

THE REVIVAL AND COLLAPSE OF THE HUNGARIAN STOCK MARKET (1918-1919)

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On July 28, 1914 at the outbreak of World War I, the Budapest Stock Exchange¹ was officially closed. But by the middle of the first year of the war, a significant private trade had developed among the exchange members. This private trade was at first carried out in the reception room of the exchange building, then, with the permission of its directors, on the floor of the exchange itself. Eventually this informal trading received official recognition and continued throughout the war until the Hungarian Soviet Republic was established. The exchange was closed while the Soviet Republic was in existence and did not reopen until October 20, 1919.

This paper will analyze what happened in the market in the 9 month period between August 1918 and March 1919. This period can be divided into roughly three three-month segments. During the first three months, in the pre-armistice period (until November 3, 1918) stock prices, as measured by the market average, declined by 21.8 percent. In the second segment trading virtually stopped. This was caused by the exchange imposing minimum prices to prevent further market slide when the Károlyi government came into office. This price floor, instead of stopping the market slide, resulted in practically halting trading due to lack of activity. The market restarted when minimum prices were abolished in mid-January 1919, but stock prices continued on a slow decline. In this three month period, in spite of the political and economic turmoil, the market declined only 6.9 percent.

During the pre-armistice period bank stocks fell by 22.3 percent, flour mill stocks by 30 percent, coal mines and brickworks stocks by 15.97 percent, the stocks of steel mills and factories fell by 14.53 percent, transportation stocks by 25.03 percent, and miscellaneous stocks by 26.77 percent. When trading activity resumed in January 1919, the stock market started off slightly higher (5.7%) than when activity stopped. In the three months of 1919 before the market was closed, bank stocks declined by 11.5 percent, flour mill stocks by 6.7 percent, coal mines and brickworks by 4 percent, the stocks of steel mills and factories fell by 5.2 percent, transportation stocks rose by 11.3 percent, and miscellaneous stocks sank by 8.6 percent.²

In the period immediately following the armistice Hungary's future looked quite bleak. The country not only lost the war, but it also faced the prospect of losing large amounts of territory, as the Austro-Hungarian Monarchy was breaking into independent countries.

¹ The Budapest Stock Exchange was established on January 18, 1864: http://www.bse.hu/topmenu/about_us/history (retrieved on October 1, 2008).

² These industry groups are the same as those used by the Hungarian papers carrying the daily quotes. All averages are simple un-weighted arithmetic averages.

Furthermore, its economy was at a complete standstill and it was facing numerous labor strikes. Nevertheless, overall stock prices held quite firm during this period. An explanation for the large decline before the armistice is easy to come by, but not for the market's only slight decline in 1919.

Post-January stock market behavior, however, is more difficult to explain and could perhaps be best understood as simply as a sigh of relief from the burdens of war and a sense of optimism for the future. The country expected economic aid to come from the Allied countries as a result of the Paris Peace Conference. Another possible explanation for the market's behavior during this period would be that purchasing stocks was used as a haven from the rampant inflation during this postwar period.³ The loss in value was in the steel mill and flour mill shares were nearly identical. The fact that the value of steel mill stocks fell by 5 percent is hardly surprising since most of the iron ore mines came under Czechoslovakia's control. Flour mill stocks declined sharply due to impending land reform (which never really came about) and loss of farm lands to annexations by Hungary's neighbors. As a result it was expected that the country would be left with excess capacity. Transportation stocks outperformed the market by a wide margin – a consequence of speculative buying in the aftermath of Italian buying of Austrian transportation stocks.⁴ The loss of value of the bank stocks can be explained by the fact that many firms that the banks

³ The traditional methods of measuring inflation were useless during this period (both before and after the armistice) due to price controls on consumer goods. Even though the black market flourished during this period there are no statistics to measure it. However, the comparison of the value of a paper crown vs. a gold crown could perhaps give us some indication of inflation.

⁴ The stock market prices were taken from the daily papers, the Hungarian language "Pesti Napló," and the German language "Pester Lloyd," both published in Hungary. The daily papers which reported on market activity presented the high and lows for each day, not the opening and closing prices that we are accustomed to seeing today. To indicate whether the stock price was going up, the quote was given as, for example, Co. X 100-105. When the stock price was going down the quote was Co. X 105-100. Since the trading day was very short, we assumed that the closing price was the second quote.

