Where do we get the money to pay for great infrastructure projects?

by Frank Hahn

The Schiller Institute held a conference in Berlin, Germany Nov. 22-23, to discuss Lyndon LaRouche's proposed "Productive Triangle," a plan for intensively building up the infrastructure and industry of the area enclosed in the triangle linking Paris, Berlin, and Vienna. This area would form the core for a new world economic order of high-technology development, with "spiral arms" reaching out to eastern Europe and the former Soviet republics, as well as to the Third World. This speech by Frank Hahn of the Schiller Institute in Hanover, Germany, was delivered to the conference on Nov. 23, and has been translated and slightly abridged here. See also last week's EIR *for a special documentary report on the Hamiltonian system of credit creation, featuring excerpts from Alexander Hamilton's* Report on Manufactures.

Certain people do not let themselves be inspired even by the most glowing speeches about the wonderful effects of the magnetic railway, the building of science cities, etc. Unimpressed, they pose two cardinal questions again and again: "Who is going to pay for all of that?" and "How is it possible that *they* can pay all that; are *they* not broke?" (What is meant by *they,* are the highly indebted countries of eastern Europe and the developing sector.)

With a little common sense, we can answer both questions once and for all. Take the first: It strikes me that last Friday, on the New York Stock Exchange alone, some people lost $130 billion—with this amount alone we could build the Berlin-Warsaw-Minsk magnetic levitation line! . . .

As for the second question, one might reply that the U.S. automaker Chrysler currently has uncovered debt obligations in the range of $75 billion. Compared to that, the former Soviet Union, with its laughable $64 billion external debts, has an economy that is very solid. More than that, think of Chrysler's security—some aging models of cars, which no one will want in two years—while the nations of the former U.S.S.R. are endowed with an infinite potential for wealth.

Thus it is a very relative business, who gets money and capital. The money is "lacking" for specific sensible projects, while in other places it is squandered senselessly. Take an example from Latin America: While $70 billion is denied by the IMF for building a continent-wide drainage and canal system, still the individual nations are put under so much pressure, that in the last 10 years they have had to pay $400 billion in interest alone to the creditor banks.

That means that we need political decisions and state interventions, in order to guide a smooth flow of capital and credit in the right direction, so that necessary productive investment, for putting people, machines, and raw materials to work, is not left by the wayside for lack of capital.

This problem has been a topic of political-economic discussion for centuries. But there is hardly any question that has been so unnecessarily mystified, as the problem of credit creation. If the state gets involved in the creation of credit, it is claimed, then you will get the bogeymen of galloping inflation, astronomical taxes, and finally the complete ruin of society. Let us examine three historic examples, taken from discussions of political economy of the past 200 years.

Hamiltonian credit creation

The actual inventor of state credit creation of the modern period was the first secretary of the treasury of the U.S.A., Alexander Hamilton. After the victorious American War of Independence, he was faced with a similar problem as that facing Brazil or Poland today. This war had been financed by drawing upon internal and external credit, and the question was asked: When shall we pay all that back, and above all, how? To solve that problem, Hamilton made a brilliant move. He offered the creditors in various European countries to be paid, not in cash, but in Treasury notes issued by the U.S. National Bank. In this way, the creditors of the Old World were invited to participate in the future profits of the U.S. economy—a prospect so genuinely alluring, that almost all of the creditors went along with Hamilton. Indeed, in Europe the word got around that U.S. Treasury bonds were the most profitable paper to be had. This euphoria was absolutely justified, not because this paper had any kind of magical value, but because behind it, or behind the guarantee of the redemption of this paper, there stood a commitment to transform the U.S.A. into the most highly developed manu-

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facturing state of its time. Investments in infrastructure, industry, and agriculture, had priority over all others.

That is exactly what we in Europe must do today. If the governments of Germany, France, Austria, Italy, and eastern Europe will unify themselves around the program of the Productive Triangle, then there will be a way to find the necessary capital for it, so that the countries of eastern Europe could pay their debts simply in the form of Treasury notes from their respective national banks. These Treasury notes might then be discounted by appropriate financial institutions in the framework of the European Monetary System, and thus transformed into new credits for financing great infrastructural projects.

