Vienna, December 3, 1935.

No. 625.

Subject: DEVELOPMENTS IN THE AUSTRIAN INTERNAL AND EXTERNAL SITUATION.

The Honorable

The Secretary of State,

Washington.

Sir:

I have the honor to refer to my confidential despatch No. 613, of November 22, 1935, and to my telegram of December 2, 10 a.m., and to supplement these with the following further information on developments in the Austrian internal and external situation.

The principal developments in the Austrian situation...
situation since I forwarded my despatch No. 613 have been the visit of the Hungarian Minister President and Minister for Foreign Affairs to Vienna and the speech of the Austrian Foreign Minister in the Bundestag on Austrian foreign policy.

In my confidential despatch No. 623 of December 2, 1935, as well as in my telegram of December 2, 10 a.m., above referred to, I have reported in full on the visit of the Hungarian Minister President and Minister for Foreign Affairs to Vienna on November 28 and 29. It is sufficient, therefore, to say here that although these visits between Budapest and Vienna have become quite frequent since the Rome protocols came into effect and since the relations between Austria and Hungary are on a closer and more friendly basis, this present visit was somewhat unexpected and was made without much previous preparation. In view of the increasing difficulties in which Italy finds herself in Europe and in Abyssinia, and particularly because of the fall of the Lira and the slowness in Italian payments for imports, those responsible for Hungarian foreign policy undoubtedly felt real necessity for a frank discussion with the Austrian Government of the common stand which should be assumed. As reported in my telegram and despatch, the general European situation in all its aspects as they may affect Austria and Hungary were discussed during the visit, but I am informed that no definite decision was taken on any political or economic question, except that both Governments...
Governments were definitely in agreement to maintain their position that in spite of Italian pressure they will remain in the League, even though Italy should leave it. The meeting was an evidence of the grave concern which is felt in Vienna and Budapest over the increasing difficulties of Italy. Both Governments realize the unfavorable repercussions which their attitude at Geneva on sanctions has had, particularly in England and in France, and it seems unquestionable that they have decided to base their future policy more definitely on the League and on the support of England and France. Both Governments are in an exceedingly delicate position, and the object of this meeting last week was not so much to reach definite decisions, but rather to discuss frankly how far a common attitude could be maintained by both Governments in the face of increasing Italian difficulties. Perhaps the most definite result of the meeting will be seen in less response to the Italian pressure which has been so continuously exerted in both capitals.

It may be observed also that I am reliably informed that during the conversations between the responsible heads of the Austrian and Hungarian Governments, the Hungarian Minister-President, Gömbös, did not fail to let his pro-German orientation become apparent in exploring the possibility of Austria joining in conversations which might lead to more friendly and close relations with Germany. These approaches by Gömbös met with no response from the Austrian...
Austrian Government and were not supported by Dr. Kanya, the Hungarian Minister for Foreign Affairs, who is of the opinion that no worthwhile agreements can be made with the present Government in Germany. The Austrian Government let it be known that it had earnestly explored the possibility of better relations with Germany through the conversations which the Austrian Foreign Minister had had with the German Minister in Vienna, and that these conversations had so far led to no appreciable result and that it was not likely that under present conditions they could have any appreciable result.

Of even greater significance than this visit was the speech on Austrian foreign policy which the Foreign Minister made in the Bundestag on November 28, on the morning of the arrival of the Hungarian guests. As in my despatch No. 654, of December 2, I have fully covered this speech, I shall not repeat on it in detail in this despatch, except to state that this declaration of Austrian foreign policy had become urgently necessary as a result of the attitude of the Austrian Government itself and the need for clarification in its position in London and in Paris. In this speech, while stressing the importance to Austria of Italian friendship, which had shown itself in such real ways, the Foreign Minister spoke in a more conservative tone than he had used in his previous public utterances during the past month and immediately passed to a review of the relations with France and England. He stressed the importance which
which Austria had received from these two powers and the friendly understanding of her position which had been shown in London and Paris. The Minister reviewed the Austrian position on sanctions and based it definitely on Austria's economic and geographical situation rather than one of special friendship with Italy. The speech was carefully prepared and was intended to calm doubts and apprehensions which had arisen concerning the attitude of the Government and of the Foreign Minister. In the opinion of objective, as well as most interested diplomatic observers here, the speech was reassuring and went as far as the Government could go at this time in the extremely delicate position in which it undoubtedly finds itself. It was disappointing in Italy and particularly so in Germany, but was received acceptably in London and in Paris and by most of Austria's immediate neighbors.