Although there were about 130 stocks listed on the Budapest Stock Exchange during the period under examination, the list was narrowed to just 48 companies because trading activity was very light and sporadic on the rest of the list. Once selected, these 48 stocks were classified into six industry groups, which were identical to the categories that were listed in the newspapers. For each week in the period under examination, the closing price for each stock traded was recorded for Monday and Thursday. Only stocks that traded 90% of the time were included in this study. If a stock was not traded on either Monday or Thursday of the week, the data was taken from the following day.

The data from the "Pester Lloyd" is now accessible on the internet: <http://anno.onb.ac.at/cgi-content/anno?apm=0&zoom=1>.

The stocks were classified by industry groups as follows:

Industry group	Companies in group
Banks and savings and loans	15
Flour mills	1
Steel mills and machine tools	4
Coal mines and brickworks	8
Transportation	7
Miscellaneous	13
Total	48

had stocks in, or were the banks' customers, in the newly drawn map of Europe were outside Hungary. The political and economic disorder also made attracting deposits difficult.

In late July 1918, "Pesti Napló," a Hungarian daily, reported that "due to uncertainty there is no observable trend in the market. The price ranges are generally narrow, and speculation seems to be in the Hungarian issues as the market in Vienna is nearly dead."⁵ While reports from the war front were discouraging, the news on the domestic front was more encouraging. On August 4, it was reported that the Austro-Hungarian Bank would open a Spanish office on September 15 in order to promote trade between Spain and the monarchy. On August 7, Schlick-Nicholson, a Hungarian machine tool and shipbuilding company, announced that it would build a new machine tool factory in Budapest. As a result the market gained in the first two weeks of August. In the third week of August, however, leaders of the Central Powers met to reach a common understanding regarding steps to be taken to reach an armistice with the Allies. The market reacted by trading at a slightly lower level because of the uncertainty of the peace terms. Only flour mill stocks closed higher for the week, as it was announced that mill workers were now exempt from military call-ups.

The last week of August and the first fortnight of September saw a firmness in the market and an increase in trading activity, despite the bad news from the fronts. This was due mostly to the increasing activity of the new issues market, especially among bank stocks. "Pesti Napló"'s market analyst wrote that "a number of firms are trying to take advantage of the strength of the stock market and the expectations are of stock splits and new issues." On August 25, the National Forestry Company (*Országos Fatermelő Rt.*) announced that it would call a special shareholders meeting for September 3, to raise its capital stock from six million to twelve million crowns. The National Bank (*Országos Bank*) also announced plans to raise its capital stock. However, on September 3, the Government notified the Hungarian Bank (*Magyar Bank*) that it would allow a 20-million crown increase in its capital stock despite a request for a 40-million crown increase. On the very same day a government decree was signed limiting the new issue of stock. This dampened the interest in the market and prices fell.

On September 14, Count István Burian, joint foreign minister of the Austro-Hungarian monarchy, asked the Entente nations to begin discussions on the conditions for peace. He made it clear that a peace on the basis of Wilson's 'Fourteen Points' would be unacceptable. Until mutually acceptable terms were proposed, he favored the continuation of the war. As a result, when the market reopened after a three-day break for the Jewish holidays, prices fell. In the following week the market recovered slightly.

War bulletins and rumors about impending changes in foreign policy made the market very nervous. From the battle fronts came news of the capitulation of the Bulgarian army, of the impending resignation of German Chancellor Georg Hertling, and of the Allied troops in the Balkans' imminent crossing of the Hungarian border. On the exchange a major dealer declared bankruptcy. As a result panic broke out and the market dropped for the week. Many members asked the exchange's Board of Directors to close the market

⁵ "Pesti Napló," July 31, 1918.

temporarily to prevent a further drop in prices. However, on September 24, after a meeting, the Association of Securities Dealers decided to set maximum limits on inter-day fluctuations of 5 to 10 percent. This measure stopped the further plummeting of prices.⁶

On September 27 the exchange members agreed that on that day the trading will be allowed above preset minimum prices. For stocks that were priced above 1,000 kr, the minimum price was 10% less than the previous day's prices; for stocks below 1,000 kr. the minimum price was set 5% below the previous day's closing prices. When prices fell to the given predetermined minimum trading came to a halt for the lack of buyers. "Pesti Napló" reported that "some banks intervened and repurchased some of their own stocks at the minimum prices."⁷

