

# “Resources in the Service of the Nation” – Alternative Options for the City Loan of 1925 and Its Spending\*

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*Foreign loans acquired a dominant role in the stabilization and reorganization of the Hungarian national economy in the interwar years. The loans lent by the Speyer Banking House opened the opportunity of obtaining development resources for Hungarian cities through mortgage bonds. The localities spent the majority of the American loans on investments in infrastructure and public utility developments. The foreign loans imposed an enduring and significant burden on the cities, but they resulted in substantial and permanent changes in the lives of local governments, they contributed to the development of public utilities, public institutions and to the improvement of living conditions in the interwar years. However, we find significant differences from city to city in the utilization of the loans and the successful implementation of the capital investments. In some cities the repayment imposed a lighter burden and in other places the debt service strained the budget of the city by resulting in a persistent problem. In my study I explored the economic and economic policy circumstances of the borrowing of the city loan of 1925 and the characteristics its utilization.*

**Journal of Economic Literature (JEL) codes:** N14, N24, N44, N94

**Keywords:** loan of the League of Nations, Speyer loan, Hungarian cities, urban development, infrastructure development

## 1. Introduction

On 22 July 1925, Act XXII of 1925 on foreign loans of Hungarian cities was enacted, which enabled towns and cities with municipality rights and with a regular council to “borrow a long-term bond repayment loan denominated in foreign value, up to the amount corresponding to 1100 billion koronas, in order to cover the costs of their useful investments authorized by the governing authorities”.<sup>1</sup>

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\* The views expressed in this paper are those of the author(s) and do not necessarily reflect the official view of the Magyar Nemzeti Bank.

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The Hungarian manuscript was received on 22 March 2017.

DOI: <http://doi.org/10.25201/FER.16.3.119149>

<sup>1</sup> Act XXII of 1925 on the loan of cities. <https://1000ev.hu/index.php> (Downloaded: 9 February 2017)

The provision by the government of foreign loans available for cities was part of the large-scale stabilization programme, which was meant to serve the reorganization of the Hungarian national economy, after the First World War and the peace treaty of Trianon.<sup>2</sup> However, in order to recover the normal functioning of the country and to obtain the external resources essential for the development of the economy, it became absolutely necessary to increase the international recognition of Hungary after the treaty of Trianon and to achieve an equilibrium in government finances. After a successful stabilization, in 1925 the loans issued by the Speyer Banking House opened the opportunity of obtaining development resources for Hungarian cities by borrowing long-term loans. The municipalities affected by this credit facility spent the majority of the American loans – under the strict control of the financial governance – on infrastructural projects and public utility developments. In the subsequent decades, the amortization of foreign loans imposed a significant and enduring strain on the financial management of Hungarian cities, but the external financial resources resulted in significant and enduring changes in the lives of the municipalities. The capital investments enabled by the loans contributed to the modernization of cities, to the development of public utilities, public institutions, to the improvement of living conditions in the interwar years. In my study I intend to assess the economic, economic policy circumstances of the borrowing of the city loans of 1925 and 1926 and the characteristics of how they were spent.

## **2. The restoration of creditworthiness and the obtaining of the League of Nations loan**

After the First World War, the Hungarian economy and society had to face challenges never encountered earlier.<sup>3</sup> The extremely severe loss of territories and population owing to the peace treaty of Trianon caused such a trauma for Hungary that the country could not resolve or even process in the short term. The protracted war had already exhausted the economy of the country, the losses of the war caused a shortage of labour force, the life of the hinterland was strained by a severe shortage of goods and raw materials, acute problems of supply, then after the war the military occupation imposed on a significant part of the country, the dictatorship of the proletariat and the subsequent retribution, caused substantial damages in both human lives and properties.<sup>4</sup> The country gained its sovereignty parallel with the dissolution of the Austro-Hungarian Monarchy, under extremely adverse conditions, after the war the fundamentally changed circumstances of foreign policy and foreign economy prevented the recovery of the country to a significant extent. The sources of earlier foreign loans dried out, foreign trade practically ceased, the country did

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<sup>2</sup> In more detail: (Honvári 2001:330–51); (Honvári 2006:19–42); (Kaposi 2002:269–282)

<sup>3</sup> In more detail: *Romsics (1999:99–147)*

<sup>4</sup> *Bojtos (2013:327–388); Gyenesei (2015:77–402)*

not have a currency of its own or customs protection, while the neighbouring new nation-states imposed an economic blockade on a Hungary driven back behind the new borders. Parallel with that, the country had to face a radical change of the spatial structure of the economy, the loss of a substantial part of the raw material resources and infrastructure of the Hungarian economy, as well as the obligation to pay severe restitution. In this quagmire of economic problems mutually strengthening one another, the capacity of the national economy dropped, the drying-up of state revenues and the deepening inflationary crisis also played a determining role.

It was after signing the forced peace treaty of Trianon that the road opened up to consolidation in foreign and domestic policy and to the stabilization and reorganization of the national economy. The first major attempt to stop the inflation that started during the war and then accelerated and to restore the balance of government finances was masterminded by minister of finances Lóránt Hegedűs at the end of 1920 (*Honvári 2001:330–338*). The most important aim of the resolution plan was to address the liquidity problems of government finances and to restore the balance of the budget, but in the development of the stabilization programme the fact that the strengthening of the economy could almost exclusively rely on internal resources at that time had also be taken into consideration. The fact that the restitution obligations of Hungary had not yet been defined could also be a problem and all revenues and the entire wealth of the country was mortgaged as security to fulfil obligations. In order to control inflation, the financial governance tried to artificially tighten the supply of money and by the introduction of property tax they tried to increase the revenues of the state budget, as well as to reduce the expenditures of the state by the implementation of severe austerity measures. One of the fundamental pillars of the large-scale stabilization plan of Lóránt Hegedűs was the balance of the state budget accomplished by property redemption and the reduction of the issue of currency, but the plan of the financial minister only focused on aspects of government finances and disregarded the low profitability and significant capital requirement of the real economy (*Tomka 1996:71–74*). Therefore, in the short term it seemed that the plan managed to reduce the volume of currency in circulation and to improve the exchange rate of the temporary currency, the Hungarian korona, created by the over stamping of the former common currency of the Monarchy, in the international money markets. However, the revenues generated from property tax did not reach the desired level, and by creating a kind of deflationary crisis, the anti-inflationary financial policy resulted in adverse impacts on the real economy. The growth of the national economy fell short of the expectations, and by September 1921 it turned out that the stabilization of the Hungarian economy based on internal resources, i.e. the attempt of Lóránt Hegedűs to consolidate finances and the state budget, failed.

Thereafter, the new financial governance, which only had a very narrow economic policy latitude, started increasing the circulation of banknotes, in order to

finance state expenditures and to provide loans to the private economy (*Kaposi 2002:278–279*). Established after the termination of the common central bank of the Monarchy, the Austro-Hungarian Bank, the central financial institution, the Royal Hungarian State Bank started expanding the circulation of money by issuing fiat currency. From the end of 1921 loans provided directly by the State Bank were the only source of funding of the economy. Since the interests of loans emitted that way did not keep pace with the increasing rate of inflation, resources could be obtained at very favourable conditions. Since undertakings tried to convert their money, losing its value at an accelerating rate, by investments into the real economy, during 1922–23 a seeming and temporary economic upturn started developing (*Honvári 2001:337*). This kind of financing had a temporary favourable impact on both financial institutions and the processes of the stock market, the number of credit institutions and the turnover of the stock market increased (*Tomka 1996:76–77*), however, this did not happen in accordance with an investment strategy implemented in line with long-term economic policy objectives; thus, the development of the sectors considered important relating to the enduring growth of the national economy was not achieved.

The inflationary policy became a tool for the central depletion and redistribution of income, the increasing inflation resulted in the devaluation of the currency, which had the most negative effects on people living off wages and salary and those with savings. In contrast, by taking advantage of loans lent in high amounts, with a long maturity and fixed interest, those borrowers who primarily had loans secured by mortgage on real property – primarily landowners, municipalities – could repay their loans borrowed before the war much more easily by relying on a currency that was losing its value rapidly. In a way the state also benefited from inflation, since owing to the devaluation of the currency it was mostly relieved of the obligation to repay the non-indexed war loans borrowed during the world war. However, by the end of 1923 inflation had become so high that it started to fundamentally prevent the functioning of the Hungarian economy, which struggled with the replenishment of the losses and damages of the war and with shifting to peacetime production. The devaluation of money frustrated monetary circulation and resulted in huge capital losses for credit institutions in Hungary, which further compounded the economic problems arising from the shortage of capital. Although after the war the state became more and more involved in finances, it also contributed to the failure of controlled inflationary economic policy and the lack of success of the attempt to put the national economy on a trajectory of persistent growth that at that time Hungary did not yet have an independent central bank and a stable currency of its own, by which it would have been able to support the economic turn, e.g. by applying a policy of exchange rate regulation.

