FOLLOWING IN SCOTTISH FOOTSTEPS:

THE AMALGAMATION MOVEMENT IN

ENGLISH AND WELSH BANKING, 1870-1920

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ABSTRACT

The Amalgamation Movement was an outbreak of bank mergers and acquisitions in England and Wales that began around 1870, lasted for half a century and transformed the English and Welsh banking industry into a concentrated oligopoly dominated by five banks. This Amalgamation Movement was a response to the economic growth unleashed by the Industrial Revolution. For the first time ever, a human population was experiencing a sustained increase in its per-capita incomes. Economic growth like this made the British one of the wealthiest people on earth but it also gave rise to a monetary problem. An expanding post-Industrial Revolution British economy required a growing money supply to finance the increase in the value of the transactions undertaken. However, the supply of precious metals available to fashion into gold and silver coins was finite. Post-Industrial Revolution Britain had to erect its money supply on a foundation of credit and the obligation to furnish much of that credit ultimately fell upon the domestic banks. The solvency of the banking system became a vital economic consideration under these circumstances.

The Amalgamation Movement secured monetary stability by putting the banking industry in England and Wales under the control of five well-resourced and effective bureaucracies. Large banks subject to good administration maintained public confidence in a money supply composed of a growing proportion of bank deposits. Bank amalgamations also compensated for the loss of the inland bill of exchange, a financial security that was the English and Welsh banking industry's favourite reserve asset prior to 1870. Finally, the Amalgamation Movement accommodated the banking industry's conversion to a regime of limited liability during the 1880s. Britain acquired one of the safest banking systems in the world because of the Amalgamation Movement. The run of monetary good fortune continued until a global financial crisis in 2007/08 exposed the dangers inherent in Britain's overreliance on large banking institutions deemed to big to fail.

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v. I acknowledge the support I have received for my research through the provision of an Australian Government Research Training Program Scholarship.

Signed at Adelaide, South Australia

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Signature: ____

Philip Andrew RITSON

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GLOSSARY

Affiliate A bank controlled by another bank by means of share ownership. An affiliate remained a separated bank and was its parent bank's subsidiary.

Bank amalgamation A merger that removed the target from the banking industry. The predator absorbed most or all of the target's assets and liabilities before liquidating it.

Bank of deposit A bank that did not issue bank notes.

Bank of issue A bank that issued bank notes.

Big Five The five largest English and Welsh banks created by the Amalgamation Movement.

Bill of exchange An unconditional written order addressed by a drawer to a drawee requiring the drawee to pay on demand or at a fixed or determinable date a certain sum to a payee or to a payee's order or to the bearer. The drawee becomes the bill's acceptor by indicating a willingness to obey the order.

Correspondent The product of a principal-agent relationship whereby banks transacted business on each other's behalf in their local districts. London banks generally acquired country correspondents and acted as their agents in the Metropolis.

Country bank An English and Welsh bank that had no banking offices in London.

Economies of scale Reductions in average unit cost realised when a firm manufactures a solitary product in greater numbers.

Economies of scope Reductions in average unit cost brought about by a proliferation in the range of products manufactured.

Fiat currency Money reliant on government edict, law and/or custom to function as a means of payment and a store of value. Fiat currency has no intrinsic worth and its issuer has no obligation to redeem it.

Fixed costs Operating expenses incurred irrespective of the level of output produced.

Gross Domestic Product All the income generated over a period within a geographical area by the labour, land and capital located there.

Gross National Product All the income earned over a period by the residents of a geographical area utilising their labour and all the land and capital they own. Unlike Gross Domestic Product, Gross National Product includes the income derived from nett foreign investments.

Guarantee and suretyship association An institution that guaranteed the good conduct and fidelity of persons put in positions of trust and responsibility.

Horizontal integration Growth in the size of a firm brought about by expansion at the same level in the value chain. A firm integrates horizontally when it takes its competitors over.

Inland bill of exchange A bill of exchange drawn and payable within the British Isles and Ireland or drawn within the British Isles and Ireland upon some person resident therein.

Law of diminishing returns A principle in modern economics that states the extra output generated by an increase in one factor of production will diminish if the other factors of production remain constant.

Legal personality A privilege bestowed on natural and artificial persons that allows them to pursue or defend legal actions in a court of law. A corporation has a legal personality whereas a partnership does not.

Liquid assets Cash and other assets capable of conversion into cash at little cost and at relatively short notice.

Malthusian poverty trap A situation in which demographic growth causes mass poverty. Average living standards vary little between geographical locations and remain unchanged over the long-term in a Malthusian poverty trap because the population always grows until it exhausts the means of sustenance available to it.

Partnership A common law arrangement in which two or more people undertake a business in common and share in any profits or losses made. Partnerships are unincorporated entities. An association incorporated under an act of parliament or a royal charter is not a partnership.

Predator A bank that took another bank over during the Amalgamation Movement.

Private bank An English or Welsh bank operated as a sole proprietorship or a common law partnership.

Promissory note made payable to the bearer on demand A bank note that relied upon the issuer’s obligation to redeem it at call to function as money.

Transaction cost A cost (other than the price paid) imposed by a market exchange.

Target A bank taken over by another bank during the Amalgamation Movement.

Unincorporated joint stock company An amalgam of the laws of partnership, trust and agency. A quasi-corporation that replicated some of the advantages of incorporation (such as issuing transferable shares) without the need for an act of parliament or a royal charter.

Vertical integration Growth in the size of a firm brought about by expansion at different levels in the value chain. A firm integrates vertically when it takes its suppliers and/or its distributors over.

CHAPTER ONE

INTRODUCTION: BRITAIN'S ECONOMY DURING THE AMALGAMATION MOVEMENT

> This sudden transformation of the leading and most dynamic industrial economy into the most sluggish and conservative in the space of thirty or forty years ... is the crucial question of British economic history.[1]

This thesis examines the Amalgamation Movement, an outbreak of bank mergers and acquisitions in England and Wales that began around 1870, lasted for 50 years and laid the foundations of the twentieth-century British banking industry. The Amalgamation Movement transformed English and Welsh banking into an oligopoly dominated by the 'Big Five' who accounted for 80 per cent of the deposits taken.[2] The Big Five were the National Provincial Bank, the Westminster Bank, the Midland Bank, Lloyds Bank and Barclays Bank.[3] By 1909, every one of those five banks ranked amongst the ten biggest banks in Europe.[4]

Joseph Sykes undertook the last comprehensive analysis dedicated exclusively to the Amalgamation Movement in 1926.[5] Scholarship undertaken in the fields of economics, business, management and banking over the intervening eight decades offers contemporary historians insights into the Amalgamation Movement denied to Sykes in 1926. Significantly, Sykes's study also failed to explain why the Amalgamation Movement happened. Much of the subsequent historiography

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[1] Eric J. Hobsbawm, *Industry and Empire: From 1750 to the Present Day* (London: Penguin, 1999), 156.
[2] "Bank fusions and credit facilities: A lecture by Mr. F. E. Steele," *The Times*, 20 November 1919; Forrest Capie and Ghila Rodrik-Bali, "Concentration in British banking, 1870-1920," *Business History* 24, no. 3 (1982): 286.
[3] Joseph Sykes, *The Amalgamation Movement in English Banking, 1825-1924* (London: P. S. King and Son, 1926), 196-214.
[4] Youssef Cassis, "Management and strategy in the English joint stock banks, 1890-1914," *Business History* 27, no. 3 (1983): 302.
[5] Sykes, *The Amalgamation Movement in English Banking.*

dedicated to the late nineteenth-century and early twentieth-century British has done much the same thing. The question as to why English and Welsh banks amalgamated in the first place remains largely unanswered. This thesis attempts to answer that question and in so doing it reaches the following conclusions.

1. A financial crisis in 1825/26 demonstrated the small banks established in England and Wales during the Industrial Revolution constituted a threat to Britain's financial stability.
2. Those who participated in the Amalgamation Movement drew upon a precedent. Scottish experience suggested bigger banks were more likely to survive financial crises than the smaller ones found in England and Wales because they were less vulnerable to runs.
3. The limits imposed on the English and Welsh bank note issue by the *Bank Charter Act* of 1844 delayed the Amalgamation Movement by two decades. English and Welsh banks of issue would not amalgamate until the lucrative right to issue bank notes lost its significance to them.
4. The demise of the inland bill of exchange turned participation in the Amalgamation Movement into a necessity for many banks. The demise of the inland bill of exchange forced banks to seek amalgamation partners to affect a rational distribution of the banking system's liquid asset reserves.
5. The adoption of limited liability in the 1880s accelerated the rate of bank amalgamations. Limited liability removed an important safeguard of the creditors' interests by placing limits on the amount the proprietors would contribute when a bank failed. Large banks with ample reserves acquired competitive advantages because creditors deemed them less likely fail.

The conclusions listed above share a common theme. The stability of English and Welsh banking industry became a pressing consideration during the nineteenth century because post-Industrial Revolution Britain erected its growing money supply on a foundation of bank credit. Banks had to assure their creditors that they could

meet their obligations under these circumstances and the Amalgamation Movement played its part in furnishing that assurance.

This thesis draws upon primary and secondary sources to construct a narrative account of the Amalgamation Movement. However, one thing the reader will notice is the relative absence of archival material produced by the amalgamating banks themselves. One reason for the omission becomes apparent when one considers the nature of the banking industry. Most of a bank's assets were loans and advances with fixed or indeterminable maturity dates. Most of its liabilities were repayable at call or at short notice. A bank's survival depended on its creditors' confidence because those creditors could destroy the bank if they panicked and orchestrated a run on it. In addition, a bank amalgamation was a commercial transaction involving the sale of a business. A target's officers had a duty to their proprietors to maximise the amount paid by a potential predator and to express confidence in their bank's prospects even when they were negotiating the sale of its business to another bank. Bankers did not to admit their bank's failings in public for good reason and if they held such conversations in private, they rarely committed what they said to paper. A historian perusing the archival material produced during the Amalgamation Movement looking for a tacit exposition of the weaknesses a bank amalgamation was supposed to rectify will meet with disappointment.[6] One has to deduce the reasons for bank amalgamations from the economic, institutional and business contexts in which they occurred and from commentaries about the health and security of the banking industry produced at the time.

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[6] The author visited the archives of the Royal Bank of Scotland Group, Barclays Bank, Lloyds Bank, the Hongkong and Shanghai Banking Corporation and the Bank of England.

This chapter puts the Amalgamation Movement into its historical and economic context. This thesis investigates the reorganisation of the banking industry in a country with a remarkable economic and business history. The Industrial Revolution made Britain one of the first countries in the world to escape the Malthusian poverty trap.[7] This revolution also stimulated the demand for banking services, which resulted in a proliferation of the number of banks in the British Isles. Later in the nineteenth century, other countries industrialised too and began to compete with the British in the global marketplace. Consequently, the English and Welsh Amalgamation Movement occurred at a time when Britain's manufacturers lost some of the advantages early industrialisation bestowed upon them. Britain's manufacturers compounded their difficulties during this period by remaining wedded to the industries and technologies they inherited from the Industrial Revolution. The United States and Germany embraced the emerging technologies of the day more readily than the British did. Economic and business historians have expended much effort trying to account for the change in British manufacturing's fortunes after 1870, but one of them made an observation that is pertinent to this thesis. Alfred DuPont Chandler argued British manufacturing struggled after 1870 because British firms were too small. Chandler's depiction of Britain as a land populated by small firms clearly did not apply to the English and Welsh banking industry. The Amalgamation Movement yielded some of the biggest banks in world.

[7] Donald N. McCloskey, "Ancients and moderns," *Social Science History* 14, no. 3 (1990): 296; Jack A. Goldstone, "Efflorescences and economic growth in world history: Rethinking the "Rise of the West" and the Industrial Revolution," *Journal of World History* 13, no. 2 (2002); Gregory Clark, *A Farewell to Alms: A Brief Economic History of the World* (Princeton: Princeton Univeristy Press, 2007), 1-2; Deirdre N. McCloskey, *Bourgeois Dignity: Why Economics Can't Explain the Modern World* (University of Chicago Press, 2010), 1-9.

The Amalgamation Movement is a paradox. Britain's small manufacturing firms thrived prior to 1870 only to experience declining fortunes afterwards. In contrast, the Amalgamation Movement changed the English and Welsh banking industry's fortunes for the better. The small banks erected in England and Wales during the Industrial Revolution proved susceptible to financial crises; and yet, by 1920 a post-Amalgamation Movement English and Welsh banking industry was one of the most stable in the world.

SECTORAL CHANGES IN BRITAIN

For much of recorded history, an average human being consumed an annual real Gross Domestic Product (GDP) per capita[8] that had changed little since the Neolithic Revolution.[9] During the pre-industrial age, growing prosperity normally induced an increase in the number of mouths demanding nourishment.[10] Good harvests, technological breakthroughs or some other stroke of economic good fortune might yield higher standards of living in the short term but eventually population growth would erode any economic gains made. The rich always consumed more than their average share of what was available during this period but wealthy landowners like *Pride and Prejudice*'s William Darcy "were few" and "the poor plentiful."[11] Life really could be "nasty, brutish and short"[12] for a predominately agricultural workforce enduring inescapable poverty. Jane Austen (1775-1815) wrote *Pride and*

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[8] Real GDP adjusts for the effects of inflation. Real GDP per capita is a measure of the goods and services an average person produced and consumed. Stanley Fischer and Rudiger Dornbusch, *Economics*, International student ed. (Tokyo: McGraw-Hill International, 1983), 551-54.
[9] Clark, *A Farewell to Alms*: 1-2.
[10] Thomas Robert Malthus, *An Essay on the Principle of Population*, vol. 1 (New York: Cosimo Classics, 2013).
[11] Clark, *A Farewell to Alms*: 2.
[12] Thomas Hobbes, *Leviathan* (Harmondsworth Penguin, 1968), 186.

Prejudice during the Industrial Revolution.[13] According to Eric Hobsbawm, this novel was the product of a society undergoing "the most fundamental transformation of human life in the history of the world recorded in written documents."[14] The average Briton's standard of living has improved dramatically since the publication of *Pride and Prejudice*.[15]

During the Industrial Revolution, workers left the countryside to find work in an urban manufacturing economy to turn Britain into 'the workshop of the world.'[16] People knew Britain was changing at the time although few really understood just how profound the changes would be or whether they would last. As early as 1814, the merchant, statistician and magistrate Patrick Colquhoun (1745-1820) considered it "impossible to contemplate the progress of manufactures in Great Britain within the last thirty years without wonder and astonishment."[17] By 1844, Friedrich Engels (1820-1895) could argue the Industrial Revolution "altered the whole [British] civil society."[18] In the 1880s, Arnold Toynbee (1852-1883) finally introduced the term 'Industrial Revolution' to his British audience before telling them that this revolution was one of the most important events in their history.[19] The bankers engaged in the Amalgamation Movement should have known Britain's manufacturing industries

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[13] Jane Austen, *The Novels of Jane Austen: Pride and Prejudice*, Third ed., vol. Two (London: Oxford University Press, 1965); Igor Webb, *From Custom to Capital: The English Novel and the Industrial Revolution* (Ithaca: Cornell University Press, 1981).
[14] Hobsbawm, *Industry and Empire*: xi.
[15] Angus Maddison, *Dynamic Forces in Capitalist Development: A Long-Run Comparative View* (Oxford: Oxford University Press, 1991), 6-7; McCloskey, *Bourgeois Dignity: Why Economics Can't Explain the Modern World*: 117-19.
[16] Christopher M. Law, "The growth of urban population in England and Wales, 1801-1911," *Transactions of the Institute of British Geographers*, no. 41 (1967); Raphael Samuel, "Workshop of the world: Steam power and hand technology in mid-victorian Britain," *History Workshop Journal* 3, no. 1 (1977).
[17] Patrick Colquhoun, *A Treatise on the Wealth, Power and Resources of the British Empire* (London: Joseph Newman, 1814), 68.
[18] Friederich Engels, *The Condition of the Working Class in England in 1844* (Oxford: Basil Blackwell, 1958), 1.
[19] Arnold Toynbee, *Lectures on the Industrial Revolution in England* (London: Rivingtons, 1884), 85.

changed Britain beyond all recognition. However, Joseph Chamberlain's (1836-1914) campaign for tariff reform at the turn of the twentieth century also suggests the Amalgamation Movement coincided with a time when British manufacturing faced an uncertain future.[20] In 1903, Chamberlain lamented:

> We were to … lose those industries for which the country has been so celebrated, and which have made it great and prosperous in the past, and deal with inferior subsidiary industries. Sugar has gone. Let us not weep for it. Jam and pickles remain! Now, of all these workmen, these intelligent artisans, who were engaged tending and making the machinery for sugar refining in this country, I would like to know how many have found a resting-place, have found equivalent ages and comfort, in stirring up jam-pots and bottling pickles.[21]

The notion that Britain's manufacturing economy was suffering from relative decline became a recurring feature of British political debate during the twentieth century.[22]

The question as to what a government might do to restore Britain's economy to good health determined the outcome of at least two general elections after World War II. Harold Wilson's (1916-1995) Labour Party prescribed a collectivist solution, state interventionism modelled on French *dirigisme*, to win the first in 1964. Margaret Thatcher's (1925-2013) Conservatives put their faith in markets and self-interested individualism to win the second in 1979.[23] One could argue things only

[20] Sydney H. Zebel, "Joseph Chamberlain and the genesis of tariff reform," *Journal of British Studies* 7, no. 1 (1967); A. W. Coats, "Political economy and the tariff reform campaign of 1903," *Journal of Law and Economics* 11, no. 1 (1968).

[21] Samuel Henry Jeyes, *Mr. Chamberlain: His Life and Public Career*, vol. 2 (London: Gresham 1904), 330.

[22] David Edgerton, "The decline of declinism," *The Business History Review* 71, no. 2 (1997); Richard English and Michael Kenny, "British decline or the politics of declinism," *The British Journal of Politics & International Relations* 1, no. 2 (1999); Jim Tomlinson, "Thrice denied: 'Declinism'as a recurrent theme in British history in the long twentieth century," *Twentieth Century British History* 20, no. 2 (2009).

[23] "Labour Party conference: Mr. Wilson's four points for harnessing science," *The Times*, 2 October 1963; "Labour's prospectus," *The Times*, 12 September 1964; "The choice for the country," *The Times*, 30 April 1979; Geoffrey Howe, "The slow, sure path to prosperity," *The Times*, 30 April 1979; Jim Tomlinson, "Inventing 'decline': The falling behind of the British economy in the postwar years," *The Economic History Review* New Series 49, no. 4 (1996): 732; Andrew Blick, "Harold Wilson, Labour and the machinery of government," *Contemporary British History* 20, no. 3 (2006): 344-54; David

started to go wrong for the British economy after World War II. Some historians claim misguided government policy, incompetent management and belligerent trade unionists undermined the British economy's competitive strength after 1945.[24] Other historians detect the first signs of decline at an earlier date. They argued the late-Victorian economy experienced a 'climacteric' caused by *laissez-faire* government policy, complacency, entrepreneurial failure, a reluctance to embrace emerging technologies or to adopt new methods of organisation, excessive investment abroad and an inappropriate system of education and training.[25]

The British manufacturing economy's share of total employment peaked in the 1870s, then embarked upon a slow decline and finally collapsed because of the

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Harvey, *A Brief History of Neoliberalism* (Oxford: Oxford University Press, 2007), 55-63; Tomlinson, "Thrice denied," 235-36.

[24] Nicholas F. R. Crafts, "Reversing relative economic decline? The 1980s in historical perspective," *Oxford Review of Economic Policy* 7, no. 3 (1991); Maurice W. Kirby, "Institutional rigidities and economic decline: Reflections on the British experience," *The Economic History Review* New Series 45, no. 4 (1992); Timothy Whisler, *The British Motor Industry, 1945-94: A Case Study in Industrial Decline* (Oxford: Oxford University Press, 1999); Nicholas Comfort, *The Slow Death of British Industry: A Sixty-Year Suicide, 1952-2012* (London: Biteback Publishing, 2012).

[25] E. H. Phelps Brown and S. J. Handfield-Jones, "The climacteric of the 1890's: A study in the expanding economy," *Oxford Economic Papers* New Series 4, no. 3 (1952); Eric J. Hobsbawm, *Industry and Empire: From 1750 to the Present Day* (London: Weidenfeld and Nicolson, 1969); David S. Landes, *The Unbound Prometheus: Technological Change and Industrial Development in Western Europe from 1750 to Present* (London: Cambridge University Press, 1969); Nicholas F. R. Crafts, "Victorian Britain did fail," *The Economic History Review* New Series 32, no. 4 (1979); Sidney Pollard, "Capital exports, 1870–1914: Harmful or beneficial?," *The Economic History Review* New Series 38, no. 4 (1985); William P. Kennedy, "Economic growth and structural change in the United Kingdom, 1870-1914," *The Journal of Economic History* 42, no. 1 (1982); Bernard Elbaum and William Lazonick, "The decline of the British economy: An institutional perspective," *The Journal of Economic History* 44, no. 2 (1984); Bernard Elbaum and William Lazonick, "An institutional perspective on British decline," in *The Decline of the British Economy*, ed. Bernard Elbaum and William Lazonick (Oxford: Oxford University Press, 1986); Correlli Barnett, *The Audit of War: The Illusion and Reality of Britain as a Great Nation* (London: Macmillan, 1986); Sidney Pollard, *Britain's Prime and Britain's Decline: The British Economy 1870-1914* (London: Edward Arnold Publishers, 1989); Bernard Elbaum, "Cumulative or comparative advantage? British competitiveness in the early 20th century," *World Development* 18, no. 9 (1990); Martin J. Wiener, *English Culture and the Decline of the Industrial Spirit*, Second ed. (Cambridge: Cambridge University Press, 2004).

deindustrialisation of the late twentieth century.[26] Services accounted for most of Britain's employment growth since 1870.[27] One part of the British services economy proved extraordinarily resilient during this period. An imaginary line drawn around Lancashire and Yorkshire's West Riding enclosed the world's preeminent industrial region in 1860. At the same time, the City of London was the world's leading financial centre. By 1990, deindustrialisation had stripped Lancashire and the West Riding of most of their manufacturing capacity but London continued to rank alongside New York and Tokyo as one of the world's great financial centres.[28] The economic historian William Rubinstein once suggested the things the City of London does well (services, finance, commerce and trade) have always constituted Britain's core economic strengths. According to Rubinstein:

> Britain's was *never* fundamentally an industrial and manufacturing economy; rather, it was *always*, even at the height of the Industrial Revolution, essentially a commercial, financial, and service based economy whose comparative advantage ... lay with commerce and finance.... Britain's industrial decline ... can be seen, with greater accuracy, as a transfer of resources and entrepreneurial energies into other forms of business life.[29]

This thesis examines one of Rubinstein's alleged transfers of 'resources and entrepreneurial energies into other forms of business life.' The English and Welsh banking industry expanded rapidly during the Industrial Revolution as every city or

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[26] Stephen N. Broadberry, "How did the United States and Germany overtake Britain? A sectoral analysis of comparative productivity levels, 1870-1990," *The Journal of Economic History* 58, no. 2 (1998): 385; Tomlinson, "Thrice denied," 240.
[27] Colin Clark, *The Conditions of Economic Progress* (London: Macmillan, 1940); Martin Wolfe, "The concept of economic sectors," *The Quarterly Journal of Economics* 69, no. 3 (1955); Broadberry, "How did the United States and Germany overtake Britain?; Broadberry, "Explaining Anglo-German productivity differences in services."; Yasusada Murata, "Engel's law, Petty's law and agglomeration," *Journal of Development Economics* 87, no. 1 (2008).
[28] William D. Rubinstein, *Capitalism, Culture, and Decline in Britain, 1750-1990* (London: Routledge, 1993), 36-40. See also: Youssef Cassis, "British finance: Success and controversy," in *Capitalism in a Mature Economy: Financial Institutions, Capital Exports and British Industry*, ed. J. J. Van Helten and Y. Cassis (Aldershot: Edward Elgar, 1990), 2.
[29] Rubinstein, *Capitalism, Culture, and Decline in Britain*: 24. Italics in original.

town of any significance in England and Wales acquired at least one private bank.[30] At the time, these private banks were small-scale affairs because the law limited every one of them to a maximum of just six members.[31] The typical English and Welsh bank had changed little prior to the Amalgamation Movement. As late as 1860, most of the 397 banks in England and Wales were organisationally no more sophisticated than their predecessors during the Industrial Revolution were because 300 of them were private banks. The average English and Welsh bank only possessed 3.1 branches in 1860.[32] The Amalgamation Movement changed the face of English and Welsh banking industry beyond all recognition. By 1920, the Big Five banking corporations dominated the English and Welsh banking industry. These five banks administered national branch networks made up of hundreds of branches from their head offices in London.[33]

The Amalgamation Movement's reorganisation of the English and Welsh banking industry was an atypical event given what was happening to the rest of the British economy during this period. The next section explains the English and Welsh banking industry embarked upon its period of radical change at a time when much of Britain's economy appeared to lose some of the dynamism it had exhibited during the Industrial Revolution. Some historians have argued the period 1870-1920 coincided with the onset of Britain's relative economic decline.

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[30] Francis Baring, *Observations on the Establishment of the Bank of England and on the Paper Circulation of the Country* (London: Sewell, Cornhill and Debrett, 1797), 15.
[31] L. S. Pressnell, *Country Banking in the Industrial Revolution* (Oxford: Clarendon, 1956).
[32] Philip L. Cottrell, *Industrial Finance 1830-1914: The Finance and Organization of English Manufacturing Industry* (London: Methuen & Co., 1979), 16; Lucy Newton and Philip L. Cottrell, "Joint-stock banking in the English provinces 1826-1857: To branch or not to branch?," *Business and Economic History* 27, no. 1 (1998); Shizuya Nishimura, *The Decline of Inland Bills of Exchange in the London Money Market, 1855-1913* (Cambridge: Cambridge University Press, 1971), 80.
[33] Sykes, *The Amalgamation Movement in English Banking*; Capie and Rodrik-Bali, "Concentration in British banking."; Richard S. Grossman, "Rearranging deck chairs on the Titanic: English banking concentration and efficiency, 1870–1914," *European Review of Economic History* 3, no. 3 (1999).

RELATIVE ECONOMIC DECLINE?

Rondo Cameron once claimed the Industrial Revolution was "a long drawn out process, in no sense inevitable, which scarcely deserves the epithet 'revolutionary.'"[34] The Industrial Revolution may have been slow but the sustained period of economic growth it initiated had no historical precedent. Table 1.1 indicates that by 1820, Britain's real Gross Domestic Product (GDP) per capita was higher than that of the Netherlands, which made Britain the global economic leader and the British one of the richest people in the world.[35] Table 1.2 suggests Britain's economic good fortune persisted into the middle of nineteenth century. Only a resource-rich economy like the United States of America's could grow more quickly on a per capital basis than the British economy between 1820 and 1870. The British remained one of the richest people in the world in 1870.

Table 1.1
Estimated Annual Real GDP per Capita
Measured at Purchasing Power Parity (1985 United States Dollars)

	1820	1870	1913	1950	1973
Great Britain	$1,405	$2,610	$4,024	$5,651	$10,063
France	$1,052	$1,571	$2,734	$4,149	$10,323
Germany	$937	$1,300	$2,606	$3,339	$10,110
Italy	$960	$1,210	$2,087	$2,819	$8,568
Japan	$588	$618	$1,114	$1,563	$9,237
Netherlands	$1,307	$2,064	$3,178	$4,706	$10,267
United States	$1,048	$2,247	$4,854	$8,611	$14,103

Source: Maddison, *Dynamic Forces in Capitalist Development*, 6-7.

[34] Rondo Cameron, "The Industrial Revolution: A misnomer," *The History Teacher* 15, no. 3 (1982): 383.

[35] Maddison, *Dynamic Forces in Capitalist Development*: 6-7; Elise S. Brezis, Paul R. Krugman, and Daniel Tsiddon, "Leapfrogging in international competition: A theory of cycles in national technological leadership," *The American Economic Review* 83, no. 5 (1993): 1212; Nicholas F. R. Crafts, "Forging ahead and falling behind: The rise and relative decline of the first industrial nation," *The Journal of Economic Perspectives* 12, no. 2 (1998): 194-96.

Table 1.2 Estimated Mean Annual Compound Growth of Real GDP per Capita Measured at Purchasing Power Parity (1985 United States Dollars)				
	1820-1870	1870-1913	1913-1950	1950-1973
Great Britain	1.2%	1.0%	0.8%	2.5%
France	0.8%	1.3%	1.1%	4.0%
Germany	0.7%	1.6%	0.7%	4.9%
Italy	0.4%	1.3%	0.8%	5.0%
Japan	0.1%	1.4%	0.9%	8.0%
Netherlands	0.9%	1.0%	1.1%	3.4%
United States	1.5%	1.8%	1.6%	2.2%
Source: Maddison, *Dynamic Forces in Capitalist Development*, 49.				

Britain's relative economic fortunes changed during the Amalgamation Movement. Other nations industrialised during the nineteenth century to compete with the British in the global marketplace. Britain's share of the world's total manufactured exports, for example, fell from 41.4 per cent in 1880 to 29.9 per cent by 1913.[36] Tables 1.1 and 1.2 indicate the British continued to get richer after 1870, but now others were getting richer too and some of them were getting richer more quickly than the British did. This disparity in post-1870 per capita economic growth rates persisted into the late twentieth century. By 1973, one really could have divided the developed world in two. Some countries like the United States, France, Germany and the Netherlands were ahead of Britain on the measure of real GDP per capita. Others like Italy and Japan would overtake Britain's real GDP per capita eventually if their economies continued to grow more quickly than the British

[36] Maurice W. Kirby, *The Decline of British Economic Power Since 1870* (London: Allen and Unwin, 1981), 139.

economy.[37] The world's first industrialised nation appeared to have contracted a wealth-inhibiting malady known as "the British Disease."[38]

Some economic historians claim Britain's post-1870 economic decline was more apparent than real. They argue the perception of lost economic hegemony was an unavoidable consequence of Britain's early industrialisation. Barry Supple suggested the only remarkable aspect to Britain's century-long descent into the developed world's middle ranks where Britons continue to enjoy one of the highest standards of living in the world was that the process took so long.[39] Similarly, Moses Abramovitz posited a 'catch-up effect' to argue economic leaders like nineteenth-century Britain grow slowly because they operate close to the technologically imposed limits to prosperity.[40] Abramovitz suggested that Britain held the economic lead because it had exploited most of the opportunities for growth available to it. Economic followers like Germany and the United States lagged behind Britain because they had yet to exploit all the opportunities for growth at their disposal. Rectifying that omission allowed these followers to catch the British up in a process that demanded their economies grow more quickly than the British economy to achieve parity. According to Abramovitz, the perception of Britain's relative economic decline was nothing more a product of nineteenth-century Britain's unsustainable developmental superiority. Economic leadership denied the British the growth-enhancing benefits of the catch-up effect.

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[37] Moses Abramovitz, "Catching up, forging ahead, and falling behind," *The Journal of Economic History* 46, no. 2 (1986): 396-97; Maddison, *Dynamic Forces in Capitalist Development*: 6-7, 49; Crafts, "Forging ahead and falling behind," 195-97.
[38] George Cyril Allen, *The British Disease: A Short Essay on the Nature and Causes of the Nation's Lagging Wealth* (London: Institute of Economic Affairs, 1976).
[39] Barry Supple, "Fear of failing: Economic history and the decline of Britain," *The Economic History Review* New Series 47, no. 3 (1994): 444-47.
[40] Abramovitz, "Catching up, forging ahead, and falling behind," 386-87.

Deidre (née Donald) McCloskey exonerated late nineteenth-century Britain from the allegation that it failed economically. According to her, late nineteenth-century Britain "performed as one would expect a prosperous and competitive economy to perform."[41] McCloskey's analysis suggested that Britain confronted insurmountable resource constraints during this period.[42] Victorian Britain possessed little unemployed labour and was running short of agricultural workers awaiting transfer into more productive pursuits. In addition, accumulating capital to raise the productivity of the labour at Britain's disposal would have required either more savings or less foreign investment to fund it. Britain's rate of consumption would have had to fall to levels that have few historical precedents to finance greater investment at home. Repatriating money invested abroad to achieve the same outcome would have entailed greater risk and a loss of income. In 1882, the jurist and statistician Leone Levi (1821-1888) claimed "With the British investor, the simple question is which form of investment pays best."[43] In 1909, Winston Churchill (1874-1965) noted that British investors earned "£1,100,000 a year regularly ... without lifting a finger" from the Suez Canal.[44] Both Levi and Churchill suggested British investors only bought foreign securities because they offered better risk-adjusted returns than the domestic investment alternatives forgone. Redirecting funds invested abroad into inferior domestic investments should have impoverished the British. McCloskey concluded late nineteenth-century Britain grew "as rapidly

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[41] Donald N. McCloskey, "Editor's introduction," in *Essays on a Mature Economy: Britain after 1840*, ed. Donald N. McCloskey (Princeton, New Jersey: Princeton University Press, 1971), 7.
[42] Donald N. McCloskey, "Did Victorian Britain fail?," *The Economic History Review* New Series 23, no. 3 (1970); McCloskey, "Editor's introduction."; Donald N. McCloskey, "No it did not: A reply to Crafts," *The Economic History Review* New Series 32, no. 4 (1979).
[43] Loene Levi, "Imports and exports," *The Times*, 3 January 1882, 12.
[44] "Mr. Churchill in Manchester," *The Times*, 7 December 1909, 7.

as permitted by ... its resources and the effective exploitation of available technology."[45]

McCloskey depicted a late nineteenth-century British economy growing more slowly than others did because it had come closer than most to realising its full potential. McCloskey's Britain utilised its savings rationally to accumulate all the capital it could deploy productively at home before investing the excess in better opportunities overseas. By the outbreak of World War I, Britons held the world's largest stock of foreign securities.[46] According to Maurice Kirby, "No country, before or since, has invested as high a proportion of its resources aboard over such a sustained period."[47] In 1882, Leone Levi defended this foreign investment, arguing a country as rich as Britain should export some of its wealth to keep it productively employed.[48] McCloskey made a similar point in the 1970s. She argued the British invested abroad because they had no need for "two Forth Bridges, two Bakerloo Lines, two London housing stocks [and] two Port Sunlights" and rightly declined to fund their construction.[49]

McCloskey claimed late nineteenth-century Britain enriched rather than impoverished itself by funding other people's economic development. Other economic historians have argued vehemently that greater investment at home could have put British labour to more productive uses. In 1882, Leone Levi conceded an unnamed correspondent had challenged his views on foreign investment. This

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[45] McCloskey, "Did Victorian Britain fail?," 459.
[46] Kirby, *The Decline of British Economic Power*: 14; Pollard, "Capital exports," 489-92.
[47] Kirby, *The Decline of British Economic Power*: 14.
[48] Loene Levi, "Imports and exports," *The Times*, 19 November 1881.
[49] McCloskey, "No it did not," 539.

correspondent asked Levi whether foreign investments afforded "foreign countries a better yield for labour than England?"[50] In 1905, the Italian-born economist, politician and journalist Leo Chiozza Money (1870-1944) warned, "Large sections of the British people have … worked for the benefit of the foreigner and of the British colonist, never realising their own country sorely needed all the capital that their labour could create."[51] A doctoral thesis submitted to the University of London in 1914 declared foreign investment "a running sore" sapping "the lifeblood of British industry" whilst "adding fresh strength to our most formidable rivals and competitors."[52] In the 1970s, William Kennedy made what had already become an oft-repeated allegation that British capital markets denied the nation's manufacturers with the funds they needed "to exploit opportunities [for firth growth] which did exist."[53] The next section explains how the world underwent a period of technological change during the Amalgamation Movement. Some economic historians claim Britain's failure to exploit the technological advances on offer denied it a never to be repeated opportunity to enrich its people further.

THE SECOND INDUSTRIAL REVOLUTION

According to David Landes, a "Second Industrial Revolution" began during the late-nineteenth century.[54] Breakthroughs in ferrous and non-ferrous metallurgy, inorganic and organic chemistry, electrical and mechanical engineering, and transportation and communications gave rise to new industries, new modes of

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[50] Levi, "Imports and exports."
[51] L. G. Chiozza Money, *Riches and Poverty*, Fourth ed. (London: Methuen, 1908), 147.
[52] Cited in Charles Kenneth Hobson, *The Export of Capital* (London: Constable and Company, 1914), ix.
[53] William P. Kennedy, "Foreign investment, trade and growth in the United Kingdom, 1870-1913," *Explorations in Economic History* 11, no. 4 (1974): 440.
[54] David S. Landes, *The Unbound Prometheus: Technological Change and Industrial Development in Western Europe from 1750 to Present*, Second ed. (Cambridge: Camridge University Press, 2003), 235.

production and new methods of industrial organisation during this period. Alfred DuPont Chandler described this Second Industrial Revolution as follows:

> Old industries were transformed, including the making of steel, copper and aluminum; the refining of oil and sugar; the processing of grain and other agricultural products; and the canning and bottling of the products thus processed. New industries were created. In chemicals, new processes produced man-made dyes, medicines, fibres and fertilisers. New mass-produced office, agricultural and sewing machines ... came on the market, as did heavy machinery for a wide variety of industrial uses. The most revolutionary of the new technologies were those that generated and transmitted electricity for lighting, urban traction and industrial power. These new industries drove economic growth and played a critical role in the rapid reshaping of commercial, agrarian and rural economies into modern, urban industrial ones.[55]

The British were slow to exploit the opportunities afforded by the Second Industrial Revolution and their efforts tended to focus on light industries rather than heavy ones when they did exploit those opportunities.[56] The Second Industrial Revolution gave the United States great firms like Standard Oil (oil refining), U.S. Steel (ferrous metals), DuPont (chemicals), Westinghouse and General Electric (electrical engineering), Ford and General Motors (automobiles) and Singer (sewing machines). Germany acquired Bayer, BASF, Hoechst (chemicals) together with AEG and Siemens (electrical engineering). In contrast, Britain's most visible contribution to the Second Industrial Revolution lay in the emergence of branded consumer products like Cadbury, Rowntree and Fry's (confectionary), Schweppes (soft drinks), Sunlight, Lifebuoy and Lux (soap and detergents), Huntley and Palmer

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[55] Alfred D. Chandler, "Organizational capabilities and the economic history of the industrial enterprise," *The Journal of Economic Perspectives* 6, no. 3 (1992): 81.

[56] Alfred D. Chandler, "The growth of the transnational industrial firm in the United States and the United Kingdom: A comparative analysis," *The Economic History Review* New Series 33, no. 3 (1980): 400-01; Kennedy, "Economic growth and structural change in the United Kingdom," 105-06; Paul Warwick, "Did Britain change? An inquiry into the causes of national decline," *Journal of Contemporary History* 20, no. 1 (1985): 101; Geoffrey Jones, "Global perspectives and British paradoxes," *The Business History Review* 71, no. 2 (1997): 292; Gary B. Magee, "Manufacturing and technological change," in *The Cambridge Economic History of Modern Britain Volume II: Economic Maturity, 1860-1939*, ed. Roderick Floud and Paul Johnson (Cambridge: Cambridge University Press, 2004), 80.

(biscuits), Bovril and Marmite (beef and yeast extracts), Lea & Perrins Worcestershire Sauce and H. P. Sauce (condiments).[57] Meanwhile, mature, low-growth and labour-intensive industries inherited from the Industrial Revolution like coal, textiles, shipbuilding, railway equipment, etc. continued to account for the bulk of British industrial output and exports.[58] It was as if Britain missed the best opportunities for growth on offer because it embarked upon the Second Industrial Revolution tentatively. In 1982, William Kennedy attempted to construct a counterfactual Britain that embraced the Second Industrial Revolution with as much enthusiasm as the Americans did. His analysis suggested that by 1913, a "vigorous and effective exploitation of the technological possibilities of the period" would have yielded gains in Gross National Product (GNP)[59] "of the order of 25 per cent to 50 per cent."[60]

Economic historians have expended a great dealt of energy trying to account for Britain's failure to embark upon the Second Industrial Revolution with more vigour. The answer to that question was a relatively simple one for McCloskey who put her developmental faith in free markets and believed there were no 'free lunches.' A greater commitment to the Second Industrial Revolution would have

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[57] Chandler, "The growth of the transnational industrial firm," 400-01; Jurgen Kocka, "Capitalism and bureaucracy in German industrialization before 1914," *The Economic History Review* New Series 34, no. 3 (1981): 457-60; Alfred D. Chandler, "The emergence of managerial capitalism," *The Business History Review* 58, no. 4 (1984): 479-501; Alfred D. Chandler, "The enduring logic of industrial success," *Harvard Business Review* 68, no. 2 (1990): 134-36.

[58] Kirby, *The Decline of British Economic Power*: 16; Kennedy, "Economic growth and structural change in the United Kingdom," 107-08; Elbaum, "Cumulative or comparative advantage?" 1257-59; Roderick Floud, "Britain, 1860-1914: A survey," in *The Economic History of Britain Since 1700: Volume 2, 1860-1939*, ed. Roderick Floud and Donald McCloskey (Cambridge: Cambridge University Press, 1994), 28; Jones, "Global perspectives and British paradoxes," 292; Crafts, "Forging ahead and falling behind," 201; Magee, "Manufacturing and technological change," 88-90.

[59] GNP includes incomes generated by nett foreign investments whereas GDP excludes them. Stanley Fischer and Rudiger Dornbusch, *Economics*: 551-54.

[60] Kennedy, "Economic growth and structural change in the United Kingdom," 105. See also William P. Kennedy, *Industrial Structure, Capital Markets, and the Origins of British Economic Decline* (Cambridge: Cambridge University Press, 1987).

drawn resources away from established industries and foreign investments that generated good returns at acceptable levels of risk. The late-Victorians and their Edwardian successors must have perceived the risks and returns involved and concluded a greater commitment to the Second Industrial Revolution was not in their best interests.[61] However, some historians insisted that Britain's reluctance to commit to the Second Industrial Revolution was evidence of a wealth inhibiting economic malady.

Marxists like Eric Hobsbawm invested their developmental faith in the forces of collectivism and economic planning.[62] It is not surprising he would regard an individualistic market economy like late nineteenth-century Britain's with suspicion. Hobsbawm posited an 'early start' hypothesis to suggest early industrialisation coupled with an over reliance on the market inhibited British economic growth. Hobsbawm explained:

> A capitalist economy is not planned, but emerges from a multitude of individual decisions taken in the pursuit of self-interest.... [To] change from an old and obsolescent pattern to a new one was both expensive and difficult. It was expensive because it involved both the scrapping of old investments still capable of yielding good profits and new investments at even greater cost; for as a general rule newer technology is more expensive.... It was difficult because it would almost certainly require agreement to rationalise among a large number of individual firms or industries, none of which could be certain where the benefits of rationalisation would go, or even whether in undertaking it they were not giving away their money to outsiders or competitors. So long as satisfactory profits were to be made in the old way, and so long as the decision to modernise had to emerge from the sum-total of decisions made by individual firms, the incentive to do so would be weak.[63]

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[61] Donald N. McCloskey, *If You're So Smart: The Narrative of Economic Expertise* (Chicago: University of Chicago Press, 1990), 58-60. A similar argument is made in McCloskey, "No it did not."
[62] Friedrich A. Hayek, "The nature and history of the problem," in *Collectivist Economic Planning*, ed. Friedrich A. Hayek (Auburn: Ludwig von Mises Institute, 1967), 12-17.
[63] Hobsbawm, *Industry and Empire*: 165-66.