Hamilton brought this method to bear also with respect to the domestic economy, by issuing Treasury bonds and notes to the domestic creditor, and thus provided the liquidity needed to stimulate the domestic economy. With this as background, he stated some basic laws on the question of debt. In the *Report on Manufactures* of 1791, he says:

"But though a funded debt is not in the first instance, an absolute increase of capital, or an augmentation of real wealth; yet by serving as a new power in the operation of industry, it has within certain bounds a tendency to increase the real wealth of a community, in like manner as money borrowed by a thrifty farmer, to be laid out in the improvement of his farm may, in the end, add to his stock of real riches.

"There are respectable individuals, who from a just aversion to an accumulation of public debt, are unwilling to concede to it any kind of utility . . . who cannot be persuaded that it ought in any sense to be viewed as an increase in capital lest it should be inferred, that the more debt the more capital, the greater the burdens the greater the blessings of the community."

Prerequisite for future wealth

Thus debts are actually very healthy, since it is only through them that we can broaden the capital base of society, to allow for great investments in our future. And finally, the whole society will be richer—as also the example of the farmers shows. Already we hear the warning, the alarm bell: "Inflation, inflation!"

Now Hamilton says naturally also, that there are boundaries, beyond which the blessings of debts are changed into their opposite, namely if the credit is used to finance the "will-o-the-wisp fantasies of some do-nothing," as Hamilton puts it. Thus Hamilton would warn against giving today's yuppies credits for building a new discotheque. Such purely speculative investments, without the creation of productive wealth, make it impossible even to pay the interest on the debt.

Thus let us clearly underline, that as long as debts are contracted for productive investments, they are actually ready money, which can be worked with. This fundamental statement should make clear the actual essence of credit: namely, that state debts are only a title to the future income of the state. That is, credit means nothing other than bringing on line now, future income, in order to make investments which are a fundamental prerequisite for future wealth. Thus managed, debts are in fact capital. If, on the contrary, the state incurs debts in order to cover current expenses, for example to pay the wages of state employees, then everything goes wrong. We must here clearly distinguish between the current costs of the state, which must not overstep a specific boundary, and credits that are created by the national bank and are investment credits. These, when used productively, do not mean any additional burden on the budget, nor do they lead to higher taxes. The problem today is that the state gets its money on the capital markets at overly high interest rates, which then adds to current costs.

The other cornerstones of Hamilton's policy are:

1) the creation of a special fund for state support of new industries, investment and other improvements of industry and agriculture;

2) tax breaks for development and improvement of agrarian and industrial production;

3) protective tariffs to foster domestic industry and agriculture;

4) subsidies for domestic raw material production;

5) state-fostered improvement of transportation infrastructure.

In connection with these principles, the founding of a national bank was the decisive step for creating the money—in unlimited quantities!—for projects that should contribute to "defense of the commonweal.". . .

Germany: the program of Friedrich List

In Germany, the question of credit creation became acute with the building of the first railways. The creator of the German railways was Friedrich List, who spent 12 years in the U.S.A., where he was able to get to know the Hamiltonian system close-up. List had to face practically the same problem that we do today: Besides the skepticism and partial rejection of his railway project, the question to be cleared up was the financing. To do this, List wrote a treatise, "On a Railway System in Saxony as the Foundation of a General German Railway System," which appeared in the year 1833:

"People say that we do not have, here in our region, any such an amount of capital, not so much ready money for undertaking such a gigantic national work. . . . As for the financial point, we need not fear any further objection from sensible people, once it is pointed out that the capital so used bears the highest interest rate of return in the country. With that as a premise, no expense can be found that is too great. Furthermore, Saxony, if it is serious about the undertaking, will have at its disposal more than a hundred times more capital and cash than required. That North America possesses more capital and more cash, is not even true; most of the

settling of accounts there, is done with paper money, which we can create just as well here in Saxony. Here an amount of 4 to 6 million bank-issued bills of exchange make up one-third of the currency in circulation, while in North America, there are two and three times as many of these notes in circulation than ready cash."

List speaks here of the creation of currency, of credit. In this creation of bank notes, he say, lies "the great secret of the entrepreneur in the United States." The secret is that one does not fixate on an imaginary intrinsic value of money, but rather looks at it as an "instrument for settling payment balances." Elsewhere, List says the following on this topic:

"People will probably ask me, where will Bavaria get the money to complete such giant works [railways]? I answer, that I have not yet seen any silver or gold in any of the canals or railways. To build them we use only consumer goods, steel, stones, wood, manpower, the power of animals. But is there not a surplus of all this in Bavaria? To the extent that we transform this surplus into canals and railways, which are not yet in existence, we create permanent and enduring value, we create an instrument which doubles the productive power of the entire nation. The money, however, does not leave the country, it only settles accounts.". . .

Unifying internal markets

List then thinks this through to the notion of creating a German national bank, modeled on the American. Appropriately, he bases the plans for a Leipzig-Dresden railway link, upon the founding of a German national bank. That is so much the more trailblazing and revolutionary, because Germany at the time—1833—was much more dismembered than the Soviet republics today, nor had there as yet been any development whatsover of the consciousness of being one nation. In fact, it was not until one year later, 1834, that a "customs union" would be created, unifying the internal markets of the German states.

List again draws upon his American experience. He mentions the city of Baltimore, which issued many shares in railway- and canal-building projects to finance these projects. Could not Leipzig or Dresden do exactly the same thing, the more since such a project as the railways, in 10 years, should "increase the value of real estate, of plant and equipment, the state revenues and the standard of living of the poorer classes of people by at least 25%"? List proposed the founding of shareholders' associations, in order to "cover all of Germany with railways, and moreover stimulate the industry of 20 million people." That meant the private sector, but in increasing degree, public corporations, communities, and geographic regions should acquire shares in order to make possible the financing of great projects. That is of course not yet the pure concept of *state credit creation,* but how should that be possible, without the existence of a German *state?* Decisive here is the principle of creating credit in the form of shares, with the expectation of future social wealth. When, then—in List's words—"the railways have progressed to the point that one state reaches another with its rail line, then the time will be ripe for realizing the idea of a national bank, which would really be a way of boosting German internal transportation and making it run smoothly."

What was done in practice in Germany in the 1840s and '50s, looked quite different. The railways were primarily financed by private capital, and also run as private businesses. Discussion of state credit creation and the regulative state intervention into the economy, was nonetheless carried further and more broadly, and one can rightly say, that without a growing responsibility of the state, and state investments, the incredibly productive expansion of the German economy between 1880 and 1914, would not have taken place. The success of the economic policy of that period was based precisely upon the rejection of the British free-trade dogma.

After the First World War, with the Treaty of Versailles, the European economy was laden with a heavy burden. The horrendous reparations payments, which above all had to be carried by Germany, invaded the productive economy like a cancerous growth; the 1923 hyperinflation destroyed people's overall capacity to resist, and the political-economic and scientific-economic discussion of the 1920s took on a peculiar cast because of these events. Victory went to monetarist liberalism, and any intervention of the state into the economy was declared taboo. The "self-healing power" of the market would become—just like today—reverentially worshiped. This cult of the free-market economy led to the view that shrinking industrial production was a God-given—better said, market-given—law. It was believed that this annihilation of productive capacities was healthy; people spoke about a "purification process," as if some kind of unruly growth were being pruned. Except that a steel mill or a machine tool factory does not happen to constitute "unruly growth"; rather a "healthy shrinking" in this domain has the same effect as if a doctor were to amputate the arms and legs of a patient, so that the poor fellow should not have such a heavy body-weight to drag around, and might then be able to move more quickly!

As this amputation process plunged the world economy in 1929 ever deeper into the depression, and as in Germany, for example, unemployment rose from 2 million, to 4 and then to 6 million in the year 1932, some doubts were raised about how healthy this all was.

The proposals of Lautenbach and Draeger

In this context, I should like to introduce you to two people who rebelled against the dogma of the "self-healing forces" of the marketplace. One was a member of the Ministerial Council within the Federal Economics Ministry, Wilhelm Lautenbach. He also worked on a government commission of the Brüning government, as an adviser in attempting to solve the economic crisis and unemployment. The other was an industrialist from Lübeck, Heinrich Draeger, who

was the intellectual head of the Study Group for a Money- and Credit-Economy.

Lautenbach, who was a very active publicist, prefaced his proposals for state-financed great projects to overcome the crisis with the following fundamental considerations:

1) The so-called healthy shrinking process of industry will not stop, because industry is continuously reproducing itself at a lower level.

2) This self-cannibalization must be consciously defeated. He said, "A depression can only be defeated by a courageous tackling of great tasks of the future."

He mentions as an example the rebuilding of Tokyo after the devastating earthquake of 1923. No one thought to ask where the money for such reconstruction should be gotten! The wealth created by the completely new reconstruction absolutely exceeded all expectations.