During 1923 it became clear for the Hungarian government that a long-term foreign loan of a major amount would be required for the successful stabilization of the

economy. During 1922–1923 prime minister István Bethlen and minister of finances Tibor Kállay conducted preparatory negotiations in order to obtain a high-volume foreign loan (*Ormos 1964:42–57*). However, it turned out during the negotiations that any rescue program for the disastrous Hungarian government finances and the national economy, which struggled with a shortage of capital, could be implemented with the involvement of external resources, which was only possible with the approval of the victorious Western great powers and the support of the League of Nations. In an effort to provide collateral for the foreign loan, the prime minister requested the Restitution Committee of the League of Nations to release the mortgage imposed on the wealth of the nation and the revenues of the state. By December 1923 the delegation of the League of Nations prepared the reconstruction proposal, in which a high amount, long-term foreign loan lent to Hungary was to play a dominant role. Containing strict conditions, the reconstruction plan required the Hungarian financial governance to stop the issue of fiat money and to halt inflation, to create a balanced state budget, to establish an independent central bank and to settle the issues of restitution. Financial reconstruction had to be supplemented by a comprehensive reconstruction programme, the purpose of which was the maintenance of the favourable economic processes. The League of Nations delegated a chief commissioner to Hungary to supervise execution (*Soós et al. 1993:520–556*).

Act IV of 1924 – the statute on the restoration of the balance of government finances – enacted the programme of the reorganization of the Hungarian economy. This law authorized the minister of finances that in the implementation of the stabilization program “*he may borrow a loan resulting in the repayment of 250 million gold koronas, in order to cover those needs registered as of 30 June 1926 that are not covered by the current revenues*”.<sup>5</sup> The announcement about the subscription of the Hungarian state loan was published at the beginning of July 1924 in the international money markets, with the signature of chief commissioner of the League of Nations Jeremiah Smith and minister of finances Frigyes Korányi (*Honvári 2001:343*). This loan was placed in a total of 8 countries, almost 55 per cent of the loans of 307 million was subscribed by the Brits, each of the Americans and the Italians subscribed 12 per cent, and 8.5 per cent was absorbed by Switzerland, while the remaining part was shared by 4 countries – Sweden, the Netherlands, Czechoslovakia, and also Hungary (*Ormos 1964:135–136*). The loan was issued in 8 tranches, each of which was denominated in the currency of the country subscribing the loan, and repayment was to take place over a term of 20 years, by drawing lots or by repurchase (*Tomka 1996:82–83*). The loan of the League of Nations was received well in the United States, which is reflected by the telegram of the Speyer and Co. Banking House sent to the Hungarian Minister of finances with the date of 8 July 1924, and published by the Hungarian News Agency: “*We are happy to let you know that the American tranche of the Hungarian loan was fully subscribed.*”

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<sup>5</sup> Act IV of 1924 on Restoring Fiscal Equilibrium. <https://1000ev.hu/index.php> (Downloaded: 9 February 2017)

*We have closed the subscription list and the banking group that committed to issue the loan by its signature, was fully released. We were extremely happy to have been able to participate in this action that we trust will be just as beneficial for Hungary as it is for the American capitalists who participated in the subscription”.*<sup>6</sup>

With reference to the fact that this loan was not only designed to resolve the fiscal problems but also to create the conditions for a sustainable growth of the Hungarian economy in the form of new loans and to gain recognition for Hungary after the peace treaty of Trianon, the professional literature of economic history was right in highlighting that the loan of the League of Nations was offered with extremely adverse conditions, the subscription price of the loan was very low (80–87 per cent) and its interest rate very high at 7.5 per cent (*Honvári 2001:343–344*); (*Kaposi 2002:279–280*). It is reflective of the secondary role of the loan of the League of Nations in establishing international financial trust in the country and the resultant strengthening of sovereignty that even though in 1924 lending to Hungary seemed favourable to foreign creditors, the attempt to place these loans fully in the western European money markets failed. This is how it became necessary to place a part of the loan worth 11.6 million gold koronas with still weakened Hungarian investors. Minister of finances Frigyes Korányi issued a press release on 12 August 1924 on the success of the subscription of the loan of the League of Nations in Hungary, in which, in addition to “obligatory optimism” he also tried to highlight to the general public the further-reaching beneficial effects of the loans and the psychological aspects of subscriptions in Hungary: *“I am glad and satisfied to be informed that the subscription of the Hungarian tranche of the loan of the League of Nations was a total success. The Hungarian society has proven that it is not only aware of what is its obligation to the entire nation, but it can also exercise sober deliberation in finding the most lucrative investment opportunities for its capital. [...] On this occasion I gladly discharge my duty of conveying my patriotic thanks to every section of our society that has participated in the entire loan actions, and likewise in the establishment of the Magyar Nemzeti Bank, either by moral support, or in the form of financial involvement. [...] I consider this moral support [...] the guarantee of this great effort that we embarked on eighteen months ago under difficult circumstances, and that still involves much struggle and tribulations today. This enthusiastic support is the measure of self-confidence. And if we have trust in ourselves, then we will manage”.*<sup>7</sup>

The establishment of a central bank independent of the state, having the monopoly to issue banknotes and the creation of a stable valued national currency, was an essential condition for the economic stabilization to be successful (*Soós et al. 1993:556–566*). Magyar Nemzeti Bank, the independent Hungarian central bank, started operating

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<sup>6</sup> News of the Hungarian News Agency 1920–1956. Weekly edition, 1924–1941. 08 July 1924) <https://library.hungaricana.hu/> (Downloaded: 9 February 2017)

<sup>7</sup> News of the Hungarian News Agency 1920–1956. Weekly edition, 1924–1941. 12 August 1925) <https://library.hungaricana.hu/> (Downloaded: 9 February 2017)

on 24 June 1924, as a company limited by shares. The new central bank shouldered the public debt accumulated up to that point from the former state bank, and with it the gold and foreign currency stock of the state bank. The Magyar Nemzeti Bank stabilized the korona with the support of the Bank of England, tied to the exchange rate of the British pound. The korona, which had become a value certain currency by now, was converted into the new, gold-based official currency, the pengő as of 1 January 1927. The rates of foreign currencies against the pengő were also set, at the time of introduction 1 British pound was worth 27.8 pengős and one American dollar 5.7 pengős. The central bank maintained the convertibility of the new banknote for gold and foreign currency above the legal requirements, and in the initial period, it pursued a very modest emission and lending policy, in order to avoid the danger of another bout of inflation. By creating a stable and stable valued currency, the Magyar Nemzeti Bank significantly contributed to consolidation, to the strengthening of the international financial situation, creditworthiness of the country, and to the subsequent economic upturn (*Botos 1999:72–83*).

The reduction of expenses was a priority in the stabilization program, which was intended to be accomplished by “settling the remuneration of public servants and reducing their number”, among others, which was also accomplished by increasing the revenues of the state through the significant increase of taxes and duties and the reorganization of public services. This statute already mentions the intention to establish the central bank, but ultimately, the establishment of an autonomous financial institution independent of the government was enacted by Act V of 1924 on the establishment and patent of the Magyar Nemzeti Bank.<sup>8</sup> It enhanced the optimism about the enduring success of the economic reconstruction that, instead of the reconstruction period defined by financial experts originally until 30 June 1926, inflation stopped in the same year, the fiscal equilibrium was restored by as early as October 1924 and in the next fiscal year the balance of public finances showed a small surplus at the end of the year (*Tomka 1996:83*). The chief commissioner of the League of Nations called this fast and successful stabilization a “*surprising recovery*”, and the former minister of finances reflected on the results of the process by these words: “*The success of financial reconstruction happened within such a short time that it was a surprise for even those who accepted the political and moral responsibility for these efforts*” (*Korányi 1928:1–11*).

Successful stabilization also meant that Hungary accomplished important results in coping with the consequences of the war, and having regained a significant part of its sovereignty, in the middle of the 1920s it was capable of getting involved in the upturn of the world economy based on the utilization of American and English loans. The period between 1925 in 1929 was considered a very favourable time

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<sup>8</sup> Act V of 1924 on the establishment and patent of the Magyar Nemzeti Bank. <https://1000ev.hu/index.php> (Downloaded: 9 February 2017)

for obtaining loans in the international capital markets (Tomka 1996:83). After the resolution the opportunity opened up for the Hungarian corporate sector and municipalities to obtain the resources necessary for their missed developments by borrowing foreign (primarily American) loans, to remedying their acute capital shortages by international loans (Balla 1935:258). It was in 1925 that Hungarian cities got an opportunity to borrow the much-needed mortgage loans of significant amounts, with a long maturity, financed by the international capital market.