Hobsbawm believed late nineteenth-century Britain's misfortune was that its industrial capitalists could live off incomes bequeathed to them by the Industrial Revolution. Hobsbawm's Britain was too well off to abandon old investments that generated acceptable returns. This Britain was also too market orientated and too individualistic to invest in new technologies and new methods of production that rewarded collective effort and economic planning. The result was an absence of native demand for capital that drove British savings abroad.[64]

Mancur Olson reached the opposite conclusion to Hobsbawn. Olson thought late nineteenth-century Britain suffered from too much collectivism. Underpinning Olson's analysis was his belief that successful and stable societies like late nineteenth-century Britain play host to what he called 'distributional coalitions,' alliances made up of self-interested individuals who collude with each other to undermine competition, restrict output and increase the price others pay for their produce. Such a coalition undermines its host's capacity for economic growth by disrupting the allocative efficiency of its markets.[65] Olsen's account of Britain's economic history before and after the Industrial Revolution, therefore, depended on his belief that distributional coalitions largely disappeared from British soil at the end of the seventeenth century only to re-emerge later.[66] According to Olsen, the Industrial Revolution was the unintended consequence of the Glorious Revolution. The Glorious Revolution destroyed feudal distributional coalitions that relied on the power of the crown, the aristocracy and the established church to sustain them. The

[64] Hobsbawm, *Industry and Empire*: 168-69.
[65] Mancur Olson, *The Logic of Collective Action: Public Goods and the Theory of Groups* (Cambridge: Harvard University Press, 1971); Mancur Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities* (New Haven: Yale University Press, 1982).
[66] Olson, *The Rise and Decline of Nations*: 77-87, 131-32, 143-45; Mancur Olson, "Dictatorship, democracy, and development," *American Political Science Review* 87, no. 03 (1993).

result, according to Olson, was the most socially mobile society in Europe and an outbreak of entrepreneurial energy that gave rise to the Industrial Revolution. By the mid-to-late nineteenth century, post-Industrial Revolution Britain possessed one of the world's most prosperous economies, a stable and functioning constitutional monarchy and virtual immunity from foreign invasion, which "made it easier for the firms and families that advanced ... [since the Glorious Revolution] ... to collude to protect their interests."[67] According to Olson, Britain suffered economically because it lacked the experience of a revolution, a civil war, a foreign invasion or some other national calamity that would have disrupted its re-emerging distributional coalitions.

Hobsbawm and Olson disagreed fundamentally over the market's efficacy as a facilitator of economic growth, but agreed that Britain's sluggish growth rates had underlying economic causes. Other historians have suggested that Britain's culture lay at the heart of Britain's economic lethargy. Corelli Barnett blamed evangelical Protestantism for turning what had been an aggressively pragmatic country whose ruling elite pursued their self-interest unapologetically into a nation ruled by puritanical Christians who agonised over the morality of their actions. Accompanying these changes, he argued, was a loss of interest in industry, trade and commerce as a means of enhancing British power.[68] Similarly, Martin Wiener noted the entrepreneurs who made their fortunes during the Industrial Revolution usually sent their male offspring to a public school and then to either Oxford or Cambridge. This education, Wiener claimed, introduced the heirs to Britain's industrial fortunes to aristocratic elites who considered industrialisation a threat to the existing social

[67] Olson, *The Rise and Decline of Nations*: 84.
[68] Corelli Barnett, *The Collapse of British Power* (London: Eyre Methuen 1972); Barnett, *The Audit of War*.

order. These young aristocrats, and those who educated them, had no interest in promoting the "industrialising spirit" that had animated the Industrial Revolution.[69] Wiener observed:

> Oxbridge trained a political leadership with a minimum of interest in or knowledge of the industrial world.... If Oxbridge insulated the sons of the older elites against contact with industry, it also gradually drew sons of industrial ... families away from the occupations of their fathers, contributing to a 'haemorrhage' of business talent.[70]

Wiener believed the origins of Britain's relative economic decline lay in an education system that had promulgated "an anti-industrial bias."[71] That bias shaped government policy and denied British manufacturing the talent and resources needed to realise its potential for growth.

Yet another explanation for the failure to embrace the Second Industrial Revolution focused upon the relationship between City of London (the home to British financial capital) and the global economy.[72] Those who sought to blame the City for Britain's low rates of growth levelled two charges against it. The first was the aforementioned allegation that the City's addiction to low-risk foreign debt securities resulted in underinvestment at home.[73] The second was that the City exploited its cultural and geographical proximity to the centre of government in Westminster to obtain policies that served its interests at British manufacturing's

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[69] Bernard. Porter, "'Though not an historian myself...' Margaret Thatcher and the historians," *Twentieth Century British History* 5, no. 2 (1994): 252-53.
[70] Wiener, *English Culture and the Decline of the Industrial Spirit*: 23-24.
[71] Scott Newton and Dilwyn Porter, *Modernization Frustrated: The Politics of Industrial Decline in Britain Since 1900* (London: Unwin Hyman, 1988), 10; Jones, "Global perspectives and British paradoxes," 292.
[72] Kennedy, *Industrial Structure, Capital Markets, and the Origins of British Economic Decline*; Newton and Porter, *Modernization Frustrated*; Pollard, *Britain's Prime and Britain's Decline*.
[73] Andrew Gamble, *Britain in Decline: Economic Policy, Political Strategy and the British State* (London: Macmillan, 1981), 14-17; Pollard, "Capital exports, 1870–1914," 484-95; Forrest Capie and Terence Mills, "British bank conservatism in the late 19th century," *Explorations in Economic History* 32, no. 3 (1995): 9-10.

expense.[74] Both allegations rested on the reality that by the late nineteenth century, the City of London was the world's leading financial and trading centre and thus dependent upon incomes generated outside the United Kingdom, which fostered a cosmopolitan outlook that had little need for domestic economic success.[75] As Scott Newton and Dilwyn Porter noted, "it was as if Britain had become the territorial base for two economies, which remained relatively independent of each other."[76]

The relationship between the City and the global economy turned the former into an advocate of economic liberalism, the world's most potent globalising intellectual force during the late-nineteenth century. Policies like free trade, a commitment to *laissez faire* and an unshakable faith in the gold standard sustained by cautious fiscal policy had the City's full support.[77] The City also enjoyed privileged access to what Geoffrey Ingham called "the core institutional nexus"[78] of British policymaking in Westminster where it generally found a like-minded audience. In Andrew Gamble's words:

> The virtues of liberal political economy as an ideological doctrine would not have given it such ascendancy ... had it not also found continual reinforcement in some important features of the organisation of the British state and British economy. British economic policy and British business have long been dominated by perspectives originating in

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[74] Gamble, *Britain in Decline*: 132-40; P. J. Cain and A. G. Hopkins, "Gentlemanly capitalism and British expansion overseas (II): New imperialism, 1850-1945," *The Economic History Review* New Series 40, no. 1 (1987): 4-6; E. H. H. Green, "Rentiers versus producers? The political economy of the Bimetallic Controversy c. 1880-1898," *The English Historical Review* 103, no. 408 (1988): 611-12; Newton and Porter, *Modernization Frustrated*: xii-xv, 1-30; Supple, "Fear of failing," 451-52; R. C. Michie, "Insiders, outsiders and the dynamics of change in the City of London since 1900," *Journal of Contemporary History* 33, no. 4 (1998): 549-52.

[75] Warwick, "Did Britain change?" 101-02; Newton and Porter, *Modernization Frustrated*: 7-11; Richard Roberts, "What's in a name? merchants, merchant bankers, accepting houses, issuing houses, industrial bankers and investment bankers," *Business History* 35, no. 3 (1993): 25-31.

[76] Newton and Porter, *Modernization Frustrated*: 9.

[77] Felix Schuster, "Foreign trade and the money market," *Journal of the Intitute of Bankers* 25, no. 2 (1904). See also Gamble, *Britain in Decline*: 134-35; Kirby, *The Decline of British Economic Power*: 18-19; Cain and Hopkins, "Gentlemanly capitalism and British expansion overseas (II), 4-5; Green, "Rentiers versus producers?" 607-08.

[78] Cited in Newton and Porter, *Modernization Frustrated*: 10.

> banking and trade rather than industry.... [Financial capital] has been strengthened in numerous institutional ways. The widespread use of sterling as an international currency, the importance of London in the operation of the gold standard encouraged a tremendous expansion of banking, insurance and shipping services provided by businesses in the City.... The Bank of England ... grew to be the main channel for articulating the City's view of the national interest in economic policy. Departments like, the Treasury and the Board of Trade, have always tended to share ... [the City's] ... perspective on British national problems and therefore have endorsed the assumptions of liberal political economy.[79]

Economic liberalism may have promoted the City's interests, but it did not always serve the needs of Britain's manufacturers.[80] The gold standard gave the City monetary stability and the most trusted currency in the world, but it precluded the devaluation of the pound needed to reduce the cost of British goods on foreign markets.[81] Winston Churchill had good reason to lament that "I would rather see finance less proud and industry more content"[82] when the City's advocates pressed him for the gold standard's return in 1925. In addition, other nations protected their domestic manufacturers with tariffs, but Joseph Chamberlain's campaign for tariff reform came to nothing. Chamberlain argued tariffs would give British workers better employment opportunities and higher wages.[83] His opponents in the Liberal Party claimed free trade yielded 'big loaves' made from cheap imported grain to win

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[79] Gamble, *Britain in Decline*: 134.

[80] S. G. Checkland, "The mind of the City, 1870-1914," *Oxford Economic Papers* New Series 9, no. 3 (1957): 262-64; M. E. F. Jones, "The regional impact of an overvalued pound in the 1920s," *The Economic History Review* New Series 38, no. 3 (1985): 392-94; Cain and Hopkins, "Gentlemanly capitalism and British expansion overseas (II)" 3-6; Green, "Rentiers versus producers?" 607-12.

[81] William M. Scammell, "The working of the gold standard," *Bulletin of Economic Research* 17, no. 1 (1965); Nicholas Kaldor, "Conflicts in national economic objectives," *The Economic Journal* 81, no. 321 (1971); Jones, "The regional impact of an overvalued pound."; Green, "Rentiers versus producers?"; Michael D. Bordo and Finn E. Kydland, "The gold standard as a rule: An essay in exploration," *Explorations in Economic History* 32, no. 4 (1995); Michael D. Bordo and Hugh Rockoff, "The gold standard as a "good housekeeping seal of approval"," *The Journal of Economic History* 56, no. 02 (1996).

[82] Cited in Kaldor, "Conflicts in national economic objectives," 6. Churchill was Chancellor of the Exchequer at the time.

[83] "Mr. Chamberlain's campaign," *The Times*, 7 October 1903; "Mr. Chamberlain in the City," *The Times*, 20 January 1904.

the 1906 general election by a landslide.[84] Some economic historians argued the City of London's commitment to economic liberalism denied British manufacturers the assistance that only an interventionist state could provide.[85]

The fact that the Amalgamation Movement laid the foundations of contemporary Britain's banking industry by turning it into a concentrated oligopoly has made it a development some historians have deemed worthy of study in its own right.[86] That this Amalgamation Movement also coincided with the onset of a period of perceived economic decline makes the Amalgamation Movement even more interesting because a causal relationship might exist between the two events. The domestic banks were financial intermediaries after all that lent funds to British industry.[87] Any absence of native demand for capital implied by Hobsbawm's early start hypothesis would have denied lending opportunities to the domestic banks. Maybe the Amalgamation Movement was the industry's response to a scarcity of lending opportunities available in Britain. In addition, the Amalgamation Movement might have laid the foundations for one of Olson's distributional coalitions because bank amalgamations eliminated competitors. If this were the case, the Amalgamation Movement would have denied domestic manufacturers their due share of the nation's

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[84] Zebel, "Joseph Chamberlain and the genesis of tariff reform."; Coats, "Political economy and the tariff reform campaign."; Timothy J. McKeown, "Hegemonic stability theory and 19th century tariff levels in Europe," *International Organization* 37, no. 01 (1983); Kevin H. O'Rourke, "Tariffs and growth in the late 19th century," *The Economic Journal* 110, no. 463 (2000); Douglas A. Irwin, "Tariffs and growth in late nineteenth century America," *The World Economy* 24, no. 1 (2001).
[85] Pollard, *Britain's Prime and Britain's Decline*: 257-58.
[86] See: Sykes, *The Amalgamation Movement in English Banking*; Capie and Rodrik-Bali, "Concentration in British banking."; Cassis, "Management and strategy in the English joint stock banks."; Grossman, "Rearranging deck chairs on the Titanic."; Peter Scott and Lucy Newton, "Jealous monopolists? British banks and responses to the Macmillan Gap during the 1930s," *Enterprise and Society* 8, no. 4 (2007).
[87] Committee on Finance and Industry, *Committee on Finance and Industry Report* (London: His Majesty's Stationary Office, 1931); S. Evelyn Thomas, *The Macmillan Report: A Short Summary of its Main Points Prepared for Students* (St. Albans: Metropolitan College, 1931); J. C. Stamp, "The report of the Macmillan Committee," *The Economic Journal* 41, no. 163 (1931).

savings by increasing the rates of interest the banks charged.[88] Furthermore, the relationship between Britain's banking industry and the aristocracy was always a close one.[89] The banking industry should have thrived in a cultural environment exhibiting an anti-industrial bias like the one posited by Wiener. Finally, the Big Five English and Welsh banks maintained their head offices in London and some of the City's most influential figures held positions in their managerial hierarchies and on their boards of directors.[90] Any attempt to ascribe blame for economic decline to the City ought to consider the contribution made by the amalgamating banks.[91] However, this thesis argues there is another reason why further study into the Amalgamation Movement is important. The Amalgamation Movement created some of the biggest banks in the world at a time when the British appeared incapable of replicating the large firms found in other countries.

MANAGERIAL AND PERSONAL CAPITALISM

In 1905, the constitution theorist Albert Venn Dicey (1835-1922) observed, "combination has gradually become the soul of modern commercial systems" because "one trade after another has passed from the management of private persons into the hands of corporate bodies."[92] The Amalgamation Movement exemplified a late nineteenth-century increase in firm size that elevated the economic importance of the corporate form. However, the Amalgamation Movement would have perplexed Alfred DuPont Chandler, a historian who won a Pulitzer Prize in 1978 and

[88] Scott and Newton, "Jealous monopolists?"
[89] Cain and Hopkins, "Gentlemanly capitalism and British expansion overseas (II)" 5-6; Wiener, *English Culture and the Decline of the Industrial Spirit*: 128-29.
[90] Cain and Hopkins, "Gentlemanly capitalism and British expansion overseas (II)," 5-6; Checkland, "The mind of the City, 1870-1914."
[91] Michael Collins, "English bank lending and the financial crisis of the 1870s," *Business History* 32, no. 2 (1990).
[92] A. V. Dicey, *Lectures on the Relation Between Law and Public Opinion in England During the Nineteenth Century*, Second ed. (London: Macmillan, 1914), 245.

raised business history to the level of a credible field of study.[93] Chandler suggested the British never really came to terms with the declining importance of the individual during the late-nineteenth century. He argued that the British could not embrace the separation of ownership and control needed to create truly large firms.[94]

Chandler observed that many of the industries created by the Second Industrial Revolution were capital intensive, which imposed fixed costs of production.[95] Minimising average unit cost under these circumstances demanded that firms amortise their fixed costs over a large volume of output. To do that, either firms produced a solitary product in very large quantities to realise economies of scale or they proliferated the range of products their manufacturing facilities produced to realise economies of scope.[96] According to Chandler, achieving the high output volumes needed to realise economies of scale and scope demanded firms make three investments.[97] First, firms acquired the manufacturing facilities capable of producing output in large volumes. Second, firms invested in the marketing and distribution networks needed to sell and deliver the output produced to consumers.

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[93] Richard R. John, "Elaborations, revisions, dissents: Alfred D. Chandler, Jr.'s, "The visible hand" after twenty years," *The Business History Review* 71, no. 2 (1997); Thomas K. McCraw, "The challenge of Alfred D. Chandler, Jr.: Retrospect and prospect," *Reviews in American History* 15, no. 1 (1987); Geoffrey Jones, "Alfred Chandler and the importance of organization," *Enterprise and Society* 9, no. 3 (2008); Louis. Galambos, "Reflections on Alfred D. Chandler, Jr," *Enterprise and Society* 9, no. 3 (2008); Jack Smothers et al., "Alfred D. Chandler, Jr: Historical impact and historical scope of his works," *Journal of Management History* 16, no. 4 (2010).

[94] Alfred D. Chandler, "Institutional integration: An approach to comparative studies of the history of large-scale business enterprise," *Revue Économique* 27, no. 2 (1976); Alfred D. Chandler, *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, Massachusetts: Belknap Press, 1977); Chandler, "The growth of the transnational industrial firm in the United States and the United Kingdom."; Chandler, "The emergence of managerial capitalism."; Alfred D. Chandler and Takashi Hikino, *Scale and Scope: The Dynamics of Managerial Capitalism* (Cambridge, Massachusetts: Belknap Press, 1990); Chandler, "The enduring logic of industrial success."; Chandler, "Organizational capabilities."; Alfred D. Chandler, "What is a firm?: A historical perspective," *European Economic Review* 36, no. 2-3 (1992).

[95] Chandler and Hikino, *Scale and Scope*: 8.

[96] Chandler, "Organizational capabilities," 81-82.

[97] Chandler, "The emergence of managerial capitalism."; Chandler and Hikino, *Scale and Scope*: 8.

According to Chandler, these first two investments often yielded firms that were so big that the task of administering them overwhelmed their owners. Consequently, the largest firms made a third investment in a managerial hierarchy staffed by salaried administrators to coordinate the firm's activities on the owners' behalf. Chandler argued this third investment was revolutionary.[98] For the first time, those with "no connection with the founders" of the firms they managed and "little or no equity" invested in them coordinated the fastest growing sectors of the economy.[99] The result was an unprecedented separation of ownership and control and the emergence of what Chandler called 'managerial capitalism.'[100] A new managerial class came into being that took control of the economy's commanding heights.

To illustrate how economies of scale and scope fostered an increase in firm size during the Second Industrial Revolution, Chandler noted that in 1882 a single act of horizontal integration put somewhere between a quarter to two-fifths of the global oil refining capacity under the control of John D. Rockefeller's (1839-1937) Standard Oil Trust.[101] Standard Oil then rationalised its operations by transferring all of its production to three great oil refineries where it realised economies that saw the cost to produce a gallon of kerosene fall from 2½¢ in 1880 to less than ½¢ by 1885.[102] After that, Standard Oil integrated vertically to acquire 20,000 oil wells, 4,000 miles of pipeline and 5,000 tank cars to feed its refineries and distribute their

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[98] Chandler, *The Visible Hand*.
[99] Chandler and Hikino, *Scale and Scope*: 240. See also: Alfred D. Chandler, "The emergence of managerial capitalism."
[100] Chandler and Hikino, *Scale and Scope*: 37-38; Chandler, "The enduring logic of industrial success," 133; Chandler, "Organizational capabilities," 83.
[101] Chandler, "The emergence of managerial capitalism," 403; Chandler, "The enduring logic of industrial success," 131.
[102] Chandler, "Organizational capabilities," 82.

output.[103] In the end, Standard Oil's dominance of the American oil industry became so great that in 1911 the United States' Supreme Court deemed it in breach of America's antitrust laws and ordered its breakup.[104] That breakup created 34 successor companies, but three of them (Standard Oil of California, Standard Oil of New Jersey and Standard Oil of New York) remained so big that they became members of the global oligopoly that dominated the world's petroleum industry during the twentieth century.[105] Chandler argued Standard Oil's growth typified many firms during the Second Industrial Revolution. The pursuit of economies of scale and scope promoted oligopolistic and monopolistic market structures because a small number of large horizontally and vertically integrated firms possessed insurmountable competitive advantages. These large firms administered by managerial professionals could minimise average unit costs in a way that smaller firms managed by their proprietors could not.[106]

Chandler claimed the British embraced managerial capitalism far more reluctantly than either the Germans or Americans did. He claimed that as late as the 1930s, British firms remained small enough to operate "without the benefit of an

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[103] Chandler, "The emergence of managerial capitalism," 403; Ron Chernow, *Titan: The Life of John D. Rockefeller, Sr* (New York: Random House, 1998), 249.

[104] *Standard Oil Company of New Jersey v United States*, 221 U. S. 1(1911). See also: John S. McGee, "Predatory price cutting: The Standard Oil (NJ) case," *Journal of Law and Economics* 1 no. 1 (1958); Elizabeth Granitz and Benjamin Klein, "Monopolization by raising rivals costs: The Standard Oil case," *Journal of Law & Economics* 39, no. 1 (1996); Josh Boyd, "The rhetoric of arrogance: The public relations response of the Standard Oil Trust," *Public Relations Review* 27, no. 2 (2001).

[105] Standard Oil of California, Standard Oil of New Jersey and Standard Oil of New York sold product under brand names like Chevron, Esso/Exxon and Mobil. The other 'seven sisters,' an exclusive club that dominated the global oil industry until the 1970s, were British Petroleum, Royal Dutch Shell, Gulf Oil and Texaco. Anthony Sampson, *The Seven Sisters: The Great Oil Companies and the World They Shaped* (New York: Bantam Books, 1991).

[106] Alfred D. Chandler, "The structure of American industry in the twentieth century: A historical overview," *The Business History Review* 43, no. 03 (1969); Chandler, "The growth of the transnational industrial firm."; Chandler, "The enduring logic of industrial success."

extensive managerial hierarchy."[107] In Britain, the separation of ownership and control was far less complete than in Germany or America because the families that established Britain's firms generally remained "influential stockholders and senior executives of their companies."[108] According to Chandler, this reluctance to relinquish control to salaried administrators promoted a form of 'personal capitalism' that kept British firms small by American and German standards.[109] Acts of horizontal integration might occur in Britain, but the commitment to personal capitalism ensured the component parts of a horizontally integrated British firm remained under the control of those who owned them previously. Consequently, horizontal integration in Britain yielded nothing more than mere "federations of autonomous family enterprises"[110] in which the centralisation of authority needed to rationalise production never occurred.[111] The British commitment to personal capitalism also precluded vertical integration because a typical British firm lacked the managerial resources needed to administer another part of the value chain.[112] One of twentieth-century Britain's most successful personal capitalists, the motor vehicle manufacturer William Morris (1877-1963), expressed this uniquely British reluctance to take over his suppliers as follows:

> There is no point producing any article ... you can buy from a specialist concern.... The outside firm that makes ... one ... important part ... can keep its governing brains concentrated on the problems connected with

[107] Chandler and Hikino, *Scale and Scope*: 240. See also: Chandler, "The growth of the transnational industrial firm."
[108] Chandler and Hikino, *Scale and Scope*: 240. See also: Chandler, "The emergence of managerial capitalism."; Chandler, "The enduring logic of industrial success."
[109] Chandler and Hikino, *Scale and Scope*: 235-37.
[110] Chandler, "The emergence of managerial capitalism," 497.
[111] Chandler and Hikino, *Scale and Scope*: 286-91.
[112] Chandler, "The growth of the transnational industrial firm," 400-01; Chandler and Hikino, *Scale and Scope*: 282-83.

> that unit in a way impossible to a concern manufacturing a highly complicated article.[113]

In Chandler's view, British manufacturers missed the most lucrative opportunities for growth the Second Industrial Revolution offered because their owner-managed firms lacked the 'organisational capabilities' needed to compete with their foreign counterparts. British firms remained too small to realise economies of scale and scope.[114] His explanation as to why British manufacturers would embark upon such a commercially destructive course of action had its origins in the British class system.[115]

Like Donald Coleman before him,[116] Chandler divided those who populated British firms into 'gentlemen' and 'players.'[117] Gentlemen were 'educated amateurs,' the descendants of a firm's founding entrepreneurs who lived off the incomes generated by an inherited ownership stake in the firm. Gentlemen demanded nothing more of their firms than they supply the income needed to sustain their lifestyles. Consequently, gentlemen preferred not to put their wealth at risk by making a large investment in some new business venture. Players, on the other hand, worked as the gentlemen's servants to earn a wage or a salary. Some players aspired to become gentlemen too, but to do that they would usually have to establish a successful businesses of their own. Gentlemen received a classical education at a public school and then at Oxford, Cambridge or at one of the provincial universities that taught the

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[113] Cited in P. W. S. Andrews and E. Brunner, *The Life of Lord Nuffield: A Study in Enterprise and Benevolence* (Oxford: Basil Blackwell, 1955), 152-53; Martin Adeney, *Nuffield: A Biography* (London: Robert Hale, 1993), 69.
[114] Chandler and Hikino, *Scale and Scope*: 500. See also: Chandler, "The enduring logic of industrial success."; Chandler, "Organizational capabilities."
[115] H. V. Nelles, "Chandler's three faces of capitalism," *Labour/Le Travail* 28, no. 1 (1991): 299.
[116] Donald C. Coleman, "Gentlemen and players," *The Economic History Review* New Series 26, no. 1 (1973).
[117] Chandler and Hikino, *Scale and Scope*: 292-94.

Oxbridge curriculum. Significantly, gentlemen studied the classics. They did not study technical subjects designed to prepare them for their duties within their firms. In contrast, players were 'practical men' who served apprenticeships and clerkships to accumulate the on the job experience they needed to make them indispensable allies to the gentlemen.

According to Chandler, the division of responsibilities between gentlemen and players in a typical British firm worked well in labour-intensive industries established during the Industrial Revolution. Personal capitalism could compete when the scale of operations remained small, when a large capital investment was unnecessary and when tried and trusted rules of thumb passed down by one generation to the next yielded acceptable results. The Second Industrial Revolution even offered ambitious players new opportunities to elevate their social standing in industries that produced packaged consumer products.[118] After all, the manufacture of biscuits, confectionary, soft drinks, cordials, condiments and the like demanded relatively little capital investment. The capacity to realise economies of scale and scope in these industries would not be critical to success. In addition, Britain possessed a mature retail sector and a legion of independent wholesalers and shopkeepers who would happily stock well-advertised brands subject to high consumer demand. There was no need to invest in marketing and distribution networks when others would distribute and sell product on the manufacturer's behalf. A personal capitalist could prosper producing branded consumer products because the investment in production, marketing and distribution was so small that there was no need for an extensive managerial

[118] Roy Church and Christine Clark, "Product development of branded, packaged household goods in Britain, 1870–1914: Colman's, Reckitt's, and Lever Brothers," *Enterprise and Society* 2, no. 03 (2001).

hierarchy.[119] An ambitious player like William Hesketh Lever (1851-1925) amassed a fortune manufacturing and advertising soap and detergents without relinquishing control of his business. Lever was the son of a Bolton grocer who ended his life as a gentleman. Lever became one of Britain's most enlightened employers and a respected philanthropist, he sat in both houses of parliament and he died with the title 'First Viscount Leverhulme of the Western Isles in the Counties of Inverness and Ross and Cromarty.'[120]

Some business and economic historians questioned Chandler's contention that British firms were smaller than their American and German counterparts were.[121] Peter Wardley observed that although Britain lacked some of the exceptionally large industrial giants found elsewhere, many of the biggest enterprises in Britain remained big enough to qualify as large even by American and German standards.[122] Wardley also suggested that firms engaged in the delivery of services rather than manufacturing t ended to dominate the ranks of Britain's largest firms.[123] To illustrate, the textile manufacturer J. & P. Coates was Britain's largest manufacturer in 1904/05 although it ranked a mere eleventh on the league table of the largest

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[119] Chandler and Hikino, *Scale and Scope*: 292-94.

[120] "Biographies of new members," *The Times*, 19 February 1906; David J Jeremy, "The enlightened paternalist in action: William Hesketh Lever at Port Sunlight before 1914," *Business History* 33, no. 1 (1991); Roger Hutchinson, *The Soap Man: Lewis, Harris and Lord Leverhulme* (Edinburgh: Birlinn, 2003); Adam Macqueen, *The King of Sunlight: How William Lever Cleaned Up the World* (London: Corgy, 2005); Lee D. Parker, "Corporate social accountability through action: Contemporary insights from British industrial pioneers," *Accounting, Organizations and Society* 39, no. 8 (2014).

[121] Christopher J. Schmitz, *The Growth of Big Business in the United States and Western Europe, 1850-1939* (Cambridge: Cambridge University Press, 1995), 23-27; Magee, "Manufacturing and technological change," 78-80.

[122] Peter Wardley, "The emergence of big business: The largest corporate employers of labour in the United Kingdom, Germany and the United States c. 1907," *Business History* 41, no. 4 (1999): 94-101. The proxy for firm size used in this study was number of employees.

[123] Peter Wardley, "The anatomy of big business: Aspects of corporate development in the twentieth century," *Business History* 33, no. 2 (1991), Wardley's earlier research used total market value of issued shares rather than number of employees as a proxy for firm size.

businesses in Britain behind ten railway companies and the Bank of England. At this time, 40 of the country's 50 the biggest businesses in Britain provided services.[124]

Britain may have lacked the truly colossal manufacturing concerns found elsewhere, but it could play host to large firms many of which confined their operations to the delivery of services. The growth in firm size exhibited by the English and Welsh banks during the Amalgamation Movement, therefore, was a far less unusual development than Chandler would have expected. The next section will examine the Amalgamation Movement in detail to explain how large the biggest banks in England and Wales became.

THE AMALGAMATION MOVEMENT

Table 1.3 depicts an increase in the number of bank amalgamations in England and Wales that began during the 1860s. This increase in the rate of bank amalgamations gathered pace and persisted, unlike the outbreak of bank amalgamations recorded between 1826 and 1843. If the Amalgamation Movement appears to have lost momentum between 1908 and 1924 that is because there were far fewer banks in England and Wales left during the second decade of the twentieth century. One estimate suggests that in 1860, England and Wales played host to 397 banks, 97 of which were joint stock companies and the remaining 300 were private banks. The English and Welsh banking industry changed radically over the next 50 years. The industry more than quadrupled in size, expanding from 1,223 branches in total in 1860 to 5,930 branches by 1910.[125] The Amalgamation Movement also ensured that

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[124] Peter Wardley, "The anatomy of big business," 278-84.
[125] Nishimura, *The Decline of Inland Bills of Exchange*: 80-81.

the number of banks operating those branches fell dramatically. By 1910, private banks were in danger of total extinction. Only 34 of them remained open for business. The number of the joint stock banks had also fallen to 50.[126] The relatively small regional banks that once populated the English and Welsh banking industry disappeared by means of a merger into the largest banks' expanding branch networks.[127] The average English and Welsh bank only maintained 3.1 branches in 1860. By 1913, an average English and Welsh bank had 93.9 branches.[128]

Table 1.3
Bank Amalgamations in England and Wales, 1826-1924

	Private With Private	Joint Stock Absorbs Private	Joint Stock With Joint Stock	Private Absorbs Joint Stock	Total
1826-1843	23	93	6	0	122
1844-1861	11	23	10	0	44
1862-1889	31	66	40	1	138
1890-1907	37	76	69	1	183
1908-1924	1	24	40	0	65

Source: Sykes, *The Amalgamation Movement in English Banking*, 193-195.

The Amalgamation Movement continued during World War I to intensify the Big Five's dominance over the industry.[129] By 1918, the biggest five English and Welsh banks appeared on the brink of monopolising the banking industry in much the same way Rockefeller's Standard Oil Trust monopolised oil refining in pre-war

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[126] Francis E. Steele, *Present Day Banking: Its Methods, Tendencies and Practices* (London: Butterworth, 1909), 73; Nishimura, *The Decline of Inland Bills of Exchange*: 81.
[127] Francis E. Steele, "Bank amalgamations," *The Economic Journal* 6, no. 24 (1896); Arcturus, "Bank Amalgamations and the State (Reproduced by Permission from Sperlings Journal)," (Barclays Bank Archive (3/64), 1918); Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," in *Select Statutes, Documents & Reports Relating to British Banking, 1832-1928*, ed. T. E. Gregory (London: Oxford University Press, 1929); Sykes, *The Amalgamation Movement in English Banking, 1825-1924*.
[128] Nishimura, *The Decline of Inland Bills of Exchange*: 80-81.
[129] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations"; Sykes, *The Amalgamation Movement in English Banking*; Cassis, "Management and strategy in the English joint stock banks."

America.[130] Walter Leaf (1852-1927) (the chair of the London County and Westminster Bank) conceded in 1918 that the public now questioned whether bank amalgamations promoted "what is vaguely called a 'Money Trust' with a consequent restriction of competition."[131] Leaf had good reason to feel concerned about the public mood because the biggest English and Welsh banks would soon become the subject of a British version of the 'trust busting' undertaken in progressive-era America.[132]

On 11 March 1918, Leaf addressed his shareholders to defend an amalgamation between the London County and Westminster Bank and Parr's Bank.[133] Bank amalgamations were nothing new and had been a common occurrence for over 50 years.[134] However, the timing of this particular amalgamation made justifying it unusually difficult. On 5 February 1918, the Chancellor of the Exchequer (Bonnar Law (1858-1923)) declared bank amalgamations a matter of "public importance" in parliament before announcing his intention to appoint a committee to inquire into the subject.[135] At first, the banking industry appeared to take little or no notice of Law's announcement. On 18 February, the London City and Midland Bank's Edward Holden (1848-1919) declared his bank would amalgamate with the London Joint Stock Bank to create what would be the "largest bank in the world" according to *The*

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[130] Ellis T. Powell, *The Evolution of the Money Market (1385-1915)* (London: The Financial News, 1915), 448-49; "Company meetings: The London County and Westminster Bank Limited," *The Times*, 12 March 1918; Arcturus, "Bank Amalgamations and the State."

[131] "Company meetings: The London County and Westminster Bank Limited," 12.

[132] Arthur P. Dudden, "Men against monopoly: The prelude to trust-busting," *Journal of the History of Ideas* 18, no. 4 (1957); George Bittlingmayer, "The stock market and early antitrust enforcement," *The Journal of Law & Economics* 36, no. 1 (1993); William E. Kovacic and Carl Shapiro, "Antitrust policy: A century of economic and legal thinking," *The Journal of Economic Perspectives* 14, no. 1 (2000).

[133] "Company meetings: Parr's Bank (Limited)," *The Times*, 12 March 1918; "Company meetings: The London County and Westminster Bank Limited."

[134] Sykes, *The Amalgamation Movement in English Banking*.

[135] "Bank amalgamations: Parliament, House of Commons," *The Times*, 6 February 1918, 10.

Times.[136] The Chancellor of the Exchequer did not back down. On 5 March, he made it known that Lord Colwyn (Frederick Henry Smith (1859-1946)) would chair the Treasury Committee on Bank Amalgamations.[137]

The amalgamation between the London County and Westminster and Parr's could not have come at a more politically sensitive moment given the Chancellor of the Exchequer's announcement on 5 March 1918. To make matters worse, the Union of London and Smiths Bank also chose 11 March 1918 to put a proposed amalgamation with the National Provincial Bank of England to its shareholders.[138] Leaf would have to choose his words carefully when he addressed his shareholders because a larger than normal audience was taking an interest in the proceedings. Leaf explained that wartime experience taught many in the City and in government that large firms constituted a source of economic strength. Indeed, the need to increase the size of Britain's firms was now shaping official policy. The Board of Trade, Leaf noted, encouraged "combinations ... in various branches of our great industries ... in the belief that in such close unions lies the most effective weapon against foreign competition."[139] Felix Schuster (1854-1936) sang from a similar song sheet when he addressed the Union of London and Smiths Bank's shareholders on the same day. Schuster claimed, "Two separate banks" could not "do as much as if they were amalgamated into one."[140] Leaf and Schuster's argument was that combinations enhanced rather than stifled competition. Greater size bestowed

[136] "Another bank fushion: Largest bank in the world," *The Times*, 19 February 1918, 6.
[137] "Bank amalgamations: Names of the committee of inquiry," *The Times*, 6 March 1918.
[138] "Company meetings: Union of London and Smiths Bank (Limited) ", *The Times*, 12 March 1918.
[139] "Company meetings: The London County and Westminster Bank Limited," 12.
[140] "City notes: A defense of bank fusions," *The Times*, 12 March 1918, 11; "Company meetings: Union of London and Smiths Bank (Limited) ", 13.

advantages that allowed a bank to compete against rivals that were getting bigger too.

There was good reason to believe that many firms in Britain remained too small by international standards in 1918. Some manufacturing industries had utilised amalgamations to induce an increase in firm size prior to World War I. Notable examples included the textile spinning and finishing industries, some branches of the food processing industry, tobacco and cigarettes, soap and detergents, cement and brewing. A similar thing also happened to the insurance industry. Britain's largest manufacturers and service providers had embraced a separation of ownership and control to accommodate this increase in firm size.[141] Nevertheless, most British firms seemed too small in 1918 to sustain an internationally competitive economy. Consequently, post-war Britain played host to a Rationalisation Movement led by Lyndall Fownes Urwick (1891-1983) who became one of twentieth-century Britain's most prolific managerial thinkers. According to Urwick, rationalisation would improve British firms' "organisation of production and distribution" through the "elimination of waste, simplification and standardisation, [and] horizontal and vertical combinations."[142] British firms and governments made a concerted effort to

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[141] Leslie Hannah, *The Rise of the Corporate Economy* (London: Methuen, 1976), 22-28; James Foreman-Peck and Leslie Hannah. "Extreme divorce: The managerial revolution in UK companies before 1914," *Economic History Review* New Series 65, no. 3 (2012); Robin Pearson. "Mergers and concentration in the UK insurance industry," *Enterprises et Histoire*, 72 (2013).

[142] Lyndall F. Urwick, *The Meaning of Rationalisation* (London: Nisbet and Company, 1929), 19. See also: Lyndall F. Urwick, *Management of Tomorrow* (London: Nisbet and Company, 1933); Hannah, *The Rise of the Corporate Economy*: 27-40. For more on Urwick's life and career see: Edward Brech, Andrew Thomson, and John F. Wilson, *Lyndall Urwick, Management Pioneer: A Biography* (Oxford: Oxford University Press, 2010); Lee D. Parker and Philip A. Ritson, "Rage, rage against the dying of the light: Lyndall Urwick's scientific management," *Journal of Management History* 17, no. 4 (2011); Philip A. Ritson and Lee D. Parker, "You're in the Army now! Historical lessons for contemporary management theorists," *Journal of Management History* 22, no. 3 (2016).

foster an increase in average firm size after the war.[143] The *Railways Act* of 1921 typified the effort.[144] It combined over 120 local railway businesses into the four regional giants that became the railway industry's 'Big Four.'[145]

The English and Welsh banks were very different organisationally to most British firms at the end of the Great War. These banks had already spent half a century engaged in the Amalgamation Movement to produce a significant increase in their size. In 1918, Colywn's committee on bank amalgamations determined the banks had exhausted the advantages bestowed by greater firm size. The committee warned bank amalgamations would soon constitute a threat to competition if they continued unabated. Its report concluded:

> While we believe that there is at present no idea of a Money Trust, it appears to us not altogether impossible that circumstances might produce something approaching to it at a comparatively early date. Experience shows that, in order to preserve an approximate equality of resources and competitive power, the large English [and Welsh] banks consider it necessary to meet each important amalgamation, sooner or later, by another. If ... size ... is to prevail, it can only lead, and fairly rapidly, to the creation of a very few preponderant combinations; and if those combinations amalgamated or entered into a joint agreement as to rates and policy, etc., the Money Trust would immediately spring to birth.[146]

The committee recommended legislation that would have required the banks to seek official consent before they amalgamated.[147] The committee's recommendation even yielded a bill to that effect although its wording raised technical issues that delayed

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[143] Chandler, "The growth of the transnational industrial firm," 407-08; Chandler and Hikino, *Scale and Scope*: 358-66.
[144] 11 & 12 George V c. 55.
[145] Peter Scott, "British railways and the challenge from road haulage: 1919–39," *Twentieth Century British History* 13, no. 2 (2002). The Big Four were the Great Western Railway, the London, Midland and Scottish Railway, the London and North Eastern Railway and the Southern Railway.
[146] "Fusion of banks and Government control: Expert committee's view," *The Times*, 22 May 1918, 8; Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 225-26. See also: "Control of bank amalgamation," *The Times*, 22 May 1918.
[147] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 226.

its progress through the parliament.[148] In the end, the Big Five and the government bypassed parliament altogether and settled on a gentlemen's agreement instead. The banks would submit all future proposals to amalgamate to the Treasury and the Board of Trade and would only proceed with their consent.[149] That agreement was honoured. Bank amalgamations continued after 1919, albeit at a diminished rate. However, the Big Five assumed the authorities would never permit one of them to amalgamate with another member of the Big Five. The next structurally significant development for the banking industry occurred over five decades later. In 1968, the National Provincial Bank merged with the Westminster Bank to create the National Westminster Bank (or NatWest) whereupon the Big Five became the Big Four.[150] The next section explores the reason why bankers felt a need to increase their banks' size during the Amalgamation Movement.

WHY DID AN ENGLISH AND WELSH BANK GET BIGGER?

A growing economy like post-Industrial Revolution Britain's needs an expanding money supply to fund its transactions.[151] Unlike most other businesses, banks literally make the money a growing economy needs because banks incur transferable debts payable on demand or at relatively short notice that possess all the characteristics of money. These debts are denominated in the prevailing unit of account (in the British case, pounds sterling), they provide a means of payment and

[148] "Joint stock banks: Amalgamation Control Bill," *The Times*, 16 April 1919; "City notes: A badly-drafted Bill," *The Times*, 24 April 1919; "City notes: Bankers alternative to the Control Bill," *The Times*, 25 April 1919.

[149] W. F. Crick and J. E. Wadsworth, *A Hundred Years of Joint Stock Banking* (London: Hodder and Stoughton Publishers, 1936), 41.

[150] Roger David, *The Big Four British Banks: Organisation, Strategy and the Future* (Basingstoke: MacMillan, 1999); Forrest Capie and Mark Billings, "Evidence on competition in English commercial banking," *Financial History Review* 11, no. 1 (2004).

[151] Richard G. Lipsey, *An Introduction to Positive Economics* (London: Weidenfeld and Nicholson, 1963), 423-29.

they constitute a store of value.[152] During the Industrial Revolution, provincial English and Welsh banks put bank notes into circulation to make money.[153] After 1844, the money the English and Welsh banks supplied took an increasingly intangible form. Banks offered cheques that made payments by transferring an account balance from one bank account to another.[154] The capacity of bank debts like these to act as a store of value was critical to public confidence in the money made by the banks. As Mahatma Ghandi (1869-1948) once observed, no one wants to be the payee nominated on a “cheque drawn on a crashing bank.”[155] Public confidence in the banks’ ca pacity to pay their debts when they fell due was vital for the utility of Britain’s money supply because much of it relied on bank credit.

This thesis argues the need to put a growing English and Welsh money supply on a secure footing motivated the Amalgamation Movement. No one issued an edict to initiate the Amalgamation Movement nor was it the product of a deliberate government policy. Instead, the Amalgamation Movement proceeded as if guided by Adam Smith’s (1723-1790) ‘invisible hand’ of the market.[156] Banks that

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[152] Lipsey, *An Introduction to Positive Economics*: 402-04; Fischer and Dornbusch, *Economics*: 623-36.

[153] Anonymous, *Letter to the Right Hon. Robert Peel: Upon the Necessity of Adopting Some Parliamentary Measure to Control the Issues of Country Bankers, and to Prevent the Recurrence of the Late Shock to Public and Private Credit*, Second ed. (London: J. Hatchard & Son, 1826); Gavin Mason Bell, *The Currency Question; an Examination of the Evidence on Banks of Issue Before a Select Committee of the House of Commons in 1840* (London: Longman, Orme, Brown, Green and Longmans, 1841); Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue with Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1841).

[154] Michael Collins, "Long-term growth of the English banking sector and money stock, 1844-80," *The Economic History Review* New Series 36, no. 3 (1983).

[155] According to legend, Ghandi used the phrase “post-dated cheque drawn on a crashing bank” to dismiss a British offer of Indian independence at war’s end in exchange for Indian cooperation during World War II. M. Abel, *Remade in India: Political Modernization in the Indian Context* (Hyrderabad: ICFAI University Press), 53.

[156] Lisa Hill, "The hidden theology of Adam Smith," *European Journal of the History of Economic Thought* 8, no. 1 (2001); Peter Harrison, "Adam Smith and the history of the invisible hand," *Journal of the History of Ideas* 72, no. 1 (2011).

commanded public confidence possessed the competitive advantage. These banks made their industry safer by taking other banks over. Banks that could not command public confidence disappeared by means of an amalgamation with a safer bank. Ultimately, the endeavour proved a success. The Amalgamation Movement created one of the most stable banking industries in the world. The United Kingdom avoided a major bank failure during the twentieth-century's Great Depression for example.[157]

The following chapters examine how the Amalgamation Movement unfolded. Chapter Two explains that the amalgamating English and Welsh banks were following a precedent. Scottish experience suggested that bigger banks were safer than smaller ones, although legislative prohibitions in England and Wales limited the size of a bank before 1826. The Scots erected large banks but the English and Welsh could have never embarked upon the Amalgamation Movement whilst these legislative prohibitions remained in force. Chapter Three argues that currency legislation passed in 1844 delayed the Amalgamation Movement for another two decades. The English and Welsh banks waited until their bank notes lost their importance to them before they considered merging with each other. Chapter Four examines the trade in inland bills of exchange that sustained many of the small banks found in England and Wales prior to 1870. This trade went into decline during the last quarter of the nineteenth century, which made the acquisition of a large geographically dispersed branch network a necessity. Finally, Chapter Five claims that the adoption of limited shareholder liability in the 1880s accelerated the rate of bank amalgamations. Limited liability imposed risks upon a bank's creditors who

[157] Richard S. Grossman, "The shoe that didn't drop: Explaining banking stability during the Great Depression," *The Journal of Economic History* 54, no. 03 (1994).

could no longer rely on the bank's proprietors to compensate them if it failed. These creditors reacted by demanding reassurance that their banks would not fail in the first place. Small regional banks could not survive under these circumstances. They left the industry by means of an amalgamation with a larger and much safer rival.

