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*Personal
Adm. Sec.*

Vienna, June 26, 1936.

Dear Mr. Phillips:

I wrote you at such length on June 18th that I shall endeavor to keep this letter as brief as possible. I wish particularly to bring to your attention my strictly confidential despatch No. 813 of June 24th on the visit of Dr. Schacht to Vienna and other capitals. In view of the visits which certain officials of the German Government are making to Washington at this time and the relation which the conversations with them will have to our trade agreement program and German commercial and foreign policy generally, I think this despatch will be of particular interest to you. The latter part of the despatch will be, I believe, particularly interesting to the Department, and, as the German commercial policy in Southeastern Europe is a definite menace to our trade agreement program, I am sure the Secretary will be interested in reading the whole of this despatch.

The Schacht visit is very important if only as an indication of policy and even if the immediate results may not have been so great. As I have covered the visit from the Vienna angle so thoroughly in the despatch and as I am sure you will wish to read it, I will not go further into Schacht's trip in this letter, except to state that I have first-hand and absolutely reliable information that while in Budapest those who saw Schacht tried to touch on certain aspects of German foreign policy, and Schacht, contrary to his usual practice, refused to make any comment whatever. He was obviously under a strict injunction from Berlin not to discuss any aspects of German foreign policy. I understand that he departed from this only in Belgrade, where he assured the Yugoslavs that Berlin would stand behind them to the finish against Hapsburg restoration.

The Honorable
William Phillips,
Department of State,
Washington, D. C.

In a confidential despatch, No. 816 of June 26th, the Legation covers the Austrian internal situation and the conversations with Germany on a modus vivendi. The situation briefly is that Papen initiated conversations with the Chancellor, and the Chancellor felt that he could not refuse to discuss a modus vivendi, to which, on a certain basis, Mussolini had indicated he had no objection. As a part of the Italian policy to bring pressure on England and France, Mussolini was willing that these conversations should take place, for he felt sure that Germany would not accept the primary Austrian conditions of recognition of independence and non-immixtion. The Chancellor told the French Minister a few days ago that over the last week-end he had handed to Papen a memorandum stating the Austrian view point and the basis on which a modus vivendi could be reached. In his memorandum the Chancellor referred at the outset to a vague remark which Hitler one time made that he intended to respect Austrian independence, and then went on to say that with definite recognition of Austrian independence and agreement not to interfere in her internal affairs, he was prepared to take steps leading toward the stopping of the press campaign in both countries, the definite control of radio broadcasting which disturbed relations, and also to consider the possibility of repatriating the Austrian members of the Austrian Legion in Germany, which, as you know, has become a source of embarrassment and difficulties to the Germans. He did not go into the question of the 1,000 Marks visa fee which Germany has imposed, for Austria is not particularly interested in having it lifted, but if the Germans recognize the independence of Austria and agree to non-immixtion, this is a point on which the Austrians would have to give way. Papen, in his preliminary conversations with the Chancellor, had endeavored to get him to agree to state that Austria would also be prepared to admit several so-called "nationally minded" Austrians (which for the Germans means Nazis) into the Government. The Chancellor refused not only to consider this, but to put it in the memorandum, for he considered it immixtion in Austria's internal affairs.

Papen went to Berlin immediately after the Chancellor handed him this memorandum, and came back the day before yesterday. He saw Hitler in Berchtesgaden, but, so far, this is all we know. I doubt whether he brought back any answer, but shall know definitely soon. The Chancellor and the Foreign Office do not expect the conversations or

the negotiations to lead to anything, as they do not think Germany will agree to the open recognition of Austria's independence and the principle of non-interference. If a modus vivendi is arrived at, the Austrians would insist on its terms being made public, and Germany is not prepared, in their opinion, to go publicly on record as recognizing these two primary considerations.

One interesting feature of these conversations between the Chancellor and Papen is that at the same time that the Chancellor and Papen were talking things over, Goering's brother-in-law, Franz Hueber, who is an Austrian living in the Tyrol, was also carrying on conversations with the Chancellor's knowledge with someone in the Chancellor's confidence, whom we have not been able to identify. Hueber is a notary and rather insignificant, but was formerly Minister of Justice in the short-lived Vaugoin-Starhemberg Cabinet. He is Goering's brother-in-law, and within the last three weeks has made at least six trips to Germany. He is one of the leaders of the so-called "nationally minded" Austrians. I am told on good authority that Goering is exceedingly anxious to arrive at some arrangement with Austria. He believes that some answer to the British memorandum must be made and that Germany will be forced into conversations with France and England, no matter what answer is made to the British memorandum, and even if there is no answer at all. He considers that the "friendship" with England which is so essential for the carrying through of his program is seriously disturbed by this Austrian question. He believes that Austria will fall into the hands of Germany gradually and without any German aggressive action, if his policy with respect to England can be pushed through.

As Goering believes that conversations with England and France by Germany are unavoidable, either on the basis of the British memorandum, or Hitler's, he wants to get the Austrian question out of the way as for the time being secondary. He would even be prepared to make a modus vivendi, I am told, agreeing to respect Austria's independence, as he thinks this could be pushed aside later. But, although Goering is the second strongest man in Germany, he is not yet making foreign policy alone, and it is believed here that Hitler, Goebbels, and Rosenberg will not agree to the Austrian conditions. From the point of view of the Austrian Government, while it ardently desires improvement in Austro-German relations, German agreement to a modus vivendi on the Austrian terms would not be the best thing for Austria in the long run. It

believes that the only object of Germany in agreeing to such a modus vivendi would be to clear the way for throwing more dust into the eyes of the English and French and for gaining more time. I think all the evidence points to the Austrians being right.

Papen is tremendously interested in making these negotiations succeed, for he feels his position here keenly. After all, he has been here two years and has accomplished nothing. I hear a good many people saying that he has strengthened his position here, but I am convinced that that is not so. He puts up a good front, is seen everywhere when he can push himself forward, and feels impelled to make people feel his importance. When Suvich was recently at the Semmering, near Vienna, for a holiday and rest, Papen, I think, was the only Vienna diplomat to go to see him beside the Italian Minister, and it was generally remarked in informed circles that he only did it to push himself forward. His is a curious mentality, but a rather transparent one. The stay of Suvich at the Semmering, by the way, was purely for a rest and to see some of his family in Vienna. He came almost immediately after Ciano replaced him, and took the first chance in several years for a holiday.

As I said in my letter of June 18th, the German-Italian conversations have broken down, and there is probably less prospect of anything happening than there was before. And I expect nothing of the Berlin-Vienna conversations. I had a friend, who is a very keen observer, just return after a month's stay in Italy. He agrees that the road for agreement between Italy and England will be difficult. He says that now in Italy so many sensible people have acquired a big head and are very cocky, both as respects England and France. Once a blackmailer, always a blackmailer! This is something we shall have to keep in mind in the next few years. I believe, however, that a certain amount of prudence may be expected from Mussolini in the immediate future, for he does need money and is going to have real problems at home which he will have to meet, as well as in Abyssinia.

The bright spots in the situation which I pointed out toward the close of my letter of June 18th have not been dimmed by developments during the last week. The debates on foreign policy in both London and Paris have been encouraging. Both France and England have found it advisable to reassert their interest in Central

Europe in their respective parliaments, even if they are not yet prepared to maintain that situation by definite acts. The English press is changing its tone, and the TIMES is coming around rapidly. My conversations with Dawson while in London gave me the impression that this was coming. The dangerous isolationist sentiment which the TIMES and other papers have helped to build up, they now find it necessary to combat, and the editorial in the TIMES of June 24th, which I am sending you herewith, while still rather weak, shows the trend in the right direction. It is in many ways a significant editorial, and the heading "Toward a New Policy" shows that English policy is crystallizing, and it will, in view of developments I think, most certainly be in the direction of closer cooperation with France. The recent speeches of Duff-Cooper in England and his speech in Paris a few days ago are, I think, an indication of the line which we will see more and more in England.

As I said in my letter of June 18th, if this crystallization of policy in England is rapid enough and in the direction of Anglo-French cooperation, and if Mr. Mussolini does not make the path between London and Rome too difficult, German policy will have a major setback, and these setbacks, Berlin realizes, will be dangerous. The Germans are going to try to throw dust into the eyes of the English, but their failure to reply to the memorandum has already cleared the vision of many mistaken and too trusting, but still patriotic, Englishmen.