On October 4, I. Burian, the Austro-Hungarian foreign minister, sent President Wilson two notes suggesting an immediate cease-fire and accepting the peace terms based on the Fourteen Points.⁸ On the 6th, Berlin took the initiative by sending a note to President Wilson proposing an immediate armistice, with the Fourteen Points as a basis. On the 8th, Wilson sent his response to the German government in which he asked for further elaboration. Next day, at 4 pm, the Hungarians learned of this message and interpreted this as a positive sign and expected a similar answer to their note (which, in fact, was only answered on the 19th).⁹ The following day, the 10th, the papers reported that by 5 pm on Wednesday the price of gold and diamonds on the "coffee house exchange" dropped sharply. A kilogram of gold fell to 18,000 crowns from the September price of 26,000, and the price of diamonds fell by 30 percent. On this unofficial exchange, the price of sugar also fell, to 20 crowns a kg from the previous 30 crowns. Interviewed real estate agents reported that in anticipation of peace many landlords withdrew sell orders.¹⁰

In the ensuing weeks the stock market continued to fall, reacting mostly to political events. At various times there were rumors that the market would be closed; all of which proved false. On October 17, István Tisza announced in parliament that "we have lost the war," thus acknowledging what many (most) already knew.

On Monday, October 21, the Stock Exchange's Board of Directors shortened the trading day to an hour due to the Spanish Influenza pandemic.

On October 24, a number of Stock Exchange members demanded that the market be closed due to the unsettled political conditions. But by a vote of 17 to 11, the Board of Directors decided to keep it open. In the last week of October, with the expectation that Mihály Károlyi, a parliamentary leader with a pro-Entente reputation, would be appointed prime minister, the market stabilized expecting that his appointment would hasten the peace process. On the 26th, Charles IV notified Kaiser Wilhelm II that he was going to sue for a

⁶ Ibidem, September 25, 1918.

⁷ Ibidem, September 28, 1918.

⁸ *Austria Asks President Wilson to Consider Peace Based on His Points, Including Those of His Last Speech*, in "The New York Times," October 6, 1918, p. 1.

⁹ Victor S. Mamatey, *The United States and East Central Europe, 1914-18*, Princeton, 1957, p. 324.

¹⁰ "Pesti Napló," October 11, 1918.

separate cease-fire and peace agreement. Indeed, on the 28th, Foreign Minister Gyula Andrassy petitioned President Wilson for a separate peace. While movement was taking place on the international scene, during the night of 30-31, a bloodless revolution shook the streets of Budapest. Demonstrators demanded the appointment of Károlyi, who was the leader of the recently organized National Council. On October 31, former Prime Minister István Tisza was assassinated by a band of disgruntled soldiers. That same day, in the late afternoon, Károlyi was appointed prime minister of Hungary, and the following day the market was closed for 24 hours.¹¹

On Saturday, November 2, the Board of Directors, in light of the impending armistice and Károlyi's appointment, issued an optimistic statement saying, "that we hope that the stock exchange will play an important role in the rebuilding of the new nation and it accepts this role enthusiastically ... and hopes that its leadership will lead with its existing autonomy intact, which in the current economic conditions is vital for fulfilling the nation's goals."¹²

But, despite the reassuring speeches, trading activity on the exchange declined sharply. On November 5th, the Stock Exchange Council published the minimum prices for each stock below which trading was forbidden; the prices were set at the lowest price reached by each stock in October. On the 6th, only four stocks traded. On the 7th and 8th trading picked up slightly (10 stocks and 31 stocks, respectively). On the 9th, when news arrived that the Berlin Stock Exchange had closed, trading almost came to a complete standstill. Twenty stocks were traded on the 11th, seven stocks on the 12th; thirteen on the 13th, and only three on the 14th. At this time, it was considered whether to close the exchange completely owing to the extremely light trading. Instead, starting November 14, trading hours were reduced to 30 minutes a day (11'30 am to 12 pm); daily price limits were set to the previous day's low. On November 16, Hungary proclaimed itself a republic. However, the market did not react to the news; instead it took a wait-and-see attitude with trading activity held to a minimum.