CONCLUDING REMARKS

The Amalgamation Movement of 1870 to 1920 occurred at a time when the British ranked amongst the wealthiest people in the world. Some economic historians have also argued that the Amalgamation Movement occurred at a time when Britain's economy exhibited the first symptoms of a relative economic decline that would take more than a century to run its course. The competitive advantages early industrialisation bestowed upon the British ebbed away as the services sector displaced the nation's manufacturers as the country's most important source of employment growth. The expansion of the English and Welsh banking industry during the Amalgamation Movement was representative of broader developments in the British economy at the time.

Alfred Chandler depicted Britain as a land in which family-managed firms predominated. According to him, the British were incapable of fostering a dramatic increase in firm size during the Amalgamation Movement although Chandler underestimated just how large a British firm could become because he ignored the services industries that played host to some of the country's largest firms. By 1910, the Big Five English and Welsh banks ranked amongst the world's largest firms of their kind. In 1918, the Colwyn's Treasury Committee on Bank Amalgamations singled these large banks out for special treatment. The committee concluded the

Big Five's dominance of the banking industry constituted a threat to competition before demanding they should seek official approval before amalgamating with another bank. Banking became one of the first industries in the United Kingdom to come under regulation explicitly designed to preserve competition by slowing the rate of mergers and acquisitions.

The road to the Colwyn Committee's restriction on bank amalgamations was a long one. The next chapter explains that the journey began in seventeenth-century Scotland where the legal environment fostered banks that were bigger than the English and Welsh banks.

CHAPTER TWO

THE SCOTTISH PRECEDENT: HOW JOINT STOCK BANKING CAME TO ENGLAND AND WALES

> Now, if it had not been for this iniquitous monopoly ... what would ... have been the condition of English banking at the present day? There would probably have been thirty or forty great banks in the Metropolis, each as great as the present Bank of England, with ... branches all over the country. It would … have been the Scottish system on a much larger scale, one commensurate with the greater magnitude of the country.[1]

English and Welsh banking emerged from the Industrial Revolution in far from rude health. The industry came close to collapse during a catastrophic run in 1825. Scotland boasted a far more stable banking industry than the English and Welsh did. The Scottish banks survived the 1825 financial crisis largely unharmed. The key difference was that Scottish banks were bigger than in England and Wales. Consequently, the Scottish public invested more confidence in their banks and chose not to orchestrate a run on them in 1825. Responsibility for this difference in bank size lay with a Scotland's legal system, which gave rise to a regime known as 'free banking.'[2] Scottish banks faced no legal impediments on their size, which meant they adopted the joint-stock principle at a time when banks in England and Wales were limited to a maximum of six members.

The English and Welsh banks' coexisted with the Bank of England, a state-sponsored corporate body sustained by a symbiotic relationship with the post-

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[1] Henry Dunning Macleod, *The Theory and Practice of Banking: With Elementary Principles of Currency; Prices; Credit; and Exchanges*, vol. II (London: Longman, Brown, Green and Longmans, 1856), 519; Henry Dunning Macleod, *The Theory and Practice of Banking*, 4th ed., vol. II (London: Longmans, Green, Reader and Dyer, 1886), 394.

[2] Lawrence H. White, *Free banking in Britain: Theory, experience, and debate, 1800-1845*, 2nd ed. (London: Institute of Economic Affairs, 1995); Sheila C. Dow and John Smithin, "Free banking in Scotland, 1695–1845," *Scottish Journal of Political Economy* 39, no. 4 (1992); Charles R. Hickson and John D. Turner, "Free banking and the stability of early joint-stock banking," *Cambridge Journal of Economics* 28, no. 6 (2004).

Glorious Revolution state. The Bank of England's purpose was to act as the government's banker and to lend money to the crown. Ensuring The Bank of England's shareholders remained sufficiently remunerated to fulfil their responsibilities to the state entailed bestowing them with privileges. One of those privileges was a legislative guarantee that the Bank of England would be the only banking company in the whole of England and Wales. That guarantee shaped the English and Welsh banking industry during the Industrial Revolution.

THE BANK OF ENGLAND MONOPOLY

William of Orange's regime erected the Bank of England in 1694 to fund a war with France. The infant Bank of England lent £1,200,000 of its capital at an interest rate of eight per cent per annum to the crown.[3] From its inception, the Bank of England was a Whig institution that attracted Tory opposition.[4] The Bank's Scottish promoter William Paterson considered those who opposed Bank of England "Jacobites" who were seeking to promote a deposed king's cause.[5] Within a few years, a Tory faction nearly succeeded in erecting a rival to the Bank of England. The legislation needed to create the National Land Bank passed into law in 1697.[6] Strangely, the National Land Bank's Tory origins did not stop King William III supporting it because the scheme promised to raise more money for him than the Bank of England had done.[7]

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[3] J. Lawrence Broz and Richard S. Grossman, "Paying for privilege: The political economy of Bank of England charters, 1694–1844," *Explorations in Economic History* 41, no. 1 (2004).

[4] Henry Warren, *The Story of the Bank of England: A History of the English Banking Movement and a Sketch of the Money Market* (London: R. A. Everett & Son, 1906), 8-9; A. Andréadès, *A History of the Bank of England, 1640-1904*, 4th ed. (London: Frank Cass & Co., 1966), 67-68; John Giuseppi, *The Bank of England: A History from its Foundation in 1694* (London: Evans Brothers, 1966), 9-10.

[5] Cited in S. Bannister, *William Paterson, the Merchant, Statesman and Founder of the Bank of England: His Life and Trials* (Edinburgh: William P. Nimmo, 1858), 92; Andréadès, *A History of the Bank of England*: 67.

[6] 7 & 8 William III c. 31.

[7] National Land Bank, "Proposals Made to the Honourable House of Commons, by the Land Bank United, for Raising Two Millions or More," (London: National Land Bank, 1696).

The security of this new bank would rest on mortgaged land rather than a reserve of gold and silver as was the case with the Bank of England.[8] The National Land Bank's Tory promoters expected the aristocrats who were their natural constituency to furnish the real estate needed to sustain the bank. However, the scheme came to nothing. The National Land Bank failed to attract the subscribers it needed to commence business.[9]

The National Land Bank proved an embarrassing failure for the Tories, but the attempt to establish it influenced the structure of the English and Welsh banking industry for years to come. The prospect of a rival convinced the Bank of England and its allies that it needed protection.[10] The first concession came in 1697 in the form of legislation that promised the parliament would never establish or permit a rival banking company in England and Wales.[11] The undertaking was unenforceable because Westminster parliaments are sovereign. The 1697 parliament could not limit the legislative powers of its successors.[12] A subsequent parliament could have erected or permitted another banking company in England and Wales had it wished. Nevertheless, the Bank of England rendered valuable services to the state, which

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[8] Hugh Chamberlen, *A Brief Narrative of the Nature & Advantages of the Land-Bank, as Proposed by Dr. Hugh Chamberlen, The First Author of Founding a Bank on an Annual Revenue* (London: T. Sowle, 1695); Hugh Chamberlen, *The Several Articles or Parts of the Proposal Upon Land-Credit, Rationally Explained* (London: T. Sowle, 1695); Thomas Dalby, "Propositions for General Land-Banks," (London: Publisher Unknown, 1695); William Tindall, *Some Remarks upon the Bank and other Pretended Banks, with Reasons Humbly Offered to the Consideration of the Present Parliament for Establishing a Real Land-Fund, or a Money and Land Bank; Under a Regular Managery, with Unquestionable Controuls and Checks Upon Them* (London: E. Whitlock, 1696).

[9] Andréadès, *A History of the Bank of England, 1640-1904*: 107.

[10] Anonymous, *The Arguments and Reasons For and Against Engrafting Upon the Bank of England with Tallies, as they were Debated in the Late General Court of the Said Bank, Considered in a Letter to a Friend* (London: Publisher Unknown, 1697); Anonymous, *A Letter to a Friend, Concerning the Credit of the Nation: And with Relation to the Present Bank of England, as now Established by Act of Parliament. Written by a Member of the Said Corporation, for the Publick Good of the Kingdom* (London: E. Whitlock, 1697).

[11] 8 & 9 William III c. 20.

[12] A. V. Dicey, *Introduction to the Study of the Law of Constitution*, Third ed. (London: Macmillan and Company, 1889), 61-67.

made breaching the undertaking given in 1697 unthinkable.[13] Parliament honoured the undertaking until 1844 when the *Joint Stock Bank Act* gave other English and Welsh banks a conditional right to incorporate.[14]

The undertaking that parliament would never erect or permit another banking company implied the Bank of England should be the only banking company in England and Wales. Two defects in the 1697 legislation prevented the realisation of this objective. First, companies created for purposes other than banking might enter the banking industry through the back door without official consent. Both the Hollow Sword Blade Company and the Company of Mine Adventurers issued bank notes during the first decade of the eighteenth century.[15] The Hollow Sword Blade Company even advertised an intention to discount bills of exchange and to lend funds on security.[16] The second defect was that rivals might form large banking partnerships that could raise a lot of capital from their proprietors.[17] To close both loopholes, parliament passed further legislation. In 1707, parliament made it unlawful for a company other than the Bank of England or for a partnership whose proprietorship exceeded six to "borrow, owe or take up any sum or sums of money on their bills or notes payable on demand or at any less time than six months from the borrowing thereof."[18] These prohibitions were to become operative in September 1708. In the interim, parliament renewed the Bank of England's charter. The 1708

[13] Broz and Grossman, "Paying for privilege," 49.
[14] 7 & 8 Victoria c. 113.
[15] Corporation of the Mine Adventurers of England, "The Case of the Mine-Adventurers," (London: Corporation of the Mine Adventurers of England, 1708); Anonymous, "Some Reasons Against the Clause for Restraining all Corporations but the Bank of England, from Keeping Cash, or Borrowing Money Payable at Demand," (London: Publisher Unknown, 1708).
[16] W. Marston Acres, *The Bank of England From Within*, vol. I (London: Oxford University Press, 1931), 101; Giuseppi, *The Bank of England*: 37.
[17] Giuseppi, *The Bank of England*: 36-37.
[18] 6 Anne, c. 22.

Bank Charter Act and every subsequent *Bank Charter Act* passed until 1833 repeated the prohibitions contained in the 1707 act.[19] Borrowing on bills and notes payable on demand or at short notice encompassed the right to issue bank notes, an activity most bankers considered the defining feature of a bank.[20] Parliament appeared to have limited every banking partnership in England and Wales to a maximum of just six proprietors.

The six-partner limit shaped the English and Welsh banking industry until its partial repeal in 1826. During this period, the Bank of England opened no branches in the provinces and confined its operations to London.[21] The Bank of England shared the London market with a number of private banks that limited their membership to six even though they no longer issued bank notes. The West End banks serviced London's urban bourgeoisie and aristocrats who came to town to attend parliament. The City banks accommodated the City of London's mercantile community.[22] Only a few banks existed in the provinces prior to the Industrial Revolution. In 1750, Edmund Burke (1729-1797) estimated fewer than a dozen "banking shops" were open for business in the whole of England.[23] However, the Industrial Revolution increased the provincial demand for credit giving rise to a growing number of country banks to service this demand.[24] By 1797, the merchant banker Francis Bearing (1740-1810) could assert that "almost every town and even ...

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19 7 Anne c.7, 12 Anne c. 11; 15 George II c. 13; 4 George III c. 25; 21 George III c. 60; 39 & 40 George III c. 28.

20 L. S. Pressnell, *Country Banking in the Industrial Revolution* (Oxford: Clarendon, 1956), 5-6.

21 Giuseppi, *The Bank of England*: 92-93.

22 Pressnell, *Country Banking in the Industrial Revolution*: 75; D. M. Joslin, "London private bankers, 1720-1785," *The Economic History Review* New Series 7, no. 2 (1954).

23 Edmund Burke, "Letter I: On the overtures of peace," in *Burke Selected Works: Four Letters on the Proposals of Peace With the Regicide Directory of France* ed. E. J. Payne (Oxford: Clarendon Press, 1892), 59.

24 Pressnell, *Country Banking in the Industrial Revolution*.

villages" possessed at least one banking establishment.[25] L. S. Pressnell estimated there were 370 English and Welsh country banks open for business in 1800.[26] The six-partner limit applied to every one of these banks.[27] An average English and Welsh bank had only three proprietors in 1822.[28]

In England and Wales, a state-sponsored Bank of England coexisted with many private banks limited to a maximum of six members prior to 1826. In Scotland, the banking industry was different because the origins of the Scottish banking industry lay with the establishment of the Bank of Scotland, an event that predated the union with England and Wales. Once that union was complete, the authorities in Westminster saw no need to protect a Bank of Scotland that had never lent money to the crown. The next section will explain that Westminster would incorporate rivals to the Bank of Scotland. Two additional Scottish banking companies (the Royal Bank of Scotland and the British Linen Company) emerged during the eighteenth century.

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[25] Francis Baring, *Observations on the Establishment of the Bank of England and on the Paper Circulation of the Country* (London: Sewell, Cornhill and Debrett, 1797), 15.
[26] Pressnell, *Country Banking in the Industrial Revolution*: 11.
[27] Thomas Joplin, *An Essay on the General Principles and Present Practice of Banking in England and Scotland: With Observations Upon the Justice and Policy of an Immediate Alteration in the Charter of the Bank of England, and the Measures to be Pursued in Order to Effect It*, Second ed. (London: Ridgway & Company, 1822); Lord Liverpool, Chancellor of the Exchequer, and Bank of England, "Communications relating to an alteration of the exclusive privileges enjoyed by the Bank of England," in *Parliamentary Papers: Finance Accounts of the United Kingdom in Eight Classes for the Year 1825 Ended Fifth January 1826: Also Accounts Related to Revenue; Debt; Exchequer Bills; Taxes; Bank of England; etc. (Session 2 February to 31 May 1826)*, ed. House of Commons (London: Parliament of the United Kingdom, 1826).
[28] Pressnell, *Country Banking in the Industrial Revolution*: 226.

SCOTLAND'S THREE PUBLIC BANKS

The Bank of Scotland was the creation of the Scottish parliament in 1695.[29] At the time, Scotland was a sovereign state albeit one whose independence rested upon uncertain foundations because of the union of the crowns.[30] Scotland even became a republic after the English executed Charles I (1600-1649) at the end of the Civil War.[31] In 1695, the Scottish parliament had no desire to fund their neighbour's war with France. Consequently, the Scottish parliament stipulated the newly established Bank of Scotland would not lend money to the crown without its consent and subsequently withheld that consent. Thus, the Bank of Scotland was a very different creature to the Bank of England from the outset. The Bank of Scotland was a commercial venture designed to foster Scotland's economic development not a state bank.[32] Nevertheless, the *Act for Erecting a Bank of Scotland* did accord the infant Bank of Scotland one valuable privilege. It forbade "Persons to enter into and set up a distinct company of bank within this Kingdom, besides these persons ... in whose favours this Act is granted."[33] The Bank of Scotland had a monopoly on corporate banking in Scotland that would expire in 1716.

Defending the banking monopoly granted to the Bank of Scotland proved a difficult task at first. In 1696, the Company of Scotland for Trading with Africa and

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[29] The Act for Erecting a Bank of Scotland is reproduced in Anonymous, *Acts of Parliament in Favour of the Bank of Scotland* (Edinburgh: Alexander Kincaid, 1784). It also constitutes Appendix I of Richard Saville, *Bank of Scotland: A History, 1695-1995* (Edinburgh: Edinburgh University Press, 1996).

[30] Graham Parry, *The Golden Age Restored: The Culture of the Stuart Court, 1603-42* (Manchester: Manchester University Press, 1981).

[31] R. Spurlock, *Cromwell and Scotland: Conquest and Religion, 1650–1660* (Edinburgh: John Donald, 2007).

[32] S. G. Checkland, *Scottish Banking: A History, 1605-1973* (Glasgow: Collins, 1975), 24-26.

[33] Anonymous, *Acts of Parliament in Favour of the Bank of Scotland* 15; Andrew William Kerr, *History of Banking in Scotland* (Glasgow: David Bryce & Son, 1884), 22.

the Indies (the Darien Company) started to issue bank notes.[34] The far better capitalised Darien Company claimed that it was a trading company and as such, it was not a 'distinct company of bank' and could issue bank notes without breaching the Bank of Scotland's monopoly. The Bank of Scotland's officials determined their best course of action would be to wait the Darien Company out rather than settle the matter in court. Their strategy succeeded. The Darien Company's preparations for its ill-fated expedition to the Isthmus of Panama caused it to lose interest in its bank notes and it soon stopped issuing them. The Bank of Scotland survived the first serious threat to its existence.[35]

The Bank of Scotland's monopoly lapsed in 1716 by which time the Scottish parliament no longer existed. Scotland was now part of the United Kingdom and so the Bank of Scotland would have to apply to Westminster to renew its monopoly. The Bank of Scotland never made the application. An oft-repeated legend suggests the failure to make the application had its origins in the Jacobite rebellion of 1715. George I (1660-1727) and his supporters considered the Bank of Scotland a Jacobite institution because its Treasurer sympathised with the Old Pretender's supporters. Consequently, the Bank of Scotland's officials assumed Westminster would refuse a request to have the monopoly renewed.[36] However, an anonymous Bank of Scotland official writing in 1728 gave another reason for the failure to apply for a renewal of the monopoly. He claimed, "No ... Scotsmen who had the nation's welfare at heart

[34] Kerr, *History of Banking in Scotland*: 23-24.
[35] Checkland, *Scottish Banking*: 33-37.
[36] William Hugh Logan, *The Scottish Banker; or, a Popular Exposition of the Practice of Banking in Scotland*, Second ed. (Edinburgh: Gallie and Bayley, 1844), 77.

would ever attempt to disquiet the Bank [of Scotland]."[37] If the Bank of Scotland thought national feeling rendered it immune to competition, it was wrong. In 1727, the Royal Bank of Scotland came into existence.[38]

The Royal Bank of Scotland was a consequence of the Darien Company's disastrous Central American adventure.[39] Much of 'the equivalent' paid to Scotland pursuant to the *Acts of Union* compensated those who lost money due to the Darien Company's failure. Not everyone compensated received a cash payment. Many received long-term debt securities known as 'equivalent debentures.' By 1724, the holders of these equivalent debentures had obtained a royal charter to erect a company to represent their interests. Almost immediately, this company set out to break the monopoly held by the Bank of Scotland. Its associates undermined the Bank of Scotland's reputation, alleging that it had failed Scotland by granting too little credit.[40] For its part, the Bank of Scotland claimed the Equivalent Company was orchestrating a smear campaign against it. A Bank of Scotland official complained, "Those of the Bank [of Scotland] do show all due respect to the Equivalent [Company's] proprietors and have said nothing, but what was absolutely necessary for their own vindication" before adding they "have not met with the same chivalry from the other side."[41] The Bank of Scotland's protest came to nothing. The Bank of Scotland remained suspect in London because of its alleged connections

[37] Bank of Scotland, *An Historical Account of the Establishment, Progress and State of the Bank of Scotland; and the Several Attempts that Have Been Made Against it and the Several Interruptions and Inconveniences Which the Company has Encountered* (Edinburgh: Bank of Scotland, 1728), 27.
[38] Royal Bank of Scotland, *Warrant of the Charter Erecting the Royal Bank of Scotland* (Edinburgh: James Davidson and Company, 1729).
[39] Kerr, *History of Banking in Scotland*: 34-41; Checkland, *Scottish Banking*: 44-58.
[40] Checkland, *Scottish Banking*: 58.
[41] Bank of Scotland, *An Historical Account of the Establishment, Progress and State of the Bank of Scotland*: 28.

to the Jacobite cause.[42] On 31 May 1727, the Equivalent Company obtained the royal charter it needed to establish the Royal Bank of Scotland.[43]

Almost immediately, the Bank of Scotland (the 'Old Bank') and the Royal Bank of Scotland (the 'New Bank') embarked on a fight for survival. Both assumed Scotland was too small to sustain two banking companies.[44] The Royal Bank of Scotland held the upper hand initially. Its rival's bank notes were in circulation and every one of them imposed a contractually binding promise on the Old Bank to make a payment on demand. The New Bank and its associates accumulated Bank of Scotland notes in large numbers and presented them *en masse* for redemption. The tactic seemed to work at first because the Bank of Scotland suspended payments in March 1728.[45] After that, the Royal Bank ramped up the pressure. It petitioned the Court of Session to enforce its claim against the Bank of Scotland and appealed to the House of Lords after the Court of Session ruled in the Bank of Scotland's favour.[46] The Bank of Scotland used the time these court proceedings made

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[42] Logan, *The Scottish Banker*: 77; Kerr, *History of Banking in Scotland*: 34; Checkland, *Scottish Banking*: 57-58.

[43] Checkland, *Scottish Banking*: 59.

[44] For accounts of the ensuing conflict between the Bank of Scotland and the Royal Bank of Scotland see: Bank of Scotland, *An Historical Account of the Establishment, Progress and State of the Bank of Scotland; and the Several Attempts that Have Been Made Against it and the Several Interruptions and Inconveniences Which the Company has Encountered*; Anonymous, *A Letter Containing Remarks on the Historical Account of the Old Bank; by a Gentleman Concerned with Neither Bank* (Edinburgh: James Davidson & Company, 1728).

[45] Bank of Scotland, "An Exact State or Abbreviate of the Affairs of the Bank of Scotland, as They Stand Ballanced to the 27th March 1728, the Day Upon Which They Were Obliged to Stop Payments, Through Deficiency of Cash: And How the Same Stands This 18th June of the Said Year," (Edinburgh: Bank of Scotland, 1828).

[46] Royal Bank of Scotland, "(July 18, 1728) Unto the Right Honourable, the Lords of Council and Session, the Petition of the Royal Bank of Scotland," (Edinburgh: Royal Bank of Scotland, 1728); Bank of Scotland, "The Governor and Company of the Royal Bank of Scotland, and Andrew Cochran, Appellants. The Governor and Company of the Bank of Scotland, Respondents. The Respondents Case. To be Heard at the Bar of the House of Lords, on Thursday the lst of May, 1729," (Edinburgh: Bank of Scotland, 1728); Royal Bank of Scotland, "The Governor and Company of the Royal Bank of Scotland, and Andrew Cochran, Merchant in Glasgow, Appellants. The Governor and Company of the Bank of Scotland, Respondents. The Appellants' Case. To be Heard at the Bar of the House of Lords on Thursday the First Day of May 1729," (Edinburgh: Royal Bank of Scotland, 1729); Bank of

available to reorganise its finances. By September 1728, the Bank of Scotland was making cash payments with interest where necessary, once more. By the time the representatives of both banks made their submissions before the House of Lords, the Bank of Scotland was discharging its legal obligations, which rendered the Royal Bank of Scotland's complaint against it largely irrelevant.[47] Two evenly matched rivals realised that each of them lacked the resources needed to destroy the other outright and came to terms with each other's ongoing existence.

Two incorporated banking companies should have rendered eighteenth-century Scotland overbanked. In comparison, England and Wales only had one banking company and that was the Bank of England. Surprisingly, another royal charter laid the foundations for Scotland's third banking company in 1746.[48] The British Linen Company's objective was to facilitate Scotland's industrial development in the wake of the 1745 Jacobite Rebellion. The company received wide-ranging powers designed to promote Scottish linen manufacture.[49] The company's unusually permissive charter gave it the right to extend credit and to issue bank notes to do it. The company soon began to exploit this loophole to pursue a lucrative banking business.[50] By 1813, the company's directors could claim the British Linen Company was Scotland's third banking company in all but name. In that year, these directors told Treasury:

Scotland, "The Governor and Company of the Royal Bank of Scotland, (Called the New Bank) and Andrew Cochran, Merchant (Appellants). The Governor and Company of the Bank of Scotland, (Called the Old Bank) (Respondents). The Respondents Case to be Heard Before the Bar of the House of Lords on Thursday the 1st Day of May 1729," (Edinburgh: Bank of Scotland, 1729).

[47] Checkland, *Scottish Banking*: 62.

[48] British Linen Company, *The Charter of the British Linen Company* (Edinburgh: R. Fleming and Company, 1746).

[49] Checkland, *Scottish Banking*: 92-97.

[50] Logan, *The Scottish Banker*: 21-23; Checkland, *Scottish Banking*: 95.

> It was found ... [the company] ... could be of more service to the country, and its trade and manufactures, generally, by employing their credit and capital as bankers, granting pecuniary aid to those who applied to them, and were deemed worthy of support, issuing their notes for that purpose in the usual way, payable upon demand. It is now upwards of sixty years since the company gave up entirely the dealing in linen. From that period they have been universally considered as a third public bank....[51]

The Bank of Scotland and the Royal Bank of Scotland considered the British Linen company an unwanted interloper. In 1813, the Bank of Scotland and the Royal Bank of Scotland complained to the Treasury the British Linen Company's illicit banking business threatened to destabilise what was already an overcrowded banking industry.[52] Continued opposition from the Bank of Scotland and the Royal Bank of Scotland denied the British Linen Company the official recognition it craved until 1849. In that year, British Linen Company's charter finally conceded it had been a bank for nearly a century.[53] Even then, the British Linen Company waited until 1906 for permission to change its name to the British Linen Bank.[54]

The Bank of Scotland, the Royal Bank of Scotland and the British Linen Company were corporate bodies erected under special acts or royal charters. As such, they shared important features with other companies like the Bank of

[51] British Linen Company, "Oberservations of the Governor, Deputy Governor and Directors of the British Linen Company on the Memorial of the Governor, Deputy Governor and Directors of the Bank of Scotland and the Governor, Deputy Governor and Directors of the Royal Bank of Scotland Opposing the Application of the British Linen Company for a Charter to Eneable them to Increase their Capital," in *Proceedings in an Application at the Treasury for an Increase of Capital by the British Linen Company* ed. British Linen Company (London: E. Kirby, 1813), 19.
[52] Bank of Scotland and Royal Bank of Scotland, "Memorial of the Governor, Deputy Governor and Directors of the Bank of Scotland and the Governor, Deputy Governor and Directors of the Royal Bank of Scotland Opposing the Application of the British Linen Company for a Charter to Eneable them to Increase their Capital," ed. British Linen Company (London: E. Kirby, 1813).
[53] British Linen Company, *Charter, Erecting and Warrant of a Charter Confirming and Granting New Privileges to the British Linen Company* (Edinburgh: British Linen Company, 1849), 10; British Linen Company, *Supplementary Charter to the British Linen Company: 19th March, 1849* (Edinburgh: British Linen Company, 1849), 10.
[54] Checkland, *Scottish Banking*: 303.

England.[55] They all possessed a legal personality, which made them competent to defend or pursue legal disputes independently of their shareholders. A corporation also incurred its own debts and it was rightful owner of its property.[56] Consequently, a creditor only had recourse against the corporation's assets to recover any amounts owed to them. A creditor could not sue its proprietors to recover a debt, which bestowed the protection of limited liability upon a company's shareholders. In addition, corporations raised capital by issuing transferable shares upon which the corporation paid dividends. A shareholder could buy and sell these shares without disturbing the company's operations. Finally, corporations facilitated a separation of ownership and control. Corporations operated under the supervision of directors elected by the shareholders.

Incorporation constituted a valuable prize because of the privileges it bestowed but it was an expensive business. The of Bank of England's shareholders, for example, secured their company's continued existence by lending large sums of money to the state every time their charter came up for renewal.[57] However, one could exploit the laws of partnership, agency and trust to create an organisational form that replicated some, although not all, of a corporation's advantages at greatly reduced cost. The next section examines these unincorporated businesses on both sides of the Scottish border.

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[55] The following review of corporations is based on M. Schmitthoff, "The origin of the joint-stock company," *The University of Toronto Law Journal* 3, no. 1 (1939); Gary M. Anderson and Robert D. Tollison, "The myth of the corporation as a creation of the state," *International Review of Law and Economics* 3, no. 2 (1983).

[56] For a review of the basis upon which early incorporated enterprises held property see: Paddy Ireland, "Capitalism without the capitalist: The joint stock company share and the emergence of the modern doctrine of separate corporate personality," *The Journal of Legal History* 17, no. 1 (1996).

[57] Broz and Grossman, "Paying for privilege."

UNINCORPORATED JOINT STOCK COMPANIES

Partnerships were like a company in the sense that they facilitated collective effort. A partnership's proprietors embarked on a business enterprise in common in the pursuit of profit. However, partnerships imposed risks on their proprietors that were absent in an incorporated association. One problem was mutual agency. Anyone who shared in a partnership's profits could bind their fellow partners to a business debt.[58] Partners had to trust each other implicitly under these circumstances. In addition, partnerships lacked perpetual succession.[59] Partners terminated the partnership whenever they withdrew from the partnership. The admission of new partners needed the existing partners' consent. The absence of perpetual succession made buying and selling an ownership stake in a partnership difficult. Matters simplified enormously if the partners transferred the partnership's assets into a trust and appointed trustees to run the business as their agents.[60] The partners became the beneficiaries of a trust who lacked the capacity to commit each other to debts. There was also the option of issuing tradeable shares. The beneficiaries of a trust only needed to notify the trustees of the intention to transfer their claim against the trust to someone else to sell their shares. Finally, the trust could provide for the trustees' appointment by means of an election of the partners. Confusingly, these quasi-

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[58] See: *Grace v Smith* (1775) 96 English Reports 587; William Watson, *A Treatise on the Law of Partnership* (London: J. Butterworth, 1794), 17-24.

[59] Watson, *A Treatise on the Law of Partnership,* 398-411.

[60] John George, *A View of the Existing Law Affecting Unincorporated Joint Stock Companies* (London: S. Sweet, 1825); James William Gilbart, *A History of Banking in Ireland* (London: Longman, Rees, Orme, Brown, Green & Longman, 1836), 40-41; Bishop C. Hunt, "The joint-stock company in England, 1800-1825," *Journal of Political Economy* 43, no. 1 (1935); Armand Budington DuBois, *The English Business Company after the Bubble Act, 1720-1800* (New York: Octagon, 1971), 213-42; Anderson and Tollison, "The myth of the corporation as a creation of the state."; Margaret Patterson and David Reiffen, "The effect of the Bubble Act on the market for joint stock shares," *The Journal of Economic History* 50, no. 1 (1990); Robin Pearson, "Shareholder democracies? English stock companies and the politics of corporate governance during the industrial revolution," *The English Historical Review* 117, no. 473 (2002); Mark Freeman, Robin Pearson, and James Taylor, "'Different and better?' Scottish joint-stock companies and the law, c. 1720–1845," *The English Historical Review* 122, no. 495 (2007).

corporate, share-issuing partnership/trust arrangements called themselves 'joint stock companies' even though they had not incorporated. In a court of common law, an unincorporated joint stock company remained a partnership whose proprietors were liable for the company's debts.[61]

Unincorporated joint stock companies resolved some of the difficulties imposed by a partnership but they suffered from two legal impediments that made it impossible to use them to conduct banking business in England and Wales prior to 1826. The most obvious obstacle was the six-partner limit.[62] There was no point in erecting a share-issuing joint stock banking company when the law limited it to a maximum of six proprietors. It was easier to enter into a common law partnership instead. However, clause 18 of the *Bubble Act* of 1720 would have cast doubts over the legality of an unincorporated joint stock banking company in England and Wales even in the absence of the six-partner limit. Clause 18 declared:

> All undertakings … presuming to act as a corporate body … raising … transferable stock … transferring … shares in such stock … without legal authority, either by Act of Parliament, or by any Charter from the Crown, … [are] for ever to be deemed illegal and void.[63]

On its face, clause 18 denied an unincorporated English and Welsh joint stock company the right to raise capital by issuing transferable shares.[64] However, no one could agree on what clause 18 actually prohibited. The Attorney General

[61] Ireland, "Capitalism without the capitalist," 42-44.
[62] Pressnell, *Country Banking in the Industrial Revolution*: 226; John D. Turner, *Banking in Crisis: The Rise and Fall of British Banking Stability, 1800 to the Present* (Cambridge Cambridge Univeristy Press, 2014), 104-07.
[63] 6 George I c. 18.
[64] Ron Harris, "The Bubble Act: Its passage and its effects on business organization," *The Journal of Economic History* 54, no. 3 (1994).

complained the clause was "unintelligible" when parliament repealed it in 1825.[65] It did not help that the courts got little opportunity to clear up the confusion. Prosecutions of an alleged breach of clause 18 were rare. The 1724 case of *Rex v Cawood* constituted the only time a breach of clause 18 came before an English court during the whole of the eighteenth century.[66] The case determined nothing of any real significance. When an alleged breach of clause 18 came before a court for the second time in 1808, legal opinion remained divided as to its true meaning.[67]

A literal reading of clause 18 coupled with an understanding of the circumstances under which it passed into law suggested the need for strict interpretation. The South Sea Company asked parliament to insert clause 18 into legislation establishing two other companies (the Royal Exchange Assurance Corporation and the London Assurance Corporation) to stop other incorporated and unincorporated associations issuing shares into the notorious bull market that had developed in its shares.[68] One could argue, therefore, that parliament gave corporations like the South Sea Company an exclusive right to issue tradeable shares.

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[65] Parliament of the United Kingdom, *Parliamentary Debates: Published Under the Superintendence of T. C. Hansard. Commencing with the Accession of George IV*, vol. New Series: XIII (London: T. C. Hansard, 1826), 1019.

[66] Lord Robert Raymond, *Reports of Cases Argued and Adjudicated in the Courts of Kings Bench and Common Pleas in the Reigns of the Late King William, Queen Anne, George the First and George the Second*, vol. II (Dublin: George Wilson, 1792), 1361. See also; Charles F. F. Wordsworth, *The Law Relating to Railway, Bank, Insurance, Mining and Other Joint-Stock Companies*, Second ed. (London: Henry Butterworth, 1837), 12.

[67] *Rex v Dodd* (1808) 103 English Reports 670; Anonymous, *Report of the Arguments, Upon the Application to the Court of King's Bench, for Leave to File an Information Against Mr. Ralph Dodd, Upon the Statute of 6 Geo. I. cap. 18* (London: J. M. Richardson, 1808); Henry Day, *A Defence of Joint Stock Companies: Being an Attempt to Shew Their Legality, Expediency, and Public Benefit* (London: Longman, Hurst, Rees, and Orme, 1808).

[68] Henry N. Butler, "General incorporation in nineteenth century England: Interaction of common law and legislative processes," *International Review of Law and Economics* 6, no. 2 (1986): 173.

Some legal commentators claimed clause 18 rendered it illegal to issue transferable shares for a purposes not permitted by a royal charter or a special act of parliament.[69]

The difficulty with a strict interpretation of clause 18 was the penalty imposed for its breach. Anyone found guilty of issuing transferrable shares illegally was liable for punishment under the *Statute of Præmunire* of 1393.[70] Originally, the *Statute of Præmunire* denied Richard II's (1367-1400) subjects the right to appeal an English court's judgement to the Pope. Appeals to Rome were a serious matter for a Richard who did not want his courts' authority undermined by a foreign power.[71] Consequently, the *Statute of Præmunire* asserted a matter of constitutional importance and the penalty it imposed rendered offenders liable to incarceration at his Majesty's pleasure.[72] As William Blackstone (1723-1780) noted, the number of offenses liable to punishment under the *Statute of Præmunire* generally increased every time those in power had a matter of constitutional importance to assert.[73] It became a præmunire to sue "to Rome for any license or dispensation; or to obey any process from thence" under Henry VIII (1491-1547).[74] The claim that parliament could legislate without the Crown's assent became a præmunire under a restored Charles II (1630-1685).[75] Maintaining that James II's (1633-1701) catholic descendents had a better claim to the throne than Queen Anne (1665-1714) and the

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[69] Patterson and Reiffen, "The effect of the Bubble Act."; Harris, "The Bubble Act."
[70] 16 Richard II c. 5.
[71] William Blackstone, *Commentaries on the Laws of England*, Sixteenth ed., vol. IV (London: T. Cadell and J. Butterworth, 1825), 112.
[72] Francis Bacon, *The Works of Francis Bacon, Baron of Velum, Viscount of St. Alban and Lord High Chancellor of England in Ten Volumes*, vol. IV (London: J. Crowder and E. Hemsted, 1803), 299-300; Blackstone, *Commentaries on the Laws of England*: 112.
[73] Blackstone, *Commentaries on the Laws of England*: 113-16. See also: William T. Waugh, "The Great Statute of Praemunire," *English Historical Review* 37, no. 146 (1922); John A Guy, "Henry VIII and the praemunire manoeuvres of 1530-1531," *English Historical Review* 97, no. 384 (1982).
[74] Blackstone, *Commentaries on the Laws of England*: 113. The act was 24 Henry VIII c. 12.
[75] 13 Charles II c. 1.

protestant line nominated by parliament to succeed her became a præmunire after the Glorious Revolution.[76] The *Bubble Act* had invoked a powerful constitutional tool to punish the relatively innocuous constitutional crime of challenging the parliament's right to control the nation's capital markets. In 1825, the Attorney General expressed incredulity that the law could hold a person liable for "the heaviest penalty" under these circumstances.[77] The severity of the penalty imposed suggested the courts should adopt a permissive interpretation of clause 18. Some legal commentators maintained the prohibition on issuing transferable shares only applied to unincorporated enterprises deemed prejudicial to the public good.[78]

Clause 18 was something of a dead letter in England and Wales because of the authorities' reluctance to enforce it. When it was repealed in 1825, the Attorney General observed, "From the year 1720 … down to the present time [unincorporated joint stock] companies have been formed for the most useful and laudable purposes."[79] The authorities took no action against these businesses even though many of them issued transferable shares. However, clause 18 cast a shadow over English common law because the courts could hardly recognise an organisational form whose legality was open to question. The common law courts sustained the fiction that unincorporated joint stock companies remained mere partnerships and they dealt with them accordingly.[80] The unincorporated joint stock company was a

[76] 6 Anne c. 41.
[77] Parliament of the United Kingdom, *Parliamentary Debates: Published Under the Superintendence of T. C. Hansard. Commencing with the Accession of George IV*, New Series: XIII: 1019.
[78] Day, *A Defence of Joint Stock Companies*.
[79] Parliament of the United Kingdom, *Parliamentary Debates: Published Under the Superintendence of T. C. Hansard. Commencing with the Accession of George IV*, New Series: XIII: 1019.
[80] DuBois, *The English Business Company after the Bubble Act*: 217; Hunt, "The joint-stock company in England," 22; Anderson and Tollison, "The myth of the corporation as a creation of the state," 110; Butler, "General incorporation in nineteenth century England," 172-73; Patterson and Reiffen, "The effect of the Bubble Act," 170.

legal outsider in England and Wales, a "step-child" of the law that had "serious legal difficulties to surmount."[81] Clause 18's repeal in 1825, for example, did not stop some judges finding the common law precedents they needed to declare transferrable share-issuing unincorporated joint stock companies illegal in the 1830s.[82] If an unincorporated joint stock company ventured into court, it did so as a partnership and litigated in the names of all of its members even though their number could run into the hundreds and a single error or omission would invalidate the action.[83] The only way around the absence of a legal personality was to petition parliament for special legislation that permitted the company to pursue and defend legal actions in the name of nominated company officers.[84]

In Scotland, the courts paid less attention to the *Bubble Act* than the English and Welsh courts did. Clause 18 should have applied in Scotland. There was nothing in the *Bubble Act* to suggest it only applied to England and Wales. This was an inconvenience the Scots avoided by ignoring the clause when they went to court.[85] One of the few times a party referred to clause 18 in a Scottish court occurred in 1730 in *Masons of the Lodge of Lanark v Hamilton*.[86] The Court of Session made no determination on Hamilton's submission that his lodge had breached the clause 18, which left the question of its applicability to Scotland unresolved. The Court of Session finally resolved the issue in 1828, three years after the *Bubble Act*'s repeal.

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[81] DuBois, *The English Business Company after the Bubble Act*: 217.
[82] Examples include *Duvergier v Fellows* (1832) 5 Bing 248, 267; *Blundell v Windsor* (1837) 8 Simmons 601, 607. See: Lorraine Talbot, *Critical Company Law*, Second ed. (Abingdon: Routledge, 2016), 21-22.
[83] Hunt, "The joint-stock company in England," 11; DuBois, *The English Business Company after the Bubble Act*: 217-22.
[84] Butler, "General incorporation in nineteenth century England," 173-74.
[85] J. Roberton Christie, "Joint stock enterprise in Scotland before the companies acts," *Judicial Review* 21, no. 2 (1909): 137-38.
[86] The case is reported in Lord Henry Home of Kames, *Remarkable Decisions of the Court of Session From the Year 1730 to the Year 1752* (Edinburgh: A. Kincaid and J. Bell, 1766), 4-5.

In *MacAndrew v Robertson* the Lord President pointed to the *Bubble Act*'s saving clause,[87] noted that in Scotland unincorporated companies were in the habit of issuing transferrable shares and none of them had been declared illegal before concluding "by our law such an association is not illegal."[88]

The refusal to acknowledge the *Bubble Act* gave the Scottish courts opportunities to bestow privileges on the unincorporated joint stock companies appearing before them that English and Welsh courts could not. One was the capacity to engage in a legal action without the need to append the names of all their partners to it. In 1841, *London, Leith, Edinburgh and Glasgow Shipping Company and William Crichton v Archibald M'Corkle* resolved beyond all doubt that a Scottish unincorporated joint stock company pursued and defended legal actions in its descriptive name with the names of three partners appended.[89] However, an 1828 appeal taken the House of Lords also made it clear that in Scotland unincorporated joint stock companies defended legal actions in their descriptive names with just the names of several partners appended and had done so for a considerable period.[90] In truth, the only ambiguity as to how an unincorporated joint stock company litigated in Scotland prior to 1841 related to how it pursued legal action. In *London, Leith, Edinburgh and Glasgow Shipping Company and William Crichton v Archibald M'Corkle*, the Court of Session's Lord Medwyn (1778-1854) explained the Court of

[87] The Act was not to "be construed to extend to prohibit or restrain the carrying on of any … trade in partnership, as hath been hitherto usually and may be legally done."
[88] Patrick Shaw and Alexander Dunlop, *Cases Decided in the Court of Session From 13 November 1827 to July 11 1828*, vol. VI (Edinburgh: Thomas Clarke, 1828), 950-55.
[89] Reported in J. M. Bell, John Murray, and James Donaldson, *Cases Decided in the Court of Session From 12 November 1840 to July 20 1841*, vol. III (Edinburgh: William Blackwell, 1842), 1045-47.
[90] The case was *Commercial Banking Company of Scotland and Others v Pollock's Trustees.* It is reported in James Wilson and Patrick Shaw, *Cases Decided in the House of Lords on Appeal from the Courts of Scotland (1828-1829)*, vol. III (London: T. Caddell and M. Stevens and Sons, 1830), 365-66.

Session had always taken a pragmatic approach to the question of an unincorporated joint stock company's legal identity. He claimed an unincorporated joint stock company should know who its shareholders were. Demanding it initiate legal action in all of their names imposed no hardship on an unincorporated joint stock company whatsoever. The position of an outsider was different according to Lord Medwyn. An outsider could not know who all the shareholders were and so did not have to name them when they sued an unincorporated company. Consequently, Scotland' unincorporated joint stock companies habitually defended legal actions with the names of a few shareholders appended.[91]

Scottish law and English common law differed over the question as to whether an unincorporated joint stock company had the right to issue transferable shares and whether they possessed a workable legal identity. However, they did agree on one fundamental point. Both held an unincorporated joint stock companies' proprietors liable for its debts. In England and Wales, unlimited shareholder liability was the inevitable consequence an unincorporated company's underlying status as a partnership.[92] Scottish law adopted a similar position in the end, although it came close to taking a far more radical stance in 1757. In *Stevenson v Macnair*, the Court of Session expressed the view that the plaintiff entered a contract with an unincorporated company knowingly. He must have expected, the court reasoned, that he would have to rely on the company's resources alone to fulfil its obligations

[91] *London, Leith, Edinburgh and Glasgow Shipping Company and William Crichton* (the manager and also a partner) *v Archibald M'Corkle*, Bell, Murray, and Donaldson, *Cases Decided in the Court of Session From 12 November 1840 to July 20 1841*, III: 1046.
[92] Hunt, "The joint-stock company in England," 30-31; Butler, "General incorporation in nineteenth century England," 178-79.

to him. The court refused to hold the company's proprietors liable to him.[93] *Stevenson v Macnair* elevated a Scottish unincorporated joint stock company to the status of a *société en commandite*, a partnership form recognised in French law that facilitated the separation of ownership and control by according protection to proprietors who did not engage in the day-to-day management of the business.[94] The ruling ultimately proved too radical even for Scotland's Court of Session. Eventually, *Stevenson v Macnair* became a neglected legal aberration that accorded shareholders no protection whatsoever.[95] In the 1770s, the shareholders of the Ayr Bank (Douglas, Heron and Company) found themselves liable for all of its debts even though most of them exercised no control over the bank's day-to-day management.[96] A Scottish unincorporated joint stock company was not a *société en commandite* after all. All of its shareholders were liable to its creditors.