In the meantime, another dangerous feature in the situation has shown encouraging developments. The Czechs are going to put their loan for defensive measures through, and their defensive preparations are going forward. Henlein has been forced more than ever into the open and has made most indiscreet statements within the last two weeks which have already caused what may be a serious split in his party. Benes is doing what he can to conciliate the German minority, and, as you know, was always in favor of the suppression of Henlein's party. President Masaryk was against it and prevented the dissolution of the party before the last elections in Czechoslovakia, which resulted in giving it real standing and making it a real danger. Now the split in the party is already fairly serious; Henlein is thoroughly in the open; and, for the time being at least, weakened. The Czech Government has

just suppressed his weekly paper for six months, and is considering suppressing the daily one, and is even considering the suppression of the party as a whole as an illegal one preaching doctrines subversive to the state. Whether this suppression of the party will come about is not yet clear, and whether it would be wise, I am not altogether sure, for it might make Henlein a martyr. It would perhaps be better to continue to allow him to weaken himself by his undoubtedly subversive utterances. Czech defense measures and the difficulties developing in the Henlein party, while not yet a setback to German policy, have given Berlin something to think over and have contributed toward strengthening the situation in Southeastern Europe.

But if there are bright spots, we are not yet through this period of mistakes. Baldwin's reference in a recent speech to the oil sanctions and Abyssinia, and making us responsible for the failure of England to insist on imposing them was a bad break. From all I can gather, they left us pretty well out on a limb when we had been prepared to take really very far-going steps. It was an indefensible and an unworthy thing to do, and it was encouraging to see how the Opposition went after him. It is difficult to believe that a man like Baldwin could make such a mistake, but I am not sure that, in spite of the fact that things are going more in the right direction in England, there are not going to be more mistakes of that kind.

The Legation's despatches give the developments in the monarchist and restoration question, and, while unquestionably the monarchists are more encouraged and more active than ever and while the Government here, in view of the uncertainty in the general position, must think more of restoration, no one here seriously contemplates doing anything in the near future.

Developments, therefore, in the general picture are not altogether going in favor of Germany, and, while the way to Austria is open to her for the present, she finds it impossible to travel it. In the meantime, her own internal problems are certainly not any easier. A conversion loan of 700 million marks is to be put through, out of which it is hoped a certain amount may become available for immediate needs. This is not going to relieve the situation very much, but for the time being puts off the question of a tax increase or a capital levy. The financing of the program is going to become more and more difficult, and for the present the hope of help from

England has receded into the background. In the closing paragraph of my confidential despatch No. 813 of June 24th I refer briefly to the short term revolving credits on which German industry is now largely leaning. These are coming to the fore. We are much interested in this, but the British participation is greater than ours. There are many who believe that if these credits were curtailed, even gradually, it would starve out the Berlin Government. Little has been said about these revolving credits and the Germans are most anxious to keep them out of discussion. Garvin, in his recent articles in the OBSERVER so strongly attacking the present British policy, mentioned these revolving credits at the end. I happen to know that important persons in England who wish to avoid further mistakes in British policy toward Germany believe the time has come to do something about curtailing these credits. In that case, our own banks will have to reach some decision.

The situation within Austria remains quiet, and, as I have indicated in my letter of June 18th, I do not see anything happening in the next few months which will disturb the position here seriously. Tourists are coming here in large numbers and they mean a lot to the country. There is a feeling that later in the summer and just toward the end of the Olympic Games there will be pressure from Germany on the Nazis in Austria to disturb the peace in order to prevent the American and other visitors to the Olympic Games in Germany from coming to Austria. It seems that many of these visitors are planning to come to Austria after the Games and that this has caused some consternation in Berlin. They are so used to controlling everything and everybody in the country that they want to try to do what they can to prevent these visitors from coming to Austria. As, after all, they cannot exert any direct pressure, it is to be done through making Austria appear as a most dangerous place to visit. Whether these plans will actually be carried out is, of course, not yet certain, but I believe that the Government here is in a position to take care of Nazi disturbers of the peace.

Believe me, with all good wishes,

Cordially yours,