THE HUNGARIAN BANKING SYSTEM FROM THE TRAUMA OF TRIANON TO NATIONALIZATION

János Botos

The sumptuous formerbanking hall now fulfils protocol functions

ABSTRACT

Following defeat in the First World War, the prescriptions of the Treaty of Trianon entailed severe economic consequences for Hungary. In the wake of defeat, the inflation of the korona continued in Hungary at an even greater pace than before, halted only by stabilization measures carried out in 1924, after which the currency was replaced by the pengő. After the war, financial institutions in Hungary created the Association of Savings Banks and Banks (TÉBE) to protect and represent their interests, and – relying on earlier antecedents – the system of Interbank Agreements. Following the stabilization programme, the principal means by which banks acquired resources was to issue, and sell abroad, debentures and bonds in foreign currency. The turnover of financial institutions slowly revived in the wake of stabilization, before slowing and falling back with the impact of the economic and then financial crises; it would only attain – and then surpass – its pre-crisis level once again in the years of the Second World War.

After defeat in the latter, the inflation of the pengő that had begun in 1937–1938 accelerated and the currency suffered hyperinflation, obliterating the pengő as a monetary system. Once the forint had been introduced as the new currency, the banking sector once again set off on a growth path, although this was influenced from the summer of 1947 by the proposal, and subsequent commencement, of nationalization of financial institutions. The Communist takeover of 1947–1948 brought with it the end of the two-tier banking system and the creation of a single tier.

JEL codes: N0, N1, N2, N4

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1. AFTER THE GOLDEN AGE, A SILVER AGE BURDENED BY CRISIS AND WAR

The last decade of the 19th century and the first decade of the 20th century have rightly been described as the Golden Age of the Hungarian banking system. Subsequently, after the upheavals of the First World War, the financial stabilization programme carried out in 1924 created favourable conditions for the renewed strengthening of the banking system and the flourishing of its branches of business; the Golden Age, however, did not return, and we can speak only of a Silver Age lasting a few years at most. In 1924, the paper korona was successfully stabilized by linking to the British pound sterling, the National Bank of Hungary (MNB) was established, and the government took out foreign loans to consolidate and boost the economy. All these factors created new and more advantageous conditions for the flourishing of the banking system than in previous years. In its decisive role in the functioning of the money market, the banking system exploited these favourable opportunities to establish and operate a distinctive interconnecting web of competition and cooperation, broaden the involvement of both foreign and domestic capital, expand lending, and boost the turnover of various branches of business. Following stabilization, the banking system further strengthened and broadened the powers of the new organizations and institutions which – partly capitalizing on the experiences of earlier such attempts – were established in the wake of defeat in the First World War. A suitable context for the establishment of both formal and informal relationships was provided not only by these new organizations and institutions, but invariably also by the comfortable armchairs of the Lipótváros Casino (at Zrínyi u. 5 in Budapest's District 5, now the Danube Palace of the Interior Ministry).

1.1. The Association of Savings Banks and Banks

Simultaneous competition and cooperation essentially came about within the framework of the Association of Savings Banks and Banks (TÉBE) and the system of Interbank Agreements. Besides its activity protecting and representing the interests of financial institutions, the TÉBE[1], established on 31 January 1919, regarded the modernization of bank operations as one of its fundamental tasks. Within the framework of its activity protecting and representing banks' interests, it was not only involved in preparing regulations governing the banking sector, in certain cases initiating or expressing opinions on these, but also helped disseminate and promote consistent interpretations thereof, primarily through its circular letters, the volumes of the TÉBE Library and other publications. In addition, as we have already indicated, the organizations and bodies operated by the association created the appropriate framework and model by which leading figures on the domestic financial scene could exchange opinions both formally and informally, and compare and reconcile their standpoints and endeavours. Such bodies and committees included plenary sessions held monthly, meetings of managing directors, and consultations of the preparatory committee. This series of three meetings of the first rank was complemented by committees dealing with a variety of issues; namely bodies dealing with questions of personnel, legal affairs, taxes and duties, implementation of the peace treaty, foreign currency, mortgages, the press, charitable and cultural matters, and questions of an ad hoc nature. Also clearly demonstrating the significance of these committees is the fact that in the year following stabilization, in 1925, they sat on a combined total of 135 occasions, with dozens of circular letters reporting on their work and results. With the aim of increasing the operating efficiency and prestige of the TÉBE, the organization set up an Executive Committee from the spring of 1934. Meeting every two to three weeks, the body had operative functions and made decisions applying to financial institutions. Its members took the view that the prestige and weight of the TÉBE would be enhanced through their activities, in the eyes of the government as well. However, though regarded as of prime importance, this objective was entirely frustrated because – as *Károly Lamotte*, then chairman of the Executive Committee, stated on 23 April 1942 – "it still happens, when preparing legal measures affecting the credit sphere, that the competent circles do not avail themselves of the TÉBE's input and often make decisions without the TÉBE, or precisely in opposition to the standpoint of the TÉBE."[2]

