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Vahur Made, M.A. in History

ESTONIAN BANKING AND CURRENCY  
REFORM LOAN OF 1927: A CASE STUDY OF  
THE ESTONIAN ECONOMIC COOPERATION  
WITH THE LEAGUE OF NATIONS

Tallinn

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**E E S T I K O R G E M K O M M E R T S K O O L**  **ESTONIAN  
BUSINESS  
SCHOOL**

**RAAMATUKOGU**

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**Tallinn  
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## 1. INTRODUCTION

Estonia became a member of the League of Nations in 1921. In 1927, Estonia was able to arrange for a loan from Great Britain with the support of the League of Nations. The loan was used to implement economic and banking reforms. The procurement of the loan was an instrumental episode in the relations between Estonia and the League of Nations, as it was the largest foreign aid package received by Estonia in the period between the two World Wars. The reverberations of the loan were longer lasting than can be noted with other relations between Estonia and the League of Nations. The issue of loan was raised again in November of 1991, when Siim Kallas, the president of the Bank of Estonia, was in London, negotiating the return of gold reserves held in Great Britain prior to 1940. A final solution to the question of the loan has still not been found today.

The League of Nations loan is an intriguing theme in Estonia's recent history. At the time of taking the loan, many arguments for and against were presented. There have been many emotions as well as attempts to find political reasons for the procurement of the loan.

The objective of this article is to give an overview of the procurement of the League of Nations loan for Estonia, the associated problems in the 1920's and 1930's and the later developments of the loan question after Estonia regained its independence in 1991.

The League of Nations as an organiser of loans The first large League of Nations loan project was started in 1919 to assist with the post-war restoration of Austria. In March of 1921, the Secretariat of the League of Nations worked out a specific aid program for Austria. Eight European countries backed a loan of 26 million pounds sterling for Austria. With the help of the loan, Austria was able to change its currency to a gold standard, a Central Bank was formed, the state budget was balanced and a future reconstruction program was worked out.

Austria was forced to make far reaching political promises in order to secure the loan. Austria's finances were put under League of Nations control. The financial reforms, which were approved on October 4, 1922 by Great Britain, France, Italy and Czechoslovakia with the signing of the Geneva convention, required the balancing of the State budget within two years and guaranteeing of the loan by the pledging of its tobacco excise taxes and customs tolls. There was sharp opposition to the League of Nations loan within Austria's politicians, both from the right-wing German nationals and the social democrats. The first did not like the fact, the financial reforms hindered the union of Austria with Germany. The others did not like external interference in Austria's finances.<sup>1</sup>

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<sup>1</sup> Jelavich 1987: 175; MacCartney 1928: 93.

In 1924, the League of Nations also backed a 10 million pounds sterling loan for Hungary. Here, also were many complications. Since the Little-Entente States were against the giving of loans to Hungary, sharp conflicts arose during the negotiations between Great Britain and Hungary on the one side and France and the Little-Entente States on the other side. In the end, however, Great Britain's influence prevailed and Hungary received its loan.<sup>2</sup> Hungary pledged its tobacco and salt excise taxes and sugar taxes to secure the loan. A Central Bank was founded. But, even though foreign investment started to pour into Hungary and the economy stabilised, the parliament strongly criticised the taking of the loan and a government crisis was in the air.

The Austrian and Hungarian loan and reconstruction programmes became an example for the Dawes' plan worked out in 1924 for the stabilisation of Germany's economic situation. In 1922, Greece received a loan for 9.7 million pounds with the help of the League of Nations in order to assist with the resettlement of Greek refugees from Turkey. The loan was used to insure the Greek monetary system and economy in general. In 1927 Greece applied for a new loan, with which it carried out banking reforms. In 1925 and 1927 the Free City of Danzig received a loan to issue its own currency and to found a Central Bank. Bulgaria received a loan to help solve the problems of refugees returning from Turkey.

The League of Nations Secretariat also dealt with financial consulting. Financial consultants were sent to the governments of Albania in 1924, Portugal in 1929 and Saarland in 1931. The experiences of the League of Nations were used in the implementation of monetary reforms in Germany and Poland.<sup>3</sup>

Why did Estonia wish to take a loan from the League of Nations? The main motive was the need to increase credit resources for the development of the economy. In the 1920's the Estonian mark suffered a sharp drop in value which needed to be halted. Estonia did not have enough capital to fulfil this task, a foreign loan was needed. Estonia considered Great Britain as the main loan provider, but opportunities in the United States were also explored. It was hoped that the assistance of the League of Nations would make the securing of a loan easier.

By March of 1923, the Bank of Estonia reserves had reached their maximum, but a strong foreign trade deficit and the poor harvest of 1923 reduced them to a low level by November of 1923. The mark currency reserves were reduced by the Government's attempts to stabilise the foreign exchange rate. The sharp rise of the Dollar in relation to the Estonian Mark, which started in December and continued until August of 1924, added to these difficulties. Strict financial policies (increased interest rates and import tolls) as well as good wheat harvests were able to stabilise the dollar exchange rate.

The Bank of Estonia was more a commercial bank in the 1920's, than a traditional Central Bank. It gave a large amount of loans, of which 87% went to industry, agriculture and to co-operatives by the end of 1924. Most of the enterprises, which received loans from the Bank of Estonia, were not able to repay their loans.<sup>4</sup>

In short, a foreign loan was needed to provide credit resources for Estonian enterprises, the development of infrastructure, as well as reform of the financial system. The lack of capital was threatening to significantly set back the Estonian economy.

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<sup>2</sup> Adam 1993: 254-263.

<sup>3</sup> Hill 1946: 26-31; McClure 1933.

<sup>4</sup> League of Nations. Memorandum on... 1925: 46-50.

## 2. PROLOGUE TO THE RECEIPT OF THE LOAN

First attempts to secure a loan The idea that a large foreign loan should be taken to improve Estonia's economy was shared by the Estonian governmental circles since 1918. In 1919 Estonia received from Great Britain, the USA, France and Finland relief loans which helped to support Estonian war effort against the Soviet Russia.

In April of 1920, Estonia's representative in London, Ants Piip, notified the British Foreign Office (FO), that Estonia required a 1 million-pound loan in order to purchase food supplies and machinery and to modernise industry. As collateral, he offered Estonia's gold reserves, which had been received, from Russia as a result of the 1920 Tartu Peace Treaty. The negotiations so far had shown that several British private banks would have agreed to give the loan. Estonia wanted the British government's approval. At the same time, the British Ministry of Finance was against the loan.

After this, Estonia explored loan opportunities from The National Metal and Chemical Bank. Its owners, R. and J. Tilden-Smith turned to the FO for its support and opinion, since they were in agreement to give the loan against the gold Estonia received from Russia. According to the bankers, the loan would have to be repaid within 1-2 years by the Estonians, and the interest rate would be one percent higher than the Bank of England's.<sup>5</sup>

When the first attempts to secure a loan in London had failed, the Estonians turned to the League of Nations for help. In July of 1921, the First Secretary of the Estonian Embassy in London, Jaan Kopwille, as well as the Estonian Consul in Washington, Nikolai Kõstner met with the League of Nations International Loans manager Drummond Fraser in Geneva. They explored the possibility of securing a loan according to the Ter Meulen program. Fraser was optimistic about Estonia's chances of securing a loan through this programme.<sup>6</sup>

However, a loan according to this programme was not suitable for Estonia in the opinion of Estonia's Minister of Finance, Georg Westel. The Ter Meulen programme was meant for short term commercial credits not for long-term loans for industry agriculture and the development of infrastructure.<sup>7</sup>

In February of 1923, the Estonian Ambassador in London, Oskar Kallas recommended that Estonia should apply for a loan through the Royal Bank of Scotland, but found that other banks could also be considered. He met with the Royal Bank of Scotland management, who was interested in giving the loan, in March.<sup>8</sup>

At this time, however, the loan opportunities provided by the foreign loan act (Trade Facilities Act) of Great Britain was more interesting to the Estonian Government and the Financial Consultant at the Embassy in London, Rudolf Möllerson. Plans were made to apply for a loan to reconstruct the railway under the act. Czechoslovakia and Lithuania, who had already used this opportunity, were an example. Lithuania had received a 1 million-pound loan to build a railway and to purchase goods from Great Britain.