The combined effects of clause 18 and the six-partner rule precluded any possibility that English and Welsh bankers might erect unincorporated joint stock companies prior to 1826. English and Welsh bankers formed common law partnerships because they could not admit more than six proprietors. In addition, English and Welsh courts demanded English and Welsh banks pursue and defend legal actions in the names of all of their proprietors. Finally, the *Bubble Act* might render the promoters of an English and Welsh joint stock bank liable for severe

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[93] John Campbell et al., *Faculty Decisions: Decisions in the Court of Session from the End of the Year 1756 to the End of the Year 1760* (Edinburgh: A. Kincaid & J. Bell, 1765), 87-88.

[94] Et Martin Saint-Léon, "Commandite in France," *The Economic Journal* 17, no. 66 (1907).

[95] Freeman, Pearson, and Taylor, "'Different and better?,'" 69; R. F. Campbell, "The Law and the joint-stock company in Scotland," in *Studies in Scottish Business History*, ed. Peter L. Payne (Abingdon: Routledge, 2006), 147-48.

[96] Douglas Heron and Company (Bankers: Ayr Scotland), *The Precipitation and Fall of Mess. Douglas, Heron and Company, Late Bankers in Ayr, With the Causes of Their Distress and Ruin, Investigated and Considered, by a Committee of Inquiry, Appointed by the Proprietors* (Edinburgh: Douglas, Heron and Company, 1778). For more on the failure of the Ayr Bank see: Paul Kosmetatos, "The winding-up of the Ayr Bank, 1772–1827," *Financial History Review* 21, no. 02 (2014).

penalties if they issued transferable shares. In contrast, Scotland had no six-partner limit, its unincorporated joint stock companies possessed a workable legal identity and the courts ignored the *Bubble Act*'s prohibition on issuing transferable shares. It is not surprising that Scotland developed Britain's first unincorporated joint stock banks under these circumstances.

SCOTLAND'S UNINCORPORATED BANKING COMPANIES

Three incorporated banks might have rendered Scotland overbanked but nothing could have been further from the truth. The Bank of Scotland and the Royal Bank of Scotland generally confined their operations to Edinburgh. Both preferred to enter into alliances in places like Glasgow, Perth, Dundee and Aberdeen to conduct operations outside Edinburgh. Only the Bank of Scotland experimented with branches outside Edinburgh in the 1690s and again in the 1730s although it soon abandoned the experiment on both occasions. Later, the British Linen Company operated an embryonic branch network. The British Linen Company had putting-out agents in the provinces due to its interest in linen manufacture who could issued its bank notes to make payments.[97] However, the public three banks lacked the means needed to meet provincial Scotland's growing demand for banking services. Scotland was not overbanked after all.

The first Scottish banks to fill the provincial void were comparatively small-scale affairs that would not have looked out of place in England and Wales because they admitted six partners or less at their inception.[98] Aberdeen led the way in 1747

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[97] Checkland, *Scottish Banking*: 31-32, 96-100.
[98] Charles W. Munn, *The Scottish Provincial Banking Companies, 1747-1864* (Edinburgh: John Donald, 1981), 222-24; Graeme G. on, Charles R. Hickson, and John D. Turner, "Organisational

where Messrs Livingstone, Mowrat, Bremner and Dingwall formed the Banking Company at Aberdeen. This bank had four proprietors when it commenced business. Three years later, Glasgow's Dunlop, Houston & Company began trading as the Ship Bank. The Ship Bank had six partners when it opened its doors.[99] A third bank soon joined them in the shape of Glasgow's Arms Bank. This latter bank also began operations in 1750, although it was a much larger institution than either the Banking Company at Aberdeen or the Ship Bank. The Arms Bank boasted a proprietorship of 31 at its inception, which would have rendered it illegal in England and Wales.[100] The Bank of Scotland and the Royal Bank of Scotland viewed the emergence of their new rivals with of alarm. The Bank of Scotland and the Royal Bank of Scotland challenged the right of the Banking Company at Aberdeen, the Ship Bank and the Arms Banks to issue bank notes in the courts. The Bank of Scotland and the Royal Bank of Scotland threatened the three provincial rivals' customers by refusing to do business with them. Finally, the Bank of Scotland and the Royal Bank of Scotland adopted the time-honoured tactic of organising runs utilising their provincial rivals' bank notes. The Banking Company at Aberdeen succumbed to the pressure and closed its doors in 1753. The two Glaswegian banks survived the onslaught.[101]

The survival of Glasgow's Ship Bank and Arms Bank set a precedent for those who aspired to enter the banking industry but knew the authorities in Westminster were unlikely to grant them a special act or a royal charter to do it. More than 40 unincorporated banking institutions opened their doors in the Scottish provinces

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flexibility and governance in a civil-law regime: Scottish partnership banks during the Industrial Revolution," *Business History* 53, no. 4 (2011): 508.

[99] Kerr, *History of Banking in Scotland*: 61-65.

[100] Checkland, *Scottish Banking*: 97-103; Munn, *The Scottish Provincial Banking Companies*: 222-24; Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime," 508.

[101] Kerr, *History of Banking in Scotland*: 61-65; Checkland, *Scottish Banking*: 100-02.

between 1747 and 1836.[102] Some were no bigger than their English and Welsh counterparts were. Charles Munn argued that these smaller banks hardly deserved the title ‘company’ because most were nothing more than mere partnerships.[103] Other Scottish banks possessed far larger proprietorships, which made them too big to operate as partnerships. Most of these larger unincorporated Scottish banks identified themselves as ‘banking companies’ even though they had not incorporated.[104] The Aberdeen Banking Company, for example, had 109 partners at its inception in 1767.[105] Its constitution permitted its shareholders to transfer their “Share or Shares of Stock to any person he shall think proper.”[106] This bank and others like it did something their contemporaries in England and Wales could have never done. They issued transferable shares to a large proprietorship to raise capital.

Scotland’s unincorporated banks acquired a reputation for stability. Only 14 banks erected in Scotland between 1747 and 1836 failed and nearly half of them did so without any loss to the public.[107] The collapse of Douglas, Heron and Company (better known as the Ayr Bank) in 1772 was the most notorious Scottish bank failure during this period.[108] However, the Ayr Bank’s failure demonstrated that Scotland’s unincorporated joint stock banks were comparatively safe. The bank had a large

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[102] Checkland, *Scottish Banking*: 135, 78-79, 320-21, 72-73; Munn, *The Scottish Provincial Banking Companies, 1747-1864*: 16-22, 222-24; Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime," 508.
[103] Munn, *The Scottish Provincial Banking Companies*: 5-6.
[104] See for example: Anonymous, "The Humble Petition of the Subscribers, Private Bankers, Partners, or Managers, or Cashiers of Private Banking Companies, Carrying on the Business of Issuing and Re-issuing Promissory Notes for Payment of Sums of Money to the Bearer on Demand (Commonly Called Bank Notes), in That Part of the United Kingdom Called Scotland," (Edinburgh: Publisher Unknown, 1813).
[105] Munn, *The Scottish Provincial Banking Companies*: 222.
[106] Banking Company in Aberdeen, *The Contract of the Banking Company in Aberdeen* (Aberdeen: J. Chalmers, 1767), 8.
[107] Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime," 508.
[108] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. Edwin Cannan, 6th ed., vol. I (London: Methuen & Co, 1950), 333-34; Kerr, *History of Banking in Scotland*: 77-89.

proprietorship many of whom were wealthy landowners.[109] When the Ayr Bank failed, its proprietorship proved wealthy enough to meet all of the bank's debts. Half of the bank's shareholders became insolvent; and yet, its creditors recovered everything owed to them.[110] Robert Burns (1759-1796) called the Ayr Bank as a "villainous bubble" for good reason.[111] This bank ruined many of its shareholders but its large proprietorship ensured the Ayr Bank imposed no loss on the public.

In 1810, Scotland's preference for large banking companies reached its natural conclusion with the establishment of the Commercial Banking Company of Scotland. This was a new kind of banking institution. The promoters' intention from the outset was to erect a bank that would have a national presence.[112] The Commercial Bank's headquarters would be in Edinburgh, but its operations were to embrace the whole of Scotland.[113] To achieve this objective, the bank possessed an authorised capital of £3,000,000 divided into 6,000 transferable shares of £500 each, an unprecedented amount that reflected the scale of the promoters' ambitions.[114] The Bank of Scotland and the Royal Bank of Scotland only had an authorised capital of £1,500,000 each at the time.[115] The Bank of Scotland and the Royal Bank of Scotland recognised the threat this new entrant posed and attempted to destroy it before it gained a foothold

[109] Henry Hamilton, "The failure of the Ayr bank, 1772," *The Economic History Review* New Series 8, no. 3 (1956); Munn, *The Scottish Provincial Banking Companies*: 86-87.
[110] Hamilton, "The failure of the Ayr bank."; Kosmetatos, "The winding-up of the Ayr Bank."
[111] Robert Burns, "When I upon that bosom lean," in *The Works of Robert Burns*, ed. R. H. Cromek (Baltimore: F. Lucas and J. Cushing, 1815), 166.
[112] Kerr, *History of Banking in Scotland*: 114-16; James L. Anderson, *The Story of the Commercial Bank of Scotland Limited During its Hundred Years from 1810 to 1910* (Edinburgh: F. & E. Murray, 1910), 1-4; Checkland, *Scottish Banking*: 284-94.
[113] Kerr, *History of Banking in Scotland*: 114-16; Anderson, *The Story of the Commercial Bank of Scotland*: 1-4; Checkland, *Scottish Banking*: 284-94.
[114] Commercial Bank of Scotland, *Articles of Copartnery of the Commercial Banking Company of Scotland* (Edinburgh: Alex Lawrie & Company, 1810), 1.
[115] Checkland, *Scottish Banking*: 287.

in the industry. The Bank of Scotland and the Royal Bank of Scotland failed. The Commercial Bank of Scotland prospered after a difficult start.[116]

One should exercise caution before ascribing the stability of Scotland's unincorporated banks to their large proprietorships alone. Scottish bankers were adept at avoiding their obligations when they fell due. Scottish banks added option clauses to their bank notes until legislation banned the practice in the 1760s.[117] These option clauses reserved the right to redeem a bank note on demand or after a delay of six months at the cost of an interest payment. The option was exercisable at the bank's discretion.[118] The Scottish banks used other ways to avoid their obligations by employing what one banking historian called "petty tricks" to delay payment.[119] A Scottish bank might hint a creditor's relationship with it would suffer if he or she pressed a claim unreasonably. When a Scottish bank did pay, it might do so in partial amounts, with a bill of exchange drawn on London or inconvenience the creditor by paying in small denomination coins.[120] In 1826, an Englishman noted "any southern fool who had the temerity to ask for a hundred sovereigns [at a

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[116] Anderson, *The Story of the Commercial Bank of Scotland*: 14-20.

[117] 5 George III c. 49. See also: Select Committee on Banks of Issue, *Select Committee on Banks of Issue: Evidence of the Witnesses Connected with the Chartered and Joint-stock Banks of Scotland as Reported by the Parliamentary Committee on Banks of Issue* (London: Parliament of the United Kingdom (House of Commons), 1841), 109.

[118] Kevin Dowd, "Option clauses and the stability of a laisser faire monetary system," *Journal of Financial Services Research* 1, no. 4 (1988); James A. Gherity, "The option clause in Scottish banking, 1730-65: A reappraisal," *Journal of Money, Credit and Banking* 27, no. 3 (1995); George Selgin and Lawrence H. White, "The option clause in Scottish banking," *Journal of Money, Credit, and Banking* 29, no. 2 (1997).

[119] Kerr, *History of Banking in Scotland*: 64.

[120] Frank W. Fetter, *Developmement of British Monetary Orthodoxy* (Cambridge, Mass: Harvard University Press, 1965), 122-23; Checkland, *Scottish Banking*: 184-86; Murray N. Rothbard, "The myth of free banking in Scotland," *The Review of Austrian Economics* 2, no. 1 (1988): 232-33; Parth J Shah, "The option clause in free-banking theory and history: A reappraisal," *The Review of Austrian Economics* 10, no. 2 (1997): 12-14.

Scottish bank], might, if his nerves supported him through the cross examination … think himself in luck to be hunted only to the border.”[121]

Avoiding their obligations must have contributed something to a Scottish bank’s stability. However, a large proprietorship made a decisive difference to a Scottish bank’s chances of survival too. The Scottish banks that failed with a loss to their creditors were the smallest.[122] They averaged a mere 3.7 proprietors per bank. This compared to an average of 67.7 proprietors for the Scottish banks that failed with no loss to public (a figure inflated artificially by the Ayr Bank’s failure) and 48.7 proprietors for the banking companies that did not fail.[123] Lord Liverpool (1770-1828) noted in 1826 that Scotland’s bigger banks were less likely to fail than the smaller banks found in England and Wales. He argued the Scots felt little inclination to orchestrate runs on their bigger banks because they knew their banks’ proprietorships would compensate them if the bank failed.[124]

No one could have erected a bank as large as the Commercial Bank of Scotland in England and Wales prior to 1826. The *Bubble Act* and the six-partner limit precluded such a development. In England and Wales, the banking industry grew rapidly because of the Industrial Revolution but it remained dependent on private

[121] Henry A. Burgess, *A Letter to the Right Hon. George Canning to Explain in what Manner the Industry of the People and the Productions of the Country are Connected with and Influenced by Internal Bills of Exchange, Country Bank Notes and Country Bankers, Bank of England Notes, and Branch Banks: Written to Expose Some of the Prevailing Fallacies on these Subjects and to Prove that the Laws Passed under the Influence of those Fallacies will Greatly Obstruct and Injure the Operations of Industry and have no Power to Affect the Purposes Designed by them with a Postscript on the Tendency of the Wages of Labour in England and Ireland to Become Equal and the Consequences Resulting Therefrom Exemplified* (London: J. Ridgeway, 1826), 45.
[122] Munn, *The Scottish Provincial Banking Companies*: 222-24.
[123] Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime," 508.
[124] Lord Liverpool, Chancellor of the Exchequer, and Bank of England, "Communications relating to an alteration of the exclusive privileges enjoyed by the Bank of England."

banks limited to six members at most. The next section explains that in 1825, the English and Welsh banking industry came perilously close to collapse. That experience convinced Lord Liverpool and his government to undertake a fundamental reform of the English and Welsh banking industry.

THE *COUNTRY BANKERS ACT*

The financial crisis of 1825 was the product of a turnaround in the fortunes of an economy recovering from the Napoleonic Wars.[125] London became the focus of investment schemes that included opportunities in the newly independent states of South and Central America. One could even invest in a fictional Central American principality called Poyais.[126] By December, the inevitable collapse of the investment bubble created resulted in a run on the banks in which over a tenth of the private banks in England and Wales failed.[127] The loss of so many banks sparked a lively

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[125] Fetter, *Developmement of British Monetary Orthodoxy*: 111-22.

[126] Edward Low, "Poyais settlers," *The Times*, 24 October 1823; Edward Codd, *Proceedings of an Inquiry and Investigation Instituted by Major General Codd, His Majesty's Superintendent and Commander-in-Chief at Belize, Honduras, Relative to Poyais.* (London: Lawler and Quick, 1824).

[127] C. C. Western, *A Letter to Lord Liverpool on the Causes of the Present Embarrassment* (London: James Ridgway and Budd & Calkin, 1825); Anonymous, *Letter to the Right Hon. Robert Peel: Upon the Necessity of Adopting Some Parliamentary Measure to Control the Issues of Country Bankers, and to Prevent the Recurrence of the Late Shock to Public and Private Credit*, Second ed. (London: J. Hatchard & Son, 1826); Anonymous, *Commerce in Consternation: or, the Banking Bubble Burst!: Being a Sketch of the Rise, Progress, and Decline, of the Late Paper Panic* (London: Charles Frederick Cock, 1826); Anonymous, *The Present Critical State of the Country Developed; or, an Exhibition of the True Causes of the Calamitous Derangement of the Banking and Commercial System at the Present Alarming Crisis Shewing the Essential Distinction Between the Solidity of the National Bank of England and that of Country Banks by an Individual of Thirty Years' Practical Experience in Banking and Commercial Affairs* (London: Thomas Kelly, 1826); Richard Phillips, *Golden Rules for Bankers: With a Postscript on the Present Panic and on the Destruction of Commercial Credit* (London: Effimgham Wilson, 1826); Thomas Joplin, *Case for Parliamentary Inquiry into the Circumstances of the Panic in a Letter to Thomes Gisborne Esq. M.P.* (London: J. Ridgeway & Sons, 1835); John Wade, *Principles of Banking and Commerce as Elucidated by the Great Crisis of 1825-6, and Applicable to the Existing State of Commercial Activity and Joint-Stock Speculations* (London: Effingham Wilson, 1836), 61-92; Macleod, *The Theory and Practice of Banking*, II: 239-55; Leone Levi, *History of British Commerce and of the Economic Progress of the British Nation 1763-1878*, Second ed. (London: John Murray, 1880), 184-90; L. Neal, "The financial crisis of 1825 and the restructuring of the British financial system," *Federal Reserve Bank of St. Louis Review* 80, no. 3 (1997).

debate.[128] One could argue the banks were the authors of their own misfortune. They issued bank notes to excess during a period of excitement only to run short of the means needed to redeem them during the run. However, Scottish banks issued bank notes too and none of them succumbed to the run.[129] Lord Liverpool and his administration were convinced the Scottish banks' larger proprietorships calmed the Scottish public. Liverpool's conclusion put the desirability of the six-partner limit in doubt.

The charter granted to the Bank of England in 1800 contained the usual promise that the six-partner limit would apply to every other English and Welsh bank. That charter was not due to expire until 1833.[130] Consequently, abolishing the six-partner rule would breach a customary undertaking renewed only a quarter of a century earlier, which threatened to damage the government's relationship with the Bank of England. Liverpool and his Chancellor of the Exchequer had a delicate problem on their hands and wrote to the Governor and Deputy Governor of the Bank

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[128] See for example: Anonymous, *The Present Critical State of the Country Developed; or, an Exhibition of the True Causes of the Calamitous Derangement of the Banking and Commercial System at the Present Alarming Crisis Shewing the Essential Distinction Between the Solidity of the National Bank of England and that of Country Banks by an Individual of Thirty Years' Practical Experience in Banking and Commercial Affairs*; Richard Blanshard, *Thoughts on the Present Commercial Distress and on the Means to Prevent its Recurrence by a Merchant* (London: J. M. Richardson, 1826); Thomas Joplin, *Views on the Subject of Corn and Currency.* (London: Baldwin, Cradcok & Joy and J. Ridgway, 1826); Phillips, *Golden Rules for Bankers: With a Postscript on the Present Panic and on the Destruction of Commercial Credit*; Henry A. Burgess, *A Memorial Addressed to the Right Honourable Lord Viscount Goderich on the Fitness of the System of the Bank of England, of the Country Banks, and of the Branch Banks of England to the Wants of the People and on the Ample Means of Protection which Private Banks and the Public have Against the Monopoly of the Bank of England*, (London: J. Ridgeway, 1827); William Huskisson, "Bank Charter and promissory notes, February 10 1826," in *Speeches of the Right Honorable William Huskisson*, ed. Anonymous (London: John Murray, 1831).

[129] Thomas Joplin, *An Essay on the General Principles and Present Practice of Banking in England and Scotland: With Supplementary Observations on the Steps Proper to Form a Public Bank and the System on which its Accounts Ought to be Kept*, Fifth ed. (London: Baldwin, Cradock & Joy and J. Ridgway, 1826); Henry Parnell, *Observations on Paper Money, Banking, and Overtrading: Including Those Parts of the Evidence Taken Before the Committee of the House of Commons, which Explain the Scotch System of Banking* (London: J. Ridgeway, 1828).

[130] 39 & 40 George III c.28

of England to explain their reasons for wanting to abandon the six-partner limit.[131] Liverpool and his Chancellor of the Exchequer argued:

> The failures which have occurred in England, unaccompanied as they have been by the same occurrences in Scotland, tend to prove, that there must have been an unsolid and delusive system of Banking in one part of Great Britain, and a solid and substantial one in the other.[132]

Liverpool and the Chancellor of the Exchequer claimed the government had two courses of action available to them to rectify the banking industry's problems. The Bank of England might open branches in the provinces to drive provincial banks' notes out of circulation, although it seemed doubtful that the Bank of England possessed the resources to do this. Alternatively, Liverpool's government could abolish the six-partner limit in the provinces where the Bank of England maintained no branches. The Prime Minister and his Chancellor of the Exchequer assured the Bank of England that a six-partner limit would continue to apply in London.

The proposal to abolish the six-partner rule in the provinces was not a new idea. The Newcastle-born timber merchant and banker Thomas Joplin (1790-1847) had championed unincorporated joint stock banking in provincial England and Wales.[133] He even attempted to circumvent the six-partner rule in 1824 by proposing to erect an unincorporated joint stock bank of deposit arguing that such a bank would be legal because it would not issue bank notes.[134] Developments in Ireland suggested Joplin's campaign would eventually meet with success. The legal

[131] Lord Liverpool, Chancellor of the Exchequer, and Bank of England, "Communications relating to an alteration of the exclusive privileges enjoyed by the Bank of England." See also: W. Marston Acres, "The Bank of England From Within," (London: Oxford University Press, 1931), 422-23.
[132] Lord Liverpool, Chancellor of the Exchequer, and Bank of England, "Communications relating to an alteration of the exclusive privileges enjoyed by the Bank of England," 472.
[133] Joplin, *An Essay on the General Principles and Present Practice of Banking in England and Scotland*.
[134] Thomas Joplin, "Prospectus of a Joint-stock Banking Company with £3,000,000 of Capital to be Established in London," (London: Publisher Unknown, 1824).

framework in Ireland prior to 1821 resembled that of England and Wales. The Bank of Ireland was the only incorporated bank and a six-partner limit applied to every other Irish bank of issue. However, legislation passed in 1824 and 1825 abolished the six-partner limit in the Irish provinces. By 1825, there was nothing to prevent a provincial Irish bank of issue admitting as many partners as it wished. The six-partner limit only applied within a 50-Irish mile radius of Dublin.[135]

The Bank of England drew upon the Irish precedent when it responded to the government's proposal to abolish the six-partner limit. The Bank agreed that the six-partner limit could no longer apply in the provinces but insisted it should remain in force within 65 miles of London.[136] Liverpool acquiesced to the Bank of England's suggestion and the "Act for the better regulating of Copartnerships of certain Bankers in England" (or the *Country Bankers Act*) passed into law in 1826.[137] The *Country Bankers Act* permitted unincorporated joint stock banking companies of issue in the English and Welsh provinces although a 65-mile radius drawn around London would continue to exclude them from the Metropolis. The *Country Bankers Act* also gave the Bank of England permission to open provincial branches.

JOINT STOCK BANKING COMES TO ENGLAND AND WALES

The *Country Bankers Act* became law a year after the *Bubble Act*'s repeal, which removed the last impediment that excluded unincorporated joint stock banking

[135] Gilbart, *A History of Banking in Ireland*: 19, 41-48; William John Lawson, *The History of Banking: With a Comprehensive Account of the Progress of the Banks of England, Ireland and Scotland* (London: Richard Bentley, 1850), 386-89.
[136] Lord Liverpool, Chancellor of the Exchequer, and Bank of England, "Communications relating to an alteration of the exclusive privileges enjoyed by the Bank of England," 476. The Bank of England suggested a radius of 65 statute miles because it equated to 50 Irish-miles. In truth, the Bank of England's exclusion zone was far larger than the Bank of Ireland's because a 50 Irish-mile radius drawn around Dublin extends over the Irish Sea.
[137] 7 George IV c. 46.

companies from provincial England and Wales. After a slow start, the English and Welsh took to joint stock banking with some enthusiasm as 38 of these banks opened for business between 1826 and 1833.[138] However, the recently repealed *Bubble Act* continued to exert an influence. English common law would have impeded the banks erected under the *Country Bankers Act* by treating them as partnerships. Fortunately, the parliament anticipated the most significant legal impediment of them all. Parliament knew that the English and Welsh courts would deny these banks a legal identity and took steps to avert that inconvenience.[139] Every bank erected under the *Country Bankers Act* possessed the power to litigate in the name of designated company officers.[140]

The *Country Bankers Act* resolved one of the legal problems the newly formed joint stock banks would encounter but other unforeseen problems awaited resolution. The common law prohibited individuals suing themselves. The same person could not appear as both a defendant and a plaintiff to a legal action.[141] Unfortunately, every bank formed under the *Country Bankers Act* remained a partnership at law and its shareholders were parties to a legal action even though the bank conducted the action in the name of a company official. This meant an unincorporated joint stock bank could not sue its shareholders, shareholders could not sue their bank and two banks could not sue each other if they had just one shareholder in common. The potential for mischief only became apparent in 1838, when the courts refused to

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[138] Philip L. Cottrell and Lucy Newton, "Banking liberalisation in England and Wales," in *The State, the Financial System and Economic Modernization*, ed. Richard Sylla, Richard Tilly, and Gabriel Tortella (Cambridge: Cambridge University Press, 1999), 89.
[139] Hunt, "The joint-stock company in England," 11.
[140] S. Evelyn Thomas, *The Rise and Growth of Joint Stock Banking*, vol. I (London: Sir Isaac Pitman & Sons, 1934), 81; Hunt, "The joint-stock company in England, 1800-1825," 29.
[141] Macleod, *The Theory and Practice of Banking*, II: 507; Thomas, *The Rise and Growth of Joint Stock Banking*, I: 237-39.

entertain the Northern and Central Bank of England's attempt to recover loans worth more than £440,000 from some of its shareholders.[142]

Seemingly innocuous legislation passed in 1817 set another trap for the first English and Welsh joint stock banks. This act denied clergymen the right to profit from a trade.[143] English common law treated a clergyman who owned just one share in an incorporated joint stock bank as if he was a partner in a banking partnership. The clergyman became a banker under these circumstances, which rendered the bank illegal and all of its contracts void. Unincorporated English and Welsh joint stock banks remained blissfully unaware of the implications of the 1817 act until *Hall v Franklin* in 1838.[144] The court dismissed a claim over a debt owed to the Northern and Central Bank of England because the bank's shareholding constituency included just two Anglican clergymen.[145] According to the *Legal Observer*, the case "excited much alarm in persons interested in these and other similar companies."[146]

The Northern and Central Bank of England's legal difficulties in 1838 were symptomatic of a legal environment unprepared for the emergence of joint stock banks. Parliament intervened in 1838 and 1841 to resolve the difficulties imposed by share-owning clergymen and to permit litigation between unincorporated joint stock companies and their shareholders.[147] The English and Welsh were new to

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[142] Secret Committee on Joint Stock Banks, "Report from the Secret Committee on Joint Stock Banks; together with the minutes of evidence, appendix and index," in *Reports from the Committees in Seventeen Volumes (15 November 1837 to 16 August 1838)*, ed. House of Commons (London: Parliament on the United Kingdom, 1838), 111.
[143] 57 George III c. 99.
[144] (1838) 150 English Reports 1141.
[145] Macleod, *The Theory and Practice of Banking*, II: 507-08; Thomas, *The Rise and Growth of Joint Stock Banking*, I: 241.
[146] Legal Observer, "How far clergymen may trade," *Legal Observer*, 12 October 1839.
[147] 1 & 2 Victoria, c. 96 and 4 & 5 Victoria c. 14.

unincorporated joint stock banking and it is not surprising that the emerging banks encountered teething problems.[148] Large banks like Edinburgh's National Bank of Scotland and Glasgow's Glasgow Union Bank (later the Union Bank of Scotland), the Western Bank of Scotland, the Clydesdale Bank and the City of Glasgow Bank all emerged after 1825. These new Scottish banks harboured ambitions that matched the Commercial Bank of Scotland's desire to create a national presence.[149] Scotland's provincial joint stock banking companies had served their purpose. They would eventually disappear from the Scottish banking industry.[150] However, English and Welsh joint stock banking companies of the time remained committed to a scale of operations that resembled an increasingly defunct generation of Scottish provincial banking companies. A typical first generation English and Welsh joint stock bank company opened few branches and limited its operations to a small geographical area.[151] There was one notable exception to this preference for small regional banks. The National Provincial Bank of England was the most 'Scottish' of the first generation of English and Welsh joint stock banks.

Established in 1833, the National Provincial Bank of England was unique because its promoters were unapologetically Scottish in their outlook and ambitions. Thomas Joplin was the industry's leading advocate of Scottish joint stock banking prior to the *Country Bankers Act* and he involved himself in the National Provincial Bank of England's creation from the outset.[152] Joplin's cousin, George Fife Angas

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[148] Macleod, *The Theory and Practice of Banking*, II: 518-19.
[149] Checkland, *Scottish Banking: A History, 1605-1973*: 304-05, 25-42.
[150] Munn, *The Scottish Provincial Banking Companies, 1747-1864*: 80-100.
[151] Lucy Newton and Philip L. Cottrell, "Joint-stock banking in the English provinces 1826-1857: To branch or not to branch?," *Business and Economic History* 27, no. 1 (1998).
[152] Thomas Joplin, *The Plan of a National Establishment for Country Banking and the Principles by which it is Recommended: Also the Prospectus of the Committee which has been Formed to Carry*

(1789-1879), lent his support to the project and joined Joplin on the National Provincial Bank of England's board of directors in the early years.[153] The bank's first general manager was a Scotsman who learned his trade in Scotland. Daniel Robertson (1805-1865) trained with the Commercial Bank of Scotland before moving on to the Glasgow Union Bank.[154] The promoters' intention was to create a federation of semi-autonomous regional banks that would span the whole of England and Wales. The initial structure proved unworkable whereupon the National Provincial's head office acquired greater power than its promoters anticipated.[155] The National Provincial Bank of England also made a concession to what remained of the six-partner rule. The London head office only performed an administrative function. All of this bank's banking offices were located outside the 65-mile radius.[156] The arrangement ensured that the National Provincial Bank of England retained its all-important right to issue bank notes.

The National Provincial Bank of England's unwillingness to open banking offices in London symbolised the extent to which the world's largest financial centre remained out of bounds to unincorporated English and Welsh joint-stock banks. The next section will explain how that this situation changed in 1833.

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such an Establishment into Effect (London: W. J. Ruffy, 1831), 4-29; Thomas Joplin, *The Advantages of the Proposed National Bank of England Both to the Public and its Proprietory Briefly Explained* (London: Ridgway and Baldwin & Craddock, 1833), 6-18.

[153] Hartley Withers, *The National Provincial Bank: 1833 to 1933* (London: The National Provincial Bank, 1933), 29-31; J. F Ashby, *The Story of the Banks* (London: Hutchinson & Company, 1934), 150-57.

[154] Withers, *The National Provincial Bank*: 53-55.

[155] Thomas Joplin, *An Essay on the Condition of the National Provincial Bank of England With a View to its Improvement: In a Letter to the Shareholders by the Founder of the Establishment* (London: Richardson, 1843), 5-8.

[156] Withers, *The National Provincial Bank*: 66-68.

JOINT STOCK BANKING IN LONDON

Joplin's aborted attempt to erect a provincial joint stock bank of deposit in 1824 raised a tantalising prospect.[157] The combined effect of Bank of England's charter and the 65-mile radius imposed by the *Country Bankers Act* of 1826 would not permit an unincorporated joint stock bank of issue in London. However, no London private bank had issued bank notes for over a century. London's private banks facilitated their customers' payments by offering them cheque accounts instead.[158] These banks even maintained a clearinghouse on Lombard Street to streamline this aspect of their operations.[159] If banks of deposit always had been exempt from the six-partner rule as Joplin supposed, then there was no reason why a London bank that issued no bank notes should have limited itself to six members. However, there was a potential flaw in Joplin's reasoning. Legal opinion divided as to whether the Bank of England's charter imposed a six-partner limit on banks of issue alone or whether the prohibition encompassed banks of deposit too.[160] Ultimately, parliament had to resolve the ambiguity because a court of law never got the opportunity to resolve it.

The Bank of England's charter was due for renewal in 1833, which gave parliament the opportunity to clarify whether joint stock banks of deposit were legal in London. The 1833 *Bank Charter Act* declared banks always had the right to admit more than six proprietors if they refrained from issuing bank notes.[161] Almost

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[157] Thomas Joplin, "Prospectus of a joint-stock banking company with £3,000,000 of capital."

[158] Richard S Grossman, *Unsettled Account: The Evolution of Banking in the Industrialized World Since 1800* (Princeton: Princeton University Press, 2010), 173-74.

[159] W. F. Crick and J. E. Wadsworth, *A Hundred Years of Joint Stock Banking* (London: Hodder and Stoughton Publishers, 1936), 12.

[160] Wordsworth, *The Law Relating to Railway, Bank, Insurance, Mining and Other Joint-Stock Companies*: 44-45.

[161] 3 & 4 William IV c. 98. The declaratory clause did not entirely vindicate the stance taken by Joplin in 1824. A court of law could have interpreted the six-partner limit differently prior to the passage of the declaratory clause.

immediately, a prospectus appeared calling for subscriptions to a scheme to erect the London and Westminster Bank. The intention behind the London and Westminster Bank was to create a bank that would unite the separate realms of West End and City banking by opening branches in both parts of London.[162] From the outset, the London and Westminster Bank's competitors in London treated it like an interloper.[163] The Committee of Private Bankers refused the London and Westminster Bank's application to join the clearinghouse. The Bank of England turned down the London and Westminster Bank's request for a drawing account. However, the newly established London and Westminster Bank faced a more serious problem. The declaratory clause inserted into the *Bank Charter Act* in 1833 only declared that the London and Westminster Bank had a right to exist if it refrained from issuing bank notes. That clause did not bestow the right to litigate in the names of designated company officers provided for in the *Country Bankers Act*. The London and Westminster Bank would have to litigate in the names of all of its shareholders.

The London and Westminster Bank's officials assumed parliament's failure to give it a legal personality amounted to a legislative oversight. They sought a remedy by the most expedient means available to resolve that oversight and petitioned parliament for special legislation that would give the bank the right to pursue and

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[162] The London and Westminster's prospectus is reproduced in: James William Gilbart, *A Record of the Proceedings of the London and Westminster Bank During the First Thirteen Years of its Existence: With Portraits of its Principal Officers* (London: London and Westminster Bank, 1847), 15-17.

[163] London and Westminster Bank, *Hints by Way of Encouraging the Formation of a Joint-Stock Banking Company in London: With Some Account of the Present State of Private Banking in the Metropolis and of the Amount of Current Cash Balances in the Hands of the Bank of England and of the London Bankers.*, Third ed. (London: Effingham Wilson, 1834); Gilbart, *A Record of the Proceedings of the London and Westminster Bank During the First Thirteen Years of its Existence: With Portraits of its Principal Officers*; T. E. Gregory and A. Henderson, *The Westminster Bank Through a Century*, vol. 1 (London: Oxford University Press, 1936), 122-84.

defend legal actions in the name of a company officer.[164] The London and Westminster Bank soon discovered the government promised the Bank of England that London's joint stock banks would receive no further privileges beyond the recognition of their right to exist. The Bank of England was determined to hold the government to this undertaking. The London and Westminster Bank's supporters in parliament were dismayed at the development. William Clay (1791-1869) could not believe that the common law expected an unincorporated joint stock company like the London and Westminster Bank to undertake legal action in the name of its shareholders. Clay pointed out that parliament regularly passed special legislation to rectify this defect in other industries and noted that parliament did the same for the country banks erected under the *Country Bankers Act*.[165] Nevertheless, the London and Westminster Bank's attempt to acquire a legal personality did not meet with success. The requisite bill passed through the House of Commons with a considerable majority before the government ensured its defeat in the House of Lords.[166] The bank had to wait until 1844 before the parliament finally gave it the legal personality it craved.[167]

The London and Westminster Bank's legal difficulties failed to discourage the establishment of other unincorporated joint stock banking companies in London. In 1836, the London Joint Stock Bank doubled the number of unincorporated joint stock banking companies in the Metropolis. The number of unincorporated joint stock

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[164] London and Westminster Bank, *Case of the London and Westminster Bank* (London: London and Westminster Bank, 1834).

[165] "Parliamentary intelligence: House of Commons, Monday May 26," *The Times*, 27 May 1834; Parliament of the United Kingdom, *Debate on the Third Reading of the London and Westminster Bank Bill in the House of Commons on May 26 1834 Extracted from the Mirror of Parliament* (London: The Mirror of Parliament, 1834).

[166] Wordsworth, *The Law Relating to Railway, Bank, Insurance, Mining and Other Joint-Stock Companies*: 47.

[167] 7 & 8 Victoria c. 113.

banks in London reached four in 1839 after the emergence of the Union Bank of London and the London and County Bank. The Commercial Bank of London became the fifth unincorporated joint stock bank in London when it opened its doors in 1840.[168] Unincorporated joint stock banks of deposit became a permanent feature of London's financial services economy.

CONCLUDING REMARKS

The *Country Bankers Act* expressed Lord Liverpool's desire to follow the Scottish precedent to improve the country bank note issue by making the banks that issued it less vulnerable to a run. The reforms introduced in 1826 expressed the government's hope that an increase in bank size would stabilise the English and Welsh banking system. The next chapter explains that these reforms yielded disappointing results. Some of the banking industry's critics known as the 'Currency School' argued that the country needed stricter controls on the number of bank notes issued to correct the banking industry's problems. In 1844, the Currency School got the monetary controls they wanted whereupon Liverpool's desire to foster an increase in bank size in England and Wales became a secondary consideration. The Bank of England charter of 1844 delayed the banking industry's Amalgamation Movement for another two decades.

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[168] Commercial Bank of London, *Reasons for the Establishment of the Commercial Bank of London Addressed to the Directors and Managers of the Joint-Stock Banks as well as the Private Bankers of the United Kingdom* (London: William Nichol, 1840); James Knight, *The London Joint-Stock Banks: Their Progress, Resources and Constitution* (London: Richardson Brothers, 1858), 7-11.

CHAPTER THREE
THE AMALGAMATION MOVEMENT
AND THE BANK ACT OF 1844

> When the measure of 1826 for extending the Scotch system of banking to England and Wales was brought forward by the government, they seemed so much surprised and delighted with the discovery that the sagacity and experience of our neighbours beyond the Tweed had furnished them with an infallible remedy for all the alleged evils of our English banking system, that they deemed all previous investigation of the subject unnecessary.[1]

Chapter One explained that banks literally make money. Their transferable debts are a means of payment and a store of value. However, the money a bank makes is different to coins fashioned out of precious metals. Discs made from gold and silver have some intrinsic worth, which makes them an effective store of value whereas banks erect the money they create on a foundation of credit. Debts like these only retain their value if the bank incurring them remains equal to the task of redeeming them. The British embarked upon the Industrial Revolution at a time when the money available to them was in a precarious state. Prior to 1816, Britain ran short of small change often because good silver coins disappeared from circulation. Between 1797 and 1821, one could not redeem the Bank of England's bank notes at its office in Threadneedle Street. As the last chapter explained, a run on the English and Welsh banks in 1825 decimated the English and Welsh banks of issue.

Monetary stability became an important consideration in Britain during the first half of the nineteenth century and Lord Liverpool's administration was particularly keen to promote it. Liverpool put the country on the gold standard in 1816, legislated to restore the Bank of England's bank notes to convertibility in 1819 and

[1] "To our subscribers," *The Circular to Bankers*, 3 June 1836, 362.

attempted to secure the bank note issue by permitting joint stock banks in the English and Welsh provinces in 1826. Nevertheless, the most significant monetary reform undertaken prior to the Amalgamation Movement was the product of a later government.

This chapter argues the *Bank Charter Act* of 1844 delayed the Amalgamation Movement for over two decades by imposing disincentives to bank amalgamations. In addition, the currency reforms introduced in 1844 ensured that the Scottish banks could never cross the border to compete with the English and Welsh banks in the provinces. The Scottish banks did not participate in the Amalgamation Movement. The Chapter begins with the adoption of the gold standard in 1816, an event that laid the foundations for the conduct of British monetary policy until the outbreak of World War I. The Chapter then examines the origins and nature of the British bank note before explaining that a measure adopted in wartime to protect the Bank of England from a run gave rise to Britain's first debate on the subject of monetary policy. In 1797, the Bank of England stropped redeeming its bank notes with gold, which raised a question as to just how many bank notes the Bank of England could put into circulation before it provoked an economically destructive outbreak of inflation. Normality resumed in 1821 when the Bank of England began to redeem its bank notes once more. Nevertheless, the question as to how many bank notes the banks should issue remained unanswered until the currency reforms introduced in 1844 dictated that the national bank note issue should fluctuate in direct proportion to the amount of gold held in reserve to redeem it. This chapter claims the reforms introduced in 1844 were futile. There was not enough gold available to sustain Britain's post-Industrial Revolution economy. The British had to erect their money

supply on a foundation of credit and they overcame the restrictions imposed on their bank notes in 1844 by utilising cheques to make payments instead. The task of supplying the deposits needed to sustain this growing reliance on cheques fell to the amalgamating banks. The Amalgamation Movement began in the 1870s because bank notes lost their central importance to English and Welsh banking practice.

THE GOLD STANDARD

The British maintained a *de jure* policy of bimetallism prior to 1816. Officially, gold and silver coins ranked equally as the means of payment although Britain had effectively adopted a *de facto* gold standard long before 1816. Under the terms of the *Act for Encouraging Coinage* of 1666, the Mint turned a pound of gold into 44½ guineas, a pound of silver into 62 shillings and an edict issued on Sir Isaac Newtown's (1643-1772) advice fixed the value of a guinea at 21 shillings.[2] The problem with this arrangement was that gold and silver traded on global markets. Often, the prices on offer at the Mint undervalued silver relative to gold.[3] Those who wanted to convert their silver into coins preferred to sell it abroad where silver commanded better prices than the Mint offered. One could even make a profit

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[2] 18 Charles II c. 5; Isaac Newton, "Newton's representations on the subject of money: Representation the third to the Commissioners of His Majesty's Revenue (21 September 1717)," in *Old and Scarce Tracts on Money*, ed. John R. McCulloch (London: Political Economy Club, 1856); G. Findlay Shirras and J. H. Craig, "Sir Isaac Newton and the currency," *The Economic Journal* 55, no. 218/219 (1945).

[3] S. Ph., *A Letter to a Friend, Occasion'd from what was Published in the Daily-Courant, on Monday December 30th 1717, by Sir Isaac Newton, Relating to Coin, Shewing that the Value of the Gold Coin, Ought not to be Lessen'd, but Rather the Silver to be Raised.* (London: John Morphew, 1718); Anonymous, "Observations on the state of gold and silver in Great Britain, both in coin and bullion; and the reason why so little has been coined at his Majesty's Mint, with a method for encouraging the coinage and keeping it within due bounds," (London: Publisher Unknown, 1730); Anonymous, "Reasons for rectifying an error in the standard of our coins," (London: Publisher Unknown, 1736); Morris Cobryn, "A letter balancing the causes of the present scarcity of our silver coin, and the means of immediate remedy, and future prevention of this evil. Addressed to the Right Honourable the Earl of Powis," (London: Publisher Unknown, 1757).

melting silver coins down and exporting the output.[4] Naturally, the heaviest silver coins went into the melting pot first because they yielded the most silver. Badly worn or clipped coins stayed in circulation because they were underweight.[5] Gresham's Law took effect as bad money drove good money out of circulation.[6] Poor quality silver coins circulated. Good silver coins were either hoarded or melted down because their intrinsic worth exceeded the monetary value.