Another development of real interest since my despatch No. 613 was the address given by Mr. Post van Toninghen, the representative of the Financial Committee of the League of Nations in Austria. The lecture was given under the auspices of the Kulturband and was attended by the Federal President, the Chancellor, the Foreign Minister and practically all of the ranking members of the Government. In his address Mr. Post van Toninghen reviewed the Austrian financial position, both in government and in private banking activities and brought out the important part which the League of Nations has played in post-war years in maintaining the Austrian financial, economic, and indirectly...
indirectly also the Austrian political situation. While he referred to the effective aid in the economic and political field which Italy had more recently rendered to Austria, the address was a studied effort to emphasize in this public way that it was the League and certain financial centers in Europe and in the United States which had made possible the maintenance of the Austrian position. It was apparently deemed advisable to have Mr. Boat van Tonningen make this address on this subject at this time in view of the Austrian attitude on sanctions, which had somewhat alienated League sympathy for Austria. In this address he also found it advisable to close with the statement that although the Austrian financial situation was relatively favorable in view of all the factors concerned, it was necessary to give the most careful attention to the budget, so as not to disturb that external confidence in the financial policy of the Government, which was so important for Austria. This reference was of particular interest in view of the recent change in the head of the Ministry of Finance, to which I have referred in previous despatches, and in view of the fact that the Austrian budget is at present under discussion in the Bundestag and in the Cabinet.

The Government is at present primarily occupied with the budget which had been presented some weeks ago to the Bundestag and which is now again before the Cabinet. The reports of the Commercial Attaché of this Legation, which are available to the Depart-
ment, cover the details of the budget. It is sufficient to say here that the new Minister of Finance, Dr. Praxler, contrary to expectations, has taken the reassuring action of cutting down considerably various items in the budget as proposed to the Bundestag. The Cabinet is seriously considering further reductions in the budget. It had an all-day session yesterday and will have an all-day session today and probably tomorrow, during which all the major items in the budget will undergo close scrutiny. Very considerable cuts will undoubtedly be made. It is the intention of the Government to bring the budget as nearly into equilibrium as is possible. The Minister of Finance is proposing very real cuts in the extraordinary budget and its inclusion in the regular budget, so that, beginning this year, Austria will have no extraordinary budget. There will be considerable opposition within the Government to many of the cuts proposed by the Finance Minister, and it is still a question as to how far such cuts may be made with safety, for the Austrian Government has been very careful in its expenditures in recent years. The policies, however, of the new Finance Minister as they are so far apparent have reassured financial circles outside of Austria, both with respect to him and to Austrian financial policy.

A less favorable and somewhat disturbing development in the Austrian situation is the position with respect to the live claims of the Creditanstalt, to which I have referred in recent despatches. The Department...
Department is aware that the representatives of the Austrian Treasury who recently went to London to negotiate with the International Committee there regarding these claims came back empty-handed. I am now informed in confidence that the Government has proposed to the Committee in London a final settlement on the basis of a payment of 15 million schillings in 1937, the same amount in 1938 and in 1939. As the total of the live claims against the Credit Anstalt, which the Government has guaranteed, is well over 800 million schillings, this offer is equivalent to a payment of 45 million schillings for a debt of over 800 millions. The offer has made a very unfavorable effect in London with the International Committee, and according to the procedure prescribed in the agreement, I am informed that the London Committee proceeded yesterday with the naming of an arbitrator. The Austrian Government would name under the agreement a second arbitrator, and the two would then name a neutral third. If it should come to arbitration, it is almost certain that this offer of the Austrian Government would be rejected.

There are those in Vienna who believe that the offer of the Government is a most unacceptable one to the creditors and a most unwise one to have made at this time. It would be asking the creditors of the Credit Anstalt who have these live claims to accept less than 25% in payment. After the sacrifices which the foreign banks have already made, this additional sacrifice is one which they could not accept at...
at this time.

I am not accurately informed as to the exact share of the American banks in these 300 millions of live claims guaranteed by the Austrian Government, but I have the impression that our banks hold something over half. We have, therefore, a very real interest in this matter. I have not been approached either by the National Bank here in Austria or by the American bankers, but for the Department's information I may say that I consider the offer made by the Austrian Government through the Austrian National Bank to the International Committee in London as a most unfortunate one and altogether unsatisfactory. The further sacrifices which the creditors of the Creditanstalt are expected to make at this time are too great and do not take into account the possibility that the Austrian Government and the bank may later be able to meet these obligations in full. Should the Austrian situation continue to get better, there is a very real possibility for the live claims to be met in full. Should the position not improve so definitely, the creditors should still be able to realize more than the 25% which they are now offered.

The financial policy of the Austrian Government and of the National Bank under Dr. Kienböck has in recent years succeeded in establishing confidence in various financial centers in Europe, and this confidence has been a very precious asset to Austria. It was one of the factors which made possible the conversion of one of Austria's principal loans during the past year, which involved extraordinary savings...
for the Austrian Government. The recent offer by the Government in the Credit Anstalt claims will not add to this confidence and it has not taken into account psychological factors in London and in New York, which are principally affected. It has not taken into account also the major factors in the Austrian situation, where it is of extreme importance that in every way the status quo be maintained for it internally and externally.

Irrespective of the efforts which are being made, as described in this despatch, to bring about equilibrium in the Austrian budget, and irrespective of what may be the earnest desire of the Austrian Government to follow sound financial policy, budget equilibrium cannot be realized now nor for several years in Austria. In addition must be considered the fact that her trade balance, although in the last year more favorable to her, is still very passive. The slowness in payments by Italy already referred to in my despatches will freeze up and may eventually reduce considerably or even wipe out the very favorable trade balance which Austria has had with Italy. Under the best developments which can be expected there will be a reduction rather than an increase in Austria's trade with Italy. All this will have its reflexes on the Austrian economic situation, which has improved during the past year, but which is a very delicate organism and quickly responsive to shocks from various directions. Austria, therefore, may need an external loan, and this fact
is being left out of reckoning in the offer which the Government has made respecting the live claims.

