rates (*i.e.* throughout the crises the BNB discount rate remained high). The BNB's archives hold the documents of the discussions and decisions to refinance individual distressed banks as well. In the vast majority of cases, the condition (solvency or liquidity) of each institution, its importance for the country and for local business, the quality of guarantees, collaterals, etc. were carefully analyzed.

After 1934, due to restructuring and regulations, as well as the contraction of the banks' lending activity, the latter's liquidity reserves in accounts at the BNB grew. However, exposures to banks in the BNB's portfolio were still dominant, around 80%.

Of particular interest is the monetary authority's reaction in a systemic crisis, in the rescue of a systemic banking institution. This was the case with the BNB's reaction during the banking panic against the Credit Bank (Monday 14 - Saturday 19 July 1931), whose main shareholder was Deutsche Bank. The event was the first of its kind and mobilised the attention of the main economic and political actors in Bulgaria.

Both the dynamics of panic and the response of the BNB as LOLR are a perfect illustration of what is known from LOLR theory in a systemic crisis. The story is described in the memoirs of the director of the Credit Bank, *Marco Ryaskov* (1883-1972). Ryaskov was subsequently Governor of the BNB and Minister of Finance. He was also one of the most trained and respected economist and bankers in the country and abroad, a Dutch and German graduate. Below we take the liberty

of a lengthy quotation that tells the story of the LOLR in a highly synthesized and picturesque form.

"However, I calculated that if the run (mass withdrawal) continued the next day, the bank would be put in an untenable position. I therefore went to the management of the BNB to describe the situation and ask for assistance. The Board of the BNB was watching with great anxiety the development of the first event in the life of banking in our country and was ready to listen to my suggestions. I was easily able to convince the management of the Bank that if the Credit Bank saw itself forced to close its counters, the crisis would inevitably affect the other banks and spread throughout the country".⁷⁹

4.4 Bulgarian economists on Central Bank role and interventions during the crisis

During the early 1930s, leading Bulgarian economists, who in reality were not many, held key positions in politics, in the state administration and the BNB, and were also actors in the private financial, commercial and industrial spheres. They combined practical activities with academic and university posts. Most of them had studied or specialized, and even gained doctoral degrees in Germany, France, Austria or Switzerland. Less often in England, as in the case of Assen Hristoforov (1910-1970), who graduated from the London School of Economics and listened to the lectures of F. Hayek. Bulgarian economists were familiar with the modern trends in economic practice and theory. A number of them were participants in international conferences and forums, including these of the League of Nations (G. Danailov, N. Stoyanov, O. Anderson, A. Burov, if we mention just some of them). The influence of German, Austrian and French economists was great (C. Menger, L. Mises, W. Sombart, Ch. Rist, J. Rueff, A. Aftalion, etc.). The Bulgarian economists have mastered the new trends in the British literature on money and monetary policy (e.g., R. Hawtrey and J. M. Keynes) and Bank of England policy.⁸⁰ Trends in central banking and in banking developments in leading countries were followed and many translations were made.⁸¹

From 1924 to 1933, the BNB had as deputy governor deputy-governor Zhelyu Burilkov, who believed that monetary policy is not just an art, practice and experience, but must be the result of a scientific approach. He posited the development of the money market in Bulgaria (discounting and rediscounting) as a necessary condition for the effectiveness of the LOLR function, allowing also the transition to open market operations. He had a leading role in the rescue of the Credit Bank. About the role of the BNB Board and the Bankers' Council, which were entrusted with the function of the LOLR, he explicitly its position in a report read before the Bulgarian Economic Society 'Theory and Technique of the Central Bank'.

⁷⁹ M. Ryaskov, *Memories and Documents*, BNB edition, Sofia, 2006.

⁸⁰ Some of the older English literature in this field was also familiar from Russian translations (for example, Bagehot's *Lombard Street* was translated into Russian in 1896).

⁸¹ e. g. K. Kremer, *The Bank of England, the Reichsbank, and the Federal Reserve Banks*. Court Printing House, Sofia. 1931.