The only way Britain would keep its best silver coins in circulation was to create an incentive to spend them rather than hoard or destroy them. In 1776, Adam Smith suggested the reintroduction seigniorage, a fee charged by the Mint for minting coins. Seigniorage would reduce a silver coin's metallic content by allowing the Mint to retain a fraction of the silver handed over to produce them.[7] A similar proposal appeared in 1805 from Lord Liverpool who had served as Master of the Mint between 1799 and 1801.[8] Liverpool's long-standing interest in the nation's coins ensured that he and his government were sufficiently motivated to pass the *Act for Encouraging Coinage* in 1816.[9] Gold retained its old Mint value of £3/17/10½ per ounce although now the Mint would now turn a pound of gold into 46¾ sovereigns rather than 44½ guineas. The arrangement gave sovereigns an

[4] Anonymous, "For encouraging the coining of silver money in England, and after for kepping it here," (London: Publisher Unknown, 1693); Privy Council Committee on Coins, *Draft of a Report on the Coin of this Realm* (London: Publisher Unknown, 1798), 147.
[5] Lord Liverpool, *A Treatise on the Coins of the Realm in a Letter to the King* (Oxford: The Oxford University Press for Cadell and Davies of London, 1805), 3-6.
[6] Ernest Sykes, *Banking and Currency* (London: Butterworth & Company, 1905), 15-21.
[7] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. Edwin Cannan, 6th ed., vol. I (London: Methuen & Co, 1950), 48-51.
[8] Lord Liverpool, *A Treatise on the Coins of the Realm*: 812-103; Angela Redish, "The evolution of the gold standard in England," *The Journal of Economic History* 50, no. 04 (1990).
[9] 56 George III c.68.

arithmetically convenient monetary value of £1 or 20 shillings.[10] The 1816 act also authorised the Mint to make silver coins at the new rate of 66 shillings per pound but the Mint would retain four shillings as seigniorage and put the remaining 62 shillings into circulation. The global price of a pound of silver would now have to exceed the 66 shillings it now took to yield a pound of it before anyone would contemplate melting a silver coin down. Such a high price for silver seemed unlikely.[11]

Liverpool's measures put Britain on an official gold standard by demonetising silver in most cases. The public was entitled to use silver coins for payments up to £2 but a payee could demand sovereigns for amounts greater than this.[12] In addition, Liverpool's newly minted silver coins were nothing more than mere tokens whose monetary worth exceeded their intrinsic value. The post-1816 arrangements so overvalued a silver coin's metallic content that Britain risked being flooded with freshly minted silver coins that were liable to remain in circulation whenever the global price of silver fall below 62 shillings a pound. The 1816 act included measures that stopped the public attending at the Mint to turn silver into coins.[13]

An artificial equivalence between 20 shillings and a golden sovereign kept silver coins in circulation after 1816. The idea that an overvalued token like this might stay in circulation if gold imbued it with its monetary value was not new.

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[10] $(21 \div {}^{46.75}/_{44.50} = 20)$. See also: Joseph Hume, *Thoughts on the New Coinage with Reflections on Money and Coins and a New System of Coins and Weights on a Simple and Uniform Principle* (London: J. J. Stockdale, 1816), 8.

[11] Frank W. Fetter, *Developmement of British Monetary Orthodoxy* (Cambridge, Mass: Harvard University Press, 1965), 66-67; Redish, "The evolution of the gold standard," 802.

[12] Edwin Walter Kemmerer, *Gold and the Gold Standard: The Story of Gold Money, Past, Present and Future* (Auburn: Ludwig von Mises Institute, 1944), 45-48; Redish, "The evolution of the gold standard."

[13] Redish, "The evolution of the gold standard."

Under normal circumstances, inherently worthless pieces of paper known as bank notes maintained their monetary value in much the same way.

THE BRITISH BANK NOTE

London's goldsmiths issued the first British bank notes.[14] The goldsmiths' premises were safe havens for bullion and the public adopted the habit of depositing precious metals with them for safe-keeping. The more enterprising goldsmiths used the bullion deposited with them to finance a lending business. Initially, goldsmiths issued promissory notes made payable to their depositors on demand whenever they took a deposit. Depositors took their promissory notes back to the goldsmith to reclaim the gold and silver they needed it to make a payment. London's goldsmiths made two discoveries during the seventeenth century that revolutionised British finance. First, depositors did not need to reclaim their bullion if the goldsmith issued promissory notes made payable to the bearer on demand on demand instead. Promissory notes like these could change hands to make payments whilst the gold and silver needed to imbue them with value remained in the goldsmith's vault. Second, goldsmiths realised they no longer had to relinquish bullion to make a loan. A borrower would accept promissory notes made payable to the bearer on demand because they knew they could spend them. There was a point of dependency on gold

[14] The following is based on Ellis T. Powell, *The Evolution of the Money Market (1385-1915)* (London: The Financial News, 1915), 94-113; Stephen Quinn, "Banking Before the Bank: London's Unregulated Goldsmith-Bankers, 1660-1694" (Doctor of Philosophy, University of Illinois, 1994); Stephen Quinn, "Goldsmith-banking: Mutual acceptance and interbanker clearing in restoration London," *Explorations in Economic History* 34, no. 4 (1997); Kevin Dowd, "The invisible hand and the evolution of the monetary system," in *What is Money?*, ed. James Smithin (London: Routledge, 2000); Peter Temin and Hans-Joachim Voth, "Banking as an emerging technology: Hoare's Bank, 1702–1742," *Financial History Review* 13, no. 2 (2006); Jongchul Kim, "How modern banking originated: The London goldsmith-bankers' institutionalisation of trust," *Business History* 53, no. 6 (2011); George Selgin, "Those dishonest goldsmiths," *Financial History Review* 19, no. 03 (2012); R. D. Richards, *The Early History of the Bank of England* (London: Routledge Library Editions (Banking & Finance), 2012), 1-23.

that London's goldsmith-bankers never eradicated. Goldsmiths held bullion in reserve to act as a buffer against any imbalance in the rate at which precious metals flowed into their vaults and the rate at which they needed it to meet their obligations on their bank notes. Goldsmith-bankers learned how to sustain this fractional-reserve banking model through trial and error. Those who issued too few promissory notes constrained their lending to do it and lost opportunities to make a profit. Those who lacked the reserves needed to meet their obligations arranged to obtain bullion at short notice from somewhere else or they fell by the wayside.

Both the Bank of England and the Bank of Scotland adopted the goldsmith-bankers' fractional-reserve banking model to issue bank notes of their own soon after their establishment in 1694 and 1695 respectively.[15] The other Scottish banks followed suit, as did most of the English and Welsh country banks during the Industrial Revolution.[16] A fractional-reserve banking model usually worked well, give or take the occasional run. The infant Bank of England instituted a partial suspension of payments in 1696 and did so again during the Jacobite rebellion of 1745.[17] The Bank of Scotland suspended payments in 1728.[18] However, fractional-reserve banking had a point of vulnerability that proved particularly troublesome. The bullion held in reserve would prove insufficient to meet the demands for repayment if the public lost confidence in their bank notes. Even the best-managed

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[15] Andrew William Kerr, *History of Banking in Scotland* (Glasgow: David Bryce & Son, 1884), 23; A. Andréadès, *A History of the Bank of England, 1640-1904*, 4th ed. (London: Frank Cass & Co., 1966), 81-82.
[16] Kerr, *History of Banking in Scotland*; L. S. Pressnell, *Country Banking in the Industrial Revolution* (Oxford: Clarendon, 1956); S. G. Checkland, *Scottish Banking: A History, 1605-1973* (Glasgow: Collins, 1975).
[17] John Francis, *History of the Bank of England, its Times and Traditions* (New York: Bankers Magazine, 1862), 87; Anonymous, *Tales of the Bank of England With Anecdotes of London Bankers* (London: J. Hogg, 1882), 79-80; Richards, *The Early History of the Bank of England*: 189.
[18] Checkland, *Scottish Banking*: 60.

banks would not survive a catastrophic run. In 1797, the prospect of such a run threatened the survival of the Bank of England.

THE RESTRICTION ON PAYMENTS

Britain went to war with revolutionary France in 1793, which put the Bank of England's gold reserves under strain. The government called upon the Bank to supply it with bullion to make payments to its allies abroad.[19] Another drain on the Bank's gold reserves came from those who feared a French invasion. As one contemporary noted, these people were "subject to weak and extravagant alarms" that could render obsolete a banker's estimate as to what constituted an adequate reserve at a moment's notice.[20] Newcastle's banks were the first to succumb to a run in February 1797 after local farmers sold their cattle and descended on the city's banks to exchange the bank notes they had received for gold.[21] The run soon encompassed the neighbouring cities of Sunderland and Durham.[22] Then on 22 February 1797, 1,400 Frenchmen disembarked near Fishguard in Southern Wales. The invasion turned into a humiliating farce for the invaders.[23] The French alienated the locals by looting the surrounding countryside. In addition, the region's female populace wore red shawls and black hats, which gave them a disconcerting resemblance to British infantry from a distance. The invaders convinced themselves the British had them surrounded and soon surrendered.

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[19] Henry Warren, *The Story of the Bank of England: A History of the English Banking Movement and a Sketch of the Money Market* (London: R. A. Everett & Son, 1906), 74-75; Andréadès, *A History of the Bank of England*: 190-94.

[20] Henry Thornton, *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain* (London: J. Hatchard, 1802), 48.

[21] "Newcastle, February 20," *The Times*, 25 February 1797, 3.

[22] "We are extremely sorry again to observe," *The Times*, 24 February 1797, 2.

[23] Margaret Ellen James, *The Fishguard Invasion by the French in 1797* (London: T. Fisher Unwin, 1892); John D. Ahlstrom, "Captain and Chef de Brigade William Tate: South Carolina adventurer," *The South Carolina Historical Magazine* 88, no. 4 (1987).

News of the French landing reached London on Saturday 25 February, giving the government less than a weekend to prepare for the run on the Bank of England that would begin once it opened its doors on Monday morning. The solution chosen was an order to suspend cash payments issued on Sunday night.[24] On Monday morning, the Privy Council announced:

> It … is ... necessary ... that the directors of the Bank of England should forbear issuing any cash in payment until the sense of parliament can be taken on that subject and the proper measures adopted thereupon for maintaining the means of circulation and supporting the public and commercial credit of the kingdom at this important conjuncture.[25]

A suspension freeing the Bank of England from the obligation to redeem its bank notes had begun.[26] Parliament passed the legislation needed to formalise this new monetary arrangement on 3 May 1797.[27] The government hoped that the suspension would be a temporary measure at first. It lasted until 1821.[28]

The suspension of cash payments gave Britain its first experience of a fiat currency. The capacity of a Bank of England note to act as a means of payment and a store of value under these circumstances now relied upon custom, the public's faith that the Bank of England would have to redeem its notes eventually and legislation designed to make refusing a Bank of England note difficult. In 1811, for example, Lord Peter King (1776–1833) demanded his tenants pay their rent in gold coin or in

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[24] "News of the enemy's landing in Wales had no sooner reached town," *The Times*, February 27 1797, 2-3.

[25] Reproduced in William Cobbett, *The Parliamentary History of England from the Earliest Period to the Year 1803*, vol. XXXII (London: T. C. Hansard, 1818), 1518; William Cobbett, *Paper Against Gold* (New York: John Doyle, 1834), 159.

[26] Ian P. H. Duffy, "The discount policy of the Bank of England during the suspension of cash payments, 1797–1821," *The Economic History Review* New Series 35, no. 1 (1982).

[27] 37 George III c. 45.

[28] Duffy, "The discount policy of the Bank of England during the suspension of cash payments."; Neil Skaggs, "Thomas Tooke, Henry Thornton, and the development of British monetary orthodoxy," *Journal of the History of Economic Thought* 25, no. 2 (2003).

bank notes “of a sum sufficient to purchase the weight of ... gold requisite to discharge the rent.”[29] If others followed King’s example, every commodity in Britain might have commanded a gold price and a higher paper price.[30] Parliament responded by passing legislation in 1811 and 1812 rendering it illegal to accept bank notes and gold coins at anything other than their respective face values.[31]

King’s preference for gold as a means of payment was evidence that the time-honoured relationship between the value of the Bank of England’s bank notes and the gold it used to hold in reserve to redeem them was breaking down. The breakdown in this relationship gave rise to Britain’s first meaningful debate on the subject of monetary policy. That debate was the bullionist controversy.

THE BULLIONIST CONTROVERSY

Prior to the suspension, bankers adjusted their bank note issue to accord with their reserves. The suspension changed everything as far as the Bank of England was concerned. Liberated from the need to redeem, the Bank of England could put as many bank notes into circulation as it wished without having to worry about its reserves. Every other English and Welsh bank and the Scottish banks remained contractually obliged to redeem their bank notes but now gold was unobtainable at the Bank of England. The other banks had no choice but to use the Bank of England’s fiat currency to meet their obligations.[32] By 1810, David Ricardo (1772-1823) could claim that the discretion of the Bank of England’s directors as to how

[29] Lord King, "Speech of the Rt. Hon. Lord King, in the House of Lords," *The Belfast Monthly Magazine* 8, no. 47 (1812): 490.
[30] Parliament of the United Kingdom, *The Parliamentary Debates Dating from the Year 1803 to the Present Time*, vol. XX (London: T. C. Hansard, 1812), 945-72.
[31] 51 George III c. 127 and 52 George III c. 50.
[32] Fetter, *Developmement of British Monetary Orthodoxy*: 33-37.

many bank notes they put into circulation was determining the bank note circulation of every other bank of issue in the country.[33] The Bank of England's irredeemable bank notes displaced gold as the banking system's primary means by which it discharged its obligations.

The Bank of England made every effort to exercise its freedom from the need to redeem its bank notes responsibly. The Bank adopted a policy known as 'the real bills doctrine.' The Bank of England furnished its fiat currency to discount any short-term bill of exchange presented to it that arose from a genuine commercial transaction and imposed little risk of default. The Bank's directors believed their policy met the needs of trade. They reasoned, bills like these only came to them for discount because their holders needed the bank notes issued to make a payment. In addition, the directors thought the policy could never result in an excessive bank note issue. The bank notes issued would soon return with interest to the Bank of England when the bills matured.[34] The Bank of England also had good authority to justify its reasoning on this second point. Adam Smith argued that if a bank discounted short-term bills that were sound, then its coffers would resemble "a pond,

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[33] David Ricardo, *The High Price of Bullion: A Proof of the Depreciation of Bank Notes* (London: John Murray, 1810), 42-43; Fetter, *Developmement of British Monetary Orthodoxy*: 33-37, 48-51.

[34] Evidence of John Whitmore, John Pease and Jeremiah Harman in Select Committee on the High Price of Gold Bullion, *Report, together with minutes of evidence, and accounts, from the Select Committee on the High Price of Gold Bullion* (London: J. Johnson and Company and J. Ridgway, 1810). See also: Robert Torrens, *An Essay on Money and Paper Currency* (London: J. Johnson & Company, 1812); Lloyd Wynn Mints, *A History of Banking Theory in Great Britain and the United States* (Chicago: University of Chicago Press, 1945); Duffy, "The discount policy of the Bank of England during the suspension of cash payments."; Geoffrey Poitras, "Robert Torrens and the evolution of the real bills doctrine," *Journal of the History of Economic Thought* 20, no. 04 (1998). The first use of the phrase "real bills doctrine" appeared in Mints, *A History of Banking Theory in Great Britain and the United States*.

from which … a stream is continually running out, yet another is continually running in, … so that ... the pond keeps always equally, or very nearly equally full."[35]

The problem with the real bills doctrine was that its utility rested on a commercial consideration. A bank could economise on its reserves if it limited its activities to short-term lending on good security. Whether the real bills the doctrine represented a useful guide for the conduct of monetary policy undertaken by a central bank issuing a fiat currency was a different question entirely.[36] A key issue was that the price mechanism that should have moderated the demand for commercial credit could not operate. The usury law set the maximum rate of interest the Bank of England could charge at five per cent per annum.[37] The monetary economist, bullionist and parliamentarian Henry Thornton (1770-1815) opposed the real bills doctrine for this reason. Thornton lamented:

> To ascertain how far the desire for of obtaining loans at the Bank may be expected at any time to be carried out, we must enquire into the subject of the quantum of profit likely to be derived from borrowing there under the existing circumstances. This is to be judged by considering two points: The amount, first of interest to be paid on the sum borrowed; and secondly, of the … gain to be obtained by the employment of the borrowed capital.... We may ... consider this question as turning principally on a comparison of the rate of interest taken at the Bank with the current rate of mercantile profit.
>
> The Bank is prohibited, by the state of the law, from demanding even in time of war, an interest of more than five per cent, which is the same rate at which it discounts in a period of profound peace. It might, undoubtedly, at all seasons, sufficiently limit its paper by means of the prices at which it lends, if the legislation did not impose an obstacle to the constant adoption of this principle....
>
> Any supposition that it would be safe to permit the bank paper to limit itself because this would be to take the more *natural* course, is

[35] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, I: 323.
[36] Thomas J Sargent and Neil Wallace, "The real-bills doctrine versus the quantity theory: A reconsideration," *The Journal of Political Economy* 90, no. 6 (1982).
[37] 12 Anne c. 16.

> therefore, altogether erroneous. It implies that there is no occasion to advert to the rate of interest in consideration of which the bank paper is furnished, or to change that rate according to the varying circumstances of the country.[38]

Thornton's belief was that those who obtained bank notes at the Bank of England would have felt less inclination to do so if the cost imposed on them could rise above five per cent. To make matter worse, the suspension prevented the public removing any bank notes issued by exchanging them for gold. Thornton's argued the stream of bank notes running out of the Bank of England under these circumstances seemed likely to exceed the amount of bank notes removed from circulation by the stream running in.

Thornton argued adherence to the real bills doctrine resulted in an excessive Bank of England issue. That excess, he claimed, induced other banks to over issue too because they depended on the Bank of England's irredeemable bank notes to meet their obligations. If Thornton was right, then the result would be domestic inflation. Unfortunately for Thornton and his bullionist allies, early nineteenth-century Britain possessed no universally accepted metric of the rate of inflation.[39] Thornton had a limited number of indicators available to them to prove their point.[40] One was the market price of gold, an indicator of the rate at which one could convert bank notes into bullion through market exchanges. An increase in the price of gold would imply the purchasing power of the Bank of England's bank notes was

[38] Thornton, *An Enquiry into the Nature and Effects of the Paper Credit*: 287-88.
[39] Fetter, *Developmement of British Monetary Orthodoxy*: 138-39; Matthew Smith, "Thomas Tooke on the bullionist controversies," *The European Journal of the History of Economic Thought* 15, no. 1 (2008).
[40] See for example: Walter Boyd, *Letter to the Right Honourable William Pitt on the Influence of the Stoppage of Issues in Specie at the Bank of England on the Prices of Provisions and Other Commodities*, Second ed. (London: James Ridgway, 1811).

declining.[41] Another was the value of the pound relative to other currencies that remained on a metallic standard. A decline in the pound's value should have shown up as depreciation on the foreign exchanges.[42] The problem the bullionists faced was that committed anti-bullionists could always find non-monetary cause to undermine any attempt to prove the nation was not suffering from monetarily induced inflation. An anti-bullionist like Colonel Robert Torrens (1780-1864) could blame taxation, wartime expenditures, bad harvests and disturbances in the balance of trade for any apparent decline in the value of Britain's paper currency.[43]

The real bills doctrine exercised under the constraints imposed by the usury laws made cheap credit readily available to a wartime economy undergoing the Industrial Revolution. Consequently, the real bills doctrine became a valued part of Britain's economic landscape.[44] Witnesses called by the Select Committee on the High Price of Gold Bullion in 1811 defended the Bank's policy to the hilt.[45] The Select Committee's recommendation that the Bank of England begin redeeming its notes at the earliest possible opportunity garnished little support in parliament.[46] The bullionists had to wait until Napoleon's (1769-1821) defeat at Waterloo to put an end to the suspension on cash payments. Parliament passed the *Resumption of Cash Payments Act* in 1819.[47]

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[41] Ricardo, *The High Price of Bullion*.
[42] Thornton, *An Enquiry into the Nature and Effects of the Paper Credit*: 140-44.
[43] Torrens, *An Essay on Money and Paper Currency*; Frank W. Fetter, "Robert Torrens: Colonel of marines and political economist," *Economica* 19, no. 114 (1962).
[44] Henry James, *Considerations on the Policy or Impolicy of the Further Continuance of the Bank Restriction Act.* (London: Sherwood, Needly and Jones, 1818).
[45] Select Committee on the High Price of Gold Bullion, *Report, together with minutes of evidence, and accounts, from the Select Committee on the High Price of Gold Bullion*.
[46] Parliament of the United Kingdom, *The Parliamentary Debates Dating from the Year 1803 to the Present Time*, vol. XIX (London: T. C. Hansard, 1812), 1169.
[47] 59 George III c. 49.

Preparing for the resumption of cash payments demanded that the Bank of England curtail its lending so that its bank note issue would accord with its reserves once more. Inevitably, the result was a contraction in credit and a recession, which shook some people's confidence in the virtues of a convertible currency.[48] A Birmingham banker like Thomas Attwood (1783-1856), supplied credit to the Black Country's manufacturing economy. Attwood drew on an intellectual legacy inherited from David Hume (1711-1776),[49] to argue a monetary base constrained by the amount of gold and silver available could never keep the nation's resources fully employed.[50] John Stuart Mill (1806-1873) accused Attwood of trying to inflate Birmingham's manufacturing economy artificially at the expense of the monetary stability of the rest of the nation.[51] Attwood's claim that monetary expansion constituted a viable defence against unemployment remained an economic heresy until the Keynesian revolution of the twentieth century.[52] The Bank of England resumed cash payments in 1821.[53]

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[48] John Sinclair, *On the Approaching Crisis; or, on the Impracticability and Injustice of Resuming Cash Payments at the Bank in July 1818 and on the Means of Elevating the Internal Prosperity of the British Empire to a Height Hitherto Unparalleled* (London: J. Hatchard, 1818); William Congreve, *Of the Impracticability of the Resumption of Cash Payments of the Sufficiency of a Representative Currency in this Country under due Regulations and of the Danger of a Reduction of the Circulating Medium in the Present State of Things* (London: J. Hatchard and Sons, 1819).
[49] David Hume, "Of money," in *Writings on Economics by David Hume*, ed. Eugene Rotwein (New Brunswick: Transaction, 2007).
[50] Thomas Attwood, *The Remedy, or Thoughts on the Present Distress in a Letter to a Public Editor* (London: Whittingham and Arlis, 1816); Thomas Attwood, *Prosperity Restored, Reflections on the Causes of the Present Distress and on the Only Means of Relieving Them* (London: Baldwin, Cradock and Joy, 1817); Thomas Attwood, *A Letter to the Rt. Hon. Nicholas Vansittart, on the Creation of Money and on its Action Upon National Prosperity* (Birmingham: R. Rightson, 1817); Thomas Attwood, *Observations on Currency, Population, and Pauperism in Two Letters to Arthur Young, Esq.* (Birmingham: R. Rightson, 1818); Thomas Attwood, *Causes of the Present Distress: Speech of Thomas Attwood, Esq. at the Public Meeting, Held in Birmingham, on the 8th of May 1829 for the Purpose of Considering the Distressed State of the Country* (Birmingham: W. M. Hodgetts, 1829).
[51] John Stuart Mill, "The currency juggle," in *Dissertations and Discussions Political, Philosophical and Historical*, ed. John Stuart Mill (London: John W. Parker and Son, 1859); Fetter, *Developmement of British Monetary Orthodoxy*: 74-76.
[52] John Maynard Keynes, *A Tract on Monetary Reform* (London: Macmillan and Company, 1924).
[53] Fetter, *Developmement of British Monetary Orthodoxy*: 98.

The resumption of cash payments complemented Liverpool's reform of the nation's coins undertaken in 1816. Silver coins now stayed in circulation and the nation's bank notes were redeemable again. Gold sovereigns held the new gold standard together by imbuing silver coins and bank notes with their respective monetary values. However, one aspect of the post-1821 arrangements continued to threaten Britain's financial stability. The failure of a large number of English and Welsh banks during financial panic of 1825 alluded to in the last chapter demonstrated fractional reserve banking remained vulnerable to a run. The *Country Bankers Act* of 1826 represented yet another incremental change designed to put the nation's currency on a secure foundation by making the English and Welsh banks more stable.

Liverpool's government introduced one more measure in 1826 to foster greater reliance of gold and silver coins to make payments. Legislation in that year prohibited the issue of small bank notes.[54] No English or Welsh bank notes with a face value less than £5 circulated after 1826 until the outbreak of World War I when the Treasury issued £1 and 10-shilling notes to economise on the amount of gold and silver in circulation.[55] Liverpool's government attempted to ban small notes in Scotland too, but abandoned the idea once Sir Walter Scott (1771-1832) mounted a defence the £1 bank notes in three letters written to the *Edinburgh Weekly Journal*.[56]

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[54] 7 George IV c. 6.

[55] John Maynard Keynes, "War and the financial system: August, 1914," *The Economic Journal* 24, no. 95 (1914): 474-75.

[56] Walter Scott, *Thoughts on The Proposed Change of Currency and Other Alterations, as they Affect, or are Intended to Affect the Kingdom of Scotland* (Edinburgh: William Blackwood, 1826); Walter Scott, *A Second Letter to the Editor of the Edinburgh Weekly Journal from Malachi Malagrowther, Esq. on the Proposed Change of Currency and Other Late Alterations as they Affect or are Intended to Affect the Kingdom of Scotland* (Edinburgh: William Blackwood, 1826); Walter Scott, *A Third Letter to the Editor of the Edinburgh Weekly Journal from Malachi Malagrowther, Esq. on the*

Scott may have signed those letters in the *nom de plume* Malachi Malagrowther, but anyone who knew his work understood Malachi Malagrowther was the alleged descendant of a character in his 1822 novel *The Fortunes of Nigel*.[57]

The bank notes issued by the English and Welsh country banks and the Scottish banks were instruments of credit. Their worth depended upon the solvency of the banks that issued them. Dissatisfaction with the first generation of English and Welsh joint stock banks soon gave rise to a renewed monetary debate in which two opposing schools known as the 'banking school' and the 'currency school' argued over the future direction of British monetary policy.

THE BACKGROUND TO THE BANKING-CURRENCY DEBATE

Four developments during the 1830's had profound implications for the banking industry. The previous chapter dealt with the first. In 1833, the *Bank Charter Act* declared that joint stock banks could operate in London if they issued no bank notes. The second was the same act's abolition of the usury laws for bills of exchange with less than ninety days to maturity.[58] The third was the elevation of the Bank of England's bank notes to the status of legal tender in England and Wales.[59] The English and Welsh public became obliged to accept Bank of England notes to settle debts denominated in multiples of £5. The only exception was at an office of the Bank of England where the Bank continued to redeem its bank notes in specie to maintain their convertibility. The Bank of England became the official repository of

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Proposed Change of Currency and Other Late Alterations as they Affect or are Intended to Affect the Kingdom of Scotland (Edinburgh: William Blackwood, 1826).

[57] Walter Scott, "The Fortunes of Nigel," in *Waverley Novels* (Edinburgh: Robert Cadell, 1845).

[58] 3 & 4 William IV c. 98.

[59] 3 & 4 William IV c. 83.

the nation's bullion reserve because it was the only institution in England and Wales obliged to make payments in specie after 1833. The last development was the spread of joint stock banking following the passage of the *Country Bankers Act* in 1826.

Joint stock banks were slow to emerge in England and Wales at first. By the end of 1829, only 13 of them were open for business. Then the trickle turned into a flood as 116 joint stock institutions entered the industry between 1830 and 1839.[60] By 1837, the *Edinburgh Review* could boast the English and Welsh were in the grip of a joint stock banking "mania."[61] The *Circular to Bankers* was in no doubt as to where the epicentre of the joint stock banking mania lay. Most of the new joint stock banks were located in industrial counties like Lancashire, Yorkshire and the Midlands.[62] This joint-stock banking mania was symptomatic of a buoyant economy enjoying a cyclical upswing. Harvests were good and credit plentiful because the new joint stock banks lent generously to establish themselves.[63] Banking was one of many industries undergoing expansion. In May 1836, William Clay delivered a speech to the House of Commons in which he claimed to hold in his hand "a list of seventy contemplated companies for every species of undertaking, which have appeared in the Liverpool and Manchester papers within the last three months."[64]

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[60] Philip L. Cottrell and Lucy Newton, "Banking liberalisation in England and Wales," in *The State, the Financial System and Economic Modernization*, ed. Richard Sylla, Richard Tilly, and Gabriel Tortella (Cambridge: Cambridge University Press, 1999), 89.

[61] "The state of the currency: The Bank of England and the country banks," *The Edinburgh Review*, April 1837, 64. See also: Cottrell and Newton, "Banking liberalisation."

[62] "To our subscribers," *The Circular to Bankers*, 6 May 1836. See also: Lucy Newton and Philip L. Cottrell, "Joint-stock banking in the English provinces 1826-1857: To branch or not to branch?," *Business and Economic History* 27, no. 1 (1998).

[63] W. Marston Acres, "The Bank of England From Within," (London: Oxford University Press, 1931), 461; Richard S Grossman, *Unsettled Account: The Evolution of Banking in the Industrialized World Since 1800* (Princeton: Princeton University Press, 2010), 110.

[64] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks to Which are Added Reflections on Limited Liability, Paid-up Capital and Publicity of Accounts as Applied to Such*

Unfortunately, the economy was heading towards a downturn by the time Clay delivered his speech.

Concerns over the Bank of England's reserves saw its directors raise their rate of discount twice in 1836 to constrain their bank note issue in the face of an outflow of bullion.[65] Unusually, some of the gold taken from the Bank of England went to the United States where President Andrew Jackson's (1767-1845) preference for a metallic currency increased the demand for it.[66] Americans obtained the gold they needed by discounting bills of exchange with a country bank to obtain Bank of England notes and presented them for redemption at one of the Bank of England's branches. The Bank of England took radical action to discourage this practice. It declared that henceforth it would not rediscount a bill of exchange carrying the endorsement of a joint stock bank of issue.[67] The banks that discounted these bills could no longer present them at the Bank of England to obtain legal tender if they became subject to a run.

The first that sign that events were moving towards crisis occurred in Ireland where a run on the Agricultural and Commercial Bank of Ireland saw it suspend

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Associations with Some Remarks on an Article on Joint-Stock Companies in the Last Number of the Edinburgh Review (London: James Ridgway and Sons, 1836), 31.

[65] Acres, "The Bank of England From Within," 461.

[66] Francis Knowles, *The Monetary Crisis Considered: Being Incidentally a Reply to Mr. Horsley Palmer's Pamphlet 'On the Action of the Bank of England & C. and a Defence of the Joint-Stock Banks Against his Accusations.* (London: Pelham Richardson, 1837), 16-17; Peter L. Rousseau, "Jacksonian monetary policy, specie flows, and the panic of 1837," *The Journal of Economic History* 62, no. 02 (2002).

[67] Anonymous, *The New Monetary System by a Citizen of the World* (London: James Ridgway and Sons, 1836), 2; Acres, "The Bank of England From Within," 464; Andréadès, *A History of the Bank of England, 1640-1904*: 266.

payments on 14 November 1836.[68] Then on 28 November 1836, representatives of the Northern and Central Bank of England, one of the largest joint stock institutions in England and Wales, arrived at the Bank of England's offices seeking assistance.[69] They explained that the Northern and Central had sent an officer to London with a bag containing more than £100,000 in bank notes and bills of exchange to meet the bank's commitments in the Metropolis. Unfortunately, the officer left the bag in a hansom cab and failed to recover it. The Northern and Central Bank of England's representatives feared their bank would become the subject of a run if news of the misfortune became public knowledge. At first, the Bank of England refused to help. However, the Bank's officers changed their minds once they realised a stoppage at a bank as big as the Northern and Central would spread to the rest of the country. The Northern and Central recovered the lost bag by the time the Bank of England made a conditional offer of assistance but by then news of the lost bag was in the public domain. A run on the Northern and Central Bank seemed inevitable and it accepted

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[68] For more on the Agricultural and Commercial Bank see: James William Gilbart, *A History of Banking in Ireland* (London: Longman, Rees, Orme, Brown, Green & Longman, 1836), 117-20; Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks; Together With Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1837), 136-99, 230-68; Henry Dunning Macleod, *The Theory and Practice of Banking: With Elementary Principles of Currency; Prices; Credit; and Exchanges*, vol. II (London: Longman, Brown, Green and Longmans, 1856), 277-79; Malcolm Dillon, *The History and Development of Banking in Ireland: From the Earliest Times to the Present Day* (London: Effingham Wilson and Company, 1889), 71-79; G. L. Barrow, "Justice for Thomas Mooney," *Dublin Historical Record* 24, no. 1 (1970); Philip Ollerenshaw, *Banking in Nineteenth Century Ireland: The Belfast Banks, 1825-1914* (Manchester: Manchester University Press, 1987), 39-46.

[69] For an account of the Northern and Central Bank and its failure see: Thomas Joplin, *An Examination of the Report of the Joint Stock Bank Committee To Which is Added an Account of the Late Pressure in the Money Market and Embarrassment of the Northern and Central Bank of England*, Third ed. (London: James Ridgway, 1837), 117-22; Walter Gibson Casels, *Narrative of the Circumstances Which Have Occasioned a Dispute Between the Directors of the Northern and Central Bank of England and Walter Gibson Cassels, Manager at Manchester and Afterwards Agent for the Bank in London: With Extracts From his Letters Written Previously to the Application to the Bank of England for Assistance* (Bolougne: H. Griset, 1838); James William Gilbart, *The History and Principles of Banking*, Third ed. (London: Longman, Rees, Orme, Brown, Green and Longman, 1837), 286-69; Joseph Macardy, *Outlines of Banks, Banking and Currency* (London: H. & A. Macardy & Company, 1842), 167-79; Macleod, *The Theory and Practice of Banking*, II: 279; John Harold Clapham, *The Bank of England*, vol. II (Cambridge: Cambridge University Press, 1958), 154-56.

the Bank of England's offer of assistance. A subsequent analysis of the Northern and Central's affairs undertaken at the Bank of England's insistence revealed undisclosed deficiencies in the Northern and Central's financial position. By February 1837, the Bank of England's patience with the Northern and Central reached its limit. The Bank of England wound the Northern and Central Bank wound up with no loss to either itself or the Northern and Central Bank's creditors.

The failure of the Northern and Central Bank could not have come at a more inauspicious moment for the joint stock banks. In May 1836, William Clay used the tenth anniversary of the passage of the *Country Bankers Act* to call for a parliamentary enquiry into the joint stock banks.[70] The result was the House of Commons Secret Committee on Joint Stock Banks that delivered its first report in August 1836. That report contained no recommendations, but noted that the burden for supervising the joint stock banks currently fell upon their shareholders. The committee hoped those shareholders would remain equal to their responsibilities whilst it completed its investigations during the next parliamentary session.[71] When the committee reconvened in February 1837, it seemed imperative to find out why the Agricultural and Commercial Bank of Ireland and the Northern and Central Bank of England failed.[72] Joint stock banks were not a cure-all for the banking industry's ills that Lord Liverpool had hoped they would be.[73] Another committee investigated the banking industry in 1840 and 1841 although this time the committee's focus was

[70] Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks*.
[71] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks; Together With Minutes of Evidence and Appendix* (London: Parliament of the United Kingdom (House of Commons), 1836), x.
[72] The first witnesses called in 1837 gave evidence on the operations and failure of these banks. Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks; Together With Minutes of Evidence, Appendix and Index*: 1-199.
[73] "To our subscribers," 362.

on the industry's bank notes.[74] The advocates of the 'currency school' used the Select Committee on Banks of Issue to mount their attack on the existing arrangements in 1840. Advocates of the 'banking school' responded to the attack by giving defending the *status quo* in 1841.

THE CURRENCY SCHOOL AND THE BANKING SCHOOL

The most prominent members of the currency school were cohesive, well connected and influential. Their ranks included a Bank of England director, George Warde Norman (1793-1882).[75] The currency school also had a presence in parliament where William Clay, Samuel Jones Loyd (1796-1883) and the reformed anti-bullionist Colonel Robert Torrens were keen advocates.[76] All four were members of the Political Economy Club, a debating society founded by James Mill (1773-1836) that discussed the economic issues of the day. At various times, its membership

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[74] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue with Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1840); Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue with Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1841).

[75] Goerge Warde Norman, *Remarks Upon Some Prevalent Errors With Respect to Currency and Banking and Suggestions to the Legislature and the Public as to the Improvement of the Monetary System* (London: Pelham Richardson, 1838).

[76] Samuel Jones Loyd, *Remarks on the Management of the Circulation and on the Condition and Conduct of the Bank of England and of the Country Issuers During the Year 1839* (London: P. Richardson, 1840); Samuel Jones Loyd, *Reflections Suggested by a Perusal of Mr. Horsley Palmer's Pamphlet on the Causes and Consequences of the Pressure on the Money Market* (London: Pelham Richardson, 1837); Samuel Jones Loyd, *Tracts and Other Publications on the Metallic and Paper Currency* (London: Longman, Brown & Company, 1858); Robert Torrens, *A Letter to the Right Honourable Lord Viscount Melbourne, on the Causes of the Recent Derangement in the Money Market and on Bank Reform* (London: Longman, Rees, Orme, Brown & Green, 1837); Robert Torrens, *An Inquiry into the Practical Working of the Proposed Arrangements for the Renewal of the Charter of the Bank of England and the Regulation of the Currency: With a Refutation of the Fallacies Advanced by Mr. Tooke: to Which is added a Reply to the Objections of the Westminster Review to the Government Plan for the Regulation of the Currency* Second ed. (London: Smith, Elder and Company, 1844); Robert Torrens, *The Principles and Practical Operation of Sir Robert Peel's Act of 1844, Explained and Defended*, 3rd ed. (London: Longmans, 1858); William Clay, *Remarks on the Expediency of Restricting the Issue of Promissory Notes to a Single Issuing Body* (London: James Ridgway, 1844).

included Thomas Malthus (1766-1834), David Ricardo and John Stuart Mill.[77] Malthus, Ricardo and the younger Mill all contributed to the emergence of the modern economics discipline.[78] The economic statistician Thomas Tooke (1774-1858) was one of few recognised members of the banking school to gain admission to the Political Economy Club, although John Stuart Mill did express some sympathy for Tooke's views on monetary questions, which annoyed Torrens profoundly.[79]

The currency school advocated a 'currency principle' that owed its origins to the bullionists' critique of the real bills doctrine during the suspension on cash payments.[80] The currency principle held that bank notes were nothing more than cheap substitutes for gold coins. The public only used bank notes, the currency school argued, because it was more convenient to carry pieces of paper around than precious metals. In all other respects, gold coins were preferable to paper money because they constituted a better store of value. It followed, therefore, that the number of bank notes put into in circulation should match exactly the amount of precious metal held in reserve to redeem them. In 1840, George Warde Norman explained the currency principle in the following terms:

> I consider a metallic currency to be the most perfect currency, except so far as respects inconvenience in some respects, and cost. In everything else a metallic currency is the most perfect, and should be looked upon as the type of all other currencies; and as from their superior convenience and greater cheapness, bank notes are introduced to supply the place of a certain portion of metallic currency, I think that bank notes should be so

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[77] Political Economy Club, *Names of Members, 1821-1860, Rules of the Club and List of Questions Discussed 1833-1860* (London: Political Economy Club, 1860).

[78] Robert L Heilbroner, *The Worldly Philosophers: The Lives, Times and Ideas of the Great Economic Thinkers*, Seventh ed. (New York: Simon and Schuster, 1999).

[79] John Stuart Mill, "The currency question," *Westminster Review*, June 1844; John Stuart Mill, *Principles of Political Economy: With Some of Their Applications to Social Philosophy (People's Edition)* (London: Longmans, Green and Company, 1865), 394-410; Torrens, *The Principles and Practical Operation of Sir Robert Peel's Act*: 299-377.

[80] Torrens had to shed the anti-bullionist tendencies he displayed during the suspension to become a member of the currency school.

> managed, that they should possess all the other attributes of a metallic currency, and among those attributes, I conceive the most important to be that they should increase and decrease in the same way that a metallic currency would increase and decrease. I do not think it is possible to improve upon a metallic currency, except in the two points of convenience and cheapness.[81]

Samuel Jones Loyd was another critic of the existing monetary arrangements.[82] He was even more precise in his definition of the currency principle than George Warde Norman had been. Loyd claimed the bank note circulation "should be made to conform to what the metallic currency would be … by being kept at all times at the same amount."[83]

The currency school claimed the currency principle would stabilise the banking system, eliminate trade imbalances, ensure the convertibility of Britain's bank notes and smooth the business cycle. Drawing on David Hume's price-specie flow mechanism,[84] the currency school wanted to keep the bank note issue at what they considered its appropriate level at all times.[85] The process would work as follows. When Britain exported gold to make payments abroad, the number of bank notes circulating in Britain would fall in direct proportion to the amount of gold exported. The reduction in bank note circulation would have a deflationary effect, suppressing the price of British goods relative to foreign goods. Exports would rise and imports fall until the drain of gold stopped. At that point, the bank note circulation and prices

[81] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue*: 147.
[82] Loyd, *Reflections Suggested by a Perusal of Mr. Horsley Palmer's Pamphlet*.
[83] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue*: 211.
[84] David Hume, "Of the balance of trade," in *The Gold Standard in Theory and History* ed. Barry J. Eichengreen and Marc Flandreau (London: Routledge, 1997).
[85] Loyd, *Reflections Suggested by a Perusal of Mr. Horsley Palmer's Pamphlet*; Norman, *Remarks Upon Some Prevalent Errors With Respect to Currency and Banking*; Robert Torrens, *The Principles and Practical Operations of Sir Robert Peel's Bill of 1844 Explained and Defended Against the Objections of Tooke, Fullarton, and Wilson* (London: Longman, Green, Brown and Longmans, 1848); Torrens, *The Principles and Practical Operation of Sir Robert Peel's Act*. See also: Neil T. Skaggs, "Changing views: twentieth-century opinion on the banking school-currency school controversy," *History of Political Economy* 31, no. 2 (1999).

would stabilise. The opposite would occur when Britain received an inflow of gold from abroad. The bank note circulation would increase provoking an outbreak of inflation to make British goods more expensive at home and abroad. The result would be an increase in imports and fewer exports until finally the inflow of gold stopped. The bank note circulation and prices would then stabilise.

The currency school's attack in 1840 before the Secret Committee on Banks of Issue caught their opponents in the banking school by surprise.[86] The evidence taken in 1840 focused on the Bank of England, which gave George Warde Norman and Samuel Jones Loyd an opportunity to dissect the prevailing state of affairs in forensic detail. Thomas Tooke was the only member of the banking school called upon to give evidence in 1840.[87] The evidence taken by Secret Committee on Banks of Issue in 1841 focussed on the country banks, which gave the banking school its opportunity to rebut evidence given a year earlier. The London and Westminster's general manager James William Gilbart (1794-1863) used the occasion to defend his country correspondents' right to issue bank notes tenaciously.[88] Representatives of the Bank of Scotland, the Ayrshire Bank and the Glasgow Union Banking Company did the same for the Scottish banks.[89] When the committee's deliberations ended in 1841, the weight of contradictory testimony put before it over two years so

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[86] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue*; Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*.
[87] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue*.
[88] For more on Gilbart's views on the currency principle and his defence of his correspondents' right to issue bank notes see: James William Gilbart, *The Letters of Nehemiah: Relating to the Laws Affecting Joint Stock Banks, the Effects Likely to be Produced by the Measures of Sir Robert Peel on the System of Banking in London and Throughout the Country* (London: London and Westminster Bank, 1845).
[89] Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*: 79-148, 64-224. The Scottish banks had a long history of a largely unregulated bank note issue. See: Tyler Cowen and Randall Kroszner, "Scottish banking before 1845: A model for laissez-faire?," *Journal of Money, Credit and Banking* 21, no. 2 (1989); Lawrence H. White, *Free banking in Britain: Theory, experience, and debate, 1800-1845*, 2nd ed. (London: Institute of Economic Affairs, 1995).

overwhelmed its members that they could only agree on one thing. It would be prudent if Britain's banks disclosed the state of their circulation and their reserves more openly and more frequently.[90]

The Bank of England historian A. Andréadès observed that many people wrongly assume the banking school were free market ideologues opposed to any regulation of the bank note issue.[91] Nothing could be further from the truth. Thomas Tooke ranked alongside John Fullarton (1780-1849) (a retired banker) and James Wilson (1805-1860) (the founding editor of *The Economist*) as one of the banking school's most eloquent advocates.[92] Yet, Tooke argued that, "free trade in banking is synonymous with free trade in swindling."[93] The banking school had no objection to measures designed to improve the quality of Britain's bank notes. What they opposed were interventions designed to restrict their aggregate quantity. Advocates of the banking principle agreed with Adam Smith's assertion that:

> If bankers are … subjected to the obligation of immediate and unconditional payment of … [their] bank notes as soon as presented, their trade may, with safety to the public, be rendered in all other respects perfectly free.[94]

The banking school believed in a 'banking principle' that asserted a law of reflux. The banking school argued banks could not force the public to hold more

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[90] Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*: iii.