When in 1927 the TÉBE was merged with the National Association of Financial Institutions (POE), provincial departments of the organization were set up. The

1 For the history of the TÉBE, see Müller et al., 2014, pp. 11–40; Botos, 1994, pp. 25–52.

2 National Archives of Hungary (MNL OL) Z 51, item 390.

following year saw creation of the institution of the banking congress, which provided every member of the organization the opportunity, under equal conditions, to put forward their position on fundamental questions affecting the banking system. In the first year in 1928, two such events were held, at which questions of bank interest rates, social insurance, the reform of financial institutions, bank pension funds and participation in legislation were discussed. In the same year, a plenary session of the TÉBE decided that the balance sheets of financial institutions should be prepared biannually based on uniform principles and criteria, and that these should be published in the *Official Bulletin* attached to the *Budapest Gazette*.[3] This fulfilled the expectation that the balance sheets of financial institutions should be subject to comparison, and available to the public to inspect and study without a separate procedure. At the same time, publicly available balance sheets implicitly did not contain data on so-called secret reserves, which were created by undervaluing a portion of the assets of the given bank. These secret reserves could be mobilized in the event of a financial or liquidity-related emergency. The financial crisis that exploded in the summer of 1931 prompted the TÉBE leadership to gain representation on the National Credit Council (OHT), and thereby to take part in determining the parameters of lending activity, the interest rates that could be charged and the interest margin.[4] In both the latter cases, even tenths of a percentage point were important from the point of view of banks' profitability.

Besides its interest-protecting activity, the TÉBE took coordinated steps to reduce banks' costs and rationalize their activities and business operations. Within this framework, measures were taken primarily to standardize the technical side of banking operations. This goal was served through the design of document types and specimen letters, organization of mass reproduction of current account statements, and popularization of combined calculating and typewriting machines. The association arranged for mass production of recommended document types, making these available to its members. Likewise serving to update the activities of financial institutions, the TÉBE centrally tracked and made available to its members the interest rates of leading foreign banks, compiled descriptions of banknotes in circulation, and kept records of the data of lost or counterfeit securities, cheques and bills of exchange. It organized translation and courier services for banks, as well as the category of rapid money orders aimed at spreading the non-cash payment method. It also launched professional and language courses for the training and further training of bank employees.

3 The *Budapesti Közlöny* [Budapest Gazette] fulfilled the same role as the *Magyar Közlöny* [Hungarian Gazette] does today.

4 The share of profit, in this case the difference between the interest on outside capital and interest rates on loans.

The TÉBE generally kept well clear of day-to-day political conflicts, deviating from this basic principle only in very exceptional circumstances. Such a situation arose when Prime Minister *Gyula Gömbös* proclaimed his corporatist system. As an organization, the TÉBE – arm in arm with the Hungarian National Economic Association (OMGE), the National Association of Industrialists (GYOSZ) and the Hungarian Commercial Union (OMKE) – took a resolute stand against the declared Gömbös plan to organize interest representation in Hungary into a corporatist system. In a lengthy submission dated 31 July 1935, these bodies emphasized that there was no need in Hungary for the "organization" of society to an extent or in a direction such as in Germany or Italy. They opposed mandatory membership of interest-protecting organizations and the forced compacting of employers and employees into one body, while supporting the continued operation of the existing system of interest representation and protection in unaltered form. The coordinated action of these four major interest representation bodies contributed to ensuring that Gömbös's dreams did not become a reality.[5]

From 1938 onwards, Hungary's banking system was explicitly faced with the consequences of preparing for war. The Banking Centre (Pénzintézeti Központ) – which, among other things, was one of the early outward forms of state banking supervision, contributing through its regulatory activity to the avoidance of money market shocks – was granted the right, via Decree no. 10/1939 of the Finance Ministry, to submit Hungarian banks to annual mandatory audits, during which the institution's inspectors would also gain insight into the activities of companies and enterprises belonging to the banks' sphere of interest ((*Pénzintézeti Központ 1916–1941*, 107–108.). From May 1938, the leading bodies and institutions of the TÉBE had to confront the economic impact of anti-Jewish laws and decrees. The association's personnel committee established a narrower expert committee to humanely implement provisions governing restrictions on the employment of people of the Jewish faith or Jewish by birth, urging its members to ensure pensions or adequate severance payments for those forced onto the streets, to refrain from releasing or filling the places of those drafted into military forced labour, and to verify that each given financial institution did not qualify as Jewish-owned. These guidelines continued to be applied even after the country's German occupation.[6] All this was deemed necessary because those of Jewish faith or birth were strongly overrepresented among employees in the Hungarian financial sector in comparison to their proportion of the general population. The same was true of the ratio of ownership of financial institutions among those practising Judaism or born Jewish. In 1943, the last full year in which military operations were not yet carried out on Hungary's territory, the TÉBE's management bodies and com-

5 MNL OL Z 25, item 6.
6 MNL OL Z 83, item 9; Z 86, item 15.

mittees held 43 and 114 meetings, respectively, preparing 112 recommendations for government organs, and sending out 247 circulars to its members. In this year, the association's members numbered 392. While the TÉBE's membership did not include every financial institution operating in the country in any single year of its operation, its ranks did include all the banks that determined the functioning of the money market.