In 1931, when Lautenbach made his moves, the financial question was a very tricky one. With the collapse of the Vienna Kreditanstalt and the Danat-Bank, the wellsprings for private capital had run dry. Brüning wanted to take foreign loans to finance great state projects, which naturally drove the debt further into the stratosphere. Through the consolidation of reparations payments, the hands of the Reichsbank were tied, preventing the creation of new bank credits. That was underlined in a brutal fashion when in Germany, the discussion began about creating additional liquidity in the range of 3 billion Reichsmarks. The reaction came promptly, in the form of a thundering complaint from the other side of the Atlantic, combined with massive threats.

Lautenbach proposed the issue of bills of exchange for financing public infrastructure projects, in which a growing portion of the unemployed might be immediately put to work. In practice that should look like this:

The national railway company (Reichsbahn) wants to order new track to be laid, or bridges to be built, or wants to order new rail cars. The relevant factories or construction firms now receive a bill of exchange from the Reichsbahn and deposit it at their own bank. The bank, for its part, provides the necessary credit to the firm's current account, which can now be used for the payment of wages, materials, etc.

Now, since wages are paid in cash, while other costs can be paid by check or bill of exchange, the amount of new cash remains relatively small. That takes care of the case of the entrepreneur. The great advantage for him in the process, is that he does not have to go into debt at high interest rates, rather he is enabled to carry out necessary investments and repair work of his business, which have been left dormant during the depression. His business can thus be set back on its feet, the old debts consolidated—which again ought to make the banks happy.

Now what does the bank do with the note from the Reichsbahn? Since this bill of exchange is discountable at the Reichsbank, it takes on the character of a commercial bill of exchange, and with that, it is as good as cash or ready money. It is part of Lautenbach's plan that over 12 to 15 months the bank should convert the Reichsbahn's bill of exchange at the Reichsbank into middle- or long-term Treasury notes. The Treasury notes are backed up by a national income that is rising, and the bills of exchange either remain in the Reichsbank as part of the Reichsbahn's capital, and can be re-lent; or they can again be converted into bank notes, when the railway has made the profit required to redeem the original bills of exchange.

With this method, credit would only be given for specific projects; the interest rates would be very low, and we should not have to fear an inflationary effect; on the contrary, the consequence would be a stabilization of the currency! Says Lautenbach: "This credit expansion does not bring about further illiquidity; rather, it will increase liquidity and make more solid our credit-economy."

It was a great misfortune for Germany and Europe that these proposals were not adopted in 1931. Threats by the Americans, and the wrenching fear of inflation, remind you of the methods used today by the IMF and the World Bank vis-à-vis eastern Europe. It really is time that we learned something from history.

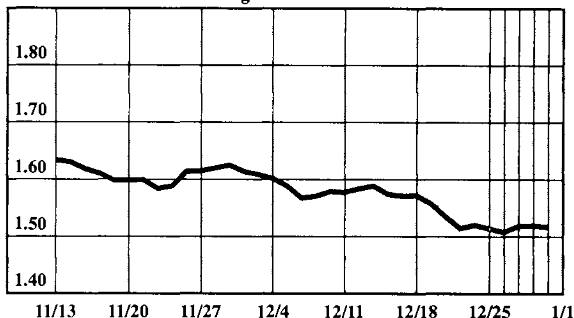
At the end of 1931 the Study Group for a Money- and Credit-Economy was formed, under the leadership of the Lübeck industrialist Heinrich Draeger. He came to the public eye in the spring of 1932 with an essay called "The Creation of Work through Productive Credit Creation." Draeger used the concept of "productive credit creation," because it implies the condition that "state credit [should only be] extended exclusively for the creation of new, durable, productive wealth, and a consequent increase of the supply of goods." He defined a 30 billion Reichsmark program for creation of jobs, which was calculated over six years, and included, among other things, great projects in city-building, infrastructure, the building of power stations, highways, dikes, etc. The method of financing corresponded in principle to that of Lautenbach. For Draeger, the Reichsbahn's bills of exchange should be given directly to the Reichsbank, in order to function as collateral for new credit creation. With that, Draeger was even more radical than Lautenbach, in that he meant that with this method the Reichsbahn should not be charged any interest, since its bills of exchange were already practically a kind of bonus, falling like a windfall into the lap of the Reichsbank. So they could not ask interest for that!