[91] Andréadès, *A History of the Bank of England*: 270.

[92] John Fullarton, *On the Regulation of Currencies; Being an Examination of the Principles on Which it is Proposed to Restrict Within Certain Fixed Limits, the Future Issues on Credit of the Bank of England and of the Other Banking Establishments Throughout the Country* (London: John Murray, 1844); James Wilson, *Capital, Currency, and Banking Being a Collection of a Series of Articles Published in the "Economist" in 1845, on the Principles of the Bank Act of 1844, and in 1847, on the Recent Monetarial and Commercial Crisis* (London: Economist, 1847).

[93] Thomas Tooke, *A History of Prices and of the State of Circulation in 1838 and 1839, with Remarks on the Corn Laws and on Some of the Alterations Proposed in our Banking System*, vol. III (London: Longman, Orme, Brown, Green and Longmans, 1840), 206.

[94] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, I: 350.

redeemable bank notes then it needed because any excess would return to the banks that issued it for redemption.[95] In 1841, for example, Gilbart (the London and Westminster Bank's general manager), asserted the right to redeem a bank note constituted a necessary check on the Bank of England's issuing powers because the Bank supplied its bank notes to governments for purposes unrelated to the needs of trade. The Bank of England's bank notes had to be capable of reflux to remove any excess issued.[96] According to the banking school, the right to redeem bank notes turned the real bills doctrine into a sound foundation for the conduct of monetary policy once more. All banks should be free to issue to expand and contract their bank note issue in accordance with the needs of trade. The banking school argued the banks could not put more redeemable bank notes into circulation than the public wanted to hold.[97]

Advocates of the banking principle regarded the currency school's currency principle with incredulity.[98] For one thing, the currency school's reliance on the price-specie flow mechanism seemed misguided. Tooke undertook an extensive analysis of prices and concluded non-monetary causes exerted a far greater influence over inflation than the money supply did.[99] Similarly, Gilbart told the Select Committee on Banks of Issue that prices did not necessarily rise to accommodate a growing bank note circulation. Sometimes, the number of bank notes in circulation

[95] Thomas Tooke, *An Inquiry into the Currency Principle: The Connection of the Currency with Prices and the Expediency of a Separation of Issue from Banking*, 2nd ed. (Longman, Brown, Green, and Longmans, 1844), 60-66; Fullarton, *On the Regulation of Currencies*: 63-65.

[96] Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*: 97-98, 118-20.

[97] Tooke, *An Inquiry into the Currency Principle*: 122-23. See also Fullarton, *On the Regulation of Currencies*: 81-97.

[98] See for example: Tooke, *An Inquiry into the Currency Principle*: 28-54.

[99] Thomas Tooke, William Newmarch, and T. E. Gregory, *A History of Prices and of the State of Circulation From 1792 to 1856, Reproduced From the Original*. (London: P. S. King, 1928).

had to increase because prices were rising.[100] In addition, the banking school asserted that a bank note was nothing more than a form of credit and fundamentally no different to other credit instruments like bills of exchange and cheques. It was futile, the banking school argued, to single bank notes out for regulation whilst leaving bills of exchange and cheques at the mercy of the needs of trade. Tooke expressed this view as follows:

> …neither is it in the power of the banks of issue … to diminish the total amount of circulation; particular banks may … refuse … to issue their own notes; but their notes so withdrawn will be replaced by notes of other banks, *or by other expedients calculated to answer the same purpose*.[101]

The banking school argued the only thing the currency principle could achieve would be greater reliance on cheques rather than bills of exchange to make payments. Bills of exchange drawn in amounts of less than £50 and £20 attracted prohibitively high rates of stamp duty.[102]

The currency school took the banking school by surprise in 1840 by preparing its attack first. Consequently, the banking school only released its most insightful critique of the currency principle after 1844 by which time parliament had enshrined the currency principle into law.[103] Robert Peel (1788-1850) was a member of the Select Committee on Bank of Issue and a committed bullionist who chaired the parliamentary committee that recommended a resumption of cash payments in

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[100] Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*: 99.

[101] Tooke, *An Inquiry into the Currency Principle*: 122. Italics added.

[102] "To our subscribers." See also: David K. Sheppard, *The Growth and Role of UK Financial Institutions, 1880-1962* (London: Methuen & Co., 1971), 5.

[103] Torrens, *The Principles and Practical Operation of Sir Robert Peel's Act*; Tooke, *An Inquiry into the Currency Principle*; Fullarton, *On the Regulation of Currencies;* Mill, "The currency question."

1819.[104] Peel recalled the days when the Bank of England's inconvertible bank notes appeared to depreciate in value with horror.[105] Bank notes were "fictitious credit" as far as Peel was concerned that would yield "severe commercial distress" when issued to excess.[106] Peel put his faith in bullion, having declared in 1819 that a pound was nothing more than "a definite quantity of gold … with an impression on it denoting it to be of a certain weight and … fineness."[107] By 1844, Peel was Prime Minister once more and the Bank of England's charter came up for renewal. Peel took the opportunity to impose the currency principle upon the banking industry.[108]

THE BANK OF ENGLAND CHARTER OF 1844

The Bank of England charter of 1844 introduced strict limits on the bank note issue of England and Wales.[109] This particular *Bank Charter Act* resurrected an idea first put forward by David Ricardo, who wanted a government agency called the 'National Bank' to take over the supply of bank notes. His plan would have forced every other bank (the Bank of England included) to use the National Bank's bank

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[104] Samuel Turner, *A Letter Addressed to the Right Hon. Robert Peel, Late Chairman of the Committee of Secrecy Appointed to Consider the State of the Bank of England with Reference to the Expediency of the Resumption of Cash Payments at the Period Fixed by Law* (London: J. Asperne, J. M. Richardson and J. Hatchard, 1819).

[105] Anonymous, *A Plan for regulating the circulation on the principle of Sir R. Peel's Act of 1819 by a Man of Business* (London: Pelham Richardson, 1840); Macleod, *The Theory and Practice of Banking: With Elementary Principles of Currency; Prices; Credit; and Exchanges*, II: 290-92; Robert Gaunt, *Sir Robert Peel: The Life and Legacy* (London: I. B. Tauris and Company, 2010), 51.

[106] Robert Peel, *Sir Robert Peel on the Crisis: The Opinion of That Eminent Statesman on the Present Crisis, as Delivered by Him in his Address to the Electors of Tamworth on Monday 28 June 1841* (London: John King, 1841), 12. See also: Robert Peel, "Banks and bankers," in *The Opinions of Sir Robert Peel Expressed in Parliament and in Public*, ed. Anonymous (London: Arthur Hall, Virtue and Company, 1850).

[107] Parliament of the United Kingdom, *The Parliamentary Debates Dating from the Year 1803 to the Present Time*, vol. XL (London: T. C. Hansard, 1819), 680.

[108] Marion R. Daugherty, "The currency-banking controversy: Part 1," *Southern Economic Journal* 9, no. 2 (1942).

[109] 7 & 8 Victoria c. 32.

notes to conduct a deposit-taking business.[110] However, Peel's *Bank Charter Act* differed from Ricardo's proposal in one respect. Peel divided the Bank of England into two departments. One department was an Issue Department that would play the role of Ricardo's National Bank. It would issue bank notes leaving the Banking Department to undertake what remained of the Bank of England's operations. The *Bank Charter Act* then imposed the currency principle upon the Issue Department.

The *Bank Charter Act* dictated that the Bank of England's Issue Department should issue and redeem the Bank of England's bank notes at the rate of £3/17/9 per ounce of gold, which was less than the £3/17/10½ per ounce on offer at the Mint. However, the Mint had a backlog of orders to deal with. One could have invested the £3/17/9 on offer at the Issue Department and ended up with more than £3/17/10½ by the time the Mint turned gold into sovereigns.[111] The Issue Department had a fiduciary issue of £14,000,000, an amount the act's framers chose carefully. Their analysis of the Bank of England's returns suggested its bank note issue could never fall below this level.[112] The Issue Department could maintain a reserve of government securities to back its fiduciary issue but had to maintain a specie reserve capable of redeeming every single bank note issued beyond £14,000,000 at the rate of £3/17/9 per ounce of gold. In addition, the Issue Department would keep its reserves separate from the Banking Department's reserves. If the Banking Department needed more Bank of England notes to conduct its business, it would

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[110] David Ricardo's Plan for a National Bank is reproduced in an appendix to Samson Ricardo, *A National Bank: The remedy for the Evils Attendant upon our Present System of Paper Currency* (London: Pelham Richardson, 1838). See also: David Ricardo, "Notes on 'Plan for a National Bank'," in *Minor Papers on the Currency Question, 1809-1823 by David Ricardo*, ed. Jacob H. Hollander (Baltimore: The Johns Hopkins Press, 1932).
[111] Philip A. Wicksteed and Lionel Robbins, *The Common Sense of Political Economy and Selected Papers and Reviews on Economic Theory*, vol. II (London: Routledge and Kegan Paul, 1933), 602-07.
[112] Torrens, *The Principles and Practical Operations of Sir Robert Peel's Bill of 1844.*: 7-9.

have to buy from the Issue Department at the official rate. If the Banking Department possessed more Bank of England notes than it needed, it would sell them back to the Issue Department at the same price. Any change in the bank notes put into circulation by the Banking Department would match the change in the Issue Department's bullion reserve exactly under these arrangements.

Peel knew that Tooke was right on one point. Other banks would put bank notes into circulation to fill any demand for them the Bank of England failed to meet.[113] Peel needed to constrain the bank note issue of every country bank in England and Wales to impose the currency principle. Peel adopted a carrot and stick approach to placate a banking community that would resist any threat to its profitability. The carrot transformed country banks into local monopolies. The *Bank Charter Act* dictated that only the banks issuing bank notes on 6 May 1844 could continue to issue them after that date. Peel's *Bank Charter Act* demanded a concession in return. Every bank of issue would report its average bank note circulation during the twelve weeks leading up to 27 April 1844. No bank could exceed the average circulation reported in 1844 once the *Bank Charter Act* became operative. A relieved Gilbart approved of the deal. He told his country correspondents:

> Upon the whole, then, in balancing our account with Sir Robert Peel, we find we owe him a debt of gratitude. This debt may have been enlarged, but still the amount is considerable. Our rights are acknowledged–our privileges are extended–our circulation guaranteed, and we are saved from conflicts with reckless competitors. The principle of currency, if erroneous, will affect us only in common with the rest of the community.[114]

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[113] Tooke, *An Inquiry into the Currency Principle*: 122.
[114] Gilbart, *The Letters of Nehemiah*: 16.

Peel's *Bank Charter Act* made the metallic reserve held by the Issue Department of the Bank of England the ultimate determinant of an expanding English and Welsh bank note issue. The Issue Department was the only bank in England and Wales granted a conditional right to increase its bank note circulation beyond the levels recorded in 1844.

Peel's concession over country banks note issue meant the *Bank Charter Act* had not turned the Bank of England's Issue Department into Ricardo's National Bank overnight. Other English and Welsh banks possessed limited rights to issue bank notes. Consequently, the *Bank Charter Act* contained provisions designed to contract the country bank note issue over time. A provincial bank would forfeit its right to issue bank notes if it became bankrupt, ceased to carry on the business of banking or stopped issuing bank notes. A banking partnership would also lose the right to issue once its membership exceeded six, which meant two amalgamating private banks could only aggregate their rights to issue if the post-amalgamation whole remained a private banking partnership with less than six proprietors.[115] Joint-stock banks acquired restrictions of their own. When a joint-stock bank absorbed a private bank, the private bank forfeited its right to issue bank notes. Amalgamations between two joint stock banks destroyed the bank note issuing privileges of the target. No joint stock bank could acquire a branch within the 65-miles radius of London and retain the right to issue. In addition, the act gave the Bank of England authority to enter into a compounding arrangement whereby a bank surrendered its right to issue in return for an annual payment. Finally, the act ensured the number of Bank of England notes in

[115] A membership greater than six created a newly established joint stock bank that could not issue bank notes.

circulation would increase over time to replace any rights to issue bank notes forfeited by the country banks. The Bank of England could apply to have its fiduciary issue expanded by two-thirds of all the rights to issue bank notes forfeited. It took 75 years for the *Bank Charter Act* to achieve its objective and turn the Bank of England's Issue Department into Ricardo's National Bank. In 1921, Somerset's Fox, Fowler and Company amalgamated with Lloyds Bank whereupon the Bank of England became the only bank of issue in the whole of England and Wales.[116]

Peel turned his attention to Scotland and Ireland in 1845. Adopting the same carrot and stick approach that worked so well in England and Wales, Peel placated existing banks by removing the threat a new entrant might compete with them. The *Bank Notes (Scotland) Act* forbade new banks of issue north of the River Tweed.[117] The measure erected such a barrier to entry that no banks emerged in Scotland after the prohibition came into force.[118] The *Bank Notes (Scotland) Act* also demanded established banks report their average bank note circulation. These banks could issue bank notes up to the averages recorded in 1845 without consequence but had to maintain a specie reserve equal in value to every additional bank note issued. Naturally, acquiring the reserves demanded by the *Bank Notes (Scotland) Act* imposed costs on Scotland's banks. Nevertheless, the Scottish banks avoided the inconvenience of being split into issue departments and banking departments like the Bank of England. The reserves demanded by the *Bank Notes (Scotland) Act* could serve more than one purpose under these circumstances. These reserves would meet the requirements of the *Bank Notes (Scotland) Act* whilst remaining available to

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[116] J. F. G. Bageshaw, *Practical Banking* (London: Isaac Pitman & Sons, 1924), 359.
[117] 8 & 9 Victoria c. 38.
[118] Checkland, *Scottish Banking*: 458.

cover the bank's deposits and putting coins in the banks tills. The Clydesdale Bank's general manager (George Readman (1818-1894)) told the Select Committee on Banks of Issue in 1875 that the Scottish public trusted their £1 bank notes implicitly. They rarely attended at their banks to withdraw sovereigns.[119] A Scottish bank could rely on the specie reserves demanded by the *Bank Notes (Scotland) Act* alone without putting its operations at risk. The restrictions imposed the Irish banks mirrored the Scottish regulations in every respect but one.[120] The Irish legislation abolished the only remaining protection accorded to the Bank of Ireland. An established Irish joint stock bank of issue could now issue bank notes within 50 Irish-miles of Dublin.

In theory, the currency principle made Britain's paper money more secure than ever. A Bank of England bank note was redeemable at a branch of the Bank of England. Every other English and Welsh bank note was redeemable in Bank of England bank notes that were now legal tender. In addition, the Bank of England maintained a specie reserve equal to the task of redeeming every single bank note liable to reflux in a run. A similar situation would eventually pertain in Scotland and Ireland where banks maintained a specie reserve capable of redeeming every note issued beyond the levels recorded in 1845. Finally, the English and Welsh country bank note issue could not grow beyond the levels established in 1844 and would only contract to be replaced by Bank of England notes as banks left the industry. However, the currency school's apparent victory in 1844/45 proved illusory. The British did find a substitute for their highly regulated bank note issue and began to utilise cheques in increasing numbers to make payment. There were no legislative

[119] Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue; Together with Proceedings of the Committee, Minutes of Evidence and Appendix* (London: Parliament of the United Kingdom (House of Commons), 1875), 187-88.
[120] 8 & 9 Victoria c. 37.

guarantees the banks would maintain the reserves needed to secure the growth in deposits generated by this increasing reliance on cheques. Furthermore, the *Bank Charter Act* put strict limits on the amount of legal tender the Bank of England could supply during a financial crisis. The government had to suspend the *Bank Charter Act* in 1847, 1857 and 1866 to stave off an impending financial meltdown.[121]

The *Bank Charter Act* influenced the structure of the English and Welsh banking industry by keeping banks granted a right to issue bank notes in 1844 in business. The *Bank Charter Act* achieved this outcome by creating a disincentive to bank amalgamations that delayed the Amalgamation Movement.

BANK AMALGAMATIONS AND THE *BANK CHARTER ACT*

Bank amalgamations are an indicator of the growth in bank size following the introduction of joint stock banking into England and Wales in 1826. Joseph Sykes estimated that 124 English and Welsh banks disappeared in amalgamations between 1826 and 1844.[122] Most of the banks that left the industry during this period were private banks that either converted to the joint stock form or merged with a joint stock bank. In 1826, Somerset's Vincent Stuckey (1771-1845), for example, consolidated the five private banks in which he had a proprietary interest into a single joint-stock institution.[123] By 1844, the joint stock banks had taken over 94 English and Welsh private banks.[124] This tentative process of consolidation was

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[121] Matthew Smith, "On central banking rules: Tooke's critique of the Bank Charter Act of 1844," *Journal of the History of Economic Thought* 25, no. 1 (2003).
[122] Joseph Sykes, *The Amalgamation Movement in English Banking, 1825-1924* (London: P. S. King and Son, 1926), 193-95.
[123] Cottrell and Newton, "Banking liberalisation," 90; Lucy Newton, "The birth of joint-stock banking: England and New England compared," *The Business History Review* 84, no. 1 (2010): 34.
[124] Sykes, *The Amalgamation Movement in English Banking*: 193-95.

unprecedented given the limits on bank size imposed by the six-partner limit prior to 1826. Nevertheless, most joint stock banks in England and Wales remained small-scale affairs.[125] The rights to issue bank notes assigned in 1844 suggest that at the time, private banks outnumbered their joint stock rivals by a ratio of 2.8:1.[126] The English and Welsh had a lot of ground to make up to replicate Scotland's larger banks.

The *Bank Charter Act* of 1844 induced a decline in the rate of bank amalgamations in England and Wales. Only 48 English and Welsh banks disappeared in amalgamation between 1845 and 1863. Mergers between private banks fell from 23 between 1826 and 1844 to just 12 between 1845 and 1863. Amalgamations between private banks and joint stock banks plummeted from 94 between 1826 and 1844 to only 24 between 1845 and 1863.[127] This slowdown in the rate of consolidation was a uniquely English and Welsh phenomenon. Inevitably, bank amalgamations now occurred less frequently in Scotland than in England and Wales because Scotland contained fewer banks to begin with. However, Scottish banks were bigger than the English and Welsh banks. The concentrating effect of a Scottish bank amalgamation was more dramatic than in England and Wales. Five of the 17 Scottish banks open for business in 1850 had exited the banking industry by 1865. One of those five left the industry due to failure. The other four banks

[125] Newton and Cottrell, "Joint-stock banking in the English provinces," 124; Charles W. Munn, "The emergence of joint-stock banking in the British Isles a comparative approach," *Business History* 30, no. 1 (1988): 77-80.
[126] Bank of England, "A list of the banks of issue 12 October 1844 showing the devolution of the rights to issue," (Bank of England Archive (G15/215), 1925).
[127] Sykes, *The Amalgamation Movement in English Banking*: 193-95.

disappeared in an amalgamation.[128] The *Bank Notes (Scotland) Act* had no discernible effect on the Scottish banks' propensity to amalgamate.

The *Bank Charter Act*'s amalgamation provisions account for the reduction in the rate of bank amalgamations after 1844. Only two private banks could aggregate their rights to issue in England and Wales if and only if the post-amalgamation whole had six members or less. In every other case, bank amalgamation between two English and Welsh banks either extinguished the target's right to issue bank notes or destroyed both banks' right to issue. The rules imposed by the *Bank Notes (Scotland) Act* were far more lenient because the Scottish legislation did not express an intention to replace Scotland's bank notes with the Bank of England's notes. The *Bank Notes (Scotland) Act* preserved Scotland's native capacity to issue bank notes by allowing two amalgamating banks to aggregate their rights to issue in every case. This difference did not escape the attention of the English and Welsh banking community. In 1849, the *Bankers' Magazine* lamented:

> In Scotland ... joint stock banks may unite together and retain their aggregate fixed issue; while in England and Wales, the union of two such banks, or of a private bank of issue with a joint stock bank is to be followed by the loss of circulation by one or both of them…. In the course of the ten years from 1826 to 1836, no less than *one hundred and fifty-four private banks were merged into joint stock banks.* Since the passing of the Bank Act of 1844, *not one* private bank of issue has united with a joint stock bank; and only four private firms have availed themselves of the permission to unite into two firms, retaining their aggregate circulation, the united firms not having more than six partners each.[129]

[128] Checkland, *Scottish Banking*: 372-73, 524.
[129] The Bankers' Magazine, "The union of English banking companies prevented by the Bank Act of 1844," *The Bankers' Magazine and Journal of the Money Market*, November 1849, 626-27. Italics in original. Sykes' estimates suggest that the claimed 154 amalgamations is an exaggeration. Sykes, *The Amalgamation Movement in English Banking*: 193-95.

The *Bankers' Magazine* warned that the *Bank Charter Act* undermined the *Country Bankers Act*'s objective by keeping English and Welsh banks unnecessarily small. The *Bank Charter Act* denied an English and Welsh bank the prospect of being taken-over on fair terms by a larger rival because "no other company of greater strength and means had any inducement to come forward and assist them."[130] A month later, an anonymous country banker complained to the *Bankers' Magazine*:

> Had the Act of 1844 allowed the union of all banks on equal terms, it is impossible to say how many comparatively small and weak banks might have been saved during the panic of 1847 by the timely union with larger and more influential companies, and this too, on terms securing the public from loss, and in many cases, the small private bankers from ruin and distress.[131]

The *Bank Charter Act* of 1844 therefore a created disincentive to amalgamation that fell most heavily on the private banks because their bank notes constituted a significant proportion of their business. Private bank disappearances by means of an amalgamation (with either a private bank or a joint stock bank) fell from 116 between 1826 and 1843 to just 34 between 1844 and 1861. In contrast, six joint stock banks disappeared in an amalgamation with another joint stock bank between 1826 and 1843 whereas ten joint stock banks amalgamated with another joint stock bank between 1844 and 1861.[132] Amalgamations between joint stock banks actually increased following the passage of the *Bank Charter Act.*

By 1865, William Gladstone (1809-1898) was the Chancellor of the Exchequer. His patience with the relatively small size of the English and Welsh banks coupled with the slow rate at which the English and Welsh country bank note was

[130] The Bankers' Magazine, "The union of English banking companies prevented by the Bank Act of 1844," 628.
[131] A Country Banker, "Injurious effect of the Bank Act of 1844 in preventing the union of banks of issue," *The Bankers' Magazine and Journal of the Money Market*, December 1849, 764.
[132] Sykes, *The Amalgamation Movement in English Banking*: 193-94.

disappearing was reaching its limit. In that year, Gladstone contemplated the possibility that Peel should have adopted a different approach to the question of bank amalgamations in 1844 and proposed legislation giving English and Welsh banks conditional rights to aggregate their bank note issue when they merged. The proposed legislation never passed into law.[133] Gladstone's proposal proved unnecessary anyway. Unbeknownst to him, the English and Welsh banks would soon embark on their Amalgamation Movement. Something was changing to make bank amalgamations a more attractive proposition than over the previous 21 years. The next section explains that deposit taking and cheques became increasingly important to the English and Welsh banks. Greater reliance on deposits and cheques diminished the importance of the right to issue bank notes, which overcame the disincentives to amalgamations imposed by the *Bank Charter Act*.

THE DEMISE OF THE COUNTRY BANK NOTE ISSUE

Table 3.1 suggests the English and Welsh country banks held onto their rights to issue bank notes tenaciously at first. The *Bank Charter Act* allocated a country bank note issue of £8,631,647. However, the country banks issued less than their full allocation of bank notes to avoid running fowl of the *Bank Charter Act*'s penalty provisions.[134] Michael Collins' estimates suggest the annual country bank note issue averaged £6,400,000 between 1846 and 1850 before increasing slightly to average

[133] "Candour is an engaging quality, but there are," *The Times*, 14 February 1865; House of Commons, *Bank Notes Issue. A Bill to Make Provision for Empowering Country Banks of Issue to Obtain Relief From Certain Restrictions Upon Payment from Time to Time of a Certain Charge in Respect Thereof* (London: Parliamant of the United Kingdom (House of Commons), 1865).

[134] Arthur Crump, *A Practical Treatise on Banking, Currency and the Exchanges* (London: Longmans, Green and Company, 1866), 204.

£6,500,000 between 1850 and 1859.[135] The country bank note issue began to fall in the 1860s and it continued to fall as the century progressed. Its value averaged £5,700,000 between 1860 and 1869 before declining to average £4,700,000 between 1870 and 1879.[136] At the same time, bank notes issued by the Bank of England began to replace the country English and Welsh bank note issue just as Peel's government hoped they would. The Bank of England's share of all the bank notes issued in England and Wales grew from 74.1 per cent between 1846 and 1850 to 88.5 per cent between 1877 and 1880.[137]

Table 3.1 Bank Notes Issued and Deposits Collected by Banks Other Than the Bank of England in England and Wales, 1846-1879				
	Bank Notes Issued (Average £)	Deposits Collected (Average £)	Change in Bank Notes Since 1846-50	Change in Deposits Since 1846-50
1846-1850	6,400,000	94,400,000	-	-
1850-1859	6,500,000	142,300,000	+2%	+51%
1860-1869	5,700,000	229,400,000	-11%	+143%
1870-1879	4,700,000	338,800,000	-27%	+259%
Bank Notes Issued and Deposits Collected by the Bank of England in England and Wales, 1846-1880				
	Bank Notes Issued (Average £)	Deposits Collected (Average £)	Change in Bank Notes Since 1846-50	Change in Deposits Since 1846-50
1846-1850	18,300,000	8,300,000	-	-
1856-1860	19,700,000	8,800,000	+8%	+6%
1866-1870	23,000,000	12,800,000	+26%	+54%
1877-1880	28,500,000	14,700,000	+56%	+77%
Sources: Collins, "Long-term growth in the English banking sector and the money stock," 384; Collins, "The business of banking: English bank balance sheets," 45.				

[135] Michael Collins, "The business of banking: English bank balance sheets, 1840–80," *Business History* 26, no. 1 (1984): 45.
[136] Collins, "The business of banking," 45.
[137] Michael Collins, "Long-term growth of the English banking sector and money stock, 1844-80," *The Economic History Review* New Series 36, no. 3 (1983): 384.

Table 3.1 also indicates the English and Welsh banks became increasingly reliant on deposits as their bank note issue declined. Deposits at English and Welsh banks other than the Bank of England averaged £94,400,000 between 1846 and 1850. These deposits rose to average £338,800,000 between 1870 and 1879.[138] This growth in deposits was a consequence of growing reliance on cheques that mobilising funds deposited in an account to make a payment. In 1845, the London and Westminster's James Gilbart had no doubt that banks other then the Bank of England would take most of the deposits created by this growing reliance on cheques. Depositors needed local banks with branches in close proximity to them and the Bank of England lacked the resources needed open enough branches to service the whole country.[139] In addition, Gilbart knew the Bank of England had a disproportionately large number of dead accounts on its books on which it would also have to pay interest. The Bank of England would struggle to pay the interest needed to attract depositors.[140] Gilbart knew the Bank of England would not be the currency principle's primarily beneficiary in the long run. The *Bank Charter Act* may have imposed a short-term cost on the country banks by restricting their bank note issue, but Table 3.1 suggests the Banks of England's deposits grew far more slowly than the non-Bank of England sector's deposits. The Bank of England's bank notes and deposits accounted for 20.9 per cent of the English and Welsh banking system's indebtedness to the public between 1846 and 1850. By 1877-80, the Bank

[138] Collins, "The business of banking, 1840–80," 45.
[139] Gilbart, *The Letters of Nehemiah*: 15. The Bank of England did maintain branches in Birmingham, Bristol, Gloucester, Hull, Leeds, Liverpool, Manchester, Newcastle, Norwich, Plymouth and Swansea. William John Lawson, *The History of Banking: With a Comprehensive Account of the Progress of the Banks of England, Ireland and Scotland* (London: Richard Bentley, 1850), 125-26.
[140] Gilbart, *The Letters of Nehemiah*: 15.

of England's total share of the English and Welsh banking industry had almost halved and stood at 10.6 per cent.[141]

The country banks defended their right to issue bank notes tenaciously before the Select Committee on Banks of Issue in 1841.[142] They did do because obtaining bank notes issued by the Bank of England to sustain their operations would have been prohibitively expensive. However, banks had less need for bank notes of any kind once their clients opened a deposit account and acquired a chequebook. The bank could simply acknowledge any amount the client borrowed in their bank account and the client could spend the funds borrowed by writing a cheque.[143] A bank only needed bank notes on those increasingly rare occasions when its customers demanded paper to make a payment to a third party. By 1875, Walter Bagehot (1826-1877) could tell the last Select Committee on Banks of Issue that Stuckey's Banking Company only issued its bank notes to convenience "small persons" such as "small farmers, stock dealers and butchers" who wanted to cash the cheques they received as payment.[144] Stuckey's Banking Company provided this facility at no charge, he said, because its right to issue bank notes avoided the cost of acquiring Bank of England paper to meet the same purpose.

The diminishing importance of the country bank note issue removed the impediment to bank amalgamations imposed by the *Bank Charter Act.* An early indicator that country banks were reassessing the value of their rights to issue bank

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[141] Collins, "Long-term growth of the English banking sector and money stock," 384.
[142] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue*; Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*.
[143] Macleod, *The Theory and Practice of Banking*, II: 407.
[144] Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 410.

notes came as early as 1865. In that year, a merger between Lloyds and Company and Moillet and Sons put Lloyds on an expansionary path that would eventually see it emerge as one of the five biggest banks England and Wales. Both banks involved were banking private banks and Lloyds turned the amalgamation into an opportunity to expand its proprietorship by incorporating on a limited liability basis. Consequently, the amalgamation invoked the provisions of the *Bank Charter Act* and turned a private bank that could issue bank notes into a joint stock banking company that could not. Lloyds would forfeit the right to issue £38,816 in Britain's industrial heartland, but its proprietors proceeded with the amalgamation anyway.[145] Then in 1866, the largest country bank of issue in England and Wales opened its first branch in London.

The National Provincial possessed the largest country bank note issue allocated by the *Bank Charter Act* in 1844.[146] Only the Bank of England had a bigger bank note circulation. The National Provincial Bank maintained its status as a bank of issue carefully since its establishment in 1833. This bank had an administrative office in the Metropolis but avoided the acquisition of any banking offices within 65-miles of London. A proposal to open a London branch in 1866, therefore, would cost the National Provincial the right to issue £422,371 in the provinces.[147] *The Times* defended the National Provincial proposal arguing there was no reason why the bank should not accept deposits in London if it confined its bank notes to the

[145] John R. McCulloch, *A Supplement to the Edition of Mr. McCulloch's Commercial Dictionary Published in 1844* (London: Longman, Brown, Green and Longmans, 1846), 11; R. S. Sayers, *Lloyds Bank in the History of English Banking* (Oxford: Clarendon Press, 1957), 220.
[146] McCulloch, *A Supplement to the Edition of Mr. McCulloch's Commercial Dictionary*: 12; Hartley Withers, *The National Provincial Bank: 1833 to 1933* (London: The National Provincial Bank, 1933), 67.
[147] McCulloch, *A Supplement to the Edition of Mr. McCulloch's Commercial Dictionary*: 12; R. H. Patterson, *The Economy of Capital, or Gold and Trade* (Edinburgh: William Blackwood and Sons, 1865), 348-49; Withers, *The National Provincial Bank*: 67.

provinces.[148] However, the *Bank Charter Act* continued to exclude English and Welsh joint stock banks of issue from the Metropolis. The National Provincial tried to salvage what it could from the situation. It approached the Bank of England to negotiate a compounding arrangement that would have furnished an annual payment to compensate for the loss of its right to issue bank notes. The Bank of England informed the National Provincial that Treasury's firm policy was that no bank should receive such a payment once it took a step that forfeited its right to issue granted by the *Bank Charter Act*.[149] Consequently, the National Provincial's London branch entailed the loss of the right to issue bank notes without any compensation whatsoever. The National Provincial's directors argued a London office made sound business sense nonetheless. They believed taking deposits in London would generate more wealth than the largest country bank note issue in England and Wales ever could.[150]

Lloyds and Company and the National Provincial Bank of England were not the only banks to surrender their rights to issue bank notes as the Amalgamation Movement got underway. Between 1881 and 1897, 13 banks did what the National Provincial failed to do and surrendered their bank note issue in exchange for an annual payment from the Bank of England. These 13 banks were the first to compound their bank note issue since 1852.[151] However, the Bank of England's

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[148] "Candour is an engaging quality, but there are."
[149] Bank of England, "Minutes of the Court of Directors," (Bank of England Archive (G4/88), 1865/66), 194-96. See alo" Bank of England, "Memorandum on the application of Stuckey's Banking Company to compound its issue," (Bank of England Archive (G15/214), 1885), 5.
[150] Withers, *The National Provincial Bank*: 68.
[151] Bank of England, "Mr Bowman's memorandum: Compositions to the country bankers under the Act of 1844," (Bank of England Archive (G15/215), 1919), 6-8.

internal records suggest the most common cause of the loss of the right issue bank notes was a bank amalgamation.

Table 3.2 Number of Banks of Issue Absorbed by Another Bank in England and Wales, 1845-1929		
	Private Banks	Joint Stock Banks
1844-1849	4	0
1850-1859	5	1
1860-1869	13	4
1870-1879	16	3
1880-1889	18	9
1890-1899	45	10
1900-1909	32	14
1910-1919	8	12
1920-1929	4	1
Source: Bank of England, "A list of the banks of issue 12 October 1844 showing the devolution of the rights to issue."		

Table 3.2 draws upon an internal Bank of England memorandum that explains what happened to the rights to issue bank notes assigned under the *Bank Charter Act* in 1844.[152] Table 3.2 suggests the rate at which banks of issue disappeared in an amalgamation increased significantly after 1860. Only nine private banks and one joint stock bank surrendered their right to issue bank notes in an amalgamation between 1844 and 1859. The equivalent numbers in the 1860s were 13 private banks and four joint stock banks. After that, the number of banks of issue absorbed in both categories increased further as the Amalgamation Movement gathered pace. Over a third of the banks assigned rights to issue bank notes surrendered them in an amalgamation between 1890 and 1909. In 1896 alone, 20 private banks, many of

[152] Bank of England, "A list of the banks of issue 12 October 1844 showing the devolution of the rights to issue."

them banks of issue, joined forces to form Barclay & Company (Limited).[153] Liberation from *Bank Charter Act* put Barclays on an expansionary path that would see it join Lloyds Bank, the National Provincial Bank of England and the Midland Bank (all of them former banks of issue) as one the Big Five. The prospect of losing the right to issue bank notes was no longer sufficient reason to refuse the opportunity to amalgamate with a rival or to move into London.

Unlike the English and Welsh banks, Scottish banks retained the right to expand their bank note issue beyond the levels recorded in 1845. Thus, bank notes remained important to Scottish banking practice. The next section explains how prospect of losing their all-important rights to issue stopped the Scottish banks crossing the border to participate in the English and Welsh Amalgamation Movement.

A SCOTTISH INVASION REPELLED

A Scottish banking invasion of England and Wales began in the mid-1860s when the Scottish joint stock banks opened their first offices in London. The National Bank of Scotland was first in 1864 followed by the Bank of Scotland in 1867 and the Royal Bank of Scotland in 1873.[154] The presence of these Scottish banks in London caused disquiet in England and Wales because the Scottish banks enjoyed a degree of preferential treatment. The National Provincial Bank of England discovered to its cost that no English or Welsh bank of issue could conduct banking operations in London and retain its right to issue bank notes; and yet, none of the Scottish banks

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[153] P. W. Mathews and Anthony W. Tooke, *History of Barclays Bank Limited* (London: Blades, 1926), 1-29.

[154] M. Gaskin, "Anglo-Scottish banking conflicts, 1874-1881," *The Economic History Review* New Series 12, no. 3 (1960): 446-47.

forfeited their right to issue once they opened their branches in London.[155] In 1875, the North and South Wales Bank's George Rae (1817-1902) complained about the discrepancy to the Select Committee of Banks of Issue of that year. He thought the Scottish banks "ought to be put on the same footing" as their English and Welsh counterparts and should sacrifice their right to issue bank notes in Scotland when they came to London.[156]

The reason for the inconsistent treatment between the English and Welsh banks and the Scottish banks when they opened branch in London was that English and Welsh banking law treated Scotland as if it were a foreign country. The only banks of issue excluded from London were those that issued bank notes in provincial England and Wales. What a Scottish bank did outside England and Wales had no bearing on its right to maintain an office in London.[157] The Scottish banks also had a precedent to justify their presence in London. The National Bank of Ireland already possessed an office in London and few seemed overly concerned that it retained its right to issue bank notes in Ireland. Why, the Scots wondered, should their banks be any different?[158] The Scottish presence in England and Wales took on a far more menacing significance in 1874 when the Clydesdale Bank opened branches in Carlisle, Whitehaven and Workington in the English county of Cumberland.[159]

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[155] Checkland, *Scottish Banking*: 482.

[156] Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 262-63.

[157] Henry Dunning Macleod, *The Theory and Practice of Banking*, 4th ed., vol. II (London: Longmans, Green, Reader and Dyer, 1886), 237-41.

[158] "The Scotch banks in England," *The Times*, 9 March 1875.

[159] "Money-market and City intelligence," *The Times*, 17 February 1875; Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 181.

Sandwiched between the Scottish border and the Lake District, Cumberland had always displayed a propensity to orientate its commercial life in a northerly direction towards Scotland. The county's haematite ore field supplied raw materials to the iron and steel industries of the Clyde and Western Scotland for example.[160] It was natural that a Glaswegian bank like the Clydesdale would select Cumberland as a viable point of entry into England.[161] The Clydesdale's administrators knew the *Bank Charter Act* denied new entrants to England and Wales the right to issue bank notes. Consequently, the Clydesdale's English branches conducted a deposit-taking business and did not issue bank notes. The only times these branches dealt in Scottish bank notes was when called upon to exchange a sovereign for a Scottish £1 note brought across the border.[162]

The Clydesdale's border raid threatened the English and Welsh banking community. Scottish banks remained bigger than most English and Welsh banks at this time and the Scots had far more experience of branch banking than the English and Welsh did.[163] The Scottish banks would have been formidable rivals had they started to take over English and Welsh banks to expand their branch networks in a southerly direction. The Chancellor of the Exchequer, George Goschen (1831-1907), proposed legislation that would have forced the Scottish banks into making an unpalatable choice. Either they confined their operations to Scotland or they opened branches in England and Wales and lost the right to issue bank notes at home.[164] The

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[160] Gaskin, "Anglo-Scottish banking conflicts, 1874-1881."
[161] Checkland, *Scottish Banking*: 483-84.
[162] Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 181.
[163] Checkland, *Scottish Banking*: 577.
[164] "Mr Goschen's Bankers' Bill," *The Times*, 12 March 1875; "At the beginning of the Session Mr Goschen," *The Times*, 17 March 1875; "There was yesterday afternoon a very spirited debate," *The*

proposed legislation went into limbo pending a recommendation from the 1875 Select Committee on Banks of Issue. The English and Welsh banks told the committee they objected to a Scottish presence on their territory because the currency legislation gave the Scottish banks two unfair advantages.[165] First, the English and Welsh banks could not retaliate. They could not open branches in Scotland because banking undertaken in the absence of a right to issue in Scotland was impossible and the *Bank Notes (Scotland) Act* forbade new banks of issue there. Second, the Scottish banks issued bank notes denominated in amounts as low as £1 against their bullion reserves, a privilege denied to any English and Welsh bank of issue. The English and Welsh feared the Scots would use their bank notes to raise cheap finance at home and deploy it to gain competitive advantages in England and Wales.

The 1875 Select Committee on Banks of Issue took evidence but failed to deliver a recommendation in that year. The committee did not reconvene in the next parliamentary session. Consequently, Goshen's proposed legislation never passed into law. On the surface, the Select Committee on Banks of Issue of 1875 changed nothing. The Scottish banks remained legally entitled to maintain banking offices in any part of England and Wales as long as they confined their bank note issue to Scotland. A defiant Clydesdale Bank even kept its branches in Cumberland. Nevertheless, the English and Welsh banking community sent a message to their Scottish counterparts in 1875.[166] The English and Welsh banking industry would

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Times, 18 March 1875; "Banking and Mr Goschen's Bill," *Blackwood's Edinburgh Magazine*, June 1875.

[165] Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 121-22, 252-53, 424-25.

[166] Checkland, *Scottish Banking*: 485.

tolerate Scottish banking offices in London. The British Linen Company, the Union Bank of Scotland and the Clydesdale all opened Metropolitan branches in 1877 for example. However, the English and Welsh banking industry would use its influence in Westminster to threaten the Scottish banks' right to issue bank notes at home if they encroached on provincial England and Wales. The Scottish banks headed the warning and became marginal participants in the Amalgamation Movement.

Britain's currency legislation gave the English and Welsh banking industry a degree of invulnerability from outside competition it ultimately denied to their Scottish counterparts. By 1919, the Amalgamation Movement had produced English and Welsh banks that were now far bigger than even the largest Scottish banks.[167] In 1919, two of the biggest banks in England and Wales looked northwards for opportunities for growth and mounted a successful counter invasion of Scotland. Barclays took over the British Linen Bank although the currency arrangements put in place in 1844/45 continued to exert an influence. An amalgamation would have resulted in the British Linen Bank's liquidation and the subsequent loss of its right to issue Scottish bank notes. Consequently, Barclays ran the British Linen Bank as an affiliate, which meant the British Linen Bank remained a bank of issue.[168] Within weeks, the London City and Midland Bank announced a similar arrangement with the Clydesdale Bank, the very same bank that attempted to invade Cumberland in 1874.[169] Takeovers like these set a precedent the British banks continued to follow

[167] Forrest Capie and Ghila Rodrik-Bali, "Concentration in British banking, 1870-1920," *Business History* 24, no. 3 (1982).
[168] "Bank affiliation: Barclays scheme," *The Times*, 10 November 1919, 376; "Barclays Bank (Limited)," *The Times*, 20 November 1919; Mathews and Tooke, *History of Barclays Bank Limited*: 376; Checkland, *Scottish Banking*: 577.
[169] "Banking alliance," *The Times*, 25 November 1919; "The Midland and Clydesdale Bank fusion," *The Times*, 23 December 1919.

during the twentieth century. British banks generally do not amalgamate with banks domiciled on the other side of the Anglo-Scottish border. They acquire subsidiaries on the other side of the River Tweed instead. When the Royal Bank of Scotland took the National Westminster Bank (NatWest Bank) over in 2000, NatWest became a subsidiary of the Royal Bank of Scotland Group.[170] The arrangement meant the Royal Bank of Scotland could remain one of contemporary Scotland's three banks of issue.[171]

CONCLUDING REMARKS

The currency legislation of 1844/45 was the last in a series of reforms designed to put Britain's money supply on a secure footing. These reforms included the recoinage of 1816, which put Britain on a gold standard and the restoration of cash payments in 1821 that made the Bank of England's notes redeemable once more. Like the *Bank Charter Act* of 1844, these reforms were the product of a conviction that only a money supply based on gold could function as a viable means of payment because gold constituted an ideal store of value because of its inherent worth. In the end, these reforms proved futile because the British became increasingly dependent on bank account balances mobilised by cheques to make payments. The banking school were right all along. Bank notes were just one of several transferable financial assets that could furnish a means of payment and ultimately the needs of trade would prevail. The post-Industrial Revolution British economy needed a means of payment erected on the foundations of bank credit to sustain itself. The gold standard may have made Britain's bank notes unassailably secure, but the

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[170] Graham Kennedy, David Boddy, and Robert Paton, "Managing the aftermath: Lessons from The Royal Bank of Scotland's acquisition of NatWest," *European Management Journal* 24, no. 5 (2006).
[171] Jan Penrose and Craig Cumming, "Money talks: Banknote iconography and symbolic constructions of Scotland," *Nations and Nationalism* 17, no. 4 (2011).

security of the money supply as a whole largely depended upon the safety of the banking system.