But, like the Ter Meulen programme, so was Westel pessimistic regarding the Trade Facilities Act. He found that taking a loan with similar conditions as Lithuania had done was unacceptable for Estonia. According to him, a pure foreign currency loan

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<sup>5</sup> Piip to Gregory 10.04.1920; Tilden-Smith to Curzon 07.05.1920. PRO. FO371/3633-No.191288,194422,197069.

<sup>6</sup> Kopwille from London 25.10.1921. ERA. 957-11-525. L. 181.

<sup>7</sup> Westel's report to the Government of Estonia 08.11.1921. ERA. 1583-1-568. L.19-19p.

<sup>8</sup> Kallas' diary notes 18.,19.26.03.1923. ERA. 957-12-26b. l. 303-304,313.

with a 10% interest rate would be suitable for Estonia. The loan would have to be long-term, 20-25 years, whereas its early pay back should be possible. A loan with these conditions could be guaranteed with Estonia's tolls and liquor monopoly. The pledging of State forests would have to be avoided. In Westel's opinion, an attempt to secure a loan from London for the City of Tallinn should be made and only then, should an application for a State loan be made.<sup>9</sup> Estonian representatives in future loan applications used these criteria set by Westel as a basis.

Kallas did not let the unsuccessful attempt with the Royal Bank of Scotland despair him. He turned directly to the president of the Bank of England, Henry Strakosch. He, together with the British Ministry of Finance specialist Otto Niemeyer, recommended that the Estonian government turn to the League of Nations Finance Committee (of which Strakosch was one of the Council members) regarding their loan application. Kallas recommended that a League of Nations expert commission visit Estonia to familiarise themselves with the economic and financial conditions of the country.<sup>10</sup>

After the negotiations with Kallas, Westel decided to send his representative, banker Klaus Scheel, to London to investigate loan possibilities. Scheel arrived in London in July 1924. Westel had given Scheel the assignment of investigating the possibilities of securing a long-term 1 million-pound loan. The objective of the loan was to guarantee 60% of Estonia's bank notes.<sup>11</sup> It is possible, that Scheel was the one, who was able to break through the English resistance to giving Estonia a loan. At the same time, it is quite sure that Scheel advised London's finance sector to set the reform of the Bank of Estonia as one condition of the loan. Scheel wanted the Bank of Estonia to halt its loan activities and stop providing the commercial banks with competition on the money market. Strakosch recommended through Scheel that the Estonian government turn once again to the League of Nations Finance Committee to apply for League of Nations support for the loan application.

Application to the League of Nations The assignment of applying to the League of Nations was now given to the Estonian Ambassador in Paris, Karl Robert Pusta. On September 1, 1924, he spoke for the first time with the General Secretary of the League of Nations, Eric Drummond, regarding the loan application. The latter recommended that Pusta talk to the Finance Committee Chairmen, Henry Strakosch and Arthur Salter.

Pusta agreed with Drummond that a Finance Committee delegation would be sent to Estonia on a familiarisation visit. The delegation would make proposals regarding the reformation of Estonia's economic conditions. Pusta told Drummond that Estonia's government's objective was to secure a loan, especially from Great Britain, and to receive a recommendation for this from the League of Nations. Pusta did express the fear that requesting a loan from the League of Nations would compare it in the eyes of the public with the financially troubled Austria, but Drummond thought that there was no point in Estonia worrying and that the loan application should be attempted. Pusta recommended to the government that his negotiations with the League of Nations financial experts not be made public. The impending visit of the League of Nations financial experts and the loan application need not be connected according to Pusta.<sup>12</sup>

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<sup>9</sup> Möllerson from London 14.12.1923; Westel to Akel 22.01.1924. ERA. 957-12-429. L.137-140,154-154p.

<sup>10</sup> Kallas to Akel, September 1926. ERA. 957-12-912. L. 51-53.

<sup>11</sup> Vaughan from Tallinn 26.07.1924. PRO. FO371/10381-N6145/6145/59,N6146/6145/59.

<sup>12</sup> Pusta to Strandmann 01.09.1924. ERA. 957-12-672. L. 2-2p.

Pusta met with the Chairmen of the Finance Committee on September 12, and presented them with Estonia's official application for a foreign loan with the assistance of the League of Nations. The sending of a delegation of financial experts to Estonia was agreed upon. The Finance Committee representatives suggested that Swedish businessman Marcus Wallenberg head up the delegation.

Pusta was against this, since he found that Sweden was too interested in Estonia's manor lands and was therefore not neutral. He spoke to Drummond and recommended that either Strakosch or the Deputy General Secretary of the League of Nations, Frenchman Joseph Avenol head up the delegation. Drummond found that, it might be good to have an American head the delegation, but with Pusta's urging Avenol announced that if the delegation visit could wait until January 1925, then he would come with Salter.<sup>13</sup> Drummond did not argue with this and even though the Finance Committee recommended Wallenberg to head the delegation for some time, Pusta was finally able push his recommendation through the Secretariat. Avenol headed the delegation, and Alexander Loveday, the head of the Economic Intelligence Service, travelled along.

Pusta's application to the Secretariat could not be kept from the public in Estonia, and it created lively discussion in the local media. The first mark of a possible loan application was made public in a speech by Finance Minister Leo Sepp to the Economic-Political Association on September 18, where the Minister mentioned the need for applying for a foreign loan. Sepp appeared in front of the parliament on September 30, where he gave a through economic political overview and also mentioned the need to secure a foreign loan to boost the exchange rate of the Mark. The "Päevaleht" stated that Estonia's wish for a foreign loan was giving it bad propaganda abroad.<sup>14</sup>

The news bomb arrived on October 2, when the "Päevaleht" announced that Estonia had applied to the League of Nations for a foreign loan. The newspaper asked why had the government taken such a step? Estonia's economy was not crumbling like Austria's or Hungary's were at one time. The newspaper expressed the opinion that the Baltic-Germans wanted to take control of Estonia's economy again with the help of the League of Nations. They found that, Estonia should take care of it's own economy and not give it to strangers to control. The government was accused of wishing to gain a stronger base for its economic policy, which had been severely criticised by the opposition and the media, with the assistance from the League of Nations.

The government's semi-official confirmation that a loan had been applied for from the League of Nations was given only on the 5<sup>th</sup> of October. The explanation printed on October 11, by Pusta (now the Minister of Foreign Affairs) stated that only advice had been requested from the League of Nations. The fact was that the League of Nations Finance Committee had the world's best financial experts and that Estonia did not approach the League of Nations with a request for help, but that the League of Nations itself approached Estonia with the offer of a loan. "Päevaleht" was not satisfied with this explanation and noted that such a step, as Estonia had taken, is only taken by states in dire situations. The Minister of Finance in his statement on September 30 had, in the words of the newspaper, confirmed that the situation of Estonia's economy was not all-bad.<sup>15</sup>

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<sup>13</sup> Pusta to Akel 15.09.1924. ERA. 957-12-672. L. 14-14p.