Despite the further decline in trading volume the directors of the exchange, in a meeting on December 3, decided against closing the exchange. They noted that market activity in Vienna picked up, and, therefore, expected a similar increase on the Budapest Stock Exchange. This proved to be a pipedream, as the Hungarian economy came to a complete halt. Production ceased in nearly all industries, not only because of lack of raw materials, but also because of the political uncertainties. For example, Romania announced that it would allow shipments of lumber to Hungary only in exchange for food. And Czechoslovakia prohibited the shipment of forestry products completely. In many factories workers demanded the resignation of managers. There were talks between the companies and the workers to meet these demands. News of impending strikes also spread. Only when the Government indicated that it would intervene, did market activity pick up again. On January 9, 1919, the committee of the Supreme Economic Council of the Paris Peace Conference, headed by Alonzo E. Taylor, with headquarters in Vienna, arrived in Budapest.

¹¹ Ibidem, November 2, 1918.

¹² Ibidem.

It was expected that, as a result of this meeting, economic aid to Hungary would be approved. This, however, never came about.¹³

Economic problems, coupled with the apparent Allied hostility to the liberal-democratic government, led to a cabinet crisis at the end of December and early January 1919. A number of ministers resigned. In spite of the crisis atmosphere in Budapest, the upcoming opening of the Paris Peace Conference and the second Coolidge Mission's visit rekindled hopes that the Hungarians were not being neglected. To solve the political crisis, the National Council appointed Károlyi President of the Republic (provisional, on January 11, 1919). Because the Paris Peace conference was to start with preliminary talks already taking place on the 13th, it was still assumed that the Hungarians would participate; consequently, the market reacted positively, and the number of stocks traded increased. Market activity returned to November levels by Monday, January 13, 1919. On the 20th, price limits were abolished and the trading day was expanded from 11 am to noon. When the market reopened it did so slightly lower (5.4%).

Beginning in January, labor problems put a damper on prices in the stock market. A "wave of strikes swept across the country, in the course of which, factories, transport and communication installations were occupied."¹⁴ Demands by workers to participate in management were spreading and at the same time production remained at a standstill. Workers also called for participation in wage policy decisions. In one extreme case, workers demanded to have their representatives present even at the opening of company mail.¹⁵

On January 21, it was announced that the workers of Schlick-Nicholson had successfully removed two managers and had replaced them with their own representatives. The Pest Hungarian Trade/Commerce Bank of Pest (*Pesti-Magyar Kereskedelmi Bank*), Schlick-Nicholson's major stock holder, immediately announced that, in light of events, it would no longer approve any new loans. It was also anticipated that because of abolition of price limits and news that Yugoslavia had instituted agrarian reform, the market would react in a negative way. Nevertheless, it was only slightly down for the week. In the last week of January, trading volume increased, but prices were mostly unchanged. On January 31, Saturday trading was allowed again, making the trading week six days long.

On the news that the Italians were buying up shares of Austrian shipping lines, the prices of Hungarian lines also went up. This created a positive atmosphere in the market and the prices closed higher for the week. However, on February 13, it was announced that the Hungarian Agrarian Reform Law was to be published on the 15th; as a result the market fell slightly. The market reacted negatively to this reform because it called for the breakup of large farming estates. The market was also waiting for some statement from the National Workers Council, which was formed on February 8, to direct public work programs and this, too, put a damper on the market. On February 22 at 11:40 am, market activity was stopped by the bell of the secretary of the exchange. Mr. Scherz, the secretary, announced that in

¹³ *Magyar Történelmi Krónológia*, ed. by Gunst Péter, Budapest, 1984, p. 441.

¹⁴ Kontler László, *A History of Hungary*, New York, 2002, p. 333.

¹⁵ "Pesti Napló," January 10, 1919.

sympathy with the Socialist demonstration and general strike the trading activity would stop for five minutes. When trading resumed, prices fell.¹⁶

In the first week of March, the market remained stable, but when, on the 7th, the government announced plans to nationalize property, prices fell. On March 17, the government decided to begin nationalization and this resulted in large demonstrations supporting the government. The market's confidence was further shaken. Furthermore, a crisis was caused by the Vix ultimatum. This memorandum called for the creation of a neutral zone between Hungary and Romania, which meant that Hungarian troops would have to withdraw and as a result depriving Hungary of still more territory. This left the government no other alternative than to resign. As a result the market closed lower and on March 21, when the Hungarian Soviet Republic came to power, the exchange closed its doors for several months, even though it was not explicitly ordered to do so. This was done because, as the papers reported, "in the stock exchange building one of the executive committees of the Council of Commissars was assigned rooms. There are guards in the doorway, who allow only people with permits into the stock exchange building. The participants of the market are forced out into the street and into the coffee house in the building. But there is no talk of business."¹⁷