The currency reforms introduced in 1844/45 failed to limit the British money supply to the amount of bullion available but they had an impact on the banking industry nonetheless. They turned the Bank of England into the only bank of issue in England and Wales and allowed the other banks to take most of the growing deposit-taking business on offer. In addition, these reforms ensured that native banks would continue to meet Scotland's demand for bank notes. The result was a barrier erected along the border that ensured Scotland remained a separate banking jurisdiction to that of England and Wales. Scottish banks and English and Welsh banks did not amalgamate with each other even when they came under common ownership. Finally, these currency reforms introduced in 1844 created a disincentive to bank amalgamations that delayed the Amalgamation Movement by more than two decades. The Amalgamation Movement had to wait until the right to issue bank notes lost its value to the English and Welsh banking industry.

The growing reliance on cheques did more than undermine bank note's importance to the banking industry. The next Chapter explains how he increased use of cheques changed the English and Welsh banks' lending practices to send a financial instrument known as the inland bill of exchange into terminal decline. The trade in these inland bills of exchange sustained many of the small regional banks found in England in Wales prior to 1870. Banks located in industrial districts raised the funds by rediscounting bills of exchange in London. Banks located in agricultural districts obtained a share of the interest these rediscounted bills

generated by sending their excess funds to London. The demise of the inland bill put an end to this system of market exchanges, which turned participation in the Amalgamation Movement into a necessity.

CHAPTER FOUR

CHANGING HANDS: THE DEMISE OF THE INLAND BILL OF EXCHANGE

> Outside the firm, price movements direct production, which is co-ordinated through a series of exchange transactions on the market. Within a firm, these market transactions are eliminated and in [their] place … [a] co-ordinator … directs production.[1]

> In many sectors of the economy, the visible hand of managerial coordination replaced what Adam Smith referred to as the invisible hand of market forces.[2]

Firms are command economies in miniature in which administrative fiat directs resources to their final use. A firm puts human, capital and/or natural resources under administrative control to achieve economic objectives.[3] As such, a firm's existence challenges the tenets of neoclassical economics because price signals are supposed to allocate resources to their best use.[4] A market economy should require no more human agency than *homo economicus*' instinctive response to changing prices to allocate resources efficiently.[5] Markets ought to regulate themselves. They have no need for administrators to coordinate them.[6] Neoclassical economics cannot

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[1] Ronald H. Coase, "The nature of the firm," *Economica* 4, no. 16 (1937): 388.

[2] Alfred D. Chandler, *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, Massachusetts: Belknap Press, 1977), 1.

[3] Coase, "The nature of the firm."

[4] Oliver Hart, "An economist's perspective on the theory of the firm," *Columbia Law Review* 89, no. 7 (1989); Paul J. McNulty, "On the nature and theory of economic organization: The role of the firm reconsidered," in *The Theory of the Firm: Critical Perspectives on Business Management*, ed. Nicolai J. Foss (London: Routledge, 2000).

[5] *Homo economicus* is a rational maximiser of his or her own self-interested used by neoclassical economics to model human choice and behaviour. See: Richard H. Thaler, "From homo economicus to homo sapiens," *The Journal of Economic Perspectives* 14, no. 1 (2000); Joseph Henrich et al., "In search of homo economicus: Behavioral experiments in 15 small-scale societies," *The American Economic Review* 91, no. 2 (2001); Doris Schroeder, "*Homo economicus* on trial: Plato, Schopenhauer and the virtual jury," *Philosophy of Management* 1, no. 2 (2001); Raphael Sassower, "Is homo economicus extinct?," *Philosophy of the Social Sciences* 40, no. 3 (2010); Toshio Yamagishi et al., "In search of *Homo economicus*," *Psychological Science* 25, no. 9 (2014).

[6] Lisa Hill, "The hidden theology of Adam Smith," *European Journal of the History of Economic Thought* 8, no. 1 (2001); James Alvey, "The hidden theology of Adam Smith: A belated reply to Hill," *European Journal of the History of Economic Thought* 11, no. 4 (2004); Peter Harrison, "Adam Smith and the history of the invisible hand," *Journal of the History of Ideas* 72, no. 1 (2011).

explain why people commit resources to firms. Nevertheless, people do establish firms and they have done so for a long time. When a firm grows in size, it takes control of resources previously allocated by the market. This is what happened in England and Wales during the Amalgamation Movement.

Prior to the Amalgamation Movement, regional banks transacted with each other at through market exchanges. Banks in industrial regions where the demand for credit was high sustained their lending by rediscounting bills of exchange in London. Agricultural banks subject to low demand for credit earned a return on their excess funds by supplying London with finance it needed to rediscount the bills of exchange sent there by the industrial banks. This system of market exchanges depended on price signals (in this case rates of interest) to allocate the nation's savings away from areas where the demand for credit was low and towards areas where the demand for credit was high. Banking in post-Amalgamation Movement England and Wales was very different. Now the largest banks possessed branches in every part of England and Wales. Branches located in agricultural districts raised finance for the bank and its industrial branches lent the funds raised to the banks' industrial clients. What Alfred Chandler referred to as the 'visible hand' of managerial coordination replaced Adam Smith's 'invisible hand' of market exchange.

This Chapter argues the demise of the market for inland bills of exchange made participation in the Amalgamation Movement a necessity for many English and Welsh banks. The intention is not to resurrect what some banking historians have called the 'King hypothesis.' This Chapter will not reiterate an old, oft repeated and

by now discredited claim that the Amalgamation Movement caused the demise of the inland bill of exchange. Instead, the Chapter claims the market for inland bills declined first, which forced banks to seek amalgamation partners because continued reliance on market exchanges to sustain their operations became prohibitively expensive. In short, the Amalgamation Movement compensated for the loss of inland bills of exchange. This chapter begins by examining the reasons why firms grow in size.

WHY DO LARGE FIRMS EXIST?

Alfred Chandler argued firms grew in size because capital-intensiveness imposed fixed costs, which meant a small number of large firms had to account for a capital-intensive industry's output. According to Chandler, oligopolies fostered the concentration of production needed to realise economies of scale and scope.[7] This meant rivals merged with each other to minimise average unit costs through the rationalisation of production.[8] Manufacturing firms could concentrate production in a small number of production facilities because they could distribute the output they produced over a wide geographical area. The only inhibitors to rationalisation Chandler recognised were impediments to the free movement of goods such as

[7] Alfred D. Chandler and Louis Galambos, "The development of large-scale economic organizations in modern America," *The Journal of Economic History* 30, no. 1 (1970); Chandler, *The Visible Hand*; Alfred D. Chandler, "The growth of the transnational industrial firm in the United States and the United Kingdom: A comparative analysis," *The Economic History Review* New Series 33, no. 3 (1980); Alfred D. Chandler, "The emergence of managerial capitalism," *The Business History Review* 58, no. 4 (1984); Alfred D. Chandler, "The enduring logic of industrial success," *Harvard Business Review* 68, no. 2 (1990); Alfred D. Chandler and Takashi Hikino, *Scale and Scope: The Dynamics of Managerial Capitalism* (Cambridge, Massachusetts: Belknap Press, 1990); Alfred D. Chandler, "What is a firm?: A historical perspective," *European Economic Review* 36, no. 2-3 (1992).

[8] Chandler, *The Visible Hand: The Managerial Revolution in American Business*: 315-44; Chandler, "The emergence of managerial capitalism," 482-84; Chandler, "The enduring logic of industrial success," 130; Alfred D. Chandler, "Organizational capabilities and the economic history of the industrial enterprise," *The Journal of Economic Perspectives* 6, no. 3 (1992): 82.

shipping costs, tariffs, import quotas and the administrative complexity associated with distribution over long distances.[9]

Banks in nineteenth-century England and Wales faced a different reality to the manufacturing firms Chandler studied. Banks supplied intangible services that they could not ship across large distances because their production and consumption often occurred simultaneously.[10] As the London and Westminster Bank's James Gilbart noted in 1845, a bank's customers had to attend at its branches to transact business with it.[11] The Amalgamation Movement could not centralise production in the way Standard Oil rationalised the American oil refining industry.[12] A bank could not service the whole of Lancashire from a super branch located in Manchester. Customers domiciled outside Manchester would have deemed the travelling times imposed excessive. Consequently, the predator banks left most of the branches they took over during the Amalgamation Movement open for business. The number of bank branches in England and Wales actually increased between 1870 and 1920.[13]

Rendering explicit the economies needed to justify the Amalgamation Movement presented a problem for those in the banking industry who set out to justify the process at the time. In 1896, an article in *The Economic Journal* claimed bank amalgamations yielded "a large reduction in working expenses" because "many economies are … possible in large concerns which are out of the question in small

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[9] Chandler, "The growth of the transnational industrial firm," 399-400.
[10] Richard L. Daft, *Organization Theory and Design*, Eighth ed. (Mason: Thomson, 2004), 256.
[11] James William Gilbart, *The Letters of Nehemiah: Relating to the Laws Affecting Joint Stock Banks, the Effects Likely to be Produced by the Measures of Sir Robert Peel on the System of Banking in London and Throughout the Country* (London: London and Westminster Bank, 1845), 15.
[12] Chandler, "Organizational capabilities," 82.
[13] Shizuya Nishimura, *The Decline of Inland Bills of Exchange in the London Money Market, 1855-1913* (Cambridge: Cambridge University Press, 1971), 80-81.

ones."[14] Its author's attempt to identify the economies realised by bank amalgamations yielded just two examples, which related to an elimination of duplicated effort. The first was that after the amalgamation a bank rarely found places on its board of directors for all of the amalgamating banks' directors. The second was that an amalgamated bank needed fewer messengers than its constituent parts had done to collect cheques from its neighbours. No doubt, these cost savings existed although the release of a few directors and the elimination of some messengers would be too small a cost saving to justify a process of concentration that directed 80 per cent of all deposits taken in England and Wales into the coffers of just five banks.[15] The economic historian Richard Grossman maintained the Amalgamation Movement was no exercise in cost minimisation.[16] Similarly, Joseph Sykes concluded in 1926 that bank expenses increased during the Amalgamation Movement. Sykes argued:

> In the case of expenses, it is apparent that the expected economies so often stressed in chairman's speeches have not materialised, and consequently what was a strong argument in favour is actually a strong argument against [bank amalgamations]…. Most bankers still seem to consider that more economies than diseconomies have resulted, and consequently do not seem alive to the results of their actions.[17]

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[14] Francis E. Steele, "Bank amalgamations," *The Economic Journal* 6, no. 24 (1896): 536. See also: Francis E. Steele, *Present Day Banking: Its Methods, Tendencies and Practices* (London: Butterworth, 1909), 19-21.

[15] Forrest Capie and Ghila Rodrik-Bali, "Concentration in British banking, 1870-1920," *Business History* 24, no. 3 (1982).

[16] Richard S. Grossman, "Rearranging deck chairs on the Titanic: English banking concentration and efficiency, 1870–1914," *European Review of Economic History* 3, no. 3 (1999); Richard S Grossman, *Unsettled Account: The Evolution of Banking in the Industrialized World Since 1800* (Princeton: Princeton University Press, 2010), 124-26.

[17] Joseph Sykes, *The Amalgamation Movement in English Banking, 1825-1924* (London: P. S. King and Son, 1926), 158.

Recent studies suggest banks struggle to realise economies of scale or scope when they grow their branch networks.[18] The administrative burden a large branch network imposes appears to make it inherently expensive to operate.

The absence of apparent economies realised by the Amalgamation Movement raises an important question. Why did a small number of banks administer large branch networks in England and Wales if a larger number of smaller banks could have provided the same geographical coverage at less cost? Chapter Two supplied a partial answer to that question. Scottish experience suggested that bigger banks were safer than smaller ones because they were less vulnerable to a run. Consequently, bigger banks had competitive advantages that motivated the Amalgamation Movement. However, there is another reason why the banks might have amalgamated. An economist by the name of Ronald Coase developed a theory of the firm in the 1930s that offers insights into the advantages bestowed by an increase in firm size. This theory helped to secure the 1991 Nobel Prize in Economics for Coase.[19]

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[18] George J. Benston, "Branch Banking and economies of scale," *The Journal of Finance* 20, no. 2 (1965); George J. Benston, Gerald A. Hanweck, and David B. Humphrey, "Scale economies in banking: A restructuring and reassessment," *Journal of Money, Credit and Banking* 14, no. 4 (1982); Thomas W. Gilligan, Michael Smirlock, and William Marshall, "Scale and scope economies in the multi-product banking firm," *Journal of Monetary Economics* 13, no. 3 (1984); Michael Smirlock, "Evidence on the (non) relationship between concentration and profitability in banking," *Journal of Money, Credit and Banking* 17, no. 1 (1985); Allen N. Berger, Gerrald A. Hanweck, and David B. Humphrey, "Competitive viability in banking: Scale, scope, and product mix economies," *Journal of Monetary Economics* 20, no. 3 (1987); Jeffrey A. Clark, "Economies of scale and scope at depository financial institutions: A review of the literature," *Economic Review* 73, no. 8 (1988); Allen N. Berger and David B. Humphrey, "The dominance of inefficiencies over scale and product mix economies in banking," *Journal of Monetary Economics* 28, no. 1 (1991); Allen N. Berger et al., "Bank concentration and competition: An evolution in the making," *Journal of Money, Credit and Banking* 36, no. 3 (2004).

[19] Stewart Schwab, "Coase defends Coase: Why lawyers listen and economists do not," *Michigan Law Review Association* 87, no. 6 (1989): 390-91; Richard A. Posner, "Nobel laureate: Ronald Coase and methodology," *The Journal of Economic Perspectives* 7, no. 4 (1993); Daniel A. Farber, "Parody lost/pragmatism regained: The ironic history of the Coase Theorem," *Virginia Law Review* (1997).

Coase was an unusual economist who studied business subjects alongside the economics he learned at the London School of Economics. In 1932, Coase graduated with a Bachelor of Commerce rather than the Bachelor of Economics usually awarded to an aspiring professional economist. Before he graduated, Coase spent time in the United States studying some large American manufacturing concerns; many of them the same firms Chandler's would study later in the century.[20] Coase also graduated at a time when the Soviet Union had embarked upon its experiment in economic planning.[21] At the time, Coase was convinced that administering an enterprise as large as the Soviet economy would exhaust the competence of Stalin's economic planners. He thought economic planning undertaken on such a scale must result in economic inefficiency. However, this not particularly insightful conclusion troubled Coase because of his encounters with real-world business practice. Coase knew capitalist market economies utilised economic planning too. The difference was merely a question of scale. Economic planners administered an entire economy in the Soviet Union whereas planning occurred at the level of a firm in a capitalist economy. The paradox of a capitalist market economy reliant on economic planning to allocate some of its resources prompted Coase to ask questions no other economist asked before.[22] Questions like, 'Why do firms exist? And what stops them growing until they take over an entire economy?' In 1937, Coase published his answers to those questions.

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[20] See: Oliver E. Williamson, "Introduction," in *The Nature of the Firm: Origins, Evolution Development*, ed. Oliver E. Williamson and Sidney G. Winter (Oxford: Oxford University Press, 1991); Ronald H. Coase, "The nature of the firm: Origin," in *The Nature of the Firm: Origins, Evolution and Development*, ed. Oliver E. Williamson and Sidney G. Winter (Oxford: Oxford University Press, 1991); Ronald H. Coase, "The nature of the firm: Meaning," in *The Nature of the Firm: Origins, Evolution and Development*, ed. Oliver E. Williamson and Sidney G. Winter (Oxford: Oxford University Press, 1991).
[21] Coase, "The nature of the firm: Origin," 38-39.
[22] Williamson, "Introduction," 4.

Coase argued market exchanges impose expenses called 'transaction costs.' A buyer and seller must negotiate the terms under which a market exchange will occur, for example, a process that takes time and requires insight into the alternatives on offer elsewhere. Coase reasoned that firms avoid these transaction costs when their administrators allocate resources entrusted to their control. Coase explained:[23]

> The main reason why it is profitable to establish a firm would seem to be that there is a cost of using the price mechanism. The most obvious cost of 'organising' production through the price mechanism is that of discovering what the relevant prices are.... The costs of negotiating and concluding a separate contract for each exchange ... must also be taken into account.... A factor of production (or the owner thereof) does not have to make a series of contracts with the factors with whom he is co-operating within the firm, as would be necessary ... if this co-operation were a direct result of the working of the price mechanism....

Coase realised administering a firm is no cost-free exercise. A firm has to invest in a managerial hierarchy that is expensive, prone to error and as much subject to the law of diminishing return as any other factor of production.[24] The cost of achieving outcomes administratively will exceed the transaction costs avoided eventually. According to Coase, a rationally managed firm will grow when the transaction cost imposed by one more market exchange exceeds the cost of achieving the same outcomes administratively. It will stop growing once the marginal transaction cost avoided equals the marginal cost of administration.

This chapter argues the Amalgamation Movement was an exercise in the avoidance of transaction costs. Banks amalgamated because the transaction costs imposed by the market exchanges increased because of the demise of the inland bill of exchange. Banks evaded these escalating transaction costs, and so never incurred

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[23] Coase, "The nature of the firm," 390-91.

[24] For more on the law of diminishing returns see: Paul A. Samuelson and William D. Nordhaus, *Microeconomics*, Seventeenth ed. (New York: McGraw-Hill, 2001), 110.

them, by amalgamating. The next section will explain how the market for inland bills allocated English and Welsh savings prior to 1870. As Coase would have predicted, these market exchanges sustained the comparatively small banks found in England and Wales.

BANK LENDING ON INLAND BILLS OF EXCHANGE

The *Bills of Exchange Act* of 1882 defined a bill of exchange as:

> ...an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified person, or to bearer.[25]

A bill of exchange is a written order issued by a drawer directing the drawee to pay an amount either on demand or at some future date to a payee, to that payee's order or to the bearer. The drawee becomes the bill's acceptor by indicating a willingness to obey the order.[26] In addition, a bill becomes a negotiable (transferable) instrument if the acceptor agrees to make payment either to the payee's order or to the bearer. Anyone holding a bill made payable to the bearer only has to relinquish possession of it to transfer the right to payment to someone else. However, the payee of a bill made payable to a payee's order has to endorse it to transfer the right to payment to an endorsee. That endorsee can endorse the bill again in favour of another endorsee and this process can continue until the bill finally matures.[27] A bill made payable to the payee's order becomes more secure every time someone endorses it. The drawer

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[25] 45 & 46 Victoria c. 61.

[26] Timothy Cunningham, *The Law of Bills of Exchange, Promissory Notes, Banknotes, and Insurances: Containing all the Statutes, Cases at Large, Arguments, Resolutions, Judgments, Decrees, and Customs of Merchants Concerning them Methodically Digested. Together with Rules and Examples for Computing the Exchange between England and the Principal Places of Trade in Europe. Also The Arbitrations of Exchange set in a Clear and Rational Light and Illustrated with Variety of Examples*, Third ed. (London: R. Baldwin, W. Owen as S. Crowder, 1766), 8-21.

[27] John Bayley, *A Short Treatise on the Law of Bills of Exchange, Cash Bills and Promissory Notes* (London: E. Brooke, 1789), 1, 12-19.

and every subsequent endorser are liable to the holder in due course if the acceptor defaults.[28] Section 4(2) of the 1882 *Bills of Exchange Act* made an important distinction.

> An inland bill is a bill which is or on the face of it purports to be (a) both drawn and payable within the British Islands, or (b) drawn within the British Islands upon some person resident therein. Any other bill is a foreign bill.[29]

Inland bills generally owed their origins in domestic commercial transactions. Manufacturers and merchants drew and endorsed bills of exchange to acquire raw materials and finished goods on credit.[30] Thus, inland bills of exchange offered a growing manufacturing economy both a source of short-term credit and a means of payment during the Industrial Revolution. Lancashire's cotton industry used bills of exchange as a substitute for bank notes during the early nineteenth century for example.[31]

The holder of a bill of exchange could do more than hold it to maturity or endorse it to make a payment. One could also obtain bank notes and coins for it by endorsing the bill in favour of someone who wanted to purchase it. Anyone purchasing bill of exchange would expect a return on his or her outlay. Consequently, discounting (exchanging a bill for less than its value at maturity)

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[28] John Barnard Byles, *A Practical Treatise on the Law of Bills of Exchange, Promissory Notes, Bank-notes, Bankers' Cash-notes and Checks: With an Appendix of Statutes and Forms of Pleading*, Fourth ed. (London: S. Sweet, 1843), 106.

[29] "British Islands" meant "any part of the United Kingdom of Great Britain and Ireland, the islands of Man, Guernsey, Jersey, Alderney, and Sark, and the islands adjacent to any of them being part of the dominions of Her Majesty."

[30] W. T. C. King, *History of the London Discount Market* (London: George Routledge & Sons, 1936), xv-xvi.

[31] Henry Thornton, *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain* (London: J. Hatchard, 1802), 43-44; Thomas S. Ashton, "The bill of exchange and private banks in Lancashire, 1790–1830," *The Economic History Review* 15, no. 1/2 (1945); L. S. Pressnell, *Country Banking in the Industrial Revolution* (Oxford: Clarendon, 1956), 19-20; Nishimura, *The Decline of Inland Bills of Exchange*: 29; James S Coleman, "Introducing social structure into economic analysis," *The American Economic Review* 74, no. 2 (1984): 84.

became standard practice because the discount generated interest.[32] In theory, the size of the discount depended on the risk of default, prevailing rates of interest and the time it would take the bill to mature. In practice, the usury laws limited the rate of discount to the equivalent of five per cent per annum until 1833 whereupon bills with less than three months to maturity gained an exemption. Parliament extended that exemption to include bills with less than twelve months to maturity in 1837.[33] Anyone with money to spare could earn interest by discounting bills of exchange but banks discounted them more often than most. According to the London and Westminster Bank's general manager, James Gilbart, inland bills were "admirably adapted to the purposes of the bankers."[34]

One of a discounted bill's great advantages to a bank was that it matured on a pre-determined date to offer certainty as to when the bank would receive payment.[35] In addition, bills offered security. The identity of the bill's acceptor, its drawer and its endorsers mattered because some were more liable to default than others were. However, inland bills arose from commercial transactions undertaken by business people who depended on each other's solvency to stay in business. That reality offered safeguards. Reneging on a bill amounted to a public declaration of insolvency that most preferred not to make. In addition, those who drew or endorsed the bill generally often did so to purchase inventories. One could expect, but never

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[32] Thornton, *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain*: 27-29.

[33] 3 & 4 William IV c. 98; 1 Victoria c. 80; 2 & 3 Victoria c. 37; 4 & 5 Victoria, c. 54.

[34] James William Gilbart, *The History and Principles of Banking*, Third ed. (London: Longman, Rees, Orme, Brown, Green and Longman, 1837), 170; Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue with Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1841), 155.

[35] George Rae, "Letters to a branch manager: Overdrawn accounts," *The Bankers' Magazine and Journal of the Money Market* 1848, 470-71; George Rae, *The Internal Management of a Country Bank: In a Series of Letters on the Functions and Duties of a Branch Manager by Thomas Bullion* (London: R. Groombridge & Sons, 1850), 8-10; Henry Dunning Macleod, *The Elements of Banking* (London: Longmans, Greene and Co., 1876), 258-59.

demand, that someone liable for the bill would sell their inventories eventually to generate the funds needed to pay the holder in due course.[36] Finally, the number of parties liable for a bill increased every time it someone endorsed it. As Adam Smith noted, the probability that every one of them would become bankrupt before the bill matured was slight.[37]

A bank could do one of three things with the inland bills it discounted. The first was to realise the interest provided by the discount and hold it to maturity. Alternatively, the bank could forgo that interest by endorsing a bill in one of two ways. First, it could endorse the bill to make a payment to a customer, which put a bill carrying the bank's endorsement back into circulation. Reissuing a bill of exchange like this turned a substandard bill into a good one if the bank's credit was good.[38] Second, the bank could discount the bill again, a practice known as rediscounting, to generate funds. Rediscounting became an indispensable feature of English and Welsh banking practice.

Inland bills were not available to every bank in equal numbers. Industrial districts like Lancashire and Yorkshire's West Riding produced a large number of bills. Banks in these places faced heavy demand from local businesspeople to discount bills for them. Agriculture's need for credit was seasonal and agriculture districts tended not to produce bills in large numbers. A typical agricultural bank

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[36] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. Edwin Cannan, 6th ed., vol. I (London: Methuen & Co, 1950), 328-29; Thornton, *An Enquiry into the Nature and Effects of the Paper Credit*: 30-32; Gilbart, *The History and Principles of Banking*: 170-99; Macleod, *The Elements of Banking*: 260-62.
[37] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, I: 329.
[38] Mea Baker and Michael Collins, "English financial markets in the 1830s: Information networks, risk assessment and banking crisis," in *Monetary and Banking History: Essays in Honor of Forrest Capie*, ed. Geoffrey Woods, Terence C. Mills, and Nicholas Crafts (Abingdon: Routledge, 2011), 55.

confronted the relative absence of bills to discount. The result was an imbalance in the demand for and supply of credit. Industrial banks lacked the capacity to discount all the bills available to them. Agricultural banks could not discount enough bills to keep their resources fully employed.[39] What the banking industry needed was an intermediary that could utilise funds raised in agricultural districts to rediscount bills for the industrial banks. That intermediary emerged in the form of the London bill market.

Prior to 1825, English and Welsh industrial banks rediscounted their bills with its correspondent in London. These London banks funded their rediscounting by rediscounting the bills again with their agricultural correspondents or by accepting deposits from them at call. In addition, London's native bill brokers traded in inland bills. Bill brokers earned an interest return by rediscounting bills for industrial banks and financed their lending by rediscounting some of the bills acquired with the agricultural banks.[40] By 1825, London was a conduit through which funds collected in agricultural districts flowed into the industrial districts playing host to the Industrial Revolution. The nature and scale of the rediscounting undertaken in London changed dramatically after 1826. The 1825 financial crisis showed London's banking community that it could not rely on the Bank of England to rediscount bills for it in an emergency.[41] London's bankers decided inland bills of exchange made poor reserve assets under these circumstances and got out of the

[39] Thomas Joplin, *An Examination of the Report of the Joint Stock Bank Committee To Which is Added an Account of the Late Pressure in the Money Market and Embarrassment of the Northern and Central Bank of England*, Third ed. (London: James Ridgway, 1837), 114; James William Gilbart, *A Practical Treatise on Banking*, Fifth ed., vol. II (London: Longman, Brown, Green and Longmans, 1849), 556; Walter Bagehot, *Lombard Street: A Description of the Money Market* (London: Henry S. King & Company, 1873), 285.
[40] G. A. Fletcher, *The Discount Houses in London* (London: Macmillan, 1976), 6-8.
[41] King, *History of the London Discount Market*: 37.

rediscounting business.[42] Furthermore, the *Country Bankers Act* of 1826 gave rise to a new generation of country joint stock banks whose shareholders demanded their banks deploy their capital profitably. The volume of bills sent to London for rediscount increased as did the amount of funds sent there to rediscount them.[43] London's bill brokers responded by scaling-up their rediscounting activities, which they now financed by offering interest to any bank willing to lend at call to them.[44] Gilbart explained the process as follows:

> A bank in an agricultural district, say at Norwich, has a superabundance of money. A manufacturing town, say Manchester, has a demand for money. The bank at Norwich will send is money to a bill broker in London. The bank at Manchester will send its bills to the same broker ... [and a] ... rediscount takes place.[45]

The post-1826 bill market contained the risks associated with default on a bill. The bills rediscounted in London were comparatively safe to begin with, but the City's bill brokers made them safer by becoming adept at distinguishing a good bill from a bad one.[46] The result was a system of market exchanges that used funds raised in agricultural districts to sustain industrial lending at relatively low cost because the risk of default was low. As Coase would have predicted, the relatively low transaction costs imposed by these market exchanges ensured English and Welsh banks remained small.[47] In comparison, large banks were common in Scotland because the Scottish banks had a different relationship with their bills of exchange.

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[42] James William Gilbart and A. S. Michie, *The History, Principles and Practice of Banking*, vol. I (George Bell & Sons, 1896), 301.
[43] King, *History of the London Discount Market*: 42-50.
[44] Fletcher, *The Discount Houses in London*: 8-14; King, *History of the London Discount Market*: 39-50.
[45] Gilbart, *A Practical Treatise on Banking*, II: 556. A Birmingham private banker expressed similar sentiments before the 1841 Select Committee on Banks of Issue. See: Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue with Minutes of Evidence, Appendix and Index*: 155.
[46] Bagehot, *Lombard Street*: 288-92.
[47] Gilbart, *A Practical Treatise on Banking*, II: 556.

Scottish banks generally held the bills of exchange they discounted to maturity.[48] In 1838, an officer of the Western Bank of Scotland expressed his horror at the English and Welsh reliance on rediscounting in the following manner:

> It is hardly possible to imagine a system better calculated ... to bring joint stock banking into discredit with the public. In this way banks ... are made dependent on the Jews and bill brokers of London; and the fate of the Northern and Central Bank of England is a notable and instructive example of the slender reliance which can be placed on such resources, when a monetary crisis arises.[49]

Scottish banks did not did not need to rediscount because they possessed large branch networks that encompassed agricultural and industrial districts. Scottish banks allocated Scotland's savings administratively.

SCOTLAND'S ADMINISTRATIVE ALTERNATIVE

One problem with rediscounted bills of exchange as far as the Scots were concerned was that every bill rediscounted in London carried the bank's endorsement. Rediscounting exposed a bank to risk because its endorsement added the bank to list of parties liable for the bill if the acceptor defaulted.[50] More importantly, a financial crisis usually put London's bill market under stress because industrial banks would send bills to London in greater numbers to raise the funds needed to stay afloat at precisely the same moment the agricultural banks withdrew the funds they sent to London to meet their obligations.[51] Overreliance on rediscounting during a financial

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[48] Joseph Macardy, *Outlines of Banks, Banking and Currency* (London: H. & A. Macardy & Company, 1842), 133; Henry Dunning Macleod, *The Theory and Practice of Banking*, 4th ed., vol. II (London: Longmans, Green, Reader and Dyer, 1886), 393.

[49] Robert Bell, *Letter to James William Gilbart, Esquire, Manager of the London and Westminster Bank: On the Relative Merits of the English and Scotch Banking Systems With Practical Suggestions for the Consolidation of the English Joint-Stock Banking Interest* (Edinburgh: Bell & Bradfute, 1838), 12. As the last chapter explained, the Northern and Central Bank of England failed in 1836

[50] Anonymous, *How to Mismanage a Bank: A Review of the Western Bank of Scotland* (Edinburgh: John & Charles Black and John Maclaren, 1859), 14-15.

[51] Bagehot, *Lombard Street*: 292-95; Fletcher, *The Discount Houses in London*: 105; Denis Patrick O'Brien, "The lender-of-last-resort concept in Britain," *History of Political Economy* 35, no. 1 (2003).

crisis was something the Scottish banks preferred to avoid. In 1838, the Bank of Scotland and the British Linen Company told the Board of Trade:

> The safeguard of the Scotch system has been the uniform practice adopted of retaining a large proportion of capital and deposits invested in government securities, capable of being converted into money, at all times and under all circumstances. This requires sacrifice, because the rate of interest is small, and, in times of difficulty, the sale involves a loss, but it has given the Scotch banks absolute security, and enabled them to pass unhurt through periods of great discredit.[52]

Scottish banks sustained their reluctance to rediscount bills of exchange because they maintained branches at far greater distances from their head offices than the English Welsh banks did. As Gilbart noted, a Scottish branch network encompassed agricultural and industrial districts, which alleviated the need to rediscount. He observed:

> The system of numerous branches enables the banks of Scotland to transfer the surplus capital of the agricultural districts to the manufacturing and commercial districts, without going through the process of rediscounting their bills. ...A bank at Edinburgh will have branches in both the agricultural and the manufacturing districts…. [A] bank whose head office is in a manufacturing town, will have branches in the agricultural districts. Thus, the surplus funds of Perth, Ayr, and Dumfries are speedily transferred to ... Glasgow, Paisley, and Dundee. Were a bank to be established at Glasgow without branches, it would probably have occasion for [re]discount … [as do] … the banks at Manchester or Leeds.[53]

Vincent Stuckey, made a similar point in 1841 before the Select Committee on banks of Issue. Stuckey's Bank was one of the few in England and Wales to possess a agricultural and industrial branches. Stuckey's Bank did not have to send funds to London because it took "as many bills of exchange as we wish to have … in our

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[52] Cited in: Macleod, *The Theory and Practice of Banking*, II: 222-23. See also: The Bankers' Magazine, "History of Banking in Scotland," *The Bankers' Magazine and Journal of the Money Market* 1877, 298.
[53] Gilbart, *A Practical Treatise on Banking*, II: 555-56.

manufacturing districts."[54] The Scottish reluctance to rediscount and the large branch networks that sustained it gave Scottish banks a degree of independence from London that facilitated another practice that was unique to Scotland. The Scottish banks offered what they called 'cash credits' to their clients generously.

First introduced by the Royal Bank of Scotland in 1728, a cash credit allowed the applicant to borrow up to a predetermined amount whenever he or she wished. In return, the applicant supplied two or more guarantors who would repay the debt incurred if the applicant defaulted. The Royal Bank of Scotland made a return on the funds lent by charging interest on any outstanding balance.[55] The Royal Bank of Scotland's initiative proved so effective at attracting business that the Bank of Scotland responded by offering them too in 1729.[56] After that, cash credits became a universal feature of the Scottish banking system.[57] David Hume praised cash credits as "one of the most ingenious ideas that has been executed in commerce."[58] Cash credits alleviated a Scottish business' need to invest in unproductive cash balances by allowing it to draw on its cash credit to make a payment, which put more of its resources to productive use.[59] Cash credits also offered the borrower flexibility. The

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[54] Select Committee on Banks of Issue, *Second Report From the Secret Committee on Banks of Issue*: 58.

[55] James William Gilbart, *The History and Principles of Banking* (London: Longman, Rees, Orme, Brown, Green and Longman, 1834), 173-75; S. G. Checkland, *Scottish Banking: A History, 1605-1973* (Glasgow: Collins, 1975), 63.

[56] Checkland, *Scottish Banking*: 67.

[57] James William Gilbart, *A Practical Treatise on Banking*, Second ed. (London: Effingham Wilson, 1828), 70, 77-83; William John Lawson, *The History of Banking: With a Comprehensive Account of the Progress of the Banks of England, Ireland and Scotland* (London: Richard Bentley, 1850), 420-21; Macleod, *The Elements of Banking*: 159-60.

[58] David Hume, "Of the balance of trade," in *The Gold Standard in Theory and History* ed. Barry J. Eichengreen and Marc Flandreau (London: Routledge, 1997), 28.

[59] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, I: 317-18; Gilbart, *The History and Principles of Banking*: 173-75; Macleod, *The Elements of Banking*: 160; Hume, "Of the balance of trade," 28.

borrower determined when he or she repaid the debt whereas the acceptor of a bill of exchange had to make the payment on a predetermined date.[60]

Cash credits were less well adapted to a bank's needs than inland bills of exchange because the former imposed uncertainties onto the banks granting them. The bank could not predict with accuracy when the borrower would make a withdrawal or a repayment on a cash credit. For that reason, Adam Smith speculated the Royal Bank of Scotland and the Bank of Scotland only resorted to cash credits in the first place because Scotland's pre-industrial economy failed to produce enough bills of exchange to keep their capital fully employed.[61] English and Welsh bankers distrusted overdrafts (the closest equivalent they offered to a cash credit) because the bank granting them relinquished control over its lending. In addition, overdrafts were not negotiable, which meant a bank could not sell them to generate cash when it needed to. In 1848, the North and South Wales Bank's George Rae compared lending on discounted bills to lending on overdrafts in the following terms:

> The safety of one particular account is one thing, the safety of the bank is quite another.... An ordinary drain upon a bank whose business was chiefly confined to the discount of legitimate business bills, could be met by simply contracting the volume of its discounts; but you do not necessarily diminish your existing overdrafts a single pound by refusing to grant fresh ones, or if the drain were too sudden and heavy to be met by the mere contraction of the discounts of the bank, a portion of its bills on hand might conceivably be converted into cash. In the worst times ... good bills could be rediscounted at a price.[62]

Mainland Britain played host to two alternative banking philosophies prior to 1870. In Scotland, large banks used their branch networks to allocated funds administratively, held onto their bills of exchange until maturity, maintained reserves

[60] Macleod, *The Elements of Banking*: 163.
[61] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, I: 316.
[62] Rae, "Letters to a branch manager: Overdrawn accounts," 470.

of liquid assets capable of conversion into cash at short notice to see them through a financial crisis and offered cash credits generously. In England and Wales, smaller banks operated amidst a market-based system that depended upon rediscounting to sustain them. Consequently, the English and Welsh banks offered overdrafts sparingly. The English and Welsh banks paid a heavy price for their dependency on a bill market that was liable to run short of cash during a financial crisis. The English and Welsh predilection for rediscounting contributed to financial crises in 1837-39, 1847 and 1857 by putting the banks that engaged in it at greater risk.[63] The fundamental problem was that someone or something other than the banks had to make good any shortfall of funds available in London during a financial crisis or a system based on market exchanges would collapse.[64] The bill market needed a lender of last resort. A reluctant Bank of England accepted that responsibility between 1830 and 1858.

REDISCOUNTING, FINANCIAL CRISES AND THE BANK OF ENGLAND

The Bank of England maintained a bill discounting business of its own although it preferred to discount the safest bills with the shortest terms to maturity and only accommodated those who met with its approval. Banks surrendering their right to issue bank notes received generous discounting privileges from the Bank of England in the 1830s.[65] The Bank of England refused to discount a bill bearing a joint stock bank of issue's endorsement in 1836.[66] However, London's bill market received a

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[63] Nicholas Dimsdale and Anthony Hotson, "Financial crises and economic activity in the UK since 1825," in *British Financial Crises Since 1825*, ed. Nicholas Dimsdale and Anthony Hotson (Oxford: Oxford University Press, 2014).
[64] Bagehot, *Lombard Street*: 292-95; Fletcher, *The Discount Houses in London*: 105; O'Brien, "The lender-of-last-resort concept in Britain."
[65] Lawson, *The History of Banking*: 126-27.
[66] Joplin, *An Examination of the Report of the Joint Stock Bank Committee*: 115-16.

boost in 1830 when the Bank of England added a number of the City's bill brokers to the list of those who could discount with it.[67] By 1841, Thomas Tooke was telling the Select Committee on Banks of Issue, "The Bank [of England] are looked to as a constant resource by the great discount brokers" and added "it would have a prodigious effect if there were to be any forcible narrowing of discounts [by the Bank of England]."[68] The London bill market now depended upon the Bank of England to carry it through a crisis.

The government suspended the *Bank Charter Act* during financial crises in 1847 and 1857, which gave the Bank of England the freedom to put as many bank notes into circulation as were needed to accommodate the banks' and the bill market's demand for liquidity.[69] These experiences convinced the Bank of England that the London bill market and the banks that depended on it had become overly reliant on its facilities. In 1858, the Bank of England announced that it would no longer discount bills for London's bill brokers. The intention was to promote financial stability. The Bank of England hoped London's bill brokers would commit more of their resources to liquid assets so they could weather the next financial storm without its help.[70] The Bank of England soon discovered it had fired the first shot in a war

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[67] King, *History of the London Discount Market*: 50-55, 88-91.

[68] Select Committee on Banks of Issue, *Report from the Secret Committee on Banks of Issue with Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1840), 364; Thomas Tooke, *A History of Prices and of the State of the Circulation from 1839 to 1847 Inclusive: With a General Review of the Currency Question and Remarks on the Act of 7 & 8 Vict. c. 32* (London: Longman, Brown, Green and Longmans, 1848), 493.

[69] Select Committee on the Bank Acts, *Report from the Select Committee on the Bank Acts; Together with the Proceedings of the Committee, Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1858), viii-xi; Stafford H. Northcote, *Twenty Years of Financial Policy* (London: Saunders, Otley and Company, 1862), 99-98, 331-32; A. Andréadès, *A History of the Bank of England, 1640-1904*, 4th ed. (London: Frank Cass & Co., 1966), 350.

[70] Ellis T. Powell, *The Evolution of the Money Market (1385-1915)* (London: The Financial News, 1915), 383-83.

with London's bill market.[71] An exchange of pamphlets occurred in 1860 debating the relative merits of the Bank of England's new policy.[72] The war of words escalated in April 1860 when the largest bill broker in London took retaliatory action against the Bank of England.[73] Overend and Gurney and its associates withdrew £1,650,000 in bank notes from the Bank of England in a single day. Overend and Gurney timed the action to perfection. The Bank had to curtail its lending to keep its bank note issue within the limits imposed on it by the *Bank Charter Act*. Having made a point, Overend and Gurney returned the bank notes withdrawn. Six years later, the Bank of England took its revenge upon Overend and Gurney.

Overend and Gurney failed in 1866 after coming under the control of a new generation of proprietors who breached one of the cardinal rules of the bill discounting business.[74] The new owners invested in railway securities and other long-term investments that would generate returns slowly and prove difficult to sell in an emergency even though most of their liabilities were payable at call. Eventually, the new policy demanded an injection of cash to sustain it. In July 1865, Overend and Gurney's proprietors took the radical step of incorporating their business as a

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[71] John Giuseppi, *The Bank of England: A History from its Foundation in 1694* (London: Evans Brothers, 1966), 119-21.

[72] A. B. C., *The Bank of England and the Discount Houses* (London: Richardson Brothers, 1860); X., *The Grievance of the Discount Houses* (London: Effingham Wilson, 1860); A. B. C., *The Bank of England and Discount Houses: A Reply to "X"* (London: Richardson Brothers, 1860).

[73] "The Bank of England and discounters," *The Times*, 23 April 1860; King, *History of the London Discount Market*: 212-16.

[74] For an account of the Overend and Gurney failure see: "The panic," *The Times*, 12 May 1866; "The panic," *The Times*, 14 May 1866; "The suspension of the Bank Charter Act," *The Times*, 14 May 1866; "Money-market and City intelligence," *The Times*, 14 May 1866; The Economist, "The Panic (Article published 19 May 1866)," in *Select Statutes, Documents & Reports Relating to British Banking, 1838-1928*, ed. T. E. Gregory (London: Oxford Univeristy Press, 1929); Stefanos Xenos, *Depredations: Or, Overend, Gurney & Company and the Greek & Oriental Steam Navigation Company* (London: Stefanos Xenos, 1869); W. F. Finlason, *A Report on the Case of The Queen v. Gurney and Others* (London: Stevens and Haynes, 1870); Geoffrey Elliot, *The Mystery of Overend and Gurney: A Financial Scandal in Victorian London* (London: Methuen, 2007); Marc Flandreau and Stafani Ugolini, "The crisis of 1866," in *British Financial Crises Since 1825*, ed. Nicholas Dimsdale and Anthony Hotson (Oxford: Oxford University Press, 2014).

limited liability company and sold shares to the public. Unfortunately, the move proved inadequate to stave off disaster. In May 1866, Overend and Gurney's share price collapsed after word of its unresolved cash flow problems reached the public, which prompted a run against Overend and Gurney. Overend and Gurney appealed to the Bank of England for assistance but to no avail. On 10 May 1866, Overend and Gurney suspended payments. The impending collapse of what *The Times* called "the greatest instrument for credit in kingdom" provoked a widespread financial panic.[75] On Black Friday (11 May 1866), a crowd besieged Lombard Street whilst a run on the country banks developed in the provinces. The Bank of England stepped into the breach by meeting demands for accommodation from those who offered good security although doing so induced a rise in the rates of interest charged. The government suspended the *Bank Charter Act* for the third and final time.

The failure of Overend and Gurney on Black Friday was a watershed event for the English and Welsh trade in inland bills of exchange. The number of inland bills sent to London for rediscount went into decline soon afterwards, as did the number of bills drawn and discounted in the provinces. The small banks of provincial England and Wales were about to lose the market exchanges that sustained their operations.

