

Policy Paper

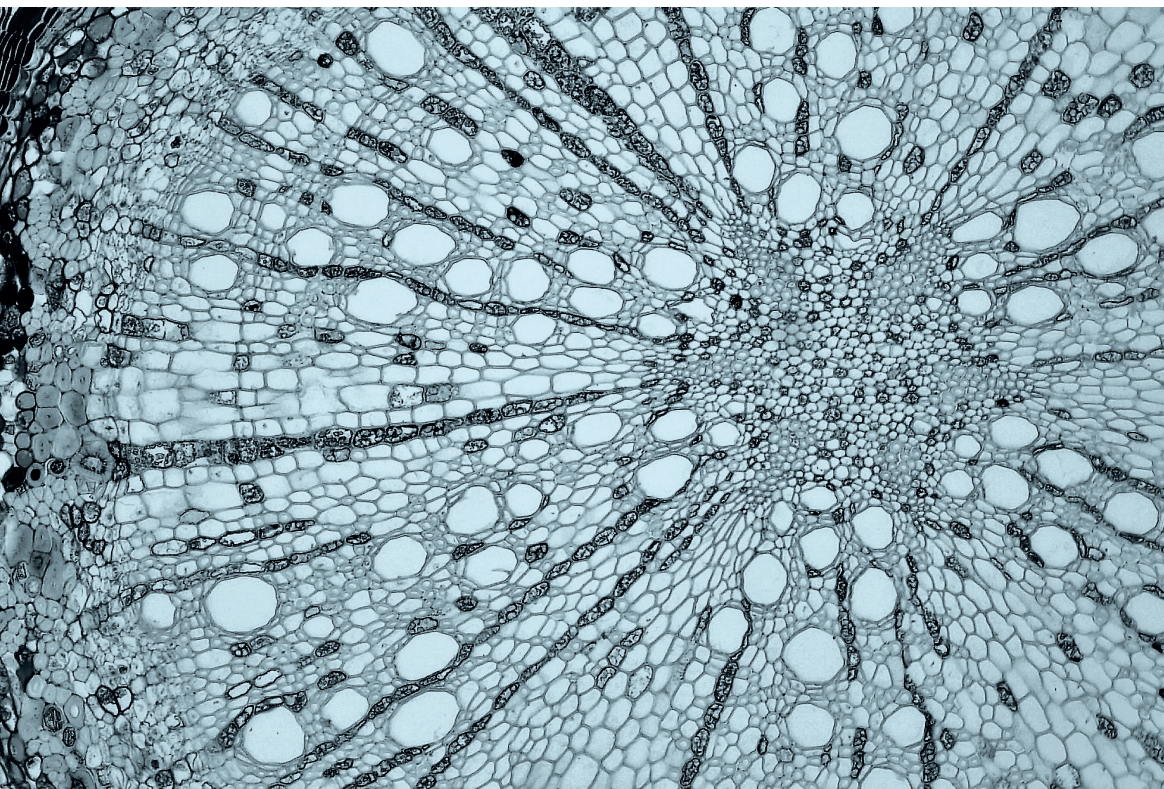
Misremembering Weimar:

Unpacking the Historic Roots of Germany's Monetary Policy Discourse

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#ECB
#Inflation
#Germany



Many Germans are highly sceptical of the ECB's monetary policy of recent years. To explain this scepticism, experts often point to the collective memory of the hyperinflation in the early 1920s in Germany. Based on new survey data, our policy paper shows that German memory of this period is in fact deeply flawed. Given this historic misunderstanding, many Germans today underestimate the risks of deflation and mistakenly perceive mass unemployment and hyperinflation as two sides of the same coin.