Based on the experiences of the First World War, as the first issue of National Investment Bonds necessary for the financing of the "Győr programme"[7] entered circulation in mid-July 1938 (with the proportion assigned to each bank determined by the TÉBE), the banks accepting the bonds began to employ the tactic whereby they had the value of the received bonds indirectly or directly refinanced by the National Bank of Hungary. With this technique they aimed to protect their liabilities from being drawn off by the state for war preparations and, in the case of later loans, the financing of military operations. In the course of the refinancing process – since the sale of the floated bonds they were obliged to assume occurred not at face value but at a lower rate, and the interest rate was somewhat more favourable than that of the refinancing loans – a larger sum of refinancing was often demanded than the value of the bonds the banks had assumed (*Botos*, 1999, 211–222.).

The activity of the TÉBE between the two World Wars proved that for a prolonged period Hungarian financial institutions were able to reconcile commercial competition with the principle and practice of solidarity among banks. The decisions of the interest-protecting organization, while not hindering business competition between banks, promoted the coordinated position and united action of banks and savings banks, preventing the state and its organs and institutions from turning them against each other or playing them against each other for their own goals. Nevertheless, it is also necessary to emphasize that it was the highly capitalized Budapest banks that played the defining role in the TÉBE's decisions. Relying on their market weight, their word often proved stronger than that of the majority of financial institutions that were greater in number, but weaker in capital and market share.

1.2. The Interbank Agreement

A portion of the financial institutions under the Austro-Hungarian Monarchy concluded an interbank agreement at the beginning of the 20th century (under the contemporary German terminology: Übereinkommen), in which they fixed the minimum charges, commissions and other conditions to be applied to customers

7 At the convention of the Party of National Unity in Győr on 5 March 1938, Prime Minister *Kálmán Darányi* announced a one billion-pengő military development and armaments programme.

in the various branches of business. This agreement was adjusted to the changed circumstances in the years of the First World War.[8] After defeat in the war – as we have already mentioned – an economic and political environment emerged with numerous new defining features. Adapting to the changing situation, the strongest Hungarian banks not only modified the conditions of the earlier agreement, but created a new, cartel-like system of Interbank Agreements, electing a three-member presidium to control it and monitor implementation of decisions, and furthermore establishing an office to fulfil this function. In 1925, once the korona had been stabilized, the participating banks once again determined the maximum rates of interest to be paid on deposits placed in the Hungarian currency, the preferential rates that could be applied, and the sanctions applying to institutions violating the agreement. This agreement was later modified and expanded on several occasions, adding further conditions extending to business carried out with foreign financial institutions, foreign exchange and currency transactions, as well as other lines of business, and fixing interest rates, commissions and other conditions. The last amendment of the Interbank Agreement in the given period occurred in November 1943 (*Botos*, 1994, 53–80.). Violation of the agreement not only carried ethical and financial sanctions up to 100,000 pengős (a horrendous amount under the conditions of the time), but the responsibility of the culpable person was also determined. Accordingly, on 13 July 1929, it was declared that "an institution which breaches the provisions of the Interbank Agreement also commits a grave ethical wrong, since it offends against the loyalty and collegiality that exists between institutions, particularly because, in this way, an institution which precisely observes the provisions is put in a disadvantageous position. Following this chain of thought, the institutions adopt the standpoint that any office-bearer who breaches the provisions of the agreement, or even only its spirit, causing considerable ethical damage to their institution, commits a serious disciplinary offence, for which the office-bearer concerned is to be dismissed by disciplinary action as punishment."[9]

The Interbank Agreements between the two World Wars never embraced all banks or all the lines of business of financial institutions, but only the areas qualified as important by the participants in the agreements. The fact that the number of signatories to the agreements did not exceed two dozen did not mean that their power was limited to only a portion of the market, since those accepting the conditions were essentially able to directly or indirectly influence the entire Hungarian money market. While the agreements were generally characterized by self-imposed limits and the circumscribing of competition, at the same time they left numerous areas free to rivalry. Competitive opportunities did not merely

8 MNL OL Z 40, archive nos. 1791, 1792; Z 51, item 738.

9 MNL OL Z 51, items 740, 741, 742, 747, 748, 749, 750; Z 65, item 51; Z 100, items 7, 9, 10.

open up within the parameters of maximum or minimum conditions, since there were always exceptional procedures and preferential treatment offered "under the counter," the scale of which sometimes came close to the critical point after which the agreements themselves would become meaningless. Not one of the signatories wished to cross this point, however, so that the system of Interbank Agreements – despite all its concerns and problems – was able to function effectively from the 1920s up until the end of the Second World War.