A differential rate of interest

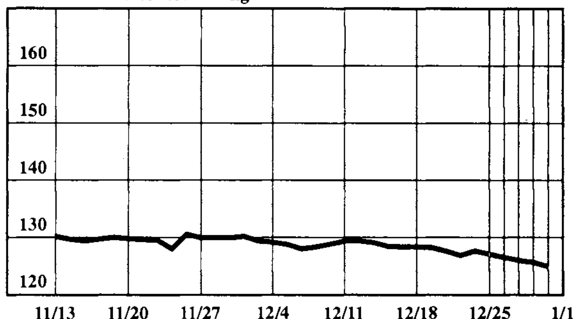
New in Draeger's proposals was a differential rate of interest charged by the banks. As we would say today: low interest rates for productive investments and high rates for speculative investment; for granting of credit must, as Draeger says, call forth a "creative effect, an expansion of the economy." Draeger wished to have it understood that the "state creation of credit should be only the first step toward

Currency Rates

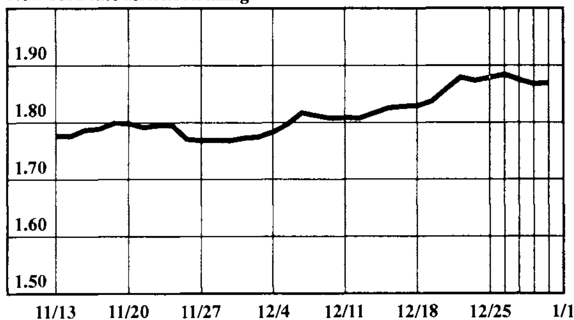
The dollar in deutschemarks
New York late afternoon fixing



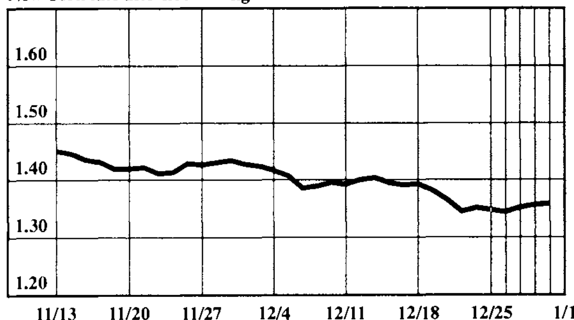
The dollar in yen
New York late afternoon fixing



The British pound in dollars
New York late afternoon fixing



The dollar in Swiss francs
New York late afternoon fixing



a fundamental change in the hitherto customary way that the private economy has obtained credit."

Unfortunately these proposals were adopted only at literally the last minute. Had people in the spring of 1932 begun to carry out this program, it might have been possible to pull the rug out from under the Nazis' feet; after all, the NSDAP [Nazi Party] was going through a severe existential crisis at the end of 1932.

But it was only the last government of the Weimar Republic and Chancellor Schleicher who seized the initiative and inaugurated a job-creation program on the model of Draeger and Lautenbach, at the level of 500 million Reichsmarks. That was Jan. 28, 1933—too late! Two days later, Adolf Hitler seized power—and took over the job-creation program from Schleicher.

At this point we hear today's free-trade dogmatists saying: "Aha, you wish to have the state create credit; the Nazis already did that!" Well, it is true that the Nazis built the Volkswagen and the Autobahns. Nonetheless, in 1945 no one took it into his head to stop building highways or producing Volkswagens, just because they had been symbols of fascist economic policy!

At the beginning, the Nazis did use the instrument of state credit creation, in order to put the unemployed back to work, earning their daily bread. In that way, they were able to consolidate their power within the country, and attract great admiration abroad. From 1934 onward, credit was created increasingly for military purposes and the production of synthetic substitutes (with autarchy in mind). With that, the original concept was transformed into its opposite: From productive, it now became unproductive credit creation. The results are known. Because of the Nazis' disdain for humanity, it could not have been otherwise, for the concept of productivity can only be recognized by those who see the people's creative thought and work, as the source of our wealth. The Nazis, however, knew only slave labor, as it was put into effect in their manpower programs of the 1930s.

Let me underscore something about the ideas of Lautenbach and Draeger: Their inadequacy lies in being limited to job creation. They lacked a deeper understanding of economic processes. . . .

We need today more than a job-creation program: We need a concept of a long-term buildup of the nations of Europe and the world. It is easy to find demagogues, dictators, and criminals who would unscrupulously use the state's sovereign rights—including the right of credit creation—to plunge their country and the world into dangerous adventures.

Let us forestall that threat, by creating economic wellbeing, technological progress, and social peace. For that we need nations to be sovereign, nations which no longer let policy be dictated to them by the IMF and the World Bank. We need nothing less than the sovereign right to state-created productive credit.