“The Central Bank must take care to maintain sound credit and monetary conditions in the country. The main condition for this is sufficient liquidity of all banking institutions. It is the additional (emergency) credit from the Central Bank, in case of need, that is the necessary element for this liquidity of the other banks. The Central Bank, with all its privileges and reserves, with its sound, foresighted and at certain times decisive leadership, is the necessary guarantee for the liquidity of the other banking institutions. Of course, this guarantee applies to those banking institutions which are well managed and justify this liquidity guarantee. This requires, however, that the Central Bank itself should possess liquid assets to an even greater extent in order to be able to play the role of liquidity guarantor for the other banks. [...] The most essential and distinctive quality of the Central Bank is to be the supreme credit institution and the ultimate reservoir of loans.”⁸²

These objectives and ways of intervention of the Central Bank, and in particular the possibility of conducting Open Market Operations were also emphasized by Nikola Stoyanov (1874-1967), a long-time director of the Bulgarian Debt Agency, an active participant in the country's international financial activities. Stoyanov supports the view that “the main purpose of the Central Bank of Issue today is to regulate monetary circulation, taking care of the stability of the national emission and to organize the credit of the sovereign, to be the bank of the banks, operating with short-term liquidity operations.”⁸³

Other economists, as Marko Ryaskov, open the way to the LOLR function but also restrict it to the Central Bank solvency constraints: “I would have to note that an issuing bank, by increasing banknote circulation, can help banks withstand a run-on deposit (as seen in the run that occurred at Credit Bank described below). In the event of a run on its foreign currency liabilities, it relies only on its foreign currency reserves, which are not inexhaustible.”⁸⁴ Mollof⁸⁵ who defended his dissertation in Paris-Sorbonne and A. Kemilev⁸⁶ (a student and translator of Aftalion) also discussed the banking crisis and the BNB intervention which they understood and approved.

5 Did Romania and Bulgaria really apply LOLR principles?

5.1 In the Romanian case

⁸² J. Burilkov, Theory and technique of the central bank, in: Journal of the Bulgarian Economic Society 34 (2). 1935, pp. 34-90. (p. 76, and pp. 81-82).

⁸³ N. Stoyanov, Reparations and Inter-Union Debts. Bulgarian State Debts. Ed. Glushkov, Sofia. 1933, p. 121.

⁸⁴ M. Ryaskov, Memories and Documents.

⁸⁵ D.V. Mollof, La crise mondiale.

⁸⁶ A. Kemilev, Banking in Bulgaria in 1935, in: Journal of the Bulgarian Economic Society, 35 (7), 1935, pp. 415 - 429.

If we consider the Romanian case, we could consider that two types of doctrines co-exist. Government, mainly identified to King Carol II and Constantin Argetoianu defended an attitude of absolute defense of the big banks, in reality for the most the defense of the Marmorosch bank. Obviously, they did not defend it because it was systemic, but probably for unclear reasons. But finally, only the result is important. Moreover, the ways they chose to defend it before nationalizing it were dangerous for the competitors. To some extent, the cautious attitude of central bankers (identified to the Manoilescu-Auboin-Bolgert trio) was in a sense complementary to the voluntarism of Government. They applied with orthodoxy the Lender of Last Resort main principles: (i) they made a distinction between illiquidity and insolvency and accepted to intervene only in the first case; (ii) they promoted a principle of horizontal solidarity between the banks, as a first rescue modality.

On the model of the conservative *Banque de France* during this period, no pro-active policy was proposed. In particular, no real Open Market policy was promoted. Note that in the Romanian case, it was more justified than in the French one: there is at this time no market for Romanian treasury bonds, except the secondary market of the 7% 1929 loan which is for the most located in Paris and New-York, without any significant contribution of Romanian banks. A second remark is that, like many other central banks, except probably the nascent and still weak Quesnay's Bank of International Settlements and, to some extent Schacht's Reichbank, there is no systemic considerations in the NBR's decisions to rescue or not small or big banks. In a sense, the non-orthodox views of politics, despite causing confusion among commentators in search of fairness and rigor, were more adapted to a systemic resolution of the crisis than the meticulous screening between acceptable and non acceptable assets by the NBR.

5.2 In the Bulgarian case

In Bulgaria as in Romania, the crisis was at the beginnings induced by the collapse of agricultural prices. Then, it was followed in the Bulgarian case by a contagion of the German version of the central Europe banking crisis. In Bulgaria, more than in Romania it was also followed by a currency crisis. Like Romania, Bulgarian economy possessed internal structural imbalances and inefficiencies that made them particularly vulnerable.

Monetary authorities reacted appropriately by mobilizing familiar LOLR measures, for the most inherited of the Bank of England's practices: Central Banks discount commercial effects and rarely government securities. The criterion used for authorize the discount of assets was among other the solvency of the bank. The implementation of a Sinking Fund was an useful initiative to avoid a total collapse of the economy and of the banking system. For the most, the BNB acted as a LOLR, even if it was learning this role as the 1931 crisis was its first experience of a systemic twin crisis.