2. BANK SECURITIES

Following the stabilization of 1924, financial institutions bolstered the funds they needed for offering credit by issuing securities (*Botos*, 2002, 138–178 and 2008, 116–138.). One of the most important elements of this was the issue and sale of debentures and industrial bonds.[10] Act XV of 1925 provided for the issuing of securities to cooperatives founded by financial institutions, as well as the segregation of collateral on securities issued before and after 1 January 1925 (Corpus Juris Hungarici CD, 1999). This act encouraged the Hungarian General Credit Bank (MÁH), the First National Savings Bank of Pest (PHET) and the Hungarian Commercial Bank of Pest (PMKB) to initiate negotiations with British, North American and German banking houses on the drawing of long-term loans, and to establish cooperatives issuing debenture bonds. There was a close relationship between debenture issues and mortgage loans, since on the one hand, if a bank was unable to sell debentures on the market, it could not extend amortizing mortgage loans, while on the other hand the stock of amortizing mortgage loans – as collateral on debentures – needed to exceed the combined face value of issued debentures. The justification for issuing abroad was that under the capital-scarce conditions in Hungary there was little opportunity at that time for banks to secure new funds by selling debentures and bonds in Hungary.

10 Industrial bonds could be issued based on Act XXI of 1928. Mortgage collateral could be registered on the assets of the given industrial concern as an effective whole – universitas rerum – in the central property register (Corpus Juris Hungarici CD, 1999).

Table 1
Face value of debentures and industrial bonds sold abroad, in millions of pengős

Year	Nominal value (in millions of pengő)
1925	17,13
1926	133,95
1927	79,93
1928	269,03
1929	33,70
1930	23,49
1931	26,40

Source: Varga (1932), 193.

It can be seen from the figures in the table that sales of bonds abroad fluctuated and plunged back to a fraction of their earlier value in the wake of the economic crisis. From the bond sales of 583.63 million pengős face value carried out between 1925 and 1931, the funds that flowed in – depending on the issue price – were actually worth a few percentage points less.

Based on Act XV of 1925, the year 1926 saw six major banks form the Hungarian Banks' Debenture-Issuing Association, which, besides the surety provided by the founding institutions, issued debentures based on loans granted for landed property assigned (transferred or ceded) to the association – where the outlaid credit was only permitted to reach 25% of the estimated value of the offered properties. In 1927, five leading financial institutions in Hungary established the Association of Hungarian Mortgage Institutions, which granted amortizing mortgage loans up to 40% of the estimated value, primarily on urban real estate and only to a lesser extent – up to one-fifth of the total at most – on agricultural properties. The issued securities of both associations were primarily denominated in gold dollars or British pounds sterling, and were introduced onto foreign bourses as well. In 1926–1931, besides the securities issued by these associations, a succession of banks, savings banks and land credit institutions, exploiting the favourable opportunities offered by international money markets, issued their own debentures and bonds in foreign currencies – the U.S. dollar, pound sterling and Swiss franc. In addition, Budapest, other major cities and counties also issued bonds. Between July 1925 and August 1929, there were 26 significant issues, with maturities ranging between 10 and 45 years, and interest of 6%–7.5%, and with issue prices – barring two exceptions of 100% and 100.50% – varying between 89% and

98.75%, so that the actual interest earned by the buyer amounted to 6.75%–8.66%. Based on the issue prices, a total of 385.6 million pengős flowed in from debentures and municipal bonds sold abroad by financial institutions between 1926 and 1931, which represented substantial extra funding if used appropriately and effectively. However, the business management of the National Bank of Hungary (MNB) monitored foreign issues, and in 1927 raised its voice against the running up of debts abroad. In 1928, a draft bill was drawn up that would restrict foreign borrowing and subject it to supervision, but it failed to be adopted in the face of opposition from major banks. *Sándor Popovics*, the governor of the MNB, also contributed to this failure by altering the central bank's earlier position, taking a stance against statist interventions in the financial sphere (*Botos*, 2002, 139–155.).

In 1929, 11 financial institutions in Hungary former an intervention syndicate for the protection of the stock market prices of debentures and bonds. Subsequently, as the economic crisis deepened, they established the share company Magyar Investment Rt. at the beginning of 1931, with the goal of carrying out transactions involving debentures and bonds on the Budapest Commodity and Stock Exchange and foreign bourses, thus preventing a substantial plunge in the value of these securities. Despite every effort to regulate and protect prices, however, the share company failed to achieve its objective, and was unable to stem the fall in prices of debentures and bonds either on the domestic or foreign bourses (*Botos*, 2002, 156–157.).