THE DECLINING MARKET FOR INLAND BILLS

The financial crises of 1857 and 1866 put any bank deemed over reliant on London's bill market into disrepute. Rediscounting became a practice utilised by what one

[75] "The shock which agitated the city of London yesterday afternoon," *The Times*, 11 May 1866.

banking historian called a "second-rate bank."[76] William Fowler (1828-1905), a financier and parliamentarian, told the Institute of Bankers in 1891:

> After the panic of 1857 was over, I remember particularly well there was a great change in the management of the banks all over England, and I know it in this way: The great business of our house about 1857 was re-discounting for country banks. That business rapidly reduced after 1857 because banks felt the imprudence of having such a mass of bills that they could not hold themselves, and therefore they kept more money in London than they previously had.... But the process went on far more rapidly after 1866.... Those lessons have never been forgotten and the great banks that were large [re-]discounters in 1866 are now large depositors in London.[77]

The industrial banks' did not stop rediscounting overnight. They were too reliant on the practice to do that. Instead, industrial bank sent fewer bills to London as time progressed although the dependency on rediscounting persisted in some places. As late as 1885, George Rae's *The Country Banker* continued to express its author's conviction that rediscounting remained a legitimate practice for banks "placed in districts of great industrial activity where deposit money is scarce and the demand for loan capital is great."[78] However, rediscounting entailed risks that many banks now preferred to avoid. Black Friday demonstrated that inland bills of exchange could be unreliable reserve assets in times of crisis.[79]

London's bill brokers traded in other securities to keep their resources occupied as the number of inland bills of exchange sent to them for rediscount declined. The number of foreign bills available in London for discount increased because of an

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[76] King, *History of the London Discount Market*: 271.

[77] Cited in King, *History of the London Discount Market*: 271-71; Nishimura, *The Decline of Inland Bills of Exchange*: 44. Fowler joined Alexander & Company (one of London's three biggest discount houses) in the 1850s.

[78] George Rae, *The Country Banker: His Clients, Cares and Work*, 4th ed. (London: John Murray, 1885), 219.

[79] Nishimura, *The Decline of Inland Bills of Exchange*: 57.

expansion in global trade.[80] In addition, the *Treasury Bills Act* of 1877 introduced a new short-term government security known as the Treasury Bill.[81] Treasury Bills resembled bills of exchange by changing hands at a discount to generate interest.[82] An increase in deposits (see Chapter Three) also contributed to the decline in number of inland bills sent to London by making industrial banks less reliant on rediscounting to fund their operations. By the 1870s, an average Lancashire bank could finance its lending out of its own resources for the first time because it collected more on deposits than it lent.[83] In 1875, Rae boasted that Liverpool's banks now possessed "a great deal more [money] than we can employ at home," which made them "very large lenders in the London market."[84] Inland bills of exchange became so scarce in London that the City's bill brokers had to appoint provincial agents to chase them down on their home turf.[85]

We will never know the number bills of exchange drawn in the provinces or discounted by industrial banks during the last decades of the nineteenth century. Those involved in these activities generally did not record these quantities with the intention of communicating them to the outside world. However, estimates based on the amount of stamp duty paid for them suggest that the stock of inland bills drawn and hence available to the industrial banks for discount also went into decline after

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[80] King, *History of the London Discount Market*: 269-82; Dimsdale and Hotson, "Financial crises and economic activity in the UK," 41-43.
[81] 40 & 41 Victoria c. 2.
[82] King, *History of the London Discount Market*: 275-78; R. S. Sayers, *The Gilletts in the London Money Market* (Oxford: Clarendon Press, 1968), 50-51.
[83] Nishimura, *The Decline of Inland Bills of Exchange*: 106-08.
[84] Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue; Together with Proceedings of the Committee, Minutes of Evidence and Appendix* (London: Parliament of the United Kingdom (House of Commons), 1875), 260.
[85] See the evidence of George Rae and John Dunn in Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 264, 325.

1870.[86] Significantly, a change in the English and Welsh banks' lending practices contributed to that decline. English and Welsh banks overcame their reluctance to offer overdrafts.

English and Welsh overdrafts were similar to Scottish cash credits in most respects but one. Those who borrowed on overdraft offered the bank security but did not rely on guarantors to do it.[87] Overdrafts accorded an English or Welsh borrower all the advantages of Scottish cash credits because the borrower could draw on it and repay it at their convenience. In addition, an overdraft gave the borrower access to coins, bank notes, cheques and telegraphic transfers to make a payment. The capacity to make immediate payment gave borrowers bargaining power when they made a purchase. The borrower did not have to offer the seller compensation for a delay in payment as would have been the case if they had utilised a bill of exchange. Consequently, overdrafts bestowed the capacity to negotiate cash discounts that offset some of the interest expense incurred on the funds borrowed.[88] English and Welsh borrowers had good reasons to prefer overdrafts to bills of exchange as a source of credit. The problem they faced was persuading their banks to give up their preference for lending on bills of exchange. However, the English and Welsh banks' attitude towards overdrafts softened during the latter decades of the nineteenth century. The result was an increase in the proportion of cash payments made with a consequent decline in the number of bills of exchange drawn. A text originally published in 1891 carrying the endorsement of the Institute of Bankers observed:

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[86] Nishimura, *The Decline of Inland Bills of Exchange*: 11-25.
[87] Charles Albert Eric Goodhart, *The Business of Banking, 1891-1914* (London: Weidenfeld and Nicolson, 1972), 153.
[88] Nishimura, *The Decline of Inland Bills of Exchange*: 55.

> The conditions under which business is carried out … is gradually changing. There is reason to believe that each year more and more transactions are conducted on a cash-basis, and that the number of bills created now bears a steadily diminishing ratio of the volume of commerce. Instead of settling by bill, a growing preference appears to be shown for payment by cheque or cable-transfer…. Scarcity of bills … is substantiated by the fact that bankers now hold fewer bills in proportion to other assets than was the case in former years.[89]

The increase in cash payments sent the number of inland bills of exchange drawn into decline after 1870.[90] The result was a decline in the number of bills of exchange available to the English and Welsh banks.

The move away from bills of exchange towards overdraft lending and cash payments coincided with the English and Welsh Amalgamation Movement. Both events began around 1870. It is tempting to impute a causal relationship between the two events given their temporal proximity. In the 1930s, W. T. C. King did precisely that when he argued:

> By far the most important of these new influences [on the increase in cash payments] was the bank amalgamation movement, bringing with it a great expansion of branch banking, and enabling many banks each to perform within its own organisation the 'equalising' function for which the bill market had previously been indispensable…. This development, by enabling the bigger banks to finance from the deposits of their 'agricultural' branches the demands of their 'industrial' branches removed one of the principle reasons for the use of the bill as the standard instrument of accommodation. From many points of view, it became a matter of indifference to the banks whether they financed their customers by discounting bills for them or by granting loans and advances, and to the customers the flexibility of the overdraft system had definite attractions. Thus, the spread of branch banks was accompanied in many trades by a gradual displacement of the internal bill by the 'open credit' system as the standard means of finance.[91]

Similarly, W. M. Scammell asserted in 1968:

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[89] George Clare, *A Money-Market Primer, and Key to the Exchanges. With Diagrams*, Second ed. (London: Effingham Wilson, 1902), 137-38. The 'other assets' referred to include overdrafts and advances.
[90] King, *History of the London Discount Market*: 273.
[91] King, *History of the London Discount Market*: 273.

> The main reason for this decline [in inland bills of exchange] lay in the changes taking place ... in the structure of the banking system. The old unitary [single office] banking system of the first part of the nineteenth century was giving way to a concentrated banking system working through a branch network. This made easy the transference of ... funds from district to district and enabled the old 'equalising function' performed by ... the practice of rediscounting, to be superseded. The overdraft loan became common as means of financing short-term trade credit and their use grew as a result of their flexibility and convenience.[92]

King's hypothesis was that the Amalgamation Movement created the branch networks needed to link industrial regions with agricultural ones. Bank amalgamations fostered an internal transfer of funds that changed the English and Welsh banks' lending practices. English and Welsh banks could now offer overdrafts liberally just as the Scottish banks offered cash credits because like the Scottish banks, the English and Welsh banks no longer needed to rediscount their bills of exchange to fund their operations. According to King, the Amalgamation Movement facilitated a growth in overdraft lending, which increased the number of cash payments made to force the number of inland bills drawn into terminal decline.

King's claim the Amalgamation Movement caused the demise of the inland bill became an often-repeated conventional wisdom until 1971 when Shizuya Nishimura identified two significant weaknesses that undermined its credibility.[93] First, bills were a far more convenient lending option than overdrafts for the banks. Both Gilbart and Rae asserted that a bank could constrict to lending on bills at will by simply refusing to discount them.[94] In addition, bills of exchange matured relatively quickly and a bank could rediscount them if the need arose. According to Nishimura, no bank would have been indifferent as to whether it lent on bills of exchange or

[92] W. M. Scammell, *The London Discount Market* (New York: Saint Martin's Press, 1968), 29.
[93] Nishimura, *The Decline of Inland Bills of Exchange*.
[94] Rae, "Letters to a branch manager," 470; Gilbart and Michie, *The History, Principles and Practice of Banking*, I: 190.

offered overdrafts. A change in the relative bargaining power of borrowers *vis-a-vis* the banks must have compelled the change in lending practices because the English and Welsh banks would not have welcomed the demise of the inland bill of exchange. The second weakness in the King hypothesis Nishimura identified related to a question of timing. The number of inland bills drawn in England and Wales started to decline in the 1870s; and yet, the Amalgamation Movement failed to produce the truly national branch networks needed to connect agricultural and industrial districts until the 1890s. Nishimura argued the demise of the inland bill could not have preceded its alleged cause by two decades. Nishimura cited the following example to make this point:

> Banks in Lancashire and Yorkshire kept comparatively aloof from the bank amalgamation movement. Since it was from Lancashire and the West Riding of Yorkshire that the greater part of inland bills were sent to London…, the linking of Lancashire and West Riding banks with those in 'agricultural' areas would have been necessary for the use of inland bills as a means of the transfer of money to have effectively discontinued. Nothing of the sort happened save in one case, that of the amalgamation of Parr's Bank, originally of Warrington in Lancashire, with Stuckey's Banking Company in Somerset. This fusion is an ideal case for King's hypothesis, but ... this occurred in 1909, much later than the decline of inland bills.[95]

According to Nishimura, the Amalgamation Movement had not caused the increase in overdraft lending and cash payments. The Amalgamation Movement may have proceeded in parallel with the demise of the inland bill but the two developments were unrelated.

This thesis argues Nishimura was right to claim the decline in the inland bill preceded the national branch networks needed to account for it. However, Nishimura was wrong to dismiss the notion that a causal relationship linked the Amalgamation

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[95] Nishimura, *The Decline of Inland Bills of Exchange*: 9-10.

Movement and the inland bill's decline. The intention is not to resurrect King's hypothesis. The Amalgamation Movement did not cause the decline of the inland bill. Instead, the decline of the inland bill turned participation in the Amalgamation Movement into a necessity. As Coase would have predicted, the loss of a means of market exchanges that imposed low transaction costs created the need for an administrative alternative to allocate the English and Welsh banking system's resources. The demise of the inland bill of exchange was a cause of the Amalgamation Movement because it necessitated an increase in average English and Welsh bank size to access the reserves needed to survive a financial crisis.

BANK RESERVES AND THE AMALGAMATION MOVEMENT

Nishimura ascribed the demise of the inland bill to two causes.[96] The first was the increase in deposits alluded to earlier that put an end to the industrial banks' dependency on rediscounting. This first cause was a necessary precondition for the rise in cash payments because without it, industrial banks would have continued to rediscount and could not have funded the overdrafts they offered. The second was suppressed demand for industrial credit brought about by the late nineteenth-century Great Depression and improvements in transport and communications that reduced the need to hold inventories to act as a buffer against uncertainty. This second development forced the banks to offer overdrafts to stimulate their lending, which set up a vicious circle. More overdrafts increased the number of cash payments made, which reduced the number of bills drawn, which forced banks to offer more overdrafts to compensate until finally cash payments predominated and the number of bills of exchange drawn and made available for discount became insignificant.

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[96] Nishimura, *The Decline of Inland Bills of Exchange*: 44-54, 55-64, 78-79.

If Nishimura was right to ascribe the demise of the inland bill to an increase in deposits coupled with suppressed demand for industrial credit, then one might ask why industrial banks bothered to participate in the Amalgamation Movement. Industrial banks had no need to join forces with banks in agricultural districts if their growing deposits financed their lending. Nishimura based his analysis on the ratio of reported bank lending to deposits, which provided him with an indicator of a region's capacity to sustain its lending from local sources.[97] As one would expect, the ratios of lending to deposits were highest in the industrial districts and lowest in agricultural districts and in London where most of the banking system's reserves resided. In 1870, London's joint stock banks and their agricultural counterparts maintained lending to deposit ratios below 80 per cent whereas the ratios in Lancashire, Yorkshire, Northumberland, Country Durham, Derbyshire, Nottinghamshire, Staffordshire, Worcestershire and Warwickshire all exceeded 100 per cent. These ratios fell across the whole of England and Wales after 1870. By 1895, London and the agricultural districts reported lending to deposit ratios below 60 per cent whilst the ratios in the industrial regions ranged from a low of 64.9 per cent for Derbyshire, Nottinghamshire, Staffordshire, Worcestershire and Warwickshire to a high of 82.1 per cent in Yorkshire's woollen and worsted districts. The industrial banks of England and Wales did not need amalgamation partners to fund their lending under these circumstances. Industrial banks funded own their lending out of their deposits at the height of the Amalgamation Movement.

[97] Nishimura, *The Decline of Inland Bills of Exchange*: 104-09.

Nishimura's analysis failed to explore how the banks responded to an ever-decreasing proportion of discounted bills of exchange held as their overdraft lending grew. The ratio of lending to deposits fell across the board, which forced some banks to reassess their attitude to risky lending opportunities that bankers traditionally avoided. Banks preferred not to invest in or lend against stocks as shares, for example, because finding buyers for them in times of financial distress would incur a significant loss.[98] In 1879, a work carrying the title *Banking Reform: An Essay on Prominent Banking Dangers and the Remedies they Demand* observed that the English and Welsh banks' exposure to securities listed on the stock exchanges was rising. The author attributed this development to the declining availability of inland bills of exchange and the growth in deposits taken.[99] The text's author argued:

> It is not … prudent banking to lock up in ... stock exchange securities any portion of money which is liable to be called up by its owners. That money ought to be in bills, in securities which represent commodities continually changing hands and undergoing realisation, securities which are therefore continually bringing the money back again into the banker's hands. If through a dearth of these, or from any other cause, a banker buys interest-bearing stock to large amounts, or lends money on such stock pawned with him as security, he at once places himself in a position of having to face indefinite losses in the event of a forced realisation.[100]

Cashed-up banks were struggling to find suitable outlets to keep their funds fully employed because of the decline in the number of bills of exchange drawn and discounted.

Some banks may have started to invest imprudently to compensate for the decline in the inland bill of exchange but others faced problems of a different kind.

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[98] Rae, *The Country Banker*: 102; Michael Collins, "English bank lending and the financial crisis of the 1870s," *Business History* 32, no. 2 (1990).

[99] Alexander Johnstone Wilson, *Banking Reform: An Essay on Prominent Banking Dangers and the Remedies they Demand* (London: Longmans, Green & Company, 1879), 25.

[100] Wilson, *Banking Reform*: 35.

Banks no longer sent bills of exchange to London as frequency as they had done in the past, but sending them there in an emergency remained an option when the need arose. In addition, bills matured comparatively quickly to furnish funds at relatively short notice.[101] Inland bills of exchange remained an inherently liquid form of lending that could generate cash at short notice. However, the proportion of bills of exchange discounted relative to the amounts lent on overdrafts declined after 1870. An examination of two banks' balance sheets (one urban the other rural) presented in *Banking Reform: An Essay on Prominent Banking Dangers and the Remedies they Demand* formed the basis of a startling observation:

> In 1873, the cash and bills of these two banks amounted to 73 per cent of the liabilities to the public, but at the end of ... [1877], they were equal to about 43½ per cent. These banks have therefore locked up their capital and available assets to an enormous extent in advances … [and overdrafts] … which may or may not be realisable.[102]

The essay's author warned these two banks typified many in England and Wales that would struggle to raise the liquidity needed to survive the next financial crisis if the proportion of cash and bills relative to advances and overdrafts continued to fall. He concluded his depiction of a banking industry struggling to adapt to the early stages of the inland bill's demise as follows:

> The supplies of real cash kept in hand by bankers have been dwindling ... at the same time the floating balance available for discount purposes has been almost valueless. Banks are drifting towards catastrophe, one may almost say without being aware of it. They have striven to make high profits in dull times and in channels not safe for bankers, and they have succeeded, but at a cost which only those who survive the next credit storm will be able to estimate.

The warning that the banking system was heading for a liquidity-induced catastrophe because of the loss of the inland bill of exchange mirrored concerns

[101] See for example the evidence of William Gordon in Select Committee on Banks of Issue, *Report of the Select Committee on Banks of Issue*: 202; Wilson, *Banking Reform*: 32-33.
[102] Wilson, *Banking Reform*: 32-33.

expressed elsewhere by those who recalled Black Friday with horror. In 1873, Walter Bagehot's *Lombard Street* called upon the Bank of England to embrace the role of lender of last resort wholeheartedly and without hesitation.[103] Bagehot argued the Bank of England should step into the breach at the first sign of financial distress and follow two rules.

> First ... loans should only be made at a very high rate of interest. This will operate as a heavy fine ... and will prevent the greatest number of applications by persons who do not require it. The rate should be raised early in the panic, so that ... no one may borrow out of idle precaution without paying well for it....
>
> Secondly ... these advances should be made on all good banking securities.... The reason is plain. The object is to stay alarm, and nothing therefore should be done to cause alarm. But the way to cause alarm is to refuse someone who has good security to offer.... If it is known that the Bank of England is freely advancing on what in ordinary times is reckoned a good security ... the alarm of the solvent ... will be stayed. But if securities, really good and usually convertible, are refused by the Bank, the alarm will not abate ... and the panic will become worse and worse.[104]

Bagehot's prescription constituted no act of charity on the Bank of England's behalf. Bagehot's recommendation would deny assistance to the opportunistic and the insolvent by charging them high rates of interest and demanding they furnish good security for the amounts they borrowed.[105] Nevertheless, his advice would make the Bank of England the ultimate guarantor of the banking system's liquidity in an emergency. Whether the Bank of England could or even should follow Bagehot's advice remained open to question.[106] In 1881, *The Times* warned Bagehot asked too much the Bank of England:

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[103] Bagehot, *Lombard Street*.
[104] Bagehot, *Lombard Street*: 197-98.
[105] Charles Albert Eric Goodhart, "Myths about the lender of last resort," *International Finance* 2, no. 3 (1999).
[106] W. D. Henderson, "English Banking," *Macmillan's Magazine* 32, no. 1 (1875): 144-46; Arthur Stanley Cobb, *Bankers' Cash Reserves: Threadneedle Street, a Reply to Lombard Street* (London: Effingham Wilson and Company, 1891).

> For many years the necessity of a cash reserve somewhere has been acknowledged by bankers, and especially by the leading bank in this country, the Bank of England; and since Mr Bagehot's 'Lombard Street' the recognition of this necessity has become an accepted part of banking theory.... But there is a peculiarity in our market and in this lies both the secret of the actual weakness of our reserve and the unwillingness of the leading … banks to accept their responsibility … [because] … our leading banks make themselves virtually dependant on the Bank of England…. The Bank of England ... cannot keep a sufficient reserve for the wants of our banking system.... Let the leading banks meet together, agree how to keep a cash reserve for themselves and put an end to their present unworthy and unsatisfactory dependence on … the Bank of England.[107]

English and Welsh banks were under pressure to maintain greater reserves of liquidity. The loss of an inherently liquid asset like the inland bill of exchange would have exasperated the need for greater liquidity.

The scale of the banking industry's latent liquidity problem became apparent in 1878/79 after the City of Glasgow Bank collapsed in October in 1878 and the West of England and South Wales District Bank failed in December of the same year. Michael Collins indicated that banks located in industrial districts, where the difference between the amounts they collected on deposits and the amounts they lent left the smallest margins for error, proved most vulnerable.[108] In Leeds, the Yorkshire Banking Company lost 28 per cent of its deposits and its bank note issue contracted by 16 per cent between June 1878 and June 1879. The bank only survived the run by curtailing its lending, rediscounting bills of exchange and borrowing from its London correspondent and the Bank of England. Similarly, the

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[107] "Bank reserves," *The Times*, 1 December 1881.

[108] Michael Collins, "The banking crisis of 1878," *The Economic History Review* New Series 42, no. 4 (1989). See also: William P. Kennedy, "Institutional response to economic growth, capital markets in Britain to 1914," in *Management Strategy and Business Development*, ed. Leslie Hannah (London: Macmillan, 1976); William P. Kennedy, *Industrial Structure, Capital Markets, and the Origins of British Economic Decline* (Cambridge: Cambridge University Press, 1987); Dieter Ziegler, "The banking crisis of 1878: Some remarks," *The Economic History Review* New Series 45, no. 1 (1992).

North and South Wales Bank reduced its lending by 29 per cent between June 1878 and June 1879 and borrowed from its London correspondent to accommodate the contraction in its deposits.[109] Many banks in the industrial North and the Midlands suffered because they lacked the cash reserves needed to absorb the shock to the banking system.[110] These banks survived by reducing their lending and/or borrowing the funds they needed to meet their obligations at a time when the banking system as a whole came perilously close to succumbing to another general panic.[111]

What the English and Welsh banking system needed was a substitute for the inland bill of exchange, one that made the liquidity accumulated in agricultural districts subject to low demand for credit available to those in the industrial districts where the demand for credit was high it to meet their obligations in an emergency. Achieving that outcome entailed taking one of two courses of action. Either the English and Welsh banks created another system of market exchanges to replace the trade in inland bills of exchange or they adopted the Scottish administrate solution and erected geographically dispersed branch networks instead. Creating a market-based alternative to the market for inland bills of exchange would have presented insurmountable problems. Inland bills of exchange were essentially other people's debts. Banks only became liable for the bills of exchange they rediscounted if the bills' acceptors, drawers and other endorsers defaulted.[112] A poorly managed bank might collapse under these circumstances and the bills of exchange it rediscounted in

[109] Collins, "The banking crisis of 1878," 510-13.
[110] Ziegler, "The banking crisis of 1878: Some remarks," 143.
[111] R. S. Sayers, *Lloyds Bank in the History of English Banking* (Oxford: Clarendon Press, 1957), 211-12.
[112] Michael Collins, *Money and Banking in the UK: A History* (Abingdon: Routledge, 2012), 97-98.

London would still mature if the bills were good. The loss of the bill of exchange meant that banks would now have to lend to each other directly to engage in market exchanges. A poorly managed bank could impose significant loss on those who lent to it if it failed, which meant those lending to it would have to protect their interests somehow. Lenders could demand high rates of interest to compensate for the risks involved, impose contractual clauses designed to protect the lender's interests and monitor the compliance with them or demand the borrower furnish collateral the lender could sell if the borrower defaulted.[113] Consequently, a system of market exchanges based on inter-bank lending would have imposed transaction costs that the trade in inland bills avoided. An active market based on direct inter-bank lending never emerged even though one banker identified a need for one to avoid the commissions charged by London's bill brokers as early as 1840.[114]

The English and Welsh banks did lend funds to each other on occasion. Country banks maintained deposits with their London correspondents for example. These London banks even allowed their country correspondents to run up overdrafts with them although the London banks generally frowned upon those who failed to furnish adequate security to cover their debts.[115] Nevertheless, the scale of the inter-bank lending involved ultimately proved insufficient to resolve the industry's liquidity problems. The English and Welsh banks adopted an administrative solution to compensate for the demise of the inland bill of exchange.

[113] Myron Scholes, George J. Benston, and Clifford W. Smith, "A transactions cost approach to the theory of financial intermediation," *The Journal of Finance* 31, no. 2 (1976): 221.
[114] Gavin Mason Bell, *The Philosophy of Joint Stock Banking* (London: Longman, Orme, Brown, Green and Longmans, 1840), 58.
[115] Goodhart, *The Business of Banking*: 30-33, 154-55.

THE ENGLISH AND WELSH ADMINISTRATIVE SOLUTION

The Spectator noted in 1918 that the English and Welsh Amalgamation Movement proceeded geographically. Banks sought amalgamation partners to obtain a foothold in neighbouring districts until finally the largest of them occupied the whole of England and Wales.[116] The Treasury Committee on Bank Amalgamations made a similar observation in the same year.[117] Banks located in agricultural and industrial districts joined forces with each other and with banks domiciled in London until they created the national branch networks needed to mobilise liquidity administratively. This development put the industry's private banks at a distinct disadvantage. The *Joint Stock Bank Companies Act* of 1857 may have permitted a private bank to expand its membership from of six to ten proprietors,[118] but most remained too small to pursue a strategy based on geographical expansion. Consequently, private banks ranked amongst the first banks taken over during the Amalgamation Movement.[119] The number of private banks in England and Wales fell from 248 in 1870 to just 81 by 1900. In contrast, the number of English and Welsh joint stock banks in the same years was 117 and 83 respectively.[120]

Bank amalgamations yielded a convergence in lending to deposit ratios across England and Wales as administration displaced market exchanges as the primary means of transferring funds. In 1880, banks in London and the agricultural districts of England and Wales lent less than 70 per cent of their deposits whilst the average

[116] "Bank Amalgamations," *The Spectator*, 23 February 1918, 199.
[117] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," in *Select Statutes, Documents & Reports Relating to British Banking, 1832-1928*, ed. T. E. Gregory (London: Oxford University Press, 1929), 324-25.
[118] 20 & 21 Victoria c. 49. See also: Macleod, *The Theory and Practice of Banking*, II: 388-89.
[119] "The decline of private banking," *Saturday Review of Politics, Literature, Science and Art*, 26 April 1890; Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 326-27; Sykes, *The Amalgamation Movement in English Banking*: 98.
[120] Nishimura, *The Decline of Inland Bills of Exchange*: 81.

for the banking system as a whole stood at 72.9 per cent. Banks domiciled in industrial districts lent more than this average. Lancashire's banks reported lending to deposit ratios of 85.9 per cent. The ratio in Yorkshire was as high as 112.8 per cent.[121] These regional differences narrowed considerably as the lending to deposit ratio fell across England and Wales. In 1913, an average English and Welsh bank only lent 65.4 per cent its deposits. Lancashire's banks exceeded this average slightly by lending 68.9 per cent of their deposits. The ratio in Derbyshire, Nottinghamshire, the Black Country, Yorkshire and Newcastle-upon-Tyne was 71.1 per cent. At the same time, banks in London and the other English and Welsh districts reported ratios of 64.6 per cent and 64.1 per cent respectively.[122] The Amalgamation Movement was yielding a banking system in which regional differences in bank lending rates disappeared as the banks took on an increasingly national character. The proportion of deposits retained by the banks to accumulate their reserves now varied far less than it had done in the past.

Banks located in those places where the inland bills remained available for discount in sufficiently high quantities to function as a viable reserve asset retained their independence longer than most. As Nishimura asserted, banks located "in Lancashire and Yorkshire" did indeed keep "comparatively aloof" from the Amalgamation Movement for longer than banks located in other districts.[123] Lancashire and Yorkshire were textile districts, the traditional stronghold of the inland bill of exchange. Banks in these counties ranked amongst the last in England and Wales to fall prey to the Amalgamation Movement because they retained the

[121] Nishimura, *The Decline of Inland Bills of Exchange*: 107.
[122] Nishimura, *The Decline of Inland Bills of Exchange*: 111.
[123] Nishimura, *The Decline of Inland Bills of Exchange*: 9-10. See also: Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 325.

option of lending on bills of exchange, and rediscounting them when needed, longer than most. At first, banks in these regions only merged with each other, usually to deny outsiders an amalgamation target needed to access the lending opportunities on offer in their districts.[124] In 1904, a proposed merger between the Manchester and Liverpool District Bank and Lloyds Bank, for example, collapsed due to opposition from the Manchester and Liverpool District's shareholders, the local business community and the public.[125] However, the northern banks succumbed to the realities imposed by the decline in the inland bill of exchange in the end.

In 1900, Lloyds acquired the Liverpool Union Bank in an amalgamation that became a necessity according to Liverpool Union's chair because "the growth in our deposits has not kept anything like pace with ... [our] ... lending opportunities."[126] The imbalance between deposits and the amounts lent presented no problem in the past. The Liverpool Union Bank had a long history of lending more than it collected.[127] However, the proportion lent on bills of exchange was declining, which meant the Liverpool Union now needed a larger deposit base to sustain its lending whilst maintaining an adequate reserve. Similarly, Parr's Bank expanded from Lancashire in 1909 to absorb Stuckey's Banking Company in the deposit-rich county of Somerset.[128] In 1914, the Vice President of the Institute of Bankers declared, "There would be no reason for surprise if some predominantly northern bank were to

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[124] Sykes, *The Amalgamation Movement in English Banking*: 57.
[125] "The proposed Manchester bank amalgamation," *The Times*, 21 January 1904.
[126] Cited in Sykes, *The Amalgamation Movement in English Banking*: 59.
[127] Nishimura, *The Decline of Inland Bills of Exchange*: 101-102 examines the condition of the Liverpool Union Bank's balance sheet between 1864 and 1883.
[128] "Bank amalgamation," *The Times*, 29 October 1909; Nishimura, *The Decline of Inland Bills of Exchange*: 9-10.

amalgamate with some prominently southern bank."[129] He was right. In 1918, Parr's Bank merged with the London County and Westminster Bank in an amalgamation that benefited both parties. The chair of Parr's board of directors declared, "We gain access to a very large area in the Home Counties. They gain a first-class introduction to Lancashire and to such leading towns in the Midlands as Leicester and Derby and a very valuable connection in the West of England."[130] Barclays Bank acquired the Union Bank of Manchester one year later, although Barclays stopped short of an amalgamation. This time, Barclays Bank was unsure whether the authorities would approve an amalgamation so soon after Treasury Committee on Bank Amalgamations. Barclays took a cautious approach to the proposed merger with the Union Bank of Manchester in 1919. It only asked for permission to acquire the Union Bank of Manchester Bank as its affiliate. Treasury acquiesced to the request, which ensured a the Union Bank of Manchester remained Barclays' affiliate until 1939 when Barclays finally obtained the permission it had always wanted to absorb it in an amalgamation.[131]

Industrial banks participated in the Amalgamation Movement to accumulate reserves. They did not need a bigger deposit base to fund their lending because their lending to deposit ratios had already fallen below 100 per cent. The industrial banks' problem was accumulating the liquid assets needed to survive a crisis. These

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[129] George Henry Pownall, *English Banking; its Development and Some Practical Problems it has to Solve: Three Lectures Delivered by George H. Pownall (Vice President of the Institute of Bankers) at the London School of Economics* (London: Blades, East & Blades, 1914), 36.

[130] "Company meetings: Parr's Bank (Limited)," *The Times*, 12 March 1918.

[131] B. P. Blackett, "Copy of the Treasury letter of consent dated 7 November," (Barclays Bank Archive (0003-0945), 1919); H. M. Treasury, "Letter to F. C. Goodenough dated 29 July," (Barclays Bank Archive (0003-0945), 1927); Barlcays Bank, "Letter to H. M. Treasury dated 16 March," (Barclays Bank Archive (0003-0945), 1939); H. M. Treasury, "Letter to the Chairman: Barclays Bank Limited dated 20 March," (Barclays Bank Archive (0003-0945), 1939); "Banking fusion," *The Times*, 24 November 1939.

banks could have built those reserves by restricting their lending or they could amalgamate with a bank that lent a smaller proportion of its deposits and had liquidity to spare. King was right to claim large branch networks substituted for bills of exchange by performing the 'equalising' function undertaken previously by London's bill brokers.[132] However, King was wrong to argue the Amalgamation Movement caused the decline of the inland bill of exchange. The opposite happened. The inland bill of exchange went into decline whereupon the banking industry turned to an increase in firm size to compensate for the loss of a valuable reserve asset. The 'visible hand' of administrative coordination compensated for the loss of the inland bill of exchange to effect a rational distribution of the banking industry's reserves. Administration made the industry's reserves of liquid assets available to every part of England and Wales.

CONCLUDING REMARKS

The Amalgamation Movement resolved the problems created by the demise of the inland bill of exchange. Agricultural banks lost the market exchanges that used to keep their deposits gainfully employed. These banks had funds to spare and needed access to the lending opportunities on offer in industrial districts. Industrial banks lost an inherently liquid debt instrument. They needed access to the deposits raised by in agricultural districts to maintain an adequate reserve. The agricultural and industrial banks merged because amalgamations accorded with their mutual interest at a time when both lost the option of engaging in market exchanges with each other. The Amalgamation Movement supplied an administrative solution to the liquidity problems created by the decline of the inland bill of exchange.

[132] King, *History of the London Discount Market*: 273.

A reserve of liquid assets capable of conversion into a means of payment at short notice became increasingly important as the Amalgamation Movement progressed. In 1913, the Midland Bank's Sir Edward Holden explained that one should conceive of a bank as an isosceles triangle. The left side of the triangle represented "balances … repayable on demand or at short notice."[133] The bank owed these amounts to its depositors, its bank note holders and its other creditors. The right hand side of the triangle represented the amounts lent on discounted bills, overdrafts, advances and other loans that generated interest. In theory, Holden argued, a bank might increase its lending "*ad libitum*" to extend the right hand side of its triangle "indefinitely" if it were not for the fact that doing so undermined the creditors' confidence in the bank's capacity to pay its debts to them when they fell due.[134] A bank had to invest in a reserve of liquidity to act as a buffer against uncertainty. Liquid assets at "the base of the triangle" were necessary, Holden said, to meeting "any want of confidence that might arise" amongst a bank's creditors.[135]

The next chapter will explain that the banking industry underwent a widespread conversion to a regime of limited shareholder liability during the 1880s, which meant the industry's creditors could no longer rely on its shareholders to compensate them when a bank failed. An adequate reserve of liquid assets became increasingly important because it offered creditors an assurance that the bank could not fail. The adoption of limited liability delivered the final blow to the small regional banks that

[133] "Sir Edward Holden on banking," *The Times*, 4 November 1913.
[134] "Sir Edward Holden on banking."
[135] "Sir Edward Holden on banking."

populated English and Welsh banking prior to the Amalgamation Movement. Limited liability ensured competitive advantage swung even further towards large banks imbued with the reserves of liquid assets needed to assure the public that they would survive a financial crisis.

CHAPTER FIVE
THE AMALGAMATION MOVEMENT AND THE CONVERSION TO LIMITED LIABILITY

> The directors of … companies … being the managers ... of other people's money than of their own, it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private ... [partnership] ... watch over their own.[1]

The Amalgamation Movement reached its peak in the 1890s. This chapter argues the banking industry's conversion to a regime of limited liability in the 1880s contributed to that peak by accelerating the rate at which bank amalgamations occurred. Limited liability imposed greater risk onto those who had the power to break a bank. A bank would exhaust its reserves very quickly if its depositors panicked and demanded it redeem its obligations to them. In theory, limited liability should have made a bank even more vulnerable to this kind of run because the banks' creditors could no longer rely on the proprietors to compensate them if their bank failed. A bank of limited liability had two courses of action open to it to reduce the risks it imposed on their creditors. The first was to reduce the creditors' exposure to loss by demanding their proprietors contribute more paid-up and uncalled capital. Paid-up capital reduced a bank's reliance on debt making it less likely to fail. Uncalled capital created a resource that creditors could draw upon if the bank did fail. The alternative was to invest in liquid asset reserves to offer creditors the reassurance that the bank would always meet its obligations in the first place. Reliance on paid-up and uncalled capital proved unacceptable to the banking industry's shareholders. Banks that demanded shareholders furnish paid-up and uncalled capital disappeared during the Amalgamation Movement. The banks that

[1] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. Edwin Cannan, 6th ed., vol. II (London: Methuen & Co, 1950), 264-65.

put their faith in liquid assets were the Amalgamation Movement's survivors. These banks prospered because they offered their creditors security without overburdening their shareholders.

The banks of limited liability also turned to bureaucracy to eliminate the risk of loss through fraud, incompetence and other forms of employee misconduct. The amalgamating banks imposed rules and regulations designed to constrain their employees' freedom of action. This focus on employee conduct was the product the 'agency problem' created by the danger that those who control an enterprise will pursue their self-interests rather than the interests of their stakeholders. The chapter begins with an examination of the agency problems associated with the administration of a joint stock bank.

BANKS AND THE AGENCY PROBLEM

Those who administer a joint stock institution of any kind often operate under a moral hazard.[2] They can promote their interests whilst leaving other people to pay for their self-indulgence. In February 1856, for example, John Sadlier (1813–1856) took prussic acid on Hampstead Heath.[3] Sadlier appeared a man of sound business judgment before he died. This Irish-born resident of London represented an Irish constituency in parliament, oversaw the conversion of his family's private bank into the Tipperary Joint Stock Bank, served on the boards of several companies and secured a term as chair of the London and County Joint Stock Bank. He had even

[2] Bengt Hölmstrom, "Moral hazard and observability," *The Bell Journal of Economics* 10, no. 1 (1979).
[3] "Death of Mr. John Sadleir, M.P. for Sligo," *The Times*, 18 February 1856.

been a junior minister in Lord Aberdeen's (1784-1860) coalition government.[4] However, Sadlier funded his apparent success fraudulently. He depended upon his younger brother's influence at the Tipperary Joint Stock Bank to borrow funds whilst his brother falsified the bank's accounts.[5] Eventually, John Sadlier's debts drove the Tipperary into insolvency.[6] John committed suicide to avoid a scandal and his brother James Sadlier (1815-1881) fled to the continent four months later.[7] The Tipperary's shareholders paid a heavy price for the Sadlier brothers' maladministration because their bank was a creature of unlimited liability. These shareholders compensated the bank's creditors for the losses the Sadliers imposed.[8] Banks of unlimited liability like the Tipperary were the norm in for much of the nineteenth century. Most of the Scottish joint stock banks were banks of unlimited liability. The Bank of Scotland, the Royal Bank of Scotland and the British Linen Company were the only exceptions. Every English and Welsh private bank and the joint stock banks established under the *Country Bankers Act* of 1826 were banks of unlimited liability too.

The villain in Charles Dickens' (1812-1870) *Little Dorrit* was a private banker respected by the "weightiest of men."[9] Unfortunately, Mr Merdle never earned the profits needed to justify his reputation. Merdle misappropriated funds invested with him to create an illusion of success. The nature of the fraud rendered it

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[4] "John Sadlier was a national calamity," *The Times*, 10 March 1856.
[5] The Bankers' Magazine, "Tipperary Joint Stock Bank," *The Bankers' Magazine and Journal of the Money Market* 1856.
[6] "Ireland (from our own correspondent)," *The Times*, 29 September 1856.
[7] Alex S. Rosser, "Businessmen in the Parliament of 1852–7: Players or spectators?," *Parliamentary History* 32, no. 3 (2013): 490.
[8] "Ireland (from our own correspondent): The Sadlier Frauds," *The Times*, 4 April 1856; "Ireland (from our own correspondent): Tipperary Joint Stock Bank," *The Times*, 21 June 1856; "Ireland (from our own correspondent): The Master of the Rolls and the Irish Executive," *The Times*, 12 July 1856.
[9] Charles Dickens, *Little Dorrit* (London: Penguin, 2003), 265.

unsustainable. Every pound misappropriated only added to Merdle's future obligations because his unsuspecting victims expected a return on their investments. Merdle's bank must run out of money eventually. Today we would call Merdle's fraud a 'Ponzi scheme' although the term was not available to Dickens.[10] When we first meet Merdle, he is suffering from an undiagnosed stress-related complaint. By the end of the novel, Merdle has killed himself.

Little Dorrit appeared in monthly instalments between December 1855 and June 1857.[11] Two days after John Sadleir killed himself, Dickens introduced Merdle to his audience for the first time. Most assume that Dickens modeled Merdle on the elder of the two Sadlier brothers for that reason.[12] Nevertheless, Dickens ignored one vital aspect of the Sadliers' fraud in *Little Dorrit*. The fictitious Merdle was a private banker who was liable for his bank's debts. Those who lost the money they entrusted to him only did so because Merdle was bankrupt. James Sadlier was an officer in a joint stock bank. The Sadliers' wrongdoing had an institutional dimension. It exposed failings in the Tipperary's corporate governance.[13]

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[10] Andrei Shleifer and Robert W Vishny, "A survey of corporate governance," *The Journal of Finance* 52, no. 2 (1997): 749; Pauline Reid, "Specters of Smith: Adam Smith's "Invisible Hand" and Charles Dickens's *Little Dorrit*," *Literature Interpretation Theory* 25, no. 4 (2014).
[11] Dickens, *Little Dorrit*: xxxiii.
[12] Lionel Stevenson, "Dickens's dark novels, 1851-1857," *The Sewanee Review* 51, no. 3 (1943): 406; Timothy Alborn, "The moral of the failed bank: Professional plots in the Victorian money market," *Victorian Studies* 38, no. 2 (1995): 224; Lyn Pykett, *Charles Dickens* (London: Palgave Macmillan, 2002), 151; Mary Poovey, *Genres of the Credit Economy: Mediating Value in Eighteenth and Nineteenth-Century Britain* (Chicago: University of Chicago Press, 2008), 375.
[13] Corporate governance "involves a set of relationships between a company's management, its board, its shareholders and other stakeholders … [to provide a] ... structure through which the objectives of the company are set and the means of attaining those objectives and monitoring performance are determined." OECD, *OECD Principles For Corprorate Governance* (Paris: Organisation for Economic Co-operation and Development, 2004), 11.

The risk that the unsuspecting might fall victim to a banker's incompetence, opportunism or recklessness was an ever-present danger during the nineteenth-century. *Little Dorrit* warned that a private banker posed a risk. However, private bankers were, as Lord Eldon (1751-1838) once said, liable for their business debts to their "last acre" and their "last shilling."[14] Rational private bankers administered their banks diligently to avoid losing everything they owned. Rational private bankers only took liberties knowingly if, like Merdle, they had nothing to lose.[15] The joint stock banks always imposed a bigger risk of misconduct than private banks because those who administered them could leave their shareholders and creditors to divide any losses imposed amongst them.[16] The separation of ownership and control created in a joint stock institution give rise to what we now call an agency problem.[17]

Agency theory argues that in an unregulated environment, the corporate governance of a joint stock enterprise is the product of a bargaining process under which those who administer the firm accept 'bonding' and 'monitoring' arrangements to surrender opportunities to act in their own interests.[18] Bonding

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[14] Cited in: P. J. McKenna, *On Partnerships with Limited Liability* (Dublin: Hodges and Smith 1854), 4. See also: William Watson, *A Treatise on the Law of Partnership*, Second ed. (London: J. Butterscotch, 1807), 167-75

[15] Walter Bagehot, "Sound banking," in *The Collected Works of Walter Bagehot*, ed. Norman St John-Stevas (London: The Economist, 1978); Walter Bagehot, "Limited liability in banking I," in *The Collected Works of Walter Bagehot*, ed. Norman St John-Stevas (London: The Economist, 1978), 397; Bagehot, "The safest bank."

[16] Bagehot, "Sound banking," 306.

[17] Eugene F. Fama, "Agency problems and the theory of the firm," *The Journal of Political Economy* (1980); Ross L. Watts and Jerold L. Zimmerman, "Agency problems, auditing, and the theory of the firm: Some evidence," *Journal of Law and Economics* 26, no. 3 (1983); Edward A Dyl, "Corporate control and management compensation: Evidence on the agency problem," *Managerial and Decision Economics* 9, no. 1 (1988); Lewis T. Evans and Neil C. Quigley, "Shareholders liability regimes, principal-agent relationships, and banking industry performance," *Journal of Law and Economics* 38, no. 2 (1995).

[18] Michael C. Jensen and William H. Meckling, "Theory of the firm: Managerial behavior, agency costs and ownership structure," *Journal of Financial Economics* 3, no. 4 (1976). See also: Fama, "Agency problems and the theory of the firm."; Eugene F. Fama and Michael C. Jensen, "Separation of ownership and control," *Journal of Law and Economics* 26, no. 2 (1983); Watts and Zimmerman,

promotes congruent interests between the administrators and others. Managers can bond with their shareholders, for example, by taking shares in the company to become shareholders too. Monitoring holds administrators accountable for their actions. An example of a monitoring arrangement is the provision of audited accounts, which give shareholders and creditors some insight into the stewardship of the company. The agency theorist's claim is that a company's administrators incur a 'residual loss' whenever the opportunity to act in their own interests remains open to them. Shareholders offer less for their shares and demand higher dividends when they know they could fall victim to managerial opportunism. Creditors lