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Greek monetary back story

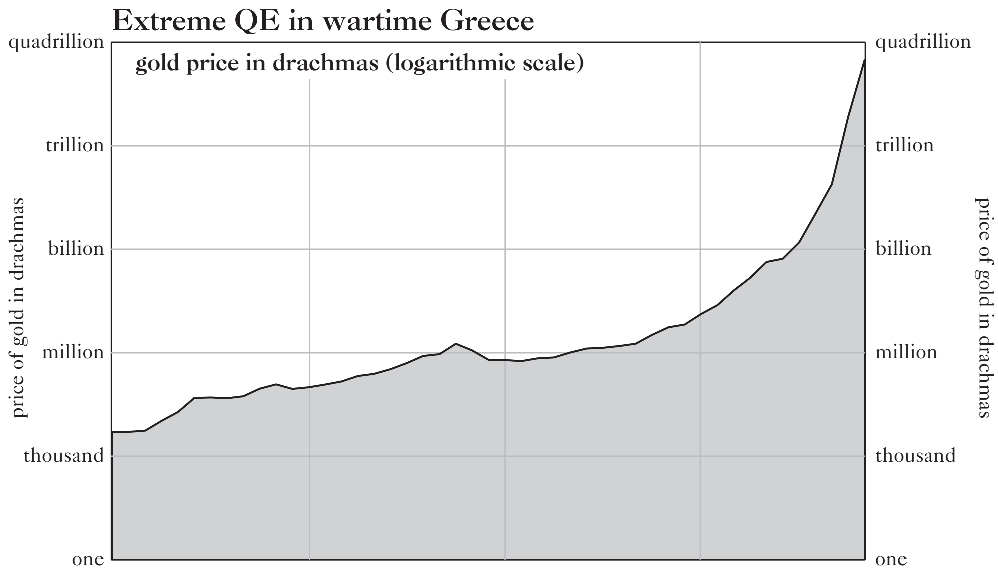
"Statements and assurances from Greece are no longer taken at face value," a German economics professor, Wolfram Schrettl, has remarked. "Who will ensure afterward that Greece continues to stand by what Greece is agreeing to now?" the German finance minister, Wolfgang Schäuble, has demanded.

Such expressions of German disdain ignite a special kind of fury in Greece. While 21st-century Greek fiscal and financial management may leave a little something to be desired, the record of German monetary stewardship in the Hellenic Republic is supremely worse. During Nazi occupation in World War II, Greece suffered famine, pestilence, wholesale killings and hyperinflation. The last-named plague is the topic at hand.

Let bygones be bygones, they say, and well they might say it in Europe, the land of ancient enmities. However, there can be no understanding the present-day Greek sensitivity to its high and mighty creditors without a rudimentary knowledge of the German-inflicted catastrophes of 1941-44. Nor can there be a full and proper appreciation of the risks inherent in paper money without a basic grounding in such abominations as the occupation-era Greek drachma or, for that matter, the post-occupation drachma—for the liberated Greek central bank took up where the German-corrupted central bank left off. Fiat currency can't seem to help itself. The insubstantial monetary material sooner or later goes up in smoke, no matter whose hand cranks the presses. These days, of course, the cranking hand is a technocratic one. "Quantitative easing" is the anodyne phrase. Yet in peace as in war, gold is the preferred refuge from state-imposed paper currency.

According to Mark Mazower's scholarly history, "Inside Hitler's Greece: The Experience of Occupation, 1941-44," between 250,000 and 300,000 Greeks died from famine at the hands of the German overlords. "In reality," Mazower writes, "there was no deliberate German plan of extermination." The extermination that did occur was rather the result of the calculated destruction of the Greek economy and the stripping of the Greek larder for the Axis armies, the German one in particular. "Who is Mr. Schäuble to revile Greece?" the 82-year-old president of Greece, Karolos Papoulias, demanded last week in response to the German finance minister's slighting comments about the country for which a teenaged Papoulias fought in World War II.