### 3. Borrowing by Hungarian cities

After the First World War, in addition to the challenges going back to the time of dualism, Hungarian cities had to face several new dilemmas. Many communities had to address problems of controlling the damages caused by the war, the revolution and the occupation, of remedying the economic and social changes caused by the new borders imposed by the peace treaty of Trianon, while the public utility and infrastructure developments, the social, public health, educational and cultural tasks deriving from processes of urbanization and population growth affected almost all types of localities. All these together caused a kind of forced modernization in the lives of rural localities, considering the fact that owing to the world war and the economic consolidation, there had been no means to implement a significant part of developments for almost one decade.

In the decades between the two world wars the relationship of Hungarian towns and cities with the central government and with public administration, as well as the tasks of municipalities were basically defined by a legal environment originating from the era of dualism. Of the efforts at the modernization of the legislative system, Act XXX of 1929 on the reform of public administration was the most outstanding, which attempted to place the administration of local municipalities on a new basis, but in reality it did not change the institutional foundations, in fact, in addition to retuning the most important elements, it even made the legacy of dualism more stringent.<sup>9</sup> As a result of the public administration Act of 1929 – since this law did not invalidate Act XXI of 1886 on municipalities, which in turn left Act XLII of 1870, the first law on municipalities intact – *“an idiosyncratic legal chain of survival and coexistence was created in the world of local public administration, consisting of counties, towns (and villages)”* (Antal 2010:6). Therefore, with all of its special characteristics, the public administration and municipality level administration after 1920 show a kind of continuity with the main direction of public administration in the era of dualism, in which the reduction of the territorial autonomies of public administration was assigned a central role by the strengthening of centralisation and by increasing the influence of agencies of the state (Fülöp 2014:207–208). This was

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<sup>9</sup> Act XXX of 1929 on the rearrangement of public administration <https://1000ev.hu/index.php> (Date of access: 09 June 2017).

also true for the financial management of cities, since *“the gradual development of law was then constantly approaching a state in which every economic action of the cities that primarily affected their asset status, required the approval of a higher-level organ, a governing authority”* (Drághfy 1941:58).

According to the legal interpretation of the interwar years, local governments, i.e. villages, towns and cities and counties participate, with a certain degree of autonomy, in the exercise of the executive powers of the state through the fulfilment of tasks delegated from the state because of practical reasons, i.e. in governance and public administration, and therefore *“governance at municipality level is essentially [...] nothing else than the involvement of the people in public administration”* (Homolyai 1943:6). The contemporaneous professional literature, which classified the public administration duties of local governments according to obligatory tasks conveying the central will of the state and voluntarily committed tasks reflecting the self-government intentions of localities was of the opinion that during the 20th century in the scope of tasks to be fulfilled by Hungarian towns and cities *“as a result of the huge rate of urbanization that started in the 19th century [...] and with the increase of cities, the advancement of culture and the increase of demands, it was mainly the weight and significance of optional tasks that have showed an increase”*; therefore, the fulfilment of urban development, cultural, educational, and public catering, public health and social tasks – and the fulfilment of the urban management tasks financing these – increased significantly (Homolyai 1943:4). The aims of urban development ideas of the time significantly overlapped with modern urban planning ideas, since the developments were designed to achieve, even during the interwar years, such results which would lead to better coverage, than before, of social needs by the localities, changing both in space and time, which means, in a complex manner, the expansion of physical, social, healthcare, cultural and educational infrastructure and services, the improvement of the living conditions of city-dwellers constituting a spatial community.

The autonomy of municipalities primarily manifests in legislation, financial self-government and the election of officials, which also fundamentally determined the implementation of development concepts. In order to ensure the success of stabilization and to avoid excessive indebtedness, after 1920 the intention of control by the state was applied more strictly in the financial operations of Hungarian cities. Act IV of 1924 already authorized the government to implement the actions necessary for the rearrangement of the finances of cities, then Act V of 1927 made the validity of budgets of cities subject to the approving consent of the minister of the interior and the minister of finances, *“in order to ensure the appropriate application of the necessary austerity in the finances of local government bodies and in the imposition of local government taxes”*. Accordingly, certain items of the city budget may be reduced, increased, deleted, and even new expense items may be added, or the approval of the budget may be rejected entirely, and it is even

possible to instruct the municipality to create a new budget (*Drághfy 1941:59–60*).<sup>10</sup> This rigidity also applied to borrowing by cities, which we will also see regarding the Speyer loans.

Referring to the New York correspondent of Reuter agency, on 11 July 1925 MTI news agency published that “*The Speyer Banking house concluded the negotiations on a loan of 10 million dollars to be lent to Hungarian cities.*”<sup>11</sup> This enabled the disbursement of the American loan affecting 48 rural cities with the mediation of Hungarian Commercial Bank of Pest.<sup>12</sup> Thereafter, the process of local governments borrowing foreign loans accelerated. This is how counties and the capital received communal loans in 1926 organized by the General Credit Bank of Hungary. The issues of mortgage bonds for the purpose of giving loans to cities and counties were becoming an increasingly dominant form of long-term foreign loans and a significant rivalry began in the mediation of the sources of funding between the two leading financial institutions of the capital city, i.e. the Hungarian Commercial Bank of Pest and the General Credit Bank of Hungary (*Tomka 1996:84–85*). While the General Credit Bank of Hungary mainly relied on the Rotschilds of London, the Hungarian Commercial Bank of Pest primarily maintain connections with American financial groups, including the Speyer Banking House. It was an early sign of the increasing role of American capital in the financing of the Hungarian economy that in August 1924 the Government delivered debentures of the loan of the League of Nations with a face value of 1.5 million dollars to the Speyer Banking House, originally subscribed in Hungary (*Honvári 2001:344*). In the market of communal loans provided to local governments a serious fight developed among competitors of the international capital market; therefore, it was considered a significant diplomatic achievement that once again the Speyer Banking House was commissioned to lend the second city loan of 6 million dollars (*Tomka 1996:85*). However, it should be noted that naturally, in addition to the agreement concluded with the Speyer Banking House, there were several instances when a mortgage loan denominated in a foreign currency had been lent until the outbreak of the financial crisis in Hungary.

Even during the war years, Hungarian cities were forced to put their development concepts on the back burner and only finance their fundamental public administration services and the maintenance of their institutions, a backlog of several decades had been accumulated in the modernization of the network of roads and public utilities and the maintenance of public buildings (*Statistical Yearbook 1928:35*). The reduced capacity of the local economy and the steadily decreasing tax potential of the residents, coupled with accelerating inflation,

<sup>10</sup> Act V of 1927 on the reduction of certain taxes and duties and on provisions regarding calculation in pengő value, furthermore, on the more effective control of the finances of local government assemblies. <https://1000ev.hu/index.php> (Downloaded: 9 June 2017).

<sup>11</sup> News of the Hungarian News Agency 1920–1956. Weekly edition, 1924–1941. Issue of Week 53, 11 July 1925 <https://library.hungaricana.hu/> (Downloaded: 9 February 2017).

<sup>12</sup> On the operating figures of the Bank for 1926 Pesti Magyar Kereskedelmi Bank (Hungarian Commercial Bank of Pest) (*Kallós 1926:137–143*).

resulted in the drying-up of revenues and the disruption of the city budget (*Inántsypap 1938:481*). A significant part of the territory of the country sided by the new borders drawn after the first world war was affected by the occupation of foreign military force, which caused damages in several communities with varying terms and intensity. These events burdened the budgets of individual cities by significant reconstruction costs in the years following the war.<sup>13</sup> The social tensions arising from the consequences of the war and the general situation of the national economy were also directly present in the lives of cities, taking care of those in need – disabled veterans, widows and orphans – and the unemployed, the restart of cancelled public works posed a significant challenge for city leadership. The acute shortage of capital jeopardized the operation of public utilities of major communities, and thus the supply of the general public; therefore, on 15 September 1924, in Nyíregyháza, in the centennial celebrations of the city, the National Congress of Hungarian Cities once again urged the settlement of the loan issues of cities.<sup>14</sup>

The contemporaneous analysis of the borrowings of cities pointed out that in the fulfilment of their public tasks defined in law, local governments *“need additional and significant funds in order to create and maintain public institutions, institutes, public utilities, general public facilities and to implement projects of urban development and create works of great significance influencing even the distant future”*, and since the localities can mainly fill these needs through the involvement of external resources, therefore *“for reasons of financial management, the loans of cities are of special significance, because owing to the nature of this matter, the increase of the needs of urban citizens coupled with efforts to build up the capacity to fulfil the constantly registered additional needs created by the fast pace of urban life, the significance of these loans is sharply increasing year by year”* (*Inántsypap 1937:802803*). During this era the borrowing right of cities was regulated by Acts XXI and XXII of 1886 on municipalities (counties and cities with municipality rights) and villages (local governments of localities), Act XXII of 1925 on city loans and Act XXII of 1929 on the reorganization of public administration. These legal frameworks ensured the borrowing rights of cities, but the borrowing of the loans was subject to the approval of the supervisory authorities, in order to prevent excessive indebtedness and to ensure the control of the government (*Lukácsi 1928:37–38*).