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1 Introduction

As the new president of the ECB, Christine Lagarde faces a huge challenge. In the Eurozone's largest economy and the very country in which her new offices are located, media, politicians and economists remain deeply sceptical of the ECB's monetary policy of recent years. Indeed, according to the most recent polls, conducted in 2018, more than half of the German public mistrusts the ECB and many seem convinced that an expansionary monetary policy is outright dangerous.¹

Many analysts point to German history when explaining German scepticism towards loose monetary policy.² The devastating effects that rampant inflation had on the young Weimar Republic are often said to be deeply engrained in the German collective memory. As a prominent exhibit for this kind of thinking, then-economy minister Rainer Brüderle declared during a Bundestag debate in 2011: "One lesson of history is this: when money gets bad, everything gets bad. We have experienced this in German history: from hyperinflation to mass poverty, all the way to the war and the fatal aberrations in Germany".³ Given this reading of their own history, Germans are said to remain deeply concerned about any form of expansionary monetary policy, even in a potentially deflationary environment.

However, contrary to what the above quote suggests, the economic history of the Weimar Republic actually hardly provides a strong case for the strict mantra of monetary restraint. In fact, the Nazis took over more than 10 years after hyperinflation had ended. The mass poverty that Rainer Brüderle alludes to was not the outcome of hyperinflation, but rather the by-product of mass unemployment, deep recession, and falling prices during the Great Depression of the early 1930s (see Figure 1). Hitler came to power after a period of *deflation*.

Still, many Germans seem untroubled by deflationary risks, yet are constantly worrying about inflation. The present paper shows that this mismatch can partly be explained by the fact that German memory of the Weimar Republic is deeply flawed. Based on new survey data, we can show that most Germans do not know that Germany's interwar period was shaped by two separate crises, but rather see them as being one and the same. Indeed, fewer than 1 in 25 Germans are aware that the Great Depression was a period of deflation, while more than 40% think it was characterized by concurrent inflation and unemployment. Looking back into a skewed version of their own history, many Germans conclude that mass unemployment and high inflation are just two sides of the same coin.

"Many Germans seem untroubled by deflationary risks, yet are constantly worrying about inflation."

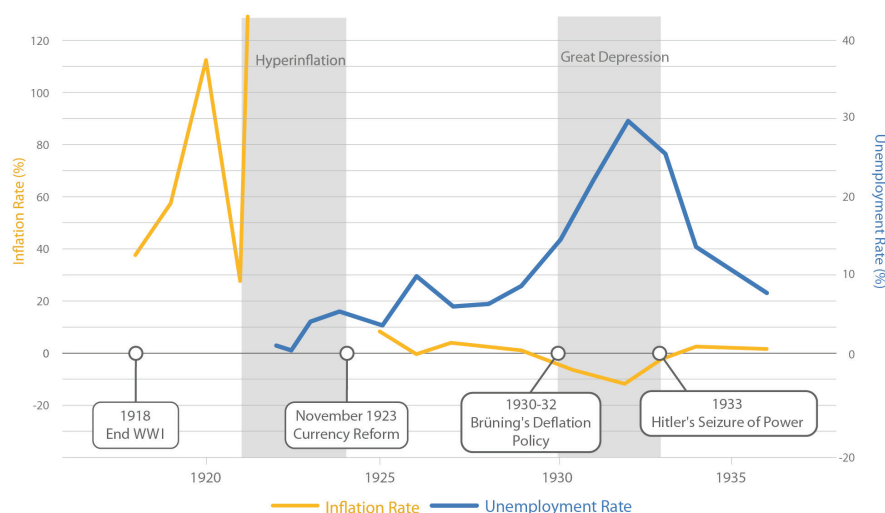
¹ For background on the methodology and the results of the present paper see Haffert, Redeker & Rommel (2019): *Misremembering Weimar – Hyperinflation, the Great Depression, and German Collective Economic Memory*. This study has benefitted from gracious funding from the University of Zurich and the Junge Akademie Germany.

² E.g. Taylor, Frederick. (2013): *The Downfall of Money: Germany's Hyperinflation and the Destruction of the Middle Class*. London: Bloomsbury; Hayo, Bernd, and Florian Neumeier (2016): *The Social Context for German Economists: Public Attitudes towards Macroeconomic Policy in Germany*. In German Macro: How It's Different and Why That Matters, eds. George Bratsiotis and David Cobham. European Policy Centre, 64–72; Shiller, Robert (1997): *Why Do People Dislike Inflation?* In *Reducing Inflation: Motivation and Strategy*, eds. Christina Romer and David Romer. Chicago: University of Chicago Press, 13–70.

³ Deutscher Bundestag (2011), 15211, own translation.

What makes this worse is that this misconception is especially prevalent among well-educated and politically interested Germans. Hence, the group of people following the ECB's monetary policy most closely is also the group most likely to draw the wrong lessons from German history. But public thinking about Weimar economic history is not just substantially flawed. We can also show that the skewed memory of the Weimar Republic still affects the way in which at least some Germans think about monetary policy today. While Germans on the political left do not react to being reminded of Weimar History those on the political right become substantially more inflation averse. Educating Germans about the reality of Weimar's inflationary history, on the other hand, has little effect. Only left-leaning respondents become slightly less inflation averse when we tell them that prices fell during the Great Depression.

Figure 1:
Inflation and Unemployment Rates during the Weimar Republic.



Own calculations based on data from: Sensch, Jürgen, (2016).⁴

These findings suggest that for the ECB, repairing the bond with Germany is going to be a complicated task. It should of course better communicate its policies to German citizens; it could in particular do more to explain the risks of deflation and draw on historic examples such as the Great Depression. But in so doing, the ECB will have to argue against a deep-seated and widespread misunderstanding of economic history, which will make many Germans question whether monetary expansion prevents unemployment and recession or rather risks creating it. In the sections that follow, we explain our findings in greater detail. In the final part, we draw policy conclusions.

⁴ Sensch, Jürgen, (1903, 2002 [2016]): *histat – Datenkompilation online: Entwicklung der Arbeitslosigkeit in Deutschland 1887–2000*.

2 German Memory and Inflation

From our newly-collected data from representative surveys conducted in Germany and the Netherlands, we can identify three important aspects of the public memory of Weimar economic history in Germany. First, many Germans have merged the period of hyperinflation following the First World War and the Great Depression into one encompassing crisis. Results from the Netherlands show that associating the Great Depression with very high levels of inflation is a specifically German phenomenon. Second, this misconception is especially pronounced amongst the most educated and politically interested Germans. Furthermore, reminding Germans of the economic history of Weimar leads to more inflation aversion amongst conservative respondents, whereas educating respondents about the facts of their country's deflationary history has little effects on what monetary policies German respondents prefer.

“Germans have merged the period of hyperinflation following the First World War and the Great Depression into one encompassing crisis.”

2.1 The Confused Memory of Weimar's Economic History

Our findings show that many Germans of the present day severely misunderstand the economic history of the Weimar Republic.⁵ Answering an open question, almost 40% mentioned inflation or related issues such as “hyperinflation” or “currency devaluation” as economic problems characterizing the German economy during the Great Depression. Indeed, respondents felt that the most devastating recession in German economic history was characterized by very *high levels* of inflation. When we asked German respondents to provide us with an estimate as to the inflation rate in 1932, more than half stated that it was larger than 10 percent, and about 15 percent even guessed that it was 100 percent or higher.

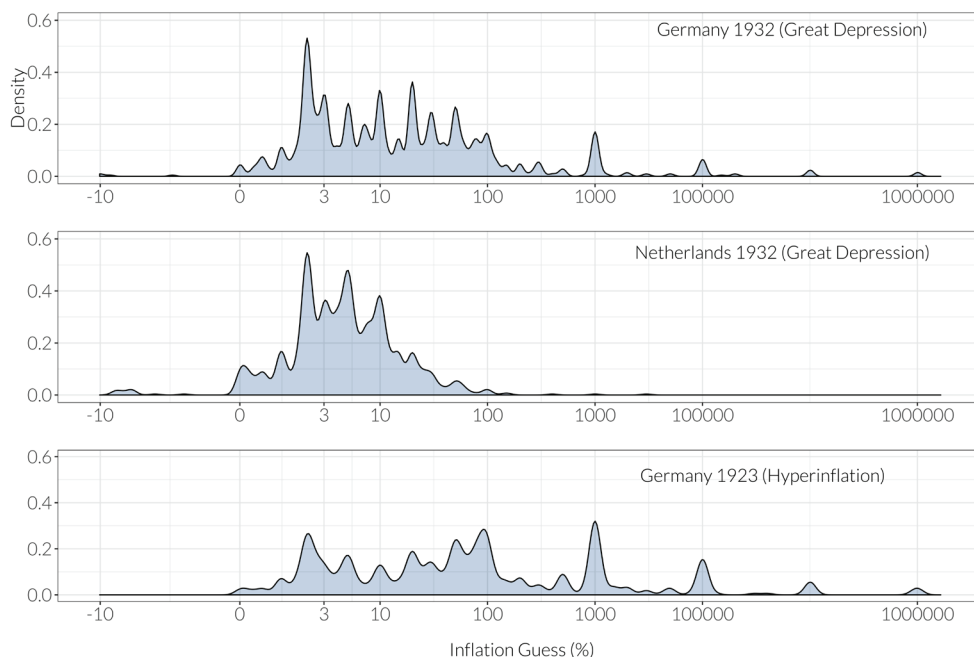
In fact, this period saw the most severe *deflation* in recent German history. In response to our open question, about 4% of our respondents correctly identify *falling* price levels as a key issue in the last years of the Weimar Republic. Even more strikingly is how many respondents think that during the Weimar Republic, inflation and mass unemployment went hand in hand. Indeed, almost a quarter of respondents indicate high unemployment and inflation as occurring concurrently during the Great Depression. This is mirrored by the fact that when we asked Germans for their estimate of the inflation rate in 1932, only 10 percent of respondents put the number at below 2 percent, and almost nobody posited negative numbers (see upper panel, Figure 2).

Interestingly, associating the Great Depression with very high levels of inflation seems to be a specifically German phenomenon. When we compare the estimates of our German respondents to those of the similar survey conducted in the Netherlands – a country that also suffered from the Great Depression in the early 1930s, but which has never experienced hyperinflation, we see that the responses differ greatly. As in Germany, only a handful of Dutch respondents are able to correctly identify the Great Depression as a period of deflation. Yet, while Dutch respondents also seem to know little about their country's deflationary history, they remain far from associating the 1930s with a time of hyperinflation. More than 60% of responses are clustered around the current inflation rate and assume inflation rates of up to 5%. Contrary to Germans, less than a fifth of Dutch respondents

⁵ We asked three different subgroups, each representative in their own right, the three set questions reported on in this section, so as to avoid biasing their answers through previous questions.

estimate that prices rose by more than 10 percent and less than 1% of respondents stated inflation rates above 100%.

Figure 2:
Distribution of Inflation Estimates across different Survey Groups.

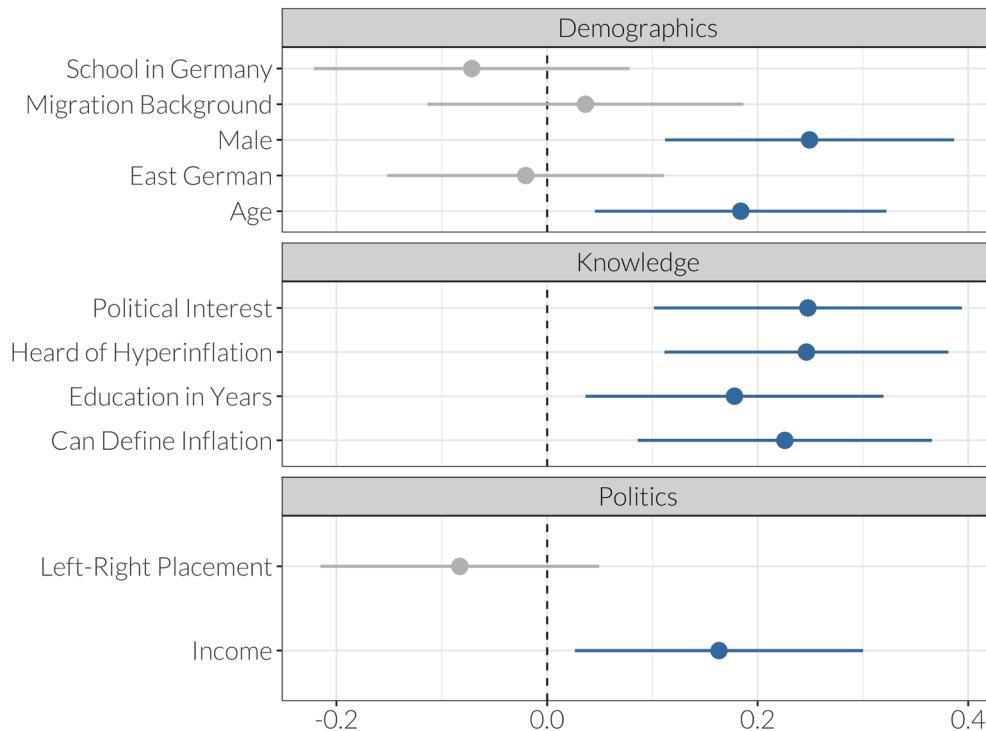


Our results also indicate that the very high inflation estimates in Germany likely stem from a conflation between the Great Depression and hyperinflation amongst respondents: Asked for their estimate of the inflation rate in 1923, having been specifically told that 1923 was the height of the hyperinflation crisis in Germany, the distribution of responses looks very similar to that for our question about 1932. Estimates pertaining to the hyperinflation crisis are on average higher than those for the Great Depression. Yet the structure and distribution of answers for these entirely different crisis episodes look remarkably similar. This similarity suggests that many people draw on the same set of images when answering either question.

2.2 Who is Misremembering Weimar?

Many Germans have, thus, misguided ideas about the historic relation between high inflation, unemployment, and recession. But not everyone seems to fall into the same trap. Depending on how we interpret the data, only about 40% of German respondents mistakenly believe that the deepest economic downturn in recent German history was a period of high inflation. Does this then suggest that only those Germans whom pay little attention to politics are confused on the matter as they are less likely to follow heated debates about monetary policy and unconventional ECB measures?

Figure 3:
What predicts high inflation estimates?



Plot point estimates and 95% confidence intervals for the standardized regression coefficients between individual characteristics and inflation estimates. Estimates coloured in blue highlight statistically significant associations with higher inflation estimates.

Figure 3 shows that in fact the opposite holds true: People tend to associate the Great Depression with higher inflation rates if they are *more educated and know more about inflation*. Respondents are also more likely to give higher estimates if they describe themselves as being generally very interested in politics. So, instead of it being a sign of knowing little, and caring less, about politics, false inflation beliefs are especially prevalent amongst those whom are likely to follow public debates and care about political decisions. Other factors positively associated with higher estimates are gender (with larger discrepancies amongst male respondents), age, and income; whereas political ideology, personal migration background, and whether respondents were born in East or West Germany play no influencing role.

“People tend to associate the Great Depression with higher inflation rates if they are more educated and know more about inflation.”

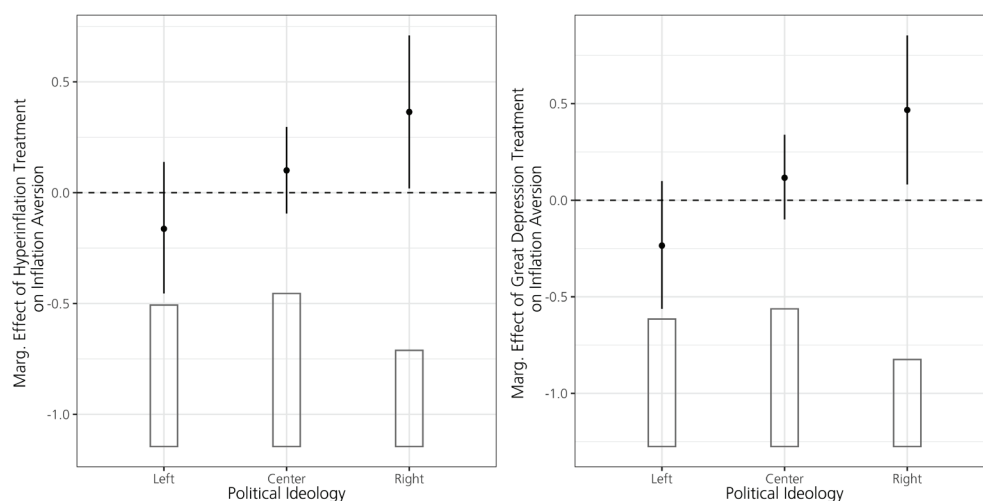
2.3 The Politics of Misremembering Weimar

The final question is whether this false memory of Weimar matters in relation to the kind of monetary policies Germans prefer today. In other words, does the fact that Weimar still features prominently in many political speeches or journalistic articles about today’s monetary policy influence the preferences Germans hold with regards to fighting unemployment or inflation? We investigate this with the help of an experiment embedded into our survey, in which we gauge whether reminding Germans of Weimar actually influences whether they think monetary policymakers should focus on keeping inflation low or fighting unemployment.

Results show that it does; but not for everyone. Whereas Germans describing themselves as being on the left of the political spectrum remain unimpressed by our reference to the economic history of Weimar, those on the right become significantly more inflation averse. That is, when we remind Germans who situate themselves of on the right of the political spectrum of Weimar's economic history in any way, they afterwards give higher priority to price stability and keeping down the rate of inflation. Significantly, it also does not make a difference whether inflation actually featured as a problem in the specific crisis we ask them about. Independent of whether we mention the period of hyperinflation, with its skyrocketing inflation rates, or the Great Depression, with its mass unemployment and falling prices, right-leaning Germans afterwards express a stronger preference for keeping inflation low.

Figure 4:

The effect of being exposed to either questions about the period of hyperinflation (left) or the Great Depression (right) on inflation aversion across political ideologies, according to the self-placement of respondents.



Point estimates and 95% confidence intervals.

Our study also shows that educating Germans about the fact that during the Great Depression, Germany actually saw deflation and falling prices rather than inflation has little effect on their monetary policy preferences. If anything, left-leaning respondents become slightly less inflation averse, but the overall effect remains small. Undoing the effects of broad misinterpretation of Germany's economic history is, thus, going to be a difficult task.

3 Summary and Implications

It is often claimed that German scepticism towards monetary expansion is rooted in the country's economic history. While there is truth to this, our findings show that what matters for public monetary policy discourse in Germany is not cool-minded analysis of the pros and cons of different policy options, set against a backdrop of appropriate lessons learned from the past. Rather, many Germans have a deeply flawed understanding of economic developments during the Weimar Republic, in which the perils of hyperinflation, and the devastating effects of the Great Depression are seen as two sides of the same coin.

This narrative not only lacks any reference to the negative consequences of deflation, it also means that, based on their account of economic history, many Germans have reason to refute the notion that combating inflation and combating unemployment and low growth can be conflicting goals. Unfortunately for the ECB, this misconception is especially common amongst highly educated and politically interested Germans, affects monetary policy preferences at least amongst conservative voters, and is hard to correct.

From the ECB's perspective, investing heavily in the way it communicates monetary policy decisions to the German public and media will thus likely not be sufficient. The ECB will also need to sharpen German awareness as to the risks of deflation as opposed to inflation, and both the Bundesbank and the German government could also do their part here. Most importantly, our study shows that German policymakers and the media should try to pay attention to the complexities of economic history when referring to the Weimar Republic. While it can be tempting to quickly jump from mass inflation to mass unemployment, treating these separate issues as one big economic crisis contributes to a harmful misreading of what lessons should be drawn from German history.

“The ECB will also need to sharpen German awareness as to the risks of deflation as opposed to inflation, and both the Bundesbank and the German government could also do their part here.”

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