Famine was a certain, if not deliberately sought, consequence of German occupation policy, but there was nothing accidental about the destruction of the drachma. The German-controlled Bank of Greece printed up the national currency as the need arose. In the opening months of 1941, before the Germans (and the Italians and Bulgarians) came to stay, a British sovereign was worth 1,200 drachmas. As the Germans cleared out, in November 1944, blowing up railroad tunnels, rolling stock, harbors and



source: Mazower, Mark: "Inside Hitler's Greece: the Experience of Occupation, 1941-1944" such as they left, a sovereign commanded 71 trillion drachmas.

A sovereign is a gold coin weighing not quite one-quarter ounce—to be exact, 0.23542 troy ounce. When Britain was on the gold standard, a sovereign was worth one pound sterling, and it circulated as the people's money. It was a popular coin in Greece, too, as Britain and Greece had joined monetary forces in 1928. Three years later, Britain went off the gold standard, and in 1932, Greece and Britain ended their so-called stabilization relationship. Cut loose from gold, the paper pound began its long descent in purchasing power measured in gold. However, from the Greek vantage point, paper sterling was a better anchor for the drachma than no anchor at all, and in 1936 the Greeks re-lashed their currency to Britain's, at the rate of 548 drachmas to the pound.

Fast-forward now to the outbreak of war in Europe in 1939. As the pound came under new inflationary pressure, so did the drachma. In Athens, the cost of living was accelerating well before Hitler mounted his attack on Greece in April 1941. In 14 months of neutrality, prices in the Greek capital had jumped by 15%.

Nowadays, Germany is the national face of monetary and fiscal rectitude. It wore a different face in wartime Greece, though the German army of occupation did observe some of the basic commercial forms. "Rather than requisition all required goods and facilities," write Dimitrios Delivanis and William C. Cleveland in their "Greek Monetary Developments, 1939-1948," "the occupation armies usually preferred to pay with newly created currency."

The German visitation lasted for 3½ years, but the real monetary damage was done in the first 18 months. In April 1941, an index of the cost of living in Athens registered 116. In October 1942, the same index stood at 15,192, a gain—if that's the word—of almost 13,000%, or an average monthly rate of rise of 722%, according to Delivanis and Cleveland. It didn't help the price picture that the Greek economy was crippled or that the Germans were making off with whatever wasn't nailed down to aid the Axis war effort. What, especially, didn't help the price picture was the breakneck growth in the local money supply, up roughly 10-fold between May 31, 1941, and Oct. 31, 1942, or the fact that, in 1942-43, newly printed drachmas financed 81% of public expenditures.

During this first act in the play of the death of the drachma, the currency's domestic purchasing power fell by 99.34%, its external purchasing power—expressed in terms of the gold sovereign—by 99.73%. These facts we commend to the 21st-century gold bulls on those discouraging days when the eternal monetary metal seems to trade as a proxy for the euro. It isn't the euro, after all, but almost the opposite. It is money, the genuine article.

"It must be concluded," write Delivanis and Cleveland, "that the almost complete collapse of the value of the drachma, both internally and externally, was largely the result of enemy exploitation. The enemy occupation authority seized all stocks of commodities that were discovered, exploited for its own benefit the productive facilities and capital equipment of the country, confiscated and exported as much as possible of the current production, and extorted, as occupation costs, payments equivalent to 7,674 million prewar drachmas between May 1, 1941, and March 31, 1942, 2,287 million prewar drachmas between April 1, 1942, and Oct. 31, 1942."

No bear market is complete without a trick rally, an Act II, and the terminal decline in the Greek currency was no exception. News of the Allied victory at El-Alamein in October-November 1942 caused a rush out of gold into scrip. A sovereign had fetched 37,144 drachmas before the battle that Churchill famously characterized as not the end of the war, nor even the beginning of the end of the war, but, "perhaps, the end of the beginning." By February 1943, it took just 14,180 drachmas to buy a sovereign—as it turned out, not a bad entry point for the final move up to an average of 71 trillion.