<sup>14</sup> Päevaleht 20.,21.09 and 01.10.1924.

<sup>15</sup> Päevaleht 02.,04.,05.,06.,11.10.1924.

Vaba Maa 05.10.1924.

Appearing in the parliament on October 17, Pusta announced that “if it was needed, then who else for to ask for friendly advice, than a neutral institution such as the League of Nations”. At the request of the government, he had invited Avenol and Loveday to Estonia, and they were to only provide Estonia with advice regarding financial and economic questions.<sup>16</sup>

Pusta was able to quiet the media with these speeches. The loan theme caused excitement again only in January 1925, when the League of Nations financial specialists’ delegation arrived in Estonia.

At the same time as steps were taken in London and Geneva, the government tried to find loan opportunities also in the USA. During 1924 Ants Piip, the Estonian Ambassador, met repeatedly with representatives of the US Ministry of Finance and different banks including the Minister of Finance, Evans Young, who had earlier been the US representative to the Baltics. According to Piip, it was difficult to procure a loan in the US, but the Estonian government was of the opinion, that Piip must continue looking for loan opportunities. The Minister of Finance, Otto Strandman wrote to Piip on September 12, 1924, that the main responsibility of his ambassadorship was to procure a large loan from the U.S. for Estonia. A loan in the amount of 10 million dollars was wanted.<sup>17</sup>

However, the procurement of a loan from the US did not succeed. Americans were sceptical about Estonia’s financial situation and political stability and so the US variant was left on the back burner. The main emphasis was put on the League of Nations.

The League of Nations financial experts’ visit to Estonia The representative of the League of Nations, Deputy General Secretary J. Avenol and the Secretariat’s Finance Committee Chairman, A. Loveday arrived in Tallinn on January 11, 1925. They were hosted by the Minister of Agriculture, August Kerem and the Union of Estonian Manufacturers, Konrad Mauritz. The latter presented Estonia’s manufacturing situation and employee-employer relations. In the meeting with Kerem, the League of Nations representatives showed a special interest in Estonia’s forestry. They inquired whether it would be possible to raise felling rates and if railways had been built to the larger forests in Estonia. They also inquired about agricultural credits, land reform, co-operatives and their central organisations.

In Kerem’s opinion, it was possible to raise felling rates only in the case of a very advantageous foreign market situation. Land reform was purely a financial undertaking in his words, and that no agricultural crisis had arisen, such as the Baltic-German politicians who had left Estonia, were zealously proclaiming in Europe at that time. The standard of living of the settlers had risen and the amount of acreage under crop had not decreased. Apparently Avenol and Lovejoy were satisfied with Kerem’s explanations, because they stated that in their opinion, the agricultural credits had given good results in Estonia. Avenol strongly supported the idea of creating an Estonian-Latvian customs union.

On January 20, Avenol gave an interview to Estonian newspapermen, where he confirmed that Estonia’s future lay in agriculture. The development of agriculture would ensure social stability in Estonia. According to Avenol, Estonia was an agricultural country, where crises related to fluctuations in the harvest were inevitable.

Touching on the subject of loan opportunities, Avenol noted that just prior to the

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<sup>16</sup> Pusta 1964: 102.

<sup>17</sup> Piip from Washington 12.09.1924. ERA. 957-12-379. L.14-15.

World War it was simple to procure foreign loans in Europe. After the War, it became very difficult and loans were received by only those states, which had proven their capabilities. At the same time, Avenol hinted that he did not consider the giving of a loan to develop Estonia's manufacturing sector possible.<sup>18</sup>

Upon their departure from Tallinn, Avenol and Loveday went to Riga to familiarise themselves also with Latvia's financial and economic situation. From there they went on to Danzig.<sup>19</sup> In February of 1925, the General Secretary of the League of Nations, Eric Drummond visited Estonia. Archive materials do not confirm that the loan question was discussed, but it is quite sure that the matter was not ignored.

In his letter of October, 1926 to Belgian Finance Minister, Albert Janssen (who later became the loan trustee for the League of Nations), Loveday notes that when he visited Estonia with Avenol, there was an ongoing competition between the manufacturer and the agricultural parties, whereas the manufacturers had managed to gain more government support. The Bank of Estonia had given out large numbers of inexpensive loans to shaky industrial enterprises. As a result, Estonia's foreign currency reserves had quickly decreased. In Loveday's estimation, the reserves consisted of 6.2 million dollars, by September of 1924 only 2.5 million dollars remained. Both Loveday and Avenol considered this policy as wrong and found that it would be better for the Estonian government to place the main emphasis on agriculture.

According to Loveday, the nucleus of the problem lay in the Bank of Estonia. The Bank of Estonia was competing with commercial banks in giving out loans and by paying interest on savings accounts. This practice needed to be quickly stopped in Loveday's opinion.<sup>20</sup> In commenting on this letter, it can be thought that behind Loveday's opinion was banker Scheel, who had travelled to London, had discussions with Loveday, and with whom Avenol met with in Tallinn as well.

Even though how the League of Nations delegation members formed their opinions is not clear; it is clear that at the beginning of 1925, the Estonian government had taken a clear step towards applying for a loan from Great Britain. The government decided on February 3, to deposit 2.5 million gold roubles received from Russia in the Bank of England. In July Midland Bank and The Royal Bank of Scotland directors visited Estonia on a fact-finding tour. Therefore there was interest towards Estonia on the behalf of potential loan givers.

### 3. RECEIPT OF THE LOAN

The loan question in the years 1925-1926 The League of Nations Secretariat's Finance committee reported on Estonia's financial situation on February 12, 1925. The Bank of Estonia was heavily criticised in the report. It was noted that it was an "anonymous" company under State control. All the shares of the Bank of Estonia belonged to the State.

The Bank was accused of giving unfounded large loans to industry, especially after the significant reduction in transit trade with Russia in 1923. According to the report, loans were given at too low an interest rate, and the loan proceeds had been used to import foreign goods. This reduced Estonia's foreign currency reserves. The State had also given thoughtless loans from tax proceeds, which reduced free gold and foreign currency reserves.

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<sup>18</sup> Päevaleht 11.,13.,18.01.1925; Vaba Maa 13.,16.,18.,20.,22.,24.01.1925.

<sup>19</sup> Report of the Embassy in Riga, January 1925. ERA. 957-12-696. L.13.

<sup>20</sup> Loveday to Janssen 18.10.1926. LNA. Secretariat. S122.

Estonian tax policy was also criticised. It was noted that industrial enterprises carried too large a tax burden and that Estonia had a customs policy that changed too often. Land reform was also criticised, which Avenol stated had caused stress in agricultural relations.

As a result, the Finance committee offered a program to reform the Bank of Estonia, which needed to be implemented as similar central bank reforms were carried out in Austria, Hungary and Free City of Danzig. The Bank of Estonia needed to be freed from government and Ministry of Finance control. The Central Bank needed to have the state precious metal reserves at its disposal and the exclusive rights to issue bank notes. Committee recommended the founding of a Mortgage bank, which would take over all loans with longer than 10-month terms from the Bank of Estonia.<sup>21</sup>

On June 27, Finance Minister, Leo Sepp, submitted a request to the Foreign Ministry to search for a financial expert from the Bank of England under the direction of the League of Nations to establish a long-term loan bank, which would organise long-term loans for industry. Kallas presented this request to the Bank of England on July 22.