In July 1931, the financial and credit crisis reached the Hungarian financial sphere. The government initially ordered a three-day closure of banks – on 14–16 July 1931 – and then imposed a temporary limit on banks' financial turnover, reintroducing foreign exchange restrictions and holding in or cutting back on state expenditures (*Horváth*, 1984). In the wake of the introduction of foreign exchange restrictions,[11] banks with foreign loans concluded standstill agreements with their creditors – partly or wholly suspending the fulfilment of obligations (*Domány*, 1936). The government aimed to remedy problems related to the repayment of foreign currency debt with the introduction of a transfer moratorium from 23 December 1931, which – with the exception of the League of Nations loan of 1924 – suspended the fulfilment of foreign debt servicing (repayment of principal and interest). From spring 1932, the repayment of foreign credit – until it became impossible with the onset of the next global conflagration – was regulated by standstill agreements. These became applicable to the 17 largest banks with short-term foreign debts – the value of which totalled 351,544,377 pengős, comprising institutional, rediscounted, overdraft and other credit, together with guarantees

11 The last prescriptions of the foreign exchange restrictions were cancelled only seven decades later, in 2001.

– as well as the amortization of debentures and industrial bonds (*Botos*, 1999, pp. 115–125, 157–165). In addition, steps were taken to ensure repayment of credit granted to the agricultural sector, to reduce the burdens on farmers taking out loans, which had serious financial consequences for financial institutions (*Botos*, 1999, pp. 144–149). In the wake of the financial crisis, the government endeavoured through mergers to resolve the liquidity problems affecting a portion of banks. Accordingly, it initiated the fusion of "weak institutions" into the Hungarian General Credit Bank (MÁH), and then the merger of the latter with the Hungarian Commercial Bank of Pest (PMKB). The plan eventually remained on the drawing board, however (*Scheurer*, 1988, p. 23).

The outbreak of the financial crisis also significantly worsened the conditions for sale of debentures and bonds. Besides growing mistrust among investors, other factors contributing to this were the introduction of the transfer moratorium, the departure of the British pound sterling from the gold standard, the devaluation of the U.S. dollar in 1933, and the latter's subsequent departure from the gold standard. In the wake of all this, prices sharply declined and sales of debentures and bonds plunged to a fraction of earlier years. Their turnover further deteriorated both at home and abroad as a consequence of the Hungarian government ordering the numerical cataloguing or nostrification of securities in 1936 – including Hungarian-issued debentures and bonds. Subsequently, only securities that had been numerically catalogued and stamped were regarded as being in domestic ownership. In this way, the aim was to completely separate domestic and foreign turnover of securities. The provision only partly achieved its intended goal, however, since only 52.28% of the debentures and bonds in circulation were registered, while 6.87% of securities still recorded as domestically held were not even numerically catalogued. Prices of foreign-denominated debentures and municipal bonds fluctuated at 45.50%–75% of face value at the end of 1934. In 1939, this increased to 88%–101% of face value, rising to 117%–159% of face value by 1941. The price rise can be attributed to the belief of investors, amid preparations for war and the subsequent conditions of global conflict, that in contrast to the expected – and then palpable – inflation of the pengő, bonds denominated in U.S. dollars, gold dollars, British pounds sterling and Swiss francs would preserve their value unchanged (*Botos*, 2002, pp. 158–160).

The outbreak of the financial and credit crisis carried with it the danger of a sharper depreciation of the pengő and the unfurling of a new wave of inflation. To reassure the public mood and cool inflationary expectations, a decree was issued on 15 August 1931 fixing claims valued in pengős in gold pengős. The legislation set down that prior to its assertion, any financial claim based on a commercial transaction or other title under civil law must be regarded as fixed in gold pengős. A gold pengő became equal to a pengő. This provision was soon supplemented by another specifying that – in the absence of any stipulation to the contrary – a pengő should always be considered a gold pengő.[12] The gold pengő decree entailed the inherent possibility of a dual currency system evolving, but in the end this did not occur. At the same time, its introduction and application had a primarily psychological effect, though the beneficial economic consequences were also not to be underestimated (*Varga*, 1931). The employment of the gold pengő could not prevent the total loss of value of the pengő during and after the Second World War, and moneyed citizens had to face the fact that as a virtual means of payment, the gold pengő could not protect against loss of wealth.

Table 2
Savings and current account deposits, stock of bills of exchange and balance sheet totals of banks, in millions of pengős, 1927–1943, year-end data

Year	Savings deposits	Current accounts	Bills of exchange	Balance total
1927	–	1393,1[13]	1372,2	3257,1
1928	834,6	878,0	1706,3	4179,6
1929	992,1	919,5	1836,1	4424,1
1930	1018,9	898,0	2009,6	4633,4
1931	811,5	797,0	1893,6	4259,3
1932	719,4	769,3	1714,1	4039,9
1933	730,7	775,0	1684,3	3893,3
1934	761,1	673,5	1729,7	3860,6
1935	800,3	701,1	1728,6	3868,0
1936	839,9	684,4	1756,0	3844,1
1937	925,9	717,3	1747,7	3973,3
1938	816,6	726,1	1653,6	3984,2
1939	876,6	835,4	1766,1	4291,9
1940	975,6	961,5	1962,5	4722,9
1941	1081,4	1282,3	2663,1	5852,1
1942	1290,1	1614,4	2633,1*	6158,0*
1943	1561,3	2123,3	–	–

Note: The data marked with * indicate the status as at 30 June of that year.
Source: Magyar Gazdaságkutató Intézet (1944), No. 53, pp. 34–35.