Act III of the eradication of the drachma resembled Act I but with the addition of many more commas and zeros to all the significant currency and inflation data. Hopes of early deliverance from the Nazi occupation dashed, Greeks resigned themselves to the likelihood of a replay of the Weimar inflation of 1922-23, an earlier episode of German-directed monetary chaos. As noted, the Athens cost-of-living index stood at 116 on the eve of the German occupation. It registered 76,171 in November 1943 and 18,850,000,000,000 in the first 10 days of November 1944.

"During the final period of the enemy occupation of Greece," the Delivanis and Cleveland account continues, "the index of note issue by the Bank of Greece rose to fantastic heights. During the period of 18 months and 10 days [i.e., May 1943 til Nov. 10, 1944], the index increased in magnitude 11,214,823 times, i.e., from 7,368 to the value of 82,630,830,289. The total increase in the period was 1,121,482,300%, representing an average monthly increase of more than 62 million percent as compared with the average monthly increase of 60% during the first period of enemy occupation from May 1941 to October 1942, and the average monthly increase of only 22.5% during the succeeding period from November 1942 to April 1943. The tremendous expansion of the note issue was caused by the growth of public expenditures, principally on account of the enemy occupation and by the cumulative, self-reinforcing effects of monetary inflation." Toward the end of the German stewardship, the Bank of Greece printed 99% of the receipts of the Greek treasury.

Gold and foreign bank notes were the de facto coin of the realm. The British Middle Eastern forces funneled an estimated 700,000 sovereigns to Greek guerillas. And the Germans, in a vain attempt to tamp down the raging inflation rate, sold gold in exchange for drachmas—as many as 1,300,000 sovereigns in 1943 and 1944. It was the bright idea of the head of the German economic mission to Greece, Hermann Neubacher, to drop sovereigns on the Greek market to try to buck up the drachma. "Astonished Greek businessmen started to question, should we be buying gold, or selling it ourselves?" relates Michael Palairet in his history, "The Four Ends of the Greek Hyperinflation, 1941-1946." "Buying gold" turned out to be the correct answer.

At a glance, the Greek hyperinflation would seem a pale copy of the Weimar episode. The size of the drachma money supply as the Germans scuttled home in 1944 was a mere 826,308,303-fold greater than the size of the money stock in the year before the outbreak of war in 1939. As for Weimar, marks in circulation in 1923 were 3,250,000,000-fold greater than the German money stock in the 12 months preceding the outbreak of war in 1914. However, note Delivanis and Cleveland, the Greek catastrophe was six years in the making as against nine for the German one. Besides, they say, as the curtain fell on the Greek tragedy, only one-third of Greeks were still transacting in the worthless national scrip, whereas, up to the bitter end, nine-tenths of the German population continued to use marks.

It can't be said that Greek monetary management represented much of an improvement over the German kind. Having seen off the enemy, the Greek authorities proceeded to print money—new drachmas—with the note issue climbing to 25,762 million from 126 million. The gold bull market and the cost of living in Athens both resumed their upward course. As for the Greek treasury, now crippled by a ferocious civil war, it liberally availed itself of the fruits of the central bank's printing press. ("Early during the occupation," Palairet writes, "the German authorities tried to get the Greek government to reform its system of tax collection, but wrote off the effort, such as it was, as unavailing.")

Sixty-odd years later, the monetary scenery is transformed. A peaceful Europe is united, more or less, under a single currency. A single central bank aims for a rate of inflation in the neighborhood of 2%—no scientific notation required to calculate the rate of currency debasement these days.

However, in the all-important realm of monetary ideas, not so much has changed. Today, as in the war, government-controlled central banks print up the money with which to finance, directly or indirectly, burgeoning fiscal deficits. Today, as in the war, governments have recourse to "financial repression," e.g., zero-percent funding costs and QE. And today, as in the war, investors with eyes to see are busily exchanging fiat currencies for tangible stores of value. *Plus ça change*, as they say in Athens.

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