After the First World War Hungarian cities borrowed loans in various amounts and in diverse forms. The localities usually had the opportunity of obtaining credit facilities for their operating type expenses that could not be financed from their budgets, while they could finance investment projects by long-term loans. Since *“Hungarian cities, towns and villages have no capitals or reserves [...], this is why they can only cover*

<sup>13</sup> In Szolnok, for example, during the time of the Romanian occupation and the dictatorship of the proletariat, in addition to the road bridge of the Tisza, the County Hall, the Castle Church and the road network of the city, several other public and private buildings sustained serious damages in 1919 (*Fülöp 2013:105–110*).

<sup>14</sup> Nyírvidek, 17 September 1924.

*their investment needs by borrowing*” but pursuant to the financial policy guidelines, “*the Government usually only allows cities to borrow loans to be repaid on a longer-term, for the purposes of works of investment nature*” (Lukácsi 1928:37–38). In the opinion of the professional literature of the time, the long-term loan “*is practically the most natural form of subsequent accumulation of wealth, arising from the regime of financial management*”, which “*enables revenues expected for the future to be brought forward, in order to create coverage for such absolutely necessary expenses that would otherwise only be satisfied at a later date and therefore public bodies can only commit to fulfilling the tasks whose fruits would be enjoyed not only by economic individuals constituting the public body at the time of borrowing, but also and importantly, by individuals of a later era as well*” (Drághfy 1941:56). The resources necessary for the accomplishment of aims serving the future became available for Hungarian cities after the successful consolidation. However, the fast influx of foreign (mostly American) loans and the appetite of the cities for loans encouraged the government to introduce strong regulatory controls for borrowing, in order to prevent the excessive and irresponsible indebtedness of the localities.

Back in 1924, the interior minister let it known to the general public of cities in a circular directive that they “*are not allowed to launch negotiations aimed at obtaining foreign loans without the knowledge and consent of the government,*” despite this, in 1926 local governments once again had to be emphatically warned that they “*have to refrain from such stand-alone, isolated loan actions for their own best interests, but also with regard to national interests*”.<sup>15</sup> The governance of interior affairs was right in concluding that “*the separate negotiations of cities on foreign loans cannot deliver the desired results, because [...] in addition to isolated loan actions of certain local government organs, it is not possible to negotiate such favourable conditions in the money market as in the case when they act with their united moral and financial powers in the open market, under the direction and with the support of the government*”. In addition, the “*random, isolated endeavours of the local governments at obtaining loans make the conduct of a planned credit policy [...] more difficult*”, while “*if the loan needs of the cities are satisfied under the direction of the government [...] it becomes possible to prevent the local government from incurring unnecessary debt, which is suitable to restrict the burdens payable to foreign entities under the heading of interest and principal repayment and therefore it becomes possible to prevent that the payment of balances of the country shift in the direction of liabilities to such an extent that would give us reason to worry about the financial order of the country, which was accomplished with so many difficulties.*” Realizing the deepening of the financial tensions of the world economy – related to the increase of foreign indebtedness of the country and to the deterioration of its balance of payments – the Interior Ministry ordered in its circular decree of 14

<sup>15</sup> Circular decree with B.M. no. 54.033/1926. on the borrowing of foreign loans. Belügyi Közlöny (Home Affairs Gazette), 1926. Volume 31, issue 42, 3 October 1926 pages 704–705.

October 1929 that the strict process developed related to the borrowing of cities be maintained and borrowing by local governments be restricted.<sup>16</sup>

Therefore, Hungarian cities with significant assets and revenues had made even earlier several failed attempts to borrow domestic or foreign loans for the maintenance of their operations and for the accomplishment of their development concepts (*Honvári 2004:47–48*). However, the Hungarian financial institutions did not have the necessary amount of capital, on the one hand, on the other hand, loans were available according to the current conditions of the money market, while the international financial groups were not willing to lend to localities individually, for lack of a state guarantee.<sup>17</sup> And even though a group of cities that did not qualify for the first Speyer loan started negotiating with English financial circles competing with the Speyer Banking House on borrowing, it was the firm opinion of the government that the initiating and coordinating role of the state is essential in the negotiations of the loan, since standalone attempts of the individual cities would deteriorate the creditworthiness of the country, small towns simply will not be able to obtain loans that way and the credit brokers would increase the interest surcharge.<sup>18</sup> Therefore, the government embraced the cause of mortgage loans to be lent to cities and initiated a survey in order to find out which cities would need loans and in what amounts, including the assessment of whether the financial capacities, assets and revenues of the cities would provide an appropriate guarantee for the repayment of the loans. As a result of the survey, it turned out that the overwhelming majority of Hungarian towns and cities needed foreign resources: 10 cities with municipality rights and 38 cities with regular councils reported their needs for a loan in a total of 139,904,000 gold koronas, of which 104,166,000 gold koronas were intended to be invested in revenue-generating projects and 35,738,000 gold koronas in non-revenue-generating projects (*Inántsý-Pap 1938:483*). There were only 6 cities that did not report a need for borrowing. The 54 localities having the rank of city at the time were thoroughly assessed for their asset position, budget appropriations, revenues and expenditures and tax revenue capabilities. It was found that the asset positions of cities, their expected revenues and the high ratio of productive investment projects to be financed from the loans provide an appropriate guarantee for the borrowing of major loans. The need to strengthen the creditworthiness of Hungarian cities, to increase the marketability of the loan bonds and to stimulate the interest of the international investment market required the centralization of city loans. In an effort to enable cities to obtain a direct connection together with the international financial markets, the government initiated negotiations with the Speyer Banking House of New York on the provision of a loan of 50 million gold

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<sup>16</sup> Circular decree with B.M. no. 79.381/1929. on the restriction of borrowing by counties, cities, towns and villages. *Belügyi Közlöny* (Home Affairs Gazette), 1929. Volume 34, issue 50, 27 October 1929 1104–1105. p.

<sup>17</sup> News of the Hungarian News Agency 1920–1956. Weekly edition, 1924–1941. Issue of Week 53, 09 July 1925 <https://library.hungaricana.hu/> (Downloaded: 9 February 2017).

<sup>18</sup> *Közgazdasági Krónika* (1925:668–669); *Makó* (2015:86–88).

koronas. At first the banking house insisted on the guarantee of the state and wanted the cities to assume joint and several guarantee for the entire amount of the loan, for which the real properties of the cities would have been mortgaged, but the cities managed to negotiate an arrangement under which they were allowed to dispose freely of their real properties after the borrowing of the loan as well and the collateral for the loan was the flow of revenues of the cities, primarily revenues from sales and wage taxes. The contemporaneous report stated that the conditions of the loans lent to the cities “[...] are generally more favourable than the so-called reconstruction loan lent to the state, because the bonds will be issued at a price of 80 per cent, as opposed to the 82 per cent of loans lent to the government”.<sup>19</sup> The negotiations resulted in the creation of a type of loan which had hardly been known earlier even in the international money markets and which involved the joint issue of bonds by the Hungarian cities requiring loans; thereby, establishing a direct link between localities interested in borrowing – with the involvement of the government – and foreign financial groups (*Inántsyt-Pap 1937:806*).

Pursuant to Act XXII of 1925, approved by the Parliament, the cities were allowed to borrow a significant volume of long-term loans primarily at the expense of their own revenues, of which every city was allowed to borrow as much as was approved by the interior minister in agreement with the financial minister, according to the resolution of the assembly of city representatives, but the amount of the annual debt service of the loan was not allowed to exceed half of the total revenue of the city from sales tax and wage taxes (*Honvári 2004:50*). The cities had to provide suretyship for the loans borrowed by them, offering all assets and public revenues as collateral, but since several cities were involved in the borrowing of the loan, the law stated that each city was only liable for the loan it borrowed itself.