In taking account of the market's activity before and after the armistice, and during the time of the Liberal Democratic Republic, it is evident that trading closely mirrored the political events that shook Hungary. Market activity before the armistice reflected the pessimism and the uncertainty that Hungary faced. The market's only slight decline after the armistice or just before the collapse of the Liberal Democratic Republic reflected partly both the uncertainty of the political situation and a relief that the war was over. There was also some room for optimism, for at this time it was still believed despite evidence to the contrary that Wilson's Tenth Point, which dealt with "Autonomy in Austria-Hungary," would preserve all or most of Hungary's territory. This contributed to the market's relative good performance at a time when there was also increased buying of shares as a hedge against inflation. The coming of a Socialist-Communist fusion government on March 21, which intended to defend the integrity of Hungary, could also have strengthened stock prices. The closing of the stock exchange, however, was symbolic of the Hungarian Soviet Republic's ill-considered intent of destroying capitalism the quickest way possible.

When the market reopened at the end of October, it did so at a much higher price level, although trading activity was slow. The new prices reflected the high rate of inflation, which was estimated between December 1918 and December 1919 to be 904%.¹⁸

An interesting factoid and worth separate analysis is that the Hungarian stocks listed on the Viennese exchange did not completely lose their value with the government

¹⁶ "Magyar Hirlap," February 22, 1919.

¹⁷ "Pesti Napló," March 23, 1919.

¹⁸ My calculations show that the stock market index on October 21, 1919 was 37% higher than in March, though this index is missing 4 stocks which were not traded that week. The inflation data *apud* Mérő Katalin, *Az Értéktőzsde Szerepe*, Budapest, 1989, p. 74.

nationalization of enterprises and continued to be listed. For example “the price of the *Rimamurányi-Salgótarjáni Vasmű* (Rimamurány-Salgótarján Iron Works) fell from 880 Kr. in the beginning of March to 774 Kr. to the end of March or that of *Magyar Általános Kőszénbánya* (Hungarian General Coalmines) fell from 1874 Kr. to 1703 Kr. in the same period.”¹⁹

APPENDIX I

Companies in the sample:

Banks and savings banks

Magyar Hitel Bank
 Osztrák Hitel Bank
 Magyar Bank
 Leszámitoló és Pénzváltó Bank
 Agrár- és Járadékbank
 Fabank
 Magyar Jelzálog Hitelbank
 Hazai Bank
 Magyar Általános Ingatlan Bank
 Forgalmi Bank
 Országos Bank
 Merkur Bank
 Kereskedelmi Hitel Bank
 Bosnyák Agrár Bank
 Lipótvárosi Takarékpénztár

Mills

Konkordia Gözmalom

Coal mines and brickworks

Beocsini Cementgyár
 Esztergom-Szászvari Kőszénbánya Rt.
 Északmagyarországi Kőszén
 Magnezit Ipar Rt.
 Magyar Általános Kőszénbánya Rt.
 Salgótarjáni Kőszénbánya Rt.
 Urikány Zsilvölgyi Magyar Szén Rt.

Steel

Koburg-féle Vasmű
 Ganz-Danubius Rt.
 Lipták Hajógyár Rt.
 Rimamurányi-Salgótarjáni Vasmű Rt.
 Schlick-Nicholson Gép- és Hajógyár Rt.

Transportation

Adria Gőzhajózási Rt.
 Atlantica Tengerhajózási Rt.
 Levante, Magyar Keleti Gőzhajózási Rt.
 Budapesti Közuti Vaspálya Társaság
 Déli vasút
 Magyar Államvasutak Rt.
 Részvénytársaság Villamos és Közlekedési
 Vállalatok Számára, Tröszt

Miscellaneous

Baróti szeszgyár
 Brassói Cellulosegyár Rt.
 Danica
 Egyesült Izzólámpa és Villamossági Rt.
 Első Magyar Papiripari Rt.
 Első Pesti Spodium- és Csoritlisztgyár Rt.
 Nasic Tanningyár
 Klotild Első Magyar Vegyigyár Rt.
 Cordatic Magyar Gumiabroncs Rt.
 Országos Fatermelő Rt.
 Slavonia Magyar Faipar Rt.
 Gu(t)tman
 Magyar Vasúti Forgalom

¹⁹ *Ibidem*, p. 73.