The fact that the offer will be totally unacceptable to the creditors is well realised in certain circles in Vienna, and I am confidentially informed that earnest efforts have been in progress yesterday and today to convince Dr. Kienböck, the head of the National Bank, that a more favorable offer should be made to the International Committee, so that the question may not come up before arbitrators in the original form. It is to be hoped that a more favorable offer will be submitted to the Committee, both in the interests of the foreign creditors and of the Austrian financial position as considered from the long term point of view.

The internal situation has undergone no appreciable change. The statement of the Foreign Minister on foreign policy has been well received within the country, where public opinion was very much dissatisfied with the too strong pro-Italian orientation of the Government and with the attitude on sanctions. The Government has bettered its position internally through the statement of policy.

Rumors, however, continue of further impending changes in the Cabinet. The Department will recall that when I reported on the recent reconstruction of the Cabinet I observed that further changes were probable, but not in the immediate future. It has been persistently rumored in the last week that the Minister for Foreign Affairs would retire, that...
that the Chancellor would take over the Ministry of Foreign Affairs and carry it on through Dr. Alexis, now attached to Prince Starhemberg as Under Secretary. The Ministry of War, now held by the Chancellor, was to be turned over to Prince Starhemberg, who would continue to carry it on through the present Under Secretary, General Sehner. That such a shift has been seriously considered is, I think, unquestionable, but, as I have previously reported, I do not believe that any changes will be made in the immediate future. The Foreign Minister has considerably clarified his position through his recent speech in the Bundestag, and the criticism of the Government with respect to its foreign policy is decreasing. The probabilities are that the Minister of Foreign Affairs will weather the real storm through which he is passing and will retain his position, for which he has many aptitudes. The change in the Cabinet which is most likely to take place is that the Chancellor will turn over the Ministry of War to Prince Starhemberg, but this will not involve any change in policy by the Government nor any real change in the internal situation. It will be more or less a logical development in the direction which the Government is taking of coordinating the irregular armed forces of which Prince Starhemberg is now the head with the regular army.

There are many rumors of other impending changes in the Government, which I shall not go into in this despatch, as I believe they have no foundation in fact.

There was considerable concern in informed quarters in Vienna over the reports that Italy had withdrawn a
considerable part of her forces on the other side of the Brenner and that the German army was concentrating troops in barracks not distant from the Austrian frontier. I have not been able to get definite confirmation of either of these reports. The Italian Government has officially denied having removed troops which have been kept on the Austrian frontier for well over a year. The Austrian Government is of the opinion that such troop removals have not taken place. Certain well informed observers here are of the opinion that the Italian Government did indicate that it was going to make such transfers, for the purpose of exercising pressure in London and in Paris. The Department has undoubtedly received definite information on this subject from other sources. The reports of the concentration of German troops in recent weeks near to the Austrian frontier are, I believe, unfounded. Although the Austrian Government would see such shifts of Italian troops from the Brenner with concern, the general impression in government and in other well informed quarters in Vienna is that the German Government has no intention for the present of taking any action against Austria. It is believed that the internal situation in Germany does not lend itself to such an aggressive action and that even in spite of unfavorable developments in Italy, Germany would refrain from action against Austria, particularly in view of the desire not to antagonize England.

I have referred in previous despatches to the efforts...
efforts which the new Minister of Social Welfare, Dr. Dobretsberger, may make to conciliate at least a part of the Social Democrats and to widen the base of the Government. I believe that interesting developments in this connection may be expected, but gradually. The Government will have to explore such a new course with caution, to determine how far it may proceed on it with safety. It is clear, as I have already pointed out, that Prince Starhemberg will offer less active resistance to a policy of conciliating the workers, but he is a man of very strong views. The plans of the new Minister of Social Welfare are taking form and they are being carefully considered within the Government, particularly in view of the recognized weakening in the Italian position. The Government sees the position of Fascist and authoritarian governments weakening. It is anxious to put into effect the provisions of the constitution in Austria which provide for elections within the so-called groups into which the population is divided, which are known as "Stände". At present all the representative of these groups in the Government have been appointed by the Government itself. The constitution provides that these representatives shall be elected by the voters belonging to each group. Although the Government does not consider the possibility of anything like general elections, the plans of Dr. Dobretsberger provide for elections in the "Stände", and it seems to be the opinion of the Government that elections could...
could be held in the workers' group and in the agricultural group with entire safety. This is a very interesting development, but it is still too early to say how far progress can be made. But it is a definite indication that the Government is trimming its sails to a new breeze which it feels in Europe, and to which it is quite prepared and quite willing to accommodate itself. I am following this development very carefully and shall not fail to report anything of interest to the Department. This new development in Austria is naturally causing real satisfaction in England and France.

Respectfully yours,

George S. Messersmith.