Therefore, pursuant to the statute the bond issuing committee issued on-sight dollar bonds in a total face value of 10 million dollars, the name of which was “*Consolidated Hungarian City Loan with 7.5% Guaranteed Gold Bond for Twenty Years*”. The Speyer Banking House purchased the bond at a price of 82 per cent, settlement was made with the cities at a price of 82.5 per cent. The annual interest was set at 7.5 per cent, the annuity of the loan was 9.73 per cent for a term of 20 years; the annuity had to be paid in 40 subsequent semi-annual instalments, beginning on 1 January 1926. Only 500 thousand dollars of this loan could be sold above the price of 89 per cent in the capital market of Amsterdam (*Közgazdasági Krónika 1925:669*). One of the reasons for this was the fact that Western European investors knew little about Hungarian cities. In order to obtain security for the payment of the interest and principal instalments of the loan, the revenues of the cities deriving from general wage taxes and their share of sales taxes were encumbered in such a manner that these city revenues had to be paid to the

<sup>19</sup> News of the Hungarian News Agency 1920–1956. Weekly edition, 1924–1941. Issue of Week 53, 09 July 1925 <https://library.hungaricana.hu/> (Downloaded: 9 February 2017).

regional Royal tax office, similarly to state taxes, and the office paid these sums – to the extent necessary for the full repayment of the loan – into a separate bank account maintained by the Magyar Nemzeti Bank. As a guarantee for repayment, it was provided that no subsequent loan would receive a higher ranking than this loan. In the manner prescribed by law, the Magyar Nemzeti Bank acted as an important intermediary in brokering the foreign loans borrowed by Hungarian cities and in mediating their repayment. Owing to the high interests and the lower initial price, the business management of the central bank tried to interfere in several ways in order to reduce the interests in the placement of foreign loans borrowed by city self-governments with Hungarian financial institutions (*Botos 1999:53–54*).

The loan was borrowed based on the notarized recognizance of cities (main bond), the loan bonds were issued on behalf of the borrowing cities by a committee of four members, each of the interior minister and the minister of finances appointed one member, one person was delegated by the cities, while the president of the committee was the delegated representative of the ministry. In order to improve the creditworthiness of the loan bonds, they were declared suitable to be used as security deposit and villages, bodies, foundations, institutions under public supervision, funds of persons under guardianship or care, furthermore, funds of entails and funds in deposit, as well as funds held at savings banks as deposits were allowed to be placed in the bond. Furthermore, city bonds and their interest coupons were exempt from the documentary and interest duties and in the case of repayment the repaid principal was tax-free.

However, in the distribution of the Speyer loan of 10 million American dollars, borrowed in 1925, it turned out that certain cities were not able to complete their planned investments by the loan amount allocated to them, while other cities were in need of additional loans in order to finance their constantly increasing and highly urgent social, public health, economic and cultural tasks; therefore, the localities once again approached the government with the request of fulfilling their additional loan needs (*Inántszy-Pap 1938:489–490*). According to the report of the cities, 9 cities with municipality rights and 34 cities with regular councils required additional loans, 80 per cent of which was intended to finance income-generating and one-fifth to finance non-income-generating investment projects. The government and the legislation authorized the borrowing of this additional foreign loan; consequently, pursuant to Section 18 of Act XV, under the agreement concluded on 27 October 1926, the cities borrowed an additional sum of 6 million from the Speyer Banking House, with an interest of 7 per cent.<sup>20</sup> The following cities received funds from the second consolidated loan: Baja, Győr, Hódmezővásárhely, Miskolc, Pécs, Sopron, Szeged and Székesfehérvár cities with municipality rights, furthermore, Budafok, Békéscsaba, Cegléd, Eger, Esztergom, Gyöngyös, Gyula,

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<sup>20</sup> Act XV of 1926 on the state budgets of 1925/26 and 1926/27. <https://1000ev.hu/index.php> (Downloaded: 2 March 2017).

Hajdúnánás, Hajdúszoboszló, Jászberény, Kaposvár, Karcag, Kiskunhalas, Komárom, Mezőtúr, Nagykanizsa, Nagykőrös, Pesterzsébet, Salgótarján, Szekszárd, Szolnok, Szombathely, Vác and Veszprém cities with regular councils.<sup>21</sup> The additional loan, for which lower interests and higher prices were negotiated, had to be borrowed from the Speyer Group once again because under an earlier agreement those cities that were the beneficiaries of the loan of 1925 – of which 27 localities were also involved in the second loan – were not allowed to issue additional loans during the term of the repayment of the loan in Hungary without offering the opportunity to the Speyer Banking House first (*Inántszy-Pap 1938:493–498*). According to the statements, of the Speyer loan of a total amount of 16 million American dollars, cities with municipality rights were permitted to borrow 7.3 million dollars and (county) cities with regular councils 8.7 million dollars. Those cities that were beneficiaries of the loan actually received an amount of 74,349,659 pengős after the deduction of the costs related to the issue and in the case of the no. 1 loan, a loan service reserve in the amount of the annuity for six months. In respect of localities with the same legal status, 90 per cent of cities with municipality rights received credits from the Speyer loan, while in the case of county cities 80 per cent of the localities applied for and received funds from the loan. Of cities with municipality rights, Szeged received the highest and Sopron the lowest amount from the loan, while Kecskemét did not receive any share of this loan type. Of the 45 (county) towns and cities with regular councils only 9 did not apply for a share of the Speyer loan, of those that applied for the loan Újpest received the highest amount and Hajdúböszörmény – which was still a town at the time – the lowest.

#### 4. The utilization of the city loans

The government clearly expected the foreign loans lent to local governments after 1925 to boost the economy, to increase the number of productive investments and to enhance the economic performance of the country. In his speech of 5 December 1925 in the national assembly, interior minister Iván Rakovszky highlighted that *“the loan of cities of the countryside will, in fact, have a beneficial and fruitful impact on our economic life, furthermore, it is also remarkable for addressing the need to reduce unemployment significantly”*.<sup>22</sup> Therefore, it was a requirement of the foreign loan needed by the cities that the loan *“must not be used for any other purpose than useful investments, therefore it must not be spent on the construction of a city hall or barracks for the gendarmerie”*.<sup>23</sup> A list of what are the investments on which the cities may spend the borrowed amounts constituted the annex of the agreement defining the terms and loan. Three-quarters of the loans borrowed by the cities had

<sup>21</sup> Circular decree with P.M. number 5.445/1926., on the implementation of the provisions regulating the conditions of the lending of an additional foreign bond loans to cities. *Belügyi Közlöny* (Home Affairs Gazette), 1926. Volume 31, Issue 49, 21 November 1926.

<sup>22</sup> The speech of minister of the interior Iván Rakovszky was published in: *8 órai újság*, 5 December 1925.

<sup>23</sup> *News of the Hungarian News Agency 1920–1956*. Weekly edition, 1924–1941. Issue of Week 53, 9 July 1925 <https://library.hungaricana.hu/> (Downloaded: 9 February 2017).

to be spent on income-generating investments and the representative of Hungarian Commercial Bank of Pest, which was involved in the disbursement of the loan, had to authorize the proposed investment projects. Based on this, commercial, industrial and economic aims included surfacing of roadways, the market hall, construction of railways and bridges, wood cutting, in the scope of urban public utilities the power plant, the gas factory, the thrash collection plant, the printing shop, the distillery, the brick and tile factory, the bread and the ice plants were defined, aims related to public health included the bathhouse, the hospital, the disinfecting plant, the water pipeline, the public toilet, the canal and the slaughterhouse, while the scope of social aims included small apartments, the workers' house and the dormitory; furthermore, in the scope of various other investments, purchase of real property and the regulation of the riverbed were listed (*Inántsy-Pap 1938:491*). It is a reflection on the capital needs of Hungarian cities at that time that the applications of a high number of localities were received before the closing of the negotiations. The cities themselves wanted to spend the loans primarily on infrastructure development and the on construction of urban public utilities. The city of Szeged intended to use the loan of 4 million gold koronas that it applied for to construct a railway line for farmhouses, Pécs wanted to borrow 3 million in order to expand its water pipe, sewage canal and power network, Kaposvár requested a loan of 1 million for the construction of the electricity plant and the market hall and to build up the canal and water pipe network of the city, Szolnok intended to build a thermal bath and a hotel. Debrecen spent the loan borrowed in 1926 on building 18 schools in areas with farmhouses and a market hall.<sup>24</sup>

However, some cities proceeded with more caution, they believed that not only was the loan very expensive and came with very adverse conditions, they also considered the encumbrance of the revenues of the city to such an extent risky, since mortgaging a significant part of revenues in the budgets of the localities could cause the disruption of everyday operations; furthermore, they also objected to the provision that originally the loan was not allowed to be used for cultural purposes or construction of housing. The general assemblies of the cities were also generally divided on the issue of borrowing the foreign loan, but most of the localities were of the opinion that the investments to be implemented for the benefit of future generations will become sources of the development, economic and cultural strengthening of the cities (*Dobrossy 1996:425*). Despite all these issues, the contemporaneous correspondent was of the opinion that *"the successful conduct of the foreign loan of cities demonstrates in a convincing manner that the benefits of the trust expressed by foreign countries to Hungary recently can be already collected"*.<sup>25</sup> After the successful borrowing of the first city loan, several

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<sup>24</sup> News of the Hungarian News Agency 1920–1956. MTI, 5 August, 1926. <https://library.hungaricana.hu/> (Downloaded: 9 February 2017).