The latter proposed two experts: Great Britain's Ministry of Finance specialist P. Nixon, who had helped to implement the League of Nations Austria aid and credit programme: and Walter Williamson, who had organised Siam's (Thailand) finances for 20 years. Kallas liked Williamson more, as he was older than Nixon was. The government also decided in favour of Williamson on January 2, 1926. His salary was set at 2000 pounds per month.<sup>22</sup>

Williamson familiarised himself with the loan procedures used by the League of Nations for Austria and Hungary, as well as materials regarding Finland, Chile, Japan, the Scandinavian countries, Great Britain, Italy and Germany's financial situations and their currency reforms upon beginning work in Estonia.<sup>23</sup>

After the presentation of the Finance Committee report, the Estonians continued to apply for a loan in London even more actively. On July 15, Kallas received a notice from the Finance Ministry of Great Britain, which stated that there were no formal obstacles to receiving a loan, but in practice a loan could not be given without the approval of the Bank of England and the Finance Ministry. A ban on foreign loans existed in Great Britain until December of 1925. The ban had been implemented in 1924 in order to protect the pound against the pressure of the dollar.<sup>24</sup>

On July 21, 1925, General Johan Laidoner went to London to negotiate the payment scheme for Estonian war and relief loans, which were received, from Britain in 1919. During the negotiations, the subject of the League of Nations supported loan was touched on.<sup>25</sup>

Estonia's negotiations in London lasted until the fall of 1926. Financial consultant Williamson spent May to June 1926 in Tallinn and then returned to London. Williamson went to Geneva with Finance Minister Sepp, where on August 9, 1926

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<sup>21</sup> Report of the League of Nations Secretariat to the Finance Committee regarding the Estonian financial situation 12.02.1925. ERA. 31-4-558. L.1-5.

LNOJ. SS. No. 33. 1925: 248.

Rahvasteliit...1925.

<sup>22</sup> Foreign Ministry to Kallas 02.01.1926. ERA. 1583-1-911. L. 3.

<sup>23</sup> Materials regarding W.Williamson's activities at the Estonian Central Bank. ERA. 1790-1-200,201,202,203.

<sup>24</sup> Kallas from London 15.07 and 06.11.1925. ERA. 20-1-396. L.66,71.

<sup>25</sup> Great Britain's Ministry of Finance to the Foreign Office 23.11.1925. PRO. FO371/10976-N6507/27/59.

Sepp handed over Estonia's official note regarding the loan to the League of Nations.<sup>26</sup>

On September 14, Strakosch and Sepp met in London. Strakosch strongly recommended that Estonia apply for a loan guarantee from the League of Nations. The Estonian delegation received an order from the government on September 20 to present an official request for a financial consultant to be sent to Estonia.<sup>27</sup>

Obviously the meeting between Strakosch and Sepp was the turning point in the loan question. The negotiations with the Finance Committee went smoothly regarding the League of Nations guarantee and on December 8, Sepp signed the Finance Committee approved loan protocol in Geneva.

The document allowed Estonia to take a loan of 1 350 000 pounds with the support of the League of Nations. The loan was meant specifically for converting the Estonian currency to a gold standard, to free the Bank of Estonia from its burdensome assets and to found a Mortgage Bank. 1 million pounds was specified for reforming of the Bank of Estonia and as compensation for the long-term assets to be taken over by the government. The rest of the loan went for founding of the Pikalaenupank (Mortgage Bank). The loan interest rate was set at 7%, in addition to this, different issuing and maintenance fees would be charged. The interest was to be paid twice yearly and the loan due date of July 1, 1967.

The loan was issued in two parts: 700 000 pounds and 4 million dollars. The loan conditions and issuing terms needed to be co-ordinated with the League of Nations Council appointed loan officer (Belgian Finance Minister Albert Janssen, who had also dealt with Danzig Free City's banking reform and League of Nations loan in 1923) and the Consultant assigned to the Bank of Estonia for three years (W. Williamson). The loan custodians were The Midland Bank on the London and Amsterdam stock exchanges (Amsterdamsche Bank 200 000 pounds) and Hallgarten & Co on the New York exchange. All obligations related to the loan were free of Estonian taxes.

The loan proceeds had to be transferred to special accounts under control of the loan custodians. Estonia guaranteed the loan with its excise tax proceeds on tobacco, beer, matches, and other goods. Estonia was not allowed to use these proceeds to pay off any other loans or to reduce their overall amount significantly without the consent of the loan custodians. The only exceptions were expenses related to the 700 000 pound railway loan taken on May 13, 1926 from Great Britain under the Trade Facilities Act. If the pledged excise tax proceeds would have been less than 150% of one quarter of the sum to be paid off on the loan per year, then extra costs would have to be incurred. The Estonian parliament had to pass laws to reform the Bank of Estonia as well as its new statutes regarding becoming the bank note issuing bank as well as the Currency law. All these laws had to be co-ordinated with the League of Nations Finance Committee. If Estonia would not have been able to fulfil its obligations the loan custodians had the right to withhold, gather or procure funds in other ways, so that the special accounts would always have enough money.<sup>28</sup>

On December 10, the League of Nations Council approved the loan protocol. Negotiations began in London and Geneva regarding the practical steps of issuing the loan.

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<sup>26</sup> Overview of loan application to the League of Nations by the Foreign Ministry 10.09, 10.12.1926 and 11.03.1927. ERA. 957-12-930. L. 1,13,31.

<sup>27</sup> Decision of the Government of Estonia 20.09.1926. ERA. 31-2-55. L. 1.

<sup>28</sup> League of Nations. Monetary and banking reform in Estonia. Report. 08.12.1926. ERA. 31-3-5187. L. 2-6; ERA. 74-1-2309. L. 1-10.

Issuing of the Loan In December, 1926, the Finance Committee formed a subcommittee with Jannsen, Niemeyer and Strakosch as its members. They were given the assignment of working out the laws for banking and finance reform in Estonia in co-operation with the Estonian government. The Bank of Estonia law, Currency law, as well as the law regarding transfer of bank note issuing to the Bank of Estonia were finished on February 22, 1927.<sup>29</sup>

In March, 1927 Laidoner and Finance Minister Nikolai Köstner were in Geneva, where the Estonian loan issue terms were hammered out in detail. On March 12, the loan issue was agreed upon with the Finance Committee. The Finance Committee appointed Willem Pospisil from the Netherlands as the general loan co-ordinator.<sup>30</sup>

On March 11, Estonian government decided to ratify the documents regarding the loan conditions signed on December 8, 1926 in Geneva by the Finance Minister. The ratifying act, as well as Estonia's new draft financial laws was sent to the League of Nations Secretariat. The League of Nations official minutes and Finance Committee's December 8<sup>th</sup> report on Estonia's financial and banking reforms were sent to Estonian Parliament (Riigikogu) on December 10<sup>th</sup>, 1926.<sup>31</sup> On April 5<sup>th</sup>, 1927, the foreign loan law was presented to the Parliament.<sup>32</sup> The Parliament passed the law on May 3<sup>rd</sup>.