12 MNL OL XXIX-L-1-p, box 55.
13 1927-ben a takarék- és folyószámlabetétek együttes összege.

The four columns of figures in the table above provide an appropriate picture of the economic role of the Hungarian banking system in the period of the pengő prior to defeat in the Second World War. The data in the four columns reflect how in the period 1927–1930, with a degree of fluctuation, business turnover picked up substantially in tandem with the stabilization and – to a limited extent – burgeoning of the Hungarian economy, amid conditions on the money market that could be described as favourable. The impact of the economic crisis, and of the financial crisis that erupted in its wake, can clearly be seen in business turnover from 1931 onwards, as savings and current account deposits, the stock of bills receivable and balance sheet totals decreased appreciably. Banks would only reach or surpass their 1930 levels of turnover around a decade later, in 1940–1941, by which time nominal data were influenced by resurging inflation from 1937–1938. Current account deposits and balance sheet totals exceeded 1930 levels in 1940, while savings deposits and bills receivable followed suit a year later. The Hungarian banking system thus needed around a decade to reach or exceed earlier levels in terms of turnover, clearly reflecting the grave and devastating consequences of the economic crash of 1929 and the financial crisis that followed in 1931. The figures from 1942–1943 were strongly impacted by the effects of the wartime boom in the economy and the ever-swelling surge in inflation.

3. THE TERMINATION OF THE TWO-TIER BANKING SYSTEM

The banking system was confronted with a fresh set of serious problems in the wake of defeat in the Second World War. A portion of the assets of financial institutions was shipped out to the territory of the Third Reich by the Arrow Cross government, the remaining valuables being plundered by the occupying Nazis, retreating Hungarian and advancing Soviet armies, who broke into and looted vaults and safes, and made away with deposits. The TÉBE and leading Budapest financial institutions took steps to recover the looted assets, without success (*Tallós*, 1989, pp. 24–28). Representing an additional loss of assets, the terms of the armistice agreement in January 1945 and subsequent decisions of the Potsdam Conference in the summer of 1945 meant that securities, share holdings and assets in German and Italian ownership or existing claims against them entered the possession of the Soviet Union as spoils of war. In this way, around a quarter of shares in the Hungarian General Credit Bank (MÁH), among others, became the property of the Soviet Union, which Hungary – together with other companies and enterprises – later had to buy back (*Tallós*, 1995, pp. 376–390).

The remaining assets of banks that could be mobilized were consumed by the highest rate of inflation in world history (*Cagan*, pp. 25–117), which permitted the state to rid itself of its domestic debt, and for those taking out credit from banks – in the absence of valorization – to pay off their debts ahead of time in the increasingly worthless pengő. Collateral for mortgage loans had practically disappeared with the repartition of land and the ravages of war, while persistently strict foreign exchange controls – besides Soviet interventions – continued to obstruct international financial relations, with politicians only too happy to lay the blame on banks as the cause of the country's financial and economic troubles. The Supreme Economic Council and other state bodies responsible for the execution of state intervention in practice continuously interfered in the affairs of the National Bank of Hungary and other financial institutions, their lending activity and business turnover alike.

Some financial institutions weakened by the losses of the Second World War attempted to bolster their impaired position through mergers with the support of central state financial bodies (*Botos*, 2008, pp. 139–140). The Banking Centre itself, for example, authorized the First National Savings Bank of Pest (PHET) to open a new branch on condition that it absorbed four other local financial institutions, because it regarded the functioning network as oversized. Amidst the battle for political power, these plans either only attained the level of agreements in principle, or materialized only in partial form. One such plan that achieved only an agreement in principle was the concept, initiated by the Home Bank (Hazai Bank) in spring 1945, to form an amalgamation with the Hungarian Discount and Exchange Bank (MLPB), Hungarian National Central Savings Bank (MOKT) and the PHET. A PHET proposal on the fusion of the aforementioned financial institutions in the summer of 1946 only partly came to fruition after politics once again intervened. Consequently, only the Home Bank was able to merge into its parent institution the PHET. In contrast to the aforementioned examples, there were also two successfully concluded banking mergers. In summer 1947, the PHET absorbed the National Credit Institution (Nemzeti Hitelintézet), while in summer 1946 the MÁH merged with the MOKT (*Tallós*, 1991, pp. 112–113). By rationalizing branch networks, these mergers helped the given banks make up for their wartime losses and regain strength. One such merger saw Central Wechselstuben AG (which was later to pursue an "adventurous" path) become the property of the MÁH, and thence enter the sphere of interests of the National Bank of Hungary following bank nationalization – as did Niederlassung Wien (better known under the name CW Bank). In 1945–1946, the rationalization of the banking market through mergers, primarily due to opposition from the Hungarian Communist Party and Social Democratic Party, only partially materialized as politics thwarted the implementation of plans in a number of instances. When mergers once more took centre stage after bank nationalization, by this time actively urged by politicians within the framework of restructuring of the banking market, the fate of the two-tier banking system was sealed.[14]

14 Budapest City Archives, XI, 1530, box 8; Archives of Political History and Trade Unions, fonds 274, group 12, custody unit 88; MNL OL Z 25, item 54; Z 50, item 6; Z 51, items 274, 276; XXIX-L-1-n, box 5; XXIX- L-2-b, box 20.

Amid the changed circumstances, the TÉBE endeavoured to revive its earlier forms of activity, however its sometime influence had largely dwindled away. With the nationalization of large banks and the companies in their sphere of interest, it became obvious that the abolition of the TÉBE was just a matter of time, since control of its operations had become the task of the Central Office of State Banks. The TÉBE dated its last letter 12 October 1948.[15] The office of Interbank Agreements was not reorganized within the context of the new economic and political conditions, with the necessary harmonization and agreements being concluded and publicized within the framework of the TÉBE. Within this process, the fees and commissions that banks were permitted to charge were determined for each branch of business. The agreement had barely entered into effect, however, when the fees that could be charged by financial institutions were fixed by decree.[16] Determining the terms of business was also assigned to the purview of the Supreme Economic Council. Once the Hungarian-owned shares of banks belonging to the first curia of the Banking Centre were taken into state ownership, the system of Interbank Agreements was also wound up and relegated among the paraphernalia of the banking sector's discarded past (*Botos*, 1994, pp. 80–81).

The financial conditions of banking activity following the Second World War were consolidated with the introduction of the forint on 1 August 1946. In the period from spring 1945 to the end of July 1946, the stock of financial institutions' current account and savings deposits, and – as long as any traffic in bills of exchange existed at all – their bills receivable, rose in numerical terms from values in the millions of pengős to quintillion (10^{30}) pengős calculated in paper money, and to billions of pengős calculated in tax pengős, while its actual value approached close to nothing. For this reason, merely as a matter of interest – and not as an indication of the actual value of banking activity – we may mention that on 27 July 1946, four days before the end of the pengő era, the stock of savings deposits of Budapest financial institutions amounted to 836 billion adópengős, and their total current account deposits to 37,982 billion adópengős (at which time traffic in bills of exchange had been suspended). Turnover following the introduction of the forint as legal tender – while strictly observing the banknote ceiling – increased at what can be described as a rapid pace. The stock of savings deposits of Budapest financial institutions rose from 12.1 million to 110 million forints between August 1946 and May 1947, while total current account deposits increased from 38.7 million to 379.3 million forints (Magyar Gazdaságkutató Intézet, No. 54, p. 15). Turnover figures for the period that followed, however, were strongly impacted by the declaration, on 9 June 1947, by the interparty conference of representatives of parties forming the governing coalition that, in the interests

15 MNL OL Z 42, bundle 611; XXIX-L-2-b, boxes 1, 2, 9, 15.

16 MNL OL Z 51, item 723.

of implementing the three-year plan beginning on 1 July 1947, "the credit institution must be nationalized to the necessary extent" (*Horváth–Szabó–Szűcs–Zalai*, 2003, p. 513). This heralded the start of the swan song of the two-tier banking system in Hungary.

Following the country's defeats in each of the two World Wars, the Hungarian banking system adapted to changed economic and political circumstances in an endeavour to reorganize its activities, compensate for the loss of assets, and reacquire its earlier weight and role. The economic and political circumstances following the First World War largely created favourable conditions for this. After the Second World War, however, in a Hungary with limited sovereignty and amid the struggle for absolute political power, the necessary conditions came about only partially and for a short period of time. In the wake of the transformation of the political regime carried out in 1947–1948, the two-tier banking system became an unnecessary burden for political decision-makers and, as we have already shown, was replaced by a single-tier banking system with the National Bank of Hungary at its centre.

4. SUMMARY

The Austro-Hungarian Monarchy, and the Kingdom of Hungary as part of it, ended the First World War in defeat in November 1918.[17] As a consequence of military defeat the dual monarchy broke up, Austria and Hungary became independent countries and, even before the peace agreement was concluded, new successor states evolved based on nationality. In the wake of defeat in the war, a significant portion of the country's territory was lost prior to the signing of the peace treaty. In Hungary, the dual political structure and power collapsed and revolutions swept through the country. With the peace agreement signed on 4 June 1920 in the so-called Grand Trianon Palace, historical Hungary – without Croatia – permanently lost two-thirds of its territory and more than half of its population, with some three million Hungarians falling under the authority of Austria, Czechoslovakia, Romania and the newly created South Slavic state.[18] The dismemberment of the country not only shattered families, kinships and friendships, but largely also destroyed previous economic relationships. Banks in Hungary lost their affiliates[19] and branches operating in territories under the authority of the new states,

17 The Hungarian history of the period discussed in this study was extensively covered by Romsics (2010).

18 Documents of the Treaty of Trianon were published by Gecsényi–Máthé (2008).

19 Affiliates were financial institutions belonging to the sphere of interests of banks operating in share company form, with which they enjoyed close business relationships while functioning as legally independent institutions.

as well as a substantial portion of their assets and receivables. The Austro-Hungarian Bank – the Monarchy's central bank – was liquidated, its place and role in Hungary temporarily assumed by the Royal Hungarian State Bank (*Bácskai*, 1993, pp. 413–499). In the wake of military defeat and the ensuing revolutions, inflation accelerated, attempts to halt it temporarily failed, the economy plunged and the state budget remained invariably in deficit, to mention only the most important impacts on the banking system (*Botos*, 2015). The system of state interventions in the financial sphere that evolved during the First World War was relaxed following the 1924 consolidation, but once again spread and strengthened apace from the end of the 1930s – first during the build-up to the Second World War, and then in the years of the war itself. After the Second World War, the state intervened in economic processes more forcefully and determinedly than before via the central control and executive power of the Supreme Economic Council, formed at the end of November 1945 (*Pető–Szakács*, 1985, pp. 62–82). The number of financial institutions in Hungary – including banks, savings banks, land credit institutions and credit cooperatives – decreased from 4,990 in 1914 – including those under liquidation – to 2,234 in 1923 (*Tomka* , 2006, p. 92; *Statistical yearbook 1923–1925*, p. 186). The falling number of financial institutions remained a typical, defining trend until the era of nationalization. By the end of 1947, financial institutions in Hungary numbered less than 500 (*Tallós*, 1989, XXXII).

The loss of assets of financial institutions after military defeat is well illustrated by the 9.1% plunge between 1913 and 1924 in the market value of bank shares listed on the Budapest Stock Exchange, and the 6.2% fall in the value of savings banks' stocks. Counting the territory within the Trianon boundaries, the stock of own equity fell from 2.8 billion pengős prior to the First World War to 0.4 billion pengős by the start of financial stabilization, while the value of external capital dropped from 4.5 billion to 0.3 billion pengős (*Botos*, 1994, p. 25). Previously granted loans – with the exception of disannexed territories, where only modest valorization occurred – were paid off ahead of time in paper koronas that were losing their value at an increasingly rapid pace. The advance payments and current accounts line of business, despite nominal growth, declined in value as a result of inflation, while savings deposits in proportion to total capital fell from 30% before the outbreak of war to 3% by 1923 (*Statistical yearbook 1923–1925*, pp. 352–354.). The country repeatedly suffered an adverse trade balance in the decade following defeat in the war, with the deficit covered by taking out foreign loans (*Varga*, 1932, p. 187). Irrespective of this, the Hungarian state budget in each of the financial years 1926–1927, 1927–1928 and 1928–1929 closed with a considerable surplus (of 151.1 million, 93.8 million and 10.4 million pengős, respectively).

In the period between the two World Wars, the leading players on the domestic banking scene were the Hungarian General Credit Bank, the Hungarian Commercial Bank of Pest, the First National Savings Bank of Pest, the Hungarian Bank and Commercial Rt. (later, until the entry into the Second World War, the Anglo-Hungarian Bank Rt.), the Hungarian Mortgage Credit Bank, and the Hungarian Discount and Exchange Bank. Financial institutions repeatedly had to face a sometimes politically-driven climate of public opinion against banks, which held them responsible for inflation, high rates of interest and the financial crisis. The incitement of this anti-bank mood from the end of the Second World War until the nationalization of banks became another weapon in the armoury in the political battle for exclusive exercise of power.

Modest economic growth followed the stabilization measures of 1924, but was stalled within a few years by the economic crisis that broke out in 1929. The economy gradually found its feet again after the first few years of the 1930s, and growth from the end of the decade became intertwined with the lead-up and events of the Second World War. During the war lasting more than half a decade, the conditions for operation of banks were fundamentally influenced by the reappearance and acceleration of inflation (*Botos*, 2016), the country's military occupation, and the conduct of military operations for almost eight months on the territory embraced by the Trianon borders. In addition, banks' conditions for operation were adversely impacted by gradually increasing state intervention, by 21 laws adopted between May 1938 and the end of the war that limited the rights and confiscated the assets of Jewish citizens, by 367 prime ministerial and ministerial decrees, and by more than 10,000 other regulations (*Botos*, 2015a).

The armistice signed on 20 January 1945, and then the Paris Peace Treaties, further reduced Hungary's territory (*Gecsényi–Máthé*, 2008), while obligating the country to make significant war reparations. Hungary was occupied militarily, with its sovereignty limited for years, and the Soviet Union intervened in its internal political struggles in the hope of achieving the change of system it desired. Banks' scope for operation was restricted not only by the loss of assets in the war, increasing state intervention and a currency depreciation that slipped into hyperinflation unprecedented in world history (*Cagan*, 1956, pp. 25–117), but also by a process of nationalization extending to an increasingly large portion of the economy. Nationalization reached the financial sector in 1947, as a consequence of which the two-tier banking system was eliminated in several steps, to be replaced for decades by a single-tier system (*Botos*, 1999 and 2004).

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