<sup>25</sup> News of the Hungarian News Agency 1920–1956. MTI, 9 July 1925 <https://library.hungaricana.hu/> (Downloaded: 9 February 2017).

other similar, long-term or high-volume lending transactions were concluded. The cities and counties received loans on 8 occasions in 1926, 9 occasions in 1927 and on as many as 14 occasions in 1928, with steadily improving conditions (Tomka 1996:85).

Realizing the increasing foreign indebtedness of the country and that of local governments, the central bank submitted a proposal to the financial governance and legislation on the restriction of long- and medium-term borrowing and on tightening the control of the utilization of the loans (Botos 1999:55–57). Naturally, the government itself has also recognized the risks of excessive borrowing of HUF loans without central regulation, but no central regulation was introduced owing to the changes of lending conditions occurring after 1929. The appetite of certain cities for loans was increasing constantly and they tried to obtain funds for urban development from other sources as well, but when new loan contracts were concluded, they often disregarded their obligations stipulated in the former loan contract, and in the new agreements they failed to maintain the priority rank of the repayment of the Speyer loan.<sup>26</sup> In the autumn of 1926 the interior governance issued a special circular decree in which it alerted the affected localities that the Ministry will not authorize the borrowing of additional loans until these conditions have been stipulated in the contract: *“The communities [...] of cities with municipality rights are requested to consider the fourth and sixth sections of the contract concluded with Speyer & Co., which impose the obligation of giving priority to the foreign loan. At the same time, I warn the communities of cities with municipality rights that any resolutions adopted by cities receiving the foreign loan and containing the assumption of obligations for valuable consideration will only receive the approval of the governing authorities if the priority of the Speyer loan is expressly stipulated in this contract, which is why it is recommended that a provision to this effect is included in the relevant contracts in advance.”*<sup>27</sup> Typically, some of the cities carried on this practice in the borrowing of the new loans as well; thus, in the spring of 1928 the interior minister issued a new decree in which it mandated the cities to ensure that *“in the case of any short-term city loan, even those secured by promissory notes only, the creditors shall expressly acknowledge the unconditional priority ranking of the Speyer loans”*.<sup>28</sup> Ultimately, all cities with municipality rights –

<sup>26</sup> In the city of Nagykanizsa the largest development financed from the Speyer loan was the establishment of the sewage network and the construction of rental apartments, but this Transdanubian community had to borrow additional loans, mainly from local financial institutions, to finance the purchase of properties valuable from the aspect of urban development (Barbarits 1929:137–138).

<sup>27</sup> Circular decree with B.M. no. 54.455/1926. on the assurance of the priority of the Hungarian Consolidated City Loan borrowed by cities. Belügyi Közlöny (Home Affairs Gazette), 1926. Volume 31, issue 47, 7 November 1926.

<sup>28</sup> Circular decree with B.M. no. 43.020/1927. on the assurance of the priority of the Hungarian Consolidated City Loan borrowed by cities. Belügyi Közlöny (Home Affairs Gazette), 1928. Volume 33, issue 25, 3 June 1928.

with the exception of Budapest, Kecskemét<sup>29</sup> and Hódmezővásárhely – and 34 cities with regular councils took the opportunity of the Speyer loan (*Közgazdasági Krónika 1925:669*). It cannot be disregarded that between 1925 in 1928 the loans lent to Hungarian cities and counties were designed to serve not only the reconstruction of infrastructure damaged or destroyed during the war, or the closing of the investment gap of several years in public utilities, but also to improve the living conditions, general welfare of the Hungarian society, as well as the processing of the trauma of the peace treaty of Trianon in an indirect way.

The loan application was made in such a manner that the general public of the city had to identify the investment intended to be financed from the loan in a resolution of the general assembly, as well as its expected costs, supported by calculations, it had to declare its intention to borrow the loan and commit to incorporate the amount of the loan to be borrowed as well as its interest and principal instalments into its annual budget, to identify and encumber the amounts arising from wage and sales tax as collateral for the loan, and to authorize the mayor to proceed regarding the loan.<sup>30</sup> The relevant general assembly resolution had to be submitted by county cities together with the approval of the municipality of the county and cities with municipality rights directly to the interior minister, who decided in agreement with the minister of finances on the approval of the government resolution and the authorization of the loan. Thereafter, the cities presented to the loan issuing committee the resolution on the borrowing of the loan, bearing the approval of the governing authority, the notarized recognizance issued for the benefit of the creditor, the committee discussed the loan, then transferred the partial amount by a voucher bearing the countersignature of the authorized representative of the bank commissioned to lend the loan. The contemporaneous report did not only state enthusiastically that by the end of September 1925 loans in the amount of almost 2.5 million dollars had been lent to Hungarian cities and those localities that participated in the loan negotiations with all the necessary documents “*received the check in a matter of minutes*”, but also concluded that “*it is beyond doubt that the American dollars will efficiently enhance the cultural and economic development of Hungarian cities*”.<sup>31</sup>

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<sup>29</sup> The city of Kecskemét obtained development resources in another way. The city borrowed a loan of 10 billion gold koronas against a promissory note, which was lent by a large financial institution of Budapest, selected from several applicants, at an interest rate of 7.9 per cent, which was higher than that of the city loan, however, all commissions and other costs were waived (*Közgazdasági Krónika 1926:844*).

<sup>30</sup> The General Assembly of the city of Szolnok with regular council adopted its resolution accordingly, on the borrowing of a “repayment loan” with a nominal value of 2,000,000 gold koronas. Jász-Nagykun-Szolnok Archives of the National Archives of Hungary, (MNL JNSZML) V. 400. Files of the assembly of representatives of the city of Szolnok 9640/1925.; *Inántsý-Pap (1938:497)*.

<sup>31</sup> Magyarország, 20 September 1925.

**Table 1**  
**Amounts of the Speyer loan authorized for and provided to cities with municipality rights**

City with municipality right	Amount of the authorized loan in dollar	Received amount in pengő
Baja	500,000	2,329,199
Debrecen	900,000	3,941,747
Győr	1,008,073.40	4,777,505
Hódmezővásárhely	600,000	3,066,799
Miskolc	843,474.20	3,928,940
Pécs	887,040	4,024,163
Sopron	266,552	1,229,977
Szeged	1,495,000	7,113,400
Székesfehérvár	800,000	3,774,114
Total	7,299,139.60	34,185,844

Source: Inántsý-Pap (1938:499).

**Table 2****Amounts of the Speyer loan authorized and lent to county cities**

County cities	Amount of the authorized loan in dollar	Received amount in pengő
Békéscsaba	520,000	2,420,220
Budafok	275,862	1,362,165
Cegléd	194,000	878,309
Eger	500,000	2,390,680
Esztergom	345,000	1,594,164
Gyöngyös	446,609	2,088,734
Gyula	200,000	1,002,520
Hajdúböszörmény	5,000	22,138
Hajdúnánás	93,000	417,197
Hajdúszoboszló	120,975	568,904
Jászberény	30,000	149,506
Kalocsa	52,000	228,756
Kaposvár	365,000	1,544,513
Karcag	72,020	317,582
Kiskunfélegyháza	270,000	1,196,479
Kiskunhalas	124,136.40	618,493
Kispest	300,000	1,329,374
Komárom	78,300	368,972
Magyaróvár	27,600	122,236
Makó	172,000	762,201
Mezőtúr	160,000	797,108
Mohács	77,000	341,113
Nagykanizsa	527,083	2,530,960
Nagykőrös	116,862	551,301
Pápa	170,000	769,159
Pestszenterzsébet	346,000	1,567,630
Rákospalota	154,300	683,108
Salgótarján	135,000	597,095
Sátoraljaújhely	315,600	1,488,552
Szekszárd	210,000	973,954
Szentendre	40,000	175,235
Szolnok	332,453	1,494,603
Szombathely	603,860	2,757,933
Újpest	700,000	3,099,175
Vác	530,000	2,529,819
Veszprém	91,200	423,927
Total	8,700,860.40	40,163,815

Source: Inántsý-Pap (1938:499).

The cities received the amount of the loan in instalments and they were obligated to place the assigned amounts at member institutions of the Centre of Financial Institutions until these have been utilized for the specified purpose. Since the cities received the first tranche of the loan in the second half of September 1925, in most cases the planned investments could only be started in the spring of 1926. The localities tried to place the available and temporarily disposable amounts with local financial institutions or with local branches of national financial institutions (*Honvári 2004:53*). The cities elaborated ambitious plans for the implementation of their development concepts and they intended to spend the borrowed loans on a variety of purposes, primarily on infrastructural, communal and community investment projects. Accordingly, the concepts with the highest allocated amounts included railway construction, construction of schools, construction of water pipelines and sewage canals, construction of power plants, surfacing of roadways, construction of roads and bridges, establishment of port waterfront facilities, flood protection works, transport development (*Közgazdasági Krónika 1925:669*). Among developments aimed at the improvement of public health we find construction of hospitals, medical facilities for lung patients, maternity hospitals and disinfecting facilities, funeral plants and establishment of waste transport services. A substantial part of city development concepts was directly and indirectly related to tourism, accordingly, the cities intended to use the foreign loans not only for infrastructure development, but also for the construction of swimming pools, restaurants and blocks of rental apartments.<sup>32</sup>

The dominant part of the loans authorized for the individual cities by the governing authorities was constituted by income-generating investments, primarily aimed at urban development, the construction of public utilities and the acquisition of assets, but even the non-income-generating investments were considered infrastructural investments serving public health, science, education, culture and urban development. Accordingly, among cities of the Great Plane, in the scope of income-generating investments the city of Debrecen intended to spend the loan on housing construction, a sewage filtering plant, the expansion of waterworks, construction of a printing shop and a slaughterhouse, the establishment of a public cemetery and public sanitation company, while in the category of non-income-generating investments the construction of schools and the museum was planned. The city of Szeged intended to spend the majority of the loans on a railway with an economic function and on the construction of the university. Being a beneficiary of the second loan, the city of Hódmezővásárhely intended to start an income-generating investment aimed at surfacing of roadways, construction of rental housing and a hospital, purchase of land and construction of a coastal swimming pool, in addition, funds were allocated to the construction of schools. Békéscsaba

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<sup>32</sup> 8 órai újság 13 October 1925.

spent the borrowed loans on road construction, construction of bathhouses and bridges, a power plant and a hospital and on the construction of schools. Jászberény planned to spend the allocated loan amounts on the surfacing of roadways, Karcag wanted to finance a community house in the cinema as well as deep drilling, while Mezőtúr wanted to spend these funds on the reconstruction of the marketplace, the establishment of a horse farm and the construction of a city hall with stores. In Szolnok the Speyer loan was spent on the construction of a bathhouse and a slaughterhouse and on schools. In cities with municipality rights 77.83 per cent of all the disbursed loans were spent on income-generating and 22.17 per cent on non-income-generating investments, in the case of county cities 85.63 per cent of the received loans served purposes of income-generating investments and 14.37 per cent were spent on non-income-generating investments (*Inántszy-Pap 1938:505*).

The borrowing of the Speyer loans and the start of the investments enabled by them coincided with the short period of economic boom preceding the Great Depression; thus, the favourable impacts could strengthen one another both at local and national economy level. This is how a contemporaneous analysis assessed this period: *During the economic upturn Hungarian cities rushed to productive work as diligent bees and gladly accepted the offered loans, with special regard to the fact that this not only strengthened their existing sources of revenue, but also opened up new sources of revenue providing them with a lucrative yield. In fact, the cities spent those loans mainly on absolutely necessary and lucrative investments, so on the one hand the income from the investment abundantly covered the amounts spent on debt service, on the other hand, the investments resulted in a significant expansion of wealth. In addition, having entered the circulation of economic life, the loan amount also increased its strength, and therefore the loans fulfilled their functions in every respect, they started and continued their productive cycles*" (*Inántszy-Pap 1937:807*).

As a result of borrowing the foreign loans, between 1925 and 1928 the indebtedness of Hungarian cities continuously increased, by the autumn of 1933 the total loan stock of Hungarian cities reached 166,514,244 pengős, within which the share of cities with municipality rights totalled 96,180,829 and that of county cities 70,333,415 pengős (*Inántszy-Pap 1937:807–816*). The amount of principal and interest instalments falling due on the loan debts of cities was as high as 21,370,280 pengős; therefore, the burden of debt service was 13.31 per cent compared to the existing debt. However, this indebtedness was not really significant compared to either the level before the First World War or the assets of the localities, since in cities with municipality right this burden was 15.73 per cent of the assets in cities with municipality right, and 19.86 per cent in county cities. It may be a basis for comparison that at the same time the loan debts of Budapest Capital amounted

to 366,447,892 pengős; therefore, in the case of the capital city the ratio between debt and assets stood at 27.94 per cent.

Two of the 10 cities with municipality rights – the free royal cities of Debrecen and Szeged – had debts exceeding 20 million pengős, while two had debts between 20 and 10 million pengős, three under 10 million pengős and two under 5 million pengős. Among the 45 county cities (cities with regular council), with the exception of two cities – Szombathely and Nyíregyháza – the loan portfolio per one locality fell in the range within 5 million pengős, loan debts of 11 cities were between 2 and 5 million pengős, those of 13 localities between 1 and 2 million pengős, while 19 cities had a debt of under 1 million pengő. In terms of the sources of the loan stock, in 1933 slightly less than 50 per cent of the loans of Hungarian cities was related to foreign financial groups, and the overwhelming majority of foreign loans (87.4 per cent) were long-term ones, in which – naturally – a portion of about 13.3 million dollars still outstanding at the time of the loan borrowed from the Speyer Banking House represented a dominant ratio. The debt stock of cities denominated in foreign currency was primarily in American dollars, while the localities borrowed their loans in British pound and Swiss francs to a smaller extent. Of the cities with municipality rights, Debrecen (4 million) and Szeged (3 million) were the most heavily indebted, among county cities Eger was on top of the list with 640,321 dollars, while among the localities in the Great Plane Békéscsaba had a loan debt of 432,385, Cegléd 156,609, Gyula 164,268, Jászberény 23,728, Karcag 55,934, Mezőtúr 169,349, Nagykőrös 91,144 and Szolnok 268,274 dollars. One-fifth of county cities Balassagyarmat, Csongrád, Hajdúhadház, Kisújszállás, Kőszeg, Nyíregyháza, Szentes, Túrkeve and Zalaegerszeg – no longer had any debts to financial institutions denominated in a foreign currency. It can be determined from the data that cities without municipality rights could obtain foreign loans at more adverse conditions – usually with higher interest –, which can be attributed to the lower international awareness of the cities, the longer distance from the centres of financial institutions as well as the fact that the value of their assets and income-generating capacities were lower. However, a contemporaneous summary on the indebtedness of Hungarian cities tried to highlight that *“in most cases the significant amounts of the roles are coupled with outstanding active assets, and it may be a consequence of the fact that the great wealth enabled the borrowing of more significant loans, or perhaps, it was exactly the investments completed by the loans that widened the frames of the asset statement of the city”*, in other words *“it is therefore not possible to infer that the indebtedness of the city is favourable or adverse merely from the amount of the loan, or even from the per capita value of the loan”* (Bene 1935:94–95). In addition, a city that failed to take the opportunity of borrowing may have missed its chance to implement major economic, public health investments, while cities that seemed heavily in debt according to primary

data could implement developments improving the quality of life of their citizens or acquired significant productive assets exactly with the help of foreign loans.

When servicing the debt, cities affected by the mortgage loan paid their revenues encumbered for the purpose of interest and principal repayment during the term of the existence of the loan – under the supervision of the regional royal Hungarian tax office – onto a special checking account of the savings bank, from which the amount was transferred to the account of the Magyar Nemzeti Bank. The Magyar Nemzeti Bank transferred the amount equalling the semi-annual annuity and the commission to the Speyer Banking House in dollars, through the trustee bank. The financial difficulties caused by the international economic crisis resulted in changes in the repayment of the Speyer loans as well. On 23 December 1931 the Hungarian Government ordered a transfer moratorium in order to save the gold and foreign currency stocks of the country; it prohibited the payment of existing foreign debts in foreign currency.<sup>33</sup> Under this order, the collected repayments of the city loans were transferred by the Magyar Nemzeti Bank to the Fund of Foreign Creditors, then the domestic bondholders could freely redeem their coupons from these amounts, while the value of coupons of foreign bondholders presented for the purpose of redemption was transferred to a blocked pengő account.