The Council of the League of Nations appointed Walter Williamson officially as the Consultant to the Bank of Estonia on March 11<sup>th</sup>, 1927. The government decided on May 4<sup>th</sup> to send Finance Minister Leo Sepp and the parliament finance committee chairman J. Laidoner to London to negotiate with the Bank of England the issuing of the foreign loan according to the foreign-loan law as approved by the parliament. The government decided that the Finance Minister could not sign the contract until the government had approved it.<sup>33</sup>

During the negotiations, it was decided to accept the Midland Bank & Co.'s bid. The final results were as follows: in Great Britain, a loan in the amount of 700 000 pounds would be issued with an interest rate of 7 % issuing rate of 94.5, and a net rate of 89.5. In the US, 4 million dollars would be issued through Hallgarten & Co. with an interest rate of 6.5%, issuing rate of 88.5 and net rate of 83.25.<sup>34</sup>

On June 21, Hallgarten & Co. in New York opened two Estonian government accounts: Estonian Government loan regarding 1927 banking and financial reform (*loan proceeds account*) and Estonian 1927 year loan (*service account*). 3 570 000 dollars was deposited in the first account on the same day.<sup>35</sup>

On January 1, 1928 monetary reform took place in Estonia and the new currency came to into circulation. The Marks and pennies in use were replaced by Crowns and cents (1 Crown = 100 cents or 100 former Marks). The Estonian Crown went to a gold standard and was tied to the pound. This remained in effect until 1931, when Great Britain abandoned the gold standard.

In October, 5500 bonds with a nominal value of 100 pounds, 100 bonds with a nominal value of 500 pounds and 100 bonds with a nominal value of 1000 pounds were issued for the London stock exchange. A total of 5700 bonds with a nominal

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<sup>29</sup> Drummond to Sepp 07.03.1927. LNA. Secretariat. S64.

<sup>30</sup> Laidoner from Geneva, March 1927. ERA. 20-1-450. L.26.

<sup>31</sup> Minutes of the sessions of the Estonian Government 1927. Minutes. 28-III.

<sup>32</sup> Ibid., Minutes. 38-I.

<sup>33</sup> Salter to Akel 18.03.1927; Government of Estonia decision 04.05.1927. ERA. 957-12-672. L.166,170.

<sup>34</sup> Laidoner from London 25.05.1927; Sepp from London 04.06.1927. ERA. 957-12-806. L. 13,15,19.

<sup>35</sup> Williamson's instructions to The Midland Bank 21.06.1927. ERA. 1790-1-213. L.1-2.

value of 700 000 pounds. Ambassador Oskar Kallas in London signed the obligations.<sup>36</sup> The issue of the bonds tradable on the New York stock exchange occurred in December. 400 bonds with a value of 500 dollars and 3800 bonds with a value of 1000 dollars were printed. There were a total of 4200-dollar bonds with a value of 4 million dollars. The Head Consul in New York, Viktor Mutt signed the obligations on behalf of Estonia.<sup>37</sup>

After the Estonian government had approved the loan documents signed on October 10, 1926 and March 12, 1927 the Finance Minister Sepp appeared in front of the parliament and explained once again the need for taking the loan. The first reason, in his words, was financial difficulties, which occurred with the re-organisation of industry and agriculture after the war. An important element was the founding of settlers' farms instead of manors. Money was also needed to help agriculture re-orient itself towards the Western-European market, where high quality standards were in effect. New production buildings and equipment was needed, land correction needed to be done. Foreign trade structure changed. Trade to the western countries created transportation problems related to the great distances. Shipping needed to be developed. Money was needed to build new dwellings. The Bank of Estonia did not have enough money to finance all this, therefore a loan was needed.<sup>38</sup>

Sepp had moved significantly towards a more agricultural direction in comparison with Westel's financial reform plans. Sepp's reasons for the need for a loan were quite similar to those brought out in the 1925 League of Nations financial experts' commission report. The development of industry and significant infrastructure development had been replaced by emphasis on agricultural development by Sepp. At the same time, it is noteworthy, that Sepp did not emphasize the need for reform of the Central Bank, which the League of Nations had repeatedly emphasised.

At this point it would be prudent to make a digest of some thoughts from the magazine "Eesti Majandus" (Estonian Economy), which in its article on Banking reform and the League of Nations in December 1926 explained the need for taking a loan from Geneva. The then leading financial magazine in Estonia noted, that it was naturally bad to burden the economy for many years with foreign debt obligations. But at the same time, it needed to be understood that Estonia's private economy success was mainly due to the inflow of foreign capital. Estonia lacked the resources for further implementation of financial reforms and industry reform had occurred through overburdening the public economy's potential.

Why did Estonia turn to the League of Nations in particular regarding the loan? In the opinion of the magazine, the question was firstly that the world credit markets were still largely closed to Estonia and it was easier to approach via the League of Nations. The League of Nations did not deal with brokering of loans, but with founding of conditions in the country needing the loan, in which case foreign investors would be willing to give the country a loan. At the same time, it was easier and less humiliating for a country to submit to League of Nations control re fulfilment of loan conditions, then that of another state. The article concluded with the confirmation, that Estonia had not turned to the League of Nations in the same situation as Austria, where the country was in a state of collapse, but with the wish to receive help to insure its present financial success.<sup>39</sup>

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<sup>36</sup> State Elder and Finance Minister to Kallas 20.10.1927. ERA. 957-12-827. L. 106-107.

<sup>37</sup> Teetsov to the government 30.12.1927. ERA. 31-3-5940. L.1-1p.

<sup>38</sup> Finance Minister's explanations to the Parliament regarding the taking of the foreign loan. Not dated. ERA. 31-3-5187. L.24-28.

<sup>39</sup> Estonian Economy 12, 1926: 425-430.

#### 4. FURTHER STATUS OF THE LOAN

W. Williamson in Estonia 1927-1930 After the issue of the loan, W. Williamson moved to Estonia to fulfil his responsibilities as the Consultant to the Bank of Estonia as appointed by the League of Nations Council. He had great powers to interfere in Estonian Economy. There was frequent correspondence between the Finance Ministers and the presidents of the Bank of Estonia. The correspondence was related to the Bank of Estonia statutes, and bank re-organisation, foreign trade financing, loans to industry, appointment of Bank of Estonia Council members, Crown currency backing reserves, Estonian gold reserves, founding of the Maapank (Land Bank) and financing questions.<sup>40</sup>

Williamson recommended that the Bank of Estonia form special relations with the Bank of England, confirming that it would be the best way for Estonia to get the best loan interest rate, which would be possible to get in Great Britain. The Bank of Estonia Council agreed with this recommendation in November 1928.<sup>41</sup>

In Estonia, the Consultant also dealt with the Russian –Baltic Ship factory shares, the taxing of a Tallinn branch of German share company dealing with trading, taxing of entertainment establishments, Russian-Estonian transit and other purely business questions.<sup>42</sup> The government decided to pay Williamson an honorarium of 105 pounds per year in addition to his salary in April of 1928.<sup>43</sup> A. Janssen and W. Williamson presented the League of Nation's annual overviews of the loan payment and Estonia's financial situation.<sup>44</sup>

Williamson left Estonia with his wife on August 23, 1930. The Bank of Estonia organised a reception in his honour at the Centum Club, to which important state, banking and financial persons were invited. Before his departure, Williamson visited State Elder O. Strandman and Finance Minister Johannes Zimmerman. The financial people gave Williamson as a gift, a photo-album with 100 photographs of Estonia's State Elders and Finance Ministers who had been in office during the time he was working in Estonia.<sup>45</sup>

The Loan issue in 1929-1939 In 1929, an international financial crisis started, which quickly lowered the loan bond prices on the London, Amsterdam and New York stock exchanges.<sup>46</sup> The loan bond prices actually started falling in January of 1929, before the October stock crash in New York. The bonds fell in all three quoting places at the same time. The bonds fell the most in New York. According to Päevaleht financial reporter, Viktor Poom, the bonds started falling already in the second half of 1928,

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<sup>40</sup> Materials regarding Williamson's activities at the Estonian Central Bank. ERA. 1790-1-211, 212, 218, 222, 224, 227, 230, 233, 234, 235, 240, 241, 245.

Ibid., ERA. 1790-2-12; ERA. 1790-3-9,10,11.

<sup>41</sup> Williamson's recommendations to the Estonian Central Bank regarding development of private relations with the Bank of England. 20.08 and 09.11.1928. ERA. 1790-1-229. L.1-5,10.

<sup>42</sup> Materials re. Williamson's activities at the Estonian Central Bank. ERA. 1790-1-221,231,236.

<sup>43</sup> Minutes of the sessions of the Government of Estonia 1928. Minutes. 34-V.

<sup>44</sup> LNOJ. 9<sup>th</sup> Year. No. 9. 1928: 1385-1388; LNOJ. 10<sup>th</sup> Year. No. 12. 1929: 1864-1867; LNOJ. 11<sup>th</sup> Year. No. 12. 1930: 1867-1869; LNOJ. 13<sup>th</sup> Year. No. 13. 1932: 214-216.

LNOJ.SS. No. 64. 1928: 285,431,453; LNOJ.SS. No. 66. 1928: 39,72; LNOJ.SS. No. 75. 1929: 271,316,348,417,474,475; LNOJ.SS. No. 77. 1929: 116-117; LNOJ.SS. No. 84. 1930: 146,522,523; LNOJ.SS. No. 86. 1930: 75, 113; LNOJ.SS. No. 93. 1931: 144,233; LNOJ.SS. No. 95. 1931: 44,98.

<sup>45</sup> See Vaba Maa 23.08.1930.

<sup>46</sup> League of Nations' loan obligation rates January 1928-October 1929. ERA. 74-1-2277. L.18.

though the significant change occurred in February-March of 1929. At the same time, the Estonian bonds fell more quickly than other foreign loan bonds.

One reason for the quick falling rates was believed to be the strengthening dollar, which pushed prices down. An article in Vaba Maa newspaper on March 20, 1929 was also apparently to blame, which disseminated stories of a planned moratorium on state loans, which lowered Estonia's economical prestige and pushed the Estonian loan bond prices below that of Bulgaria's. This situation was considered inevitable in the event of long-term loans, and it was not evident of Estonia's real financial situation. In financial overviews it was noted that Estonia had been able to fulfil its loan obligations correctly and that the excise taxes which Estonia had backed the loan with, were being paid in higher than budgeted amounts.<sup>47</sup>

In spite of the mostly optimistic statements in Estonian media, the League of Nations secretariat Finance Committee was becoming worried about the Estonian situation already by the end of 1928. The first to react was the financial newspaper Financial Times, which stated that Estonia was not fulfilling the terms for foreign loans which the League of Nations had set out. Williamson also presented complaints to the Estonian government. The Bank of Estonia president, Jüri Jaakson had to travel to Geneva to give explanations.<sup>48</sup>

Quite unexpectedly, the Estonian press was printing optimistic statements even after the October New York stock exchange crash, which significantly affected the Estonian bonds noted there. In newspapers it was noted, that the developments of November-December 1929 were hopeful, since in the US investors were showing more interest towards gold based bonds, where returns were greater. The hope was without reason. The interventions by the Estonian State and the loan custodians managed to cause the prices in Amsterdam and London to rise for some time, but the prices in New York continued to fluctuate.<sup>49</sup>

In October of 1930, the Estonian bonds suffered a steep drop on the London exchange. R. Möllerson stated in his report, that the reasons for the drop were the German election results as well as the financial problems in Great Britain, notices of revolutions in South America, as well as the activities on the New York exchange. There was a lack of buyers for the Estonian bonds at the former price, and Möllerson thought that a purchase of a few thousand pounds would raise the price immediately. In February of 1931, he had to admit that the Estonian bond drop had been lower and more serious than for other countries holding such bonds. During the first year of the loan, the bonds had sold for much more than similar Bulgarian and Polish bonds, but by the beginning of 1931, the Estonian bonds had fallen far below them. Möllerson was afraid, that investors would conclude that Estonia's economy was worse off than Poland's, and recommended active propaganda in London.<sup>50</sup> In April of 1930, Janssen visited Estonia to familiarise himself with the financial situation in Estonia. The League of Nations Council decided to end their financial supervision of Estonia on September 24, 1930.

The Estonian bonds fell seriously again on the New York stock exchange in 1931. Small banks, which in 1926-1928 purchased large amounts of foreign bonds, were now selling massively. However, there were no buyers. Thanks to the support purchases made by the Estonian government, the price was maintained at a higher

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<sup>47</sup> Vaba Maa 05.04.1928; Päevaleht 13.04.1928.

<sup>48</sup> Vaba Maa 30.08.1928.

<sup>49</sup> Päevaleht 18.09,20.11.1929, 25.01.1930.

<sup>50</sup> Möllersson from London 16.10.1930 and 05.02.1931. ERA. 957-13-155. L.155,157-158.

level than other Eastern-European and Latin-American loan bonds.<sup>51</sup>

The financial troubles building up in Great Britain started to affect Estonian finances in the fall of 1931. The Bank of Estonia notified its representative to the League of Nations in Geneva, August Schmidt, that changes needed to be made in the loan organisation. The pound had lost so much of its value that the Bank of Estonia was not able to buy it and sell at the former rates, as the bank statutes required. It seemed impossible to fulfil the statutes. Pounds backed 80% of the Estonian Crown.<sup>52</sup>

Schmidt visited the League Secretariat, where it was recommended that Estonia declare the dollar, instead of the pound, as the currency, which the Bank of Estonia would buy and sell at a fixed rate. Loveday had noted that Estonia would have difficulties if its neighbouring countries would abandon the gold standard. At the same time, in his words, the League of Nations could not let the Estonian Crown drop with the pound, as Estonia had obligations with the loan custodians.<sup>53</sup>

Kallas talked to the president of the Bank of England, Niemeyer, in London. The latter recommended that the Estonian Crown be left on a gold standard, with the reduced backing. The Crown could be backed with another country's currency. The other choice was for Estonia to tie its Crown to the Pound.<sup>54</sup>

Jannsen visited Estonia for the third time from 18-28 of August 1932. He met with the president of the Bank of Estonia, Jaakson, and the Finance Minister, Kõstner; familiarised himself with the state of the State treasury; the budget policy; and foreign loan situation.<sup>55</sup> Kõstner's being sent to Bulgaria from October of 1932, as the League of Nations financial consultant, was obviously agreed upon at this meeting. This can be treated as the removal of Kõstner from the position of Finance Minister in a complicated situation.<sup>56</sup>

After Jannsen's departure, the word that Estonia's economy was on the edge of collapse was spread throughout the Secretariat's Finance Committee. Jaakson travelled again to Geneva to give explanations. In his report at the end of September, Jannsen recommended sending a new financial consultant to Estonia.<sup>57</sup>

In January 1933 Jaakson (now Finance Minister) travelled again to Geneva. He reported to the Finance Committee on Estonia's economical problems, but noted that Estonia had severely suffered due to the decision by Great Britain to abandon the gold standard. The Bank of Estonia had sold its gold for pounds, due to which the gold backing the Estonian Crown had dropped to 10 % of its original value. The Crown dropped savings in commercial banks suffered. The amount of income from taxes and customs dropped, there were large problems with foreign trade.<sup>58</sup> In May of 1933, the US also abandoned the gold standard, due to which the return on the Estonian bonds in New York dropped immediately.<sup>59</sup>

Finally, on June 28<sup>th</sup>, 1933, the Estonian government decided to devalue the Crown and to abandon the gold standard. The Estonian Crown became equal to the Swedish Crown. A 15% foreign currency tax was implemented. The next day, the Foreign Ministry sent telegrams to the FO and to the League of Nations Finance Committee.

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<sup>51</sup> Mutt from New York 24.09.1931. ERA. 1790-2-14. L.73.

<sup>52</sup> To the representative of the Estonian Bank in Geneva 22.09.1931. ERA. 957-13-535. L. 4.

<sup>53</sup> Schmidt from Geneva 24.09.1931. ERA. 957-13-535. L.7-9.

<sup>54</sup> Kallas from London 25.09.1931. ERA. 957-13-535. L. 10-12.

<sup>55</sup> Päevaleht 10.,14.,16.,18.,20.,28.08.1932; Vaba Maa 19.,20.08.1932.

<sup>56</sup> Päevaleht 21.10.1932; Vaba Maa 21.10.1932.

<sup>57</sup> Päevaleht 31.08, 01.,21.,22.09, 16.10.1932; Vaba Maa 22.10.1932.

<sup>58</sup> Jaakson's report to the League of Nations Secretariat's financial committee. 16.01.1933. ERA. 1790-1-252. L.1-4.

<sup>59</sup> Mutt from New York 17.05.1933. ERA. 1790-2-14. L.14.

Niemeyer was very satisfied with steps taken by Estonia. He thought that they should have been taken even earlier. Jannsen stated, that even though he could not make an official statement, he personally thought the steps taken were the right ones.<sup>60</sup>

Estonia's financial situation started to improve from the summer of 1933 onwards. Jannsen visited Estonia for the fourth time in June of 1934, and was now satisfied with Estonia's financial indicators.<sup>61</sup> In its report of 1936, the Finance Committee stated that the Estonian economy had significantly improved since the crisis years, and the fulfilment of the loan obligations was progressing successfully.<sup>62</sup> Positive appraisals of Estonia's economy continued until 1939.

In October of 1933, Councillor Hans Markus, at the Estonian Embassy in London, notified the Foreign Minister that the Bank of Estonia was doing well and he was buying up Estonian League of Nations bonds. Their price had risen. Small individual investors held most of the bonds. Markus recommended that the loan position not be strengthened by any more Bank of Estonia purchases, but that the loan should be changed to a lower interest loan (5% over 5-10 years, with less guarantees than currently). In Markus' opinion, broker companies would have bought the bonds, lending Estonia the money backed by the gold reserves. According to Markus, the Bank of England was aware of this idea, and recommended that the State Elder Jaan Tõnisson be informed.<sup>63</sup>

Estonia thought the interest rates set in 1927 were too high starting from 1933-1934, and wanted to reduce it through conversion. Finance Minister Karl Selter discussed this in London and in Paris as well as with Loveday. The latter was of the opinion that the interest rate should have been lowered earlier. In his opinion, it was possible from 1937, when 10 years had passed since the issue. Loveday offered that the Finance Committee could make a positive report about Estonia just prior to the end of the 10-year period, which would be the basis for the Council decision. For the US part of the loan, Loveday thought that converting the loan would be almost impossible according to US laws making it a very expensive process. In Loveday's opinion it was more useful to issue the whole sum to be paid in London, even if it would be in contradiction with League of Nations practice to not realise a loan in only one country. Selter thought that the loan could be converted earlier than 1937. He feared that the elections in Great Britain in the fall of 1935 could change the status of the financial markets. The developments of which could make converting the loan in 1937 impossible.

Niemeyer felt in June of 1935, that since the Estonian bond had a good reputation in London, then the bondholders might not want to sell them before the maturity date without a large premium. This however, would make the purchasing of the bonds expensive. During the negotiations with Schmidt in May, Niemeyer suggested the idea of converting the loan in Estonia. Schmidt was worried that Estonia would lose a lot of foreign currency with this solution. In Schmidt's opinion, the solution would be if it would be possible for Estonia to take a new loan with a lower interest rate of which 70% would be used to convert the existing bonds and the rest would be used to replenish Estonia's foreign currency reserves.<sup>64</sup>

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<sup>60</sup> Laretei to all ambassadors 28.06.1933; Foreign Ministry to Foreign Office and League of Nations financial committee. 29.06.1933. ERA. 957-13-662. L. 18,19,21.

<sup>61</sup> Päevaleht 15.06.1934; Vaba Maa 16.06.1934.

<sup>62</sup> LNOJ. 17<sup>th</sup> Year. 1936: 671.

<sup>63</sup> Markus to Seljamaa 15.10.1934. ERA. 3828-1-21. L.159-162.

<sup>64</sup> Schmidt from London 06.06.1935 and 15.05.1936. ERA. 957-14-177. L. 6-8.

The Finance Ministry also tried to achieve a loan conversion through the League of Nations, but Schmidt found that there was no use in taking a new loan through the League of Nations as better terms, including lower interest rates, would not be possible.<sup>65</sup> His plan was to repay the entire dollar of the loan and then to take a new loan in London at 5% interest rate. The new loan would not have the backing of the League of Nations. The size of the loan would be 1.3 million pounds.<sup>66</sup>

A discussion, which occurred on December 3, 1936 between Selter and Great Britain's Consul in Tallinn, Wilfred Gallienne, warrants interest. Selter confirmed that Estonia planned to convert the League of Nations loan's British part. This would be added to the loan's US part, the size of which the Minister estimated to be about 3-4 million Crowns to the surprise of the Consul. When the Consul tried to correct him, stating that wasn't it 3-4 million dollars, Selter argued no. In his words, the majority of the bonds were held by the Bank of Estonia and Scheel's bank, and that there was only about 3-4 million Crown's worth of dollar bonds in circulation abroad.

The next day Gallienne also met with Scheel, who thought that Selter was mistaken in his estimate of the size of the dollar bond and thought that it was 6-7 million Crowns. He said that he was helping Selter with conversion of the British part of the loan and was trying to come to an agreement with Swedish banks.<sup>67</sup>

Though there are no archive materials to support it, it is quite sure that the loan conversion and the new larger loan to finance it were also discussed with the General Secretary of the League of Nations, Joseph Avenol during his visit to Estonia in August of 1937. However, the international situation was so complicated that neither the conversion of the loan or the taking of the new loan occurred. Finance Minister Leo Sepp noted still in September to Gallienne, that Estonia wanted to start negotiations to convert the loan in October 1938, and hoped that the loan could be converted in June of 1939.<sup>68</sup> It was clear in January of 1939 that the loan conversion would not occur. The general political situation was not suitable.

The Loan issue after 1940 After the occupation of Estonia by the Soviet Union, the repayments of the 1927 League of Nations loan discontinued. Estonia lacked the resources and the Soviet Union did not want to be considered the legal successor of Estonia in the matter of the loan. The loan repayments stopped. According to the Bank of Estonia, the unpaid balance of the loan was 24 594 000 Crowns as of January 1, 1939 (13 483 000 US bonds and 11 111 000 Great Britain and Holland bonds).<sup>69</sup> Taking into account the exchange rate of the US dollar and the Great Britain Pound to the Estonian Crown, the unpaid balance of the loan to be 3 600 000 dollars (the US loan was 4 million dollars) and 605 500 pounds (the British and Dutch part of the loan was 700 000 pounds).<sup>70</sup> The estimates are general and reflect the status of the loan as of January 1, 1939. But disregarding the fact that there are no facts regarding payments in 1939 and 1940, it is clear that Estonia did not repay the majority of the loan received with the help of the League of Nations in 1927.

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<sup>65</sup> Selter to Schmidt 25.06.1936; Schmidt to Selter 20.10.1936. ERA. 957-14-177. L.13-13p.,14-16.

<sup>66</sup> Collier to Waley 15.06.1937. PRO. FO371/20311-N2902/1339/59.

<sup>67</sup> Gallienne from Tallinn 03.ja 04.12.1936. PRO. FO371/20311-N6272/1339/59.

<sup>68</sup> Gallienne from Tallinn 05.09.1938. PRO. FO371/22224-N4437/93/59.

<sup>69</sup> Eesti Pank 1919-1939. Tallinn 1939. L. 95.

<sup>70</sup> Interview with Bank of Estonia Council member Raimund Hagelberg 01.07.1998 (text in possession of author).

A notice from the League of Nations loan committee from January 3, 1941 states that as of July 1, 1940 the loan agents in London and New York had not done any transactions to repay the bonds and no more money had been received for pay-outs. Since the main interested parties were in Great Britain, then the FO's response to the League of Nations notice was vital. The British Foreign Service found, that since the Soviet Union did not recognise the repayment of the Estonian loan as its responsibility and also referred to its expulsion from the League of Nations, that this would increase again the amount of assets lost by the British in the Baltics due to the Soviet occupation. The Foreign Office found that the losses incurred with the ending of the repayments of the loan were greater than the value of the Estonian gold held in Great Britain.<sup>71</sup> It can be read from the FO's comments, that London had already approached Moscow regarding the loan and received a negative answer. It is noteworthy that the Soviet Union did not justify the stopping of the repayments with the face that Estonia's obligations did not belong to them, but referred instead to its expulsion from the League of Nations.

The functions related to the loans given by the League of Nations were passed to the United Nations in 1945, with the added note "as much as is possible and recommended". The Soviet Union did not protest this position.<sup>72</sup>

We can find some additional information about the further status of the loan from August Ots' memoirs. Ots' memoirs specifically describe the status of the bonds, which were bought up by the Bank of Estonia from abroad prior to the occupation. According to Ots, in 1944, during the German occupation, the director of the Bank of Estonia, Hugo Pärtelpoeg had asked that he take the bonds to Sweden. Pärtelpoeg estimated that the value of the bonds held by the Bank of Estonia was 4.5 million Crowns.

Ots was not successful in taking the bonds to Sweden (the boat he was to use turned out to be too small for the task), but in September of 1944 the bonds were successfully transported to Stockholm. In Stockholm the bonds were left for some time in the rooms of the Estonian Committee in Sweden, packed in potato sacks and without guard. Then, the Committee member Johannes Sikkar took the bonds to his home. In 1960, Sikkar apparently took the bonds to his son in New York. Ots did not have any more information as to what happened to the bonds next or as to actual value of the bonds. He knew though, that there was interest by buyers in the bonds for some time.<sup>73</sup>

The bonds or rather their buy-back came up on the agenda in November of 1991. A Bank of Estonia delegation headed by Bank president Siim Kallas, visited London from 6-8 November (delegation members included Jüri Luik and Eerik-Niiles Kross from the Estonia's London Legation, as well as the Legation's local legal representative Allan Hughes). Meetings were held with the Government of Great Britain and representatives of the Bank of England. The Estonian delegations presented Great Britain an application for them to return the Estonian gold, which had been left in the Bank of England and which the government of Great Britain sold to the Soviet Union in 1967.

The Bank of England representatives brought up the subject of the buy-back of the pre-war bonds including the League of Nations loan bonds by Estonia. Kallas stated that Estonia recognised its obligations. At the same time, it was agreed that each side would solve private or corporate claims according to their own laws. This meant, that

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<sup>71</sup> Report of League of Nations Loan committee 03.01.1941. PRO. FO371/29260-N28/28/59.

<sup>72</sup> FO information 13.10.1945. PRO. FO371/47817-N12634/12634/55.

<sup>73</sup> Ots 1976: 172-177.

Great Britain gave Estonia free rein regarding the organisation of the buy-back of the bonds. The English did not tie the return of the Gold with the bonds anymore. On January 27, 1992 the government of Great Britain decided to return the gold to Estonia, which was done in the spring of the same year.<sup>74</sup>

After the gold negotiations, the question of the bonds has not been solved. The Estonian foreign ministry has confirmed Estonia's willingness to buy-back the bonds from their owners. A few bondholders have approached the Bank of Estonia. At the same time, the Bank of Estonia has not bought back any bonds, nor has an overview about the value of bonds still in circulation. Some bonds may have been destroyed. In the opinion of Raimund Hagelberg, a Bank of Estonia Council member, the central bank does not have any obligation to buy back the bonds, since in the loan contract of 1927, the Estonian government, and not the Bank of Estonia, took the responsibility for the loan. The New York stock exchange stopped dealing with the 1927 loan US bonds on December 7, 1995. The reason given for the decision was that no transactions had been undertaken with the bonds in a very long period of time.<sup>75</sup> The London and Amsterdam stock exchanges have not issued similar notices.

It seems that the Estonian League of Nations loan question will remain without a clear solution and will disappear from the agenda with time.

## 5. CONCLUSION

In 1927, Estonia received a loan from the Bank of England of 1 350 000 pounds with the recommendation of the League of Nations. With this the Estonian currency system was reorganised. Financial and banking reforms were carried out. The Government gave the Central Bank the exclusive right to issue bank notes. The long-term industrial loans, which were bringing the Bank of Estonia losses, were transferred to the new Mortgage Bank, which was founded specifically for the financing of industry. The loan bonds were listed on the London, Amsterdam and New York stock exchanges.

In 1922, the Finance Minister, Georg Westel, started working out currency reform plans. The Estonian economic and government circles started wanting a loan to reorganise the financial system practically right after the securing of independence in 1920. Even earlier the research for a loan was begun in London and Washington Financial circles.

The Estonian representatives firstly approached the Bank of England, who advised them to apply for a loan guarantee from the League of Nations. Estonia agreed with the recommendation and so the Estonian government's request for a loan guarantee was presented to the General Secretary of the League of Nations, Eric Drummond, and to the League of Nations Secretariat's Finance Committee by Ambassador Karl Robert Pusta in September of 1924. Estonia was visited by a delegation of League of Nations financial experts, headed by Deputy General Secretary Joseph Avenol in January of 1925. On December 8, 1926, the loan protocol was signed in Geneva and on March 12, 1927, the Bank of England began issuing the loan bonds.

The loan was received on reasonable terms. The loan interest rate was 7 percent. Estonia had to pledge its excise tax proceeds to secure the loan. The League of Nations appointed former Belgian Finance Minister, Albert Janssen as the Loan

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<sup>74</sup> Eesti rahareform 1992... 1997: 68-70.

<sup>75</sup> New York Stock Exchange to the Estonian Embassy in Washington 07.12.1995. Copy in possession of author.

custodian. They also sent English financial specialist Walter Williamson to the Bank of Estonia as a financial consultant. Williamson had the right to intercede in the Bank of Estonia's activities and to influence Estonia's financial life and laws.

During the Great Depression in 1929-1933, the 1927 loan bonds fluctuated wildly. With the support of the State, the worst was avoided. The bonds began to rise in the years 1932-1934. At the same time, Estonia began work towards a loan conversion, that is to reorganise the loan with a lower interest rate and with less collateral. The plan was to take a new loan in order to undertake the loan conversion, but international tensions in the second half of the 1930's as well as the start of the Second World War did not allow the plan to realise.

The repayment of the loan ended in 1940, whereas the main part of the loan capital was still unpaid at that point in time (the loan repayment deadline was July 1, 1967). The buy-back of the loan bonds was brought up during negotiations regarding the return of Estonia's gold held in London in 1991. Even though, the Estonian government has given promises to buy-back the bonds from bondholders, no transactions have taken place to this date in time. A final solution to the question of the loan has still not been found today.

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