In terms of loan amortization, the cities were hit by the economic crisis to varying degrees, the most severe problem was the drying-up of additional city taxes, the decrease of the revenues of the city, but owing to the proportionately bigger drop in agricultural prices, the recession affected agricultural communities, cities in the Great Plane more deeply (*Makó 2015:96–97*). In 1929-30 a significant part of Hungarian cities were no longer primarily frustrated by the burdens arising from the long-term Speyer loan, rather by the credit facilities that carried much higher interests (*Solymár 1989:103–138*). The economic crisis had a negative impact on the prices of the bonds of the Speyer loan as well, at the end of 1928 the price of the first bonds was as high as 98 per cent; however, in 1931 it dropped to 30 per cent, then following the crisis, until the end of the 1930s, it showed an increasing trend, with fluctuating prices (*Kallós 1928:83–84*). In January 1938 – while the general sentiment of the stock exchange was optimistic – in the market of unlisted fixed income papers the price of the Speyer bonds stood at 85.25 per cent; however, by May the prices dropped by 15 per cent and the Speyer bonds fell back to 67 per cent.<sup>34</sup> The cities affected by the loan contract and struggling with loan amortization problems raised the idea of purchasing back the bonds with reduced prices in a big volume as early as 1932, or the conversion of the loan and the reduction of interest, but the financial ministry did not authorize this solution (*Makó 2015:99*). In several

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<sup>33</sup> Decree with M.E. no. 6.900/1931., on the payment of certain debts to foreign parties in pengő value. Repository of Hungarian Decrees 1931 Volume 65, Royal Hungarian Ministry of the Interior Budapest, 1932 pages 1549–1551.

<sup>34</sup> Az Újság 16 January 1938. Volume XIV no. 12; Az Újság 8 May 1938. Volume XIV issue 103.

localities facing a difficult situation it was hoped that if they had possessed an appropriate amount of cash, they could even pay off the Speyer loans at one quarter of the original price, and by this the cities would get rid of not only the “*suffocating loan*”, but also “*the burden of paying high interests for a term of 10–20 years*”.<sup>35</sup>

Parallel with the deepening of the economic crisis, increasingly radical government actions had to be implemented regarding the foreign loans as well. On 28 February 1933, the Ministry of finances suspended the principal repayments of debentures and other bonds and reduced the debt service of the loans to 5 per cent.<sup>36</sup> Finally, on 22 January 1936 the government ordered the conversion of the mortgage bonds into securities held by domestic parties, under which “[...] *any payment to be made against a coupon of a debenture or bond [...] shall be allowed only if the share, the debenture or the bond is in the possession of a domestic party, and the person presenting this coupon certifies this in the manner defined by the Magyar Nemzeti Bank*”.<sup>37</sup> As a result of this process, the bonds of city loans were acquired by domestic parties to an extent of approximately 60 per cent, while the Magyar Nemzeti Bank had to spend less foreign currency on the redemption of the coupons (*Inántszy-Pap 1938:510*). Under the original agreement, the Speyer Banking House redeemed the maturing interest coupons from the debt service amount transferred to it by the Magyar Nemzeti Bank semi-annually, the part remaining after the redemption of the coupons was spent on amortization of principal, by selecting bonds with a face value corresponding to this amount by drawing lots and redeeming them at face value. However, owing to the transfer decree of 1931, the bank could not receive the debt service amount in dollars; therefore the selection of the bonds by drawing lots was cancelled. The last draw was held on 13 April 1932 for bonds of the year 1925, and on 7 October 1931 for bonds of the year 1926. The bonds were still redeemed in the first and second half of 1932, but after that only the Magyar Nemzeti Bank was allowed to redeem the maturing coupons. In order to preserve the creditworthiness of the country in the international money market, the financial government committed to pay an interest of 1.75 per cent on the interest coupons of the bonds to foreign creditors, in foreign currency. Accordingly, domestic creditors received an interest of 5 per cent in pengő, and of the foreign creditors those who intended to collect the interests in pengő also received an interest of 5 per cent on their blocked accounts, while those foreign creditors who intended to collect the interests in dollars only received an interest of 1.75 per cent (*Inántszy-Pap 1938:511*).

<sup>35</sup> Esztergom és Vidéke, 24 January 1932.

<sup>36</sup> Decree with P.M. no. 450/1933 on the definition of the measure of the deposit obligation imposed in Decree with M.E. no. 6.900/1931 on the payment of certain debts to foreign parties in pengő value. Budapesti Közlöny, Volume 67 issue 48, 28 February 1933 1–2 pp. 48. szám 1933. február 28. 1–2. p.

<sup>37</sup> Decree with M.E. no. 300/1936 on the prohibition of the import of securities, on new regulation of the redemption of the dividend coupons of shares, coupons of debentures and bonds and the payment of debts from the purchase price of goods to foreign parties in pengő. Pénzügyi Közlöny (Financial Gazette), 1936, issue 4, 01 February 1936 pages 17–19.

Hungarian cities remained heavily indebted in the decade following the economic crisis as well, the amortization of the borrowed loans remained a serious burden on the finances of local governments. The contemporaneous analysis dealing with the loan debts of cities drew light on the fact that – even though a ratio of 26 per cent between the assets of the city and the burden of the loan is not a problem – the profitability of the assets owned by the local governments and the income-generating capability of the localities are extremely low, given the current financial conditions, they can only obtain extremely adverse credit facilities for covering their operating expenses; therefore, they have no meaningful options to reduce their debts permanently. “[...] *Our cities of the countryside are in a much more adverse situation when it comes to fulfilling their credit needs than any other economic community*”, because “*a significant part of our cities have no appropriate capitals, reserve stocks or surplus cash; therefore, even the smallest disruption of the regime of expenses and revenues would generate quite serious disturbances and difficulties in the finances of the cities*” (Drághfy 1941:73–76). From this he has arrived at the conclusion that “*it is necessary to establish the rural cities’ own credit institution, which will serve the relevant needs in an appropriate manner, much more perfectly than the current conditions*” (Drághfy 1941:83). The cities tried to get rid of the burden of two decades according to the basic contract of the Speyer loan, some localities attempted to repurchase the loan bonds at a low price during the economic crisis and then after the Second World War, by borrowing new loans or selling their real properties, but these efforts failed (Dobrossy 1996:445–446). The majority of the localities that received a part of this loan were unable to repay the borrowed amounts by the original maturity, as a result of the Second World War and the economic and political processes that followed it, the fulfilment of tasks relating to foreign debt service were placed under a new system of conditions and central direction. Long-term loans originating from the era before 1945 and not repaid to foreign financiers – including the Speyer loan – were settled by the Hungarian government in the three decades between 1950 and 1970, in the form of bilateral financial agreements.

## 5. The impact and afterlife of the loans

One decade after the first disbursements the positive and negative impacts of the city loans borrowed after 1925 were clearly noticeable. As a result of the loans, several public utility developments, infrastructural, public-health, cultural, educational investments were implemented in the Hungarian cities that the localities simultaneously struggling with a shortage of funds and the need to modernize, would only have accomplished relying on their own resources with great difficulties, if at all. The newly built institutes, rental buildings, hotels, roads significantly changed the cityscape in Hungarian cities, their structures were modernized, as a result of the public utility developments, public health, educational and cultural

investments the quality of services provided by the localities increased significantly and the quality of life of the residents improved. The loans provided funds for the necessary developments, they terminated development gaps of several decades and formed the cityscapes of Hungarian cities in a future-proof manner; therefore, this period deserves to be considered a progressive era from the aspect of the elaboration of ambitious urban development concepts of the 20th century as well. Many investments served representative urban development aims motivated by ideological considerations, they also had emotional roots. We can agree with the contemporaneous summary assessing the borrowing of the loan that stated: *“Although the debt service of the Speyer loan imposed a noticeable burden on the cities, they were still willing to participate in the borrowing of the loan, because they were aware of the fact that this is how they can identify and construct the path of progress, and that this loan will enable them to utilize the unused resources available for them for the accomplishment of national aims”* (Inántszy-Pap 1938:516).

In several localities there were many debates even at the time of the borrowing of the loans, and there were cities where the investments launched from the loan exceeded the capacities of the community. It happened that the beneficial impact of the large investments on local enterprises did not prove to be enduring, and the companies owned by the city did not generate appropriate revenues despite the preliminary calculations. It can be presumed that the body of city officers were not always prepared for the fulfilment of the tasks related to the handling, utilization of the incoming loans and the coordination of the started investments either. As soon as the loans were disbursed, problems occurred concerning the legitimate utilization of the amounts and there were cities where the interior minister ordered strict investigations: *“Speyer disciplinary actions all over the country”* – was the headline of the newspaper Magyarország on 11 April 1928. The unjustifiably high number of developments could often only be completed by borrowing new loans, which could lead the cities into loan traps that could result in bankruptcy, insolvency or even the forced sale of the real properties of the city (Dobrossy 1996:426–445). The professional literature has so far noticeably somewhat neglected those cities (e.g. Esztergom, Szolnok, Kaposvár), where serious problems, economic frauds and political scandals raised their ugly heads regarding the utilization of the foreign loans (Vécs 1931:64). However, basic and exploratory research on the “afterlife” of the loans – which can be primarily reconstructed from the contemporaneous press and the records of litigations of the time – are yet to happen for the most part and since such research works would go beyond the scope of this study, these matters could even define a new direction for the research on the utilization of the loans during the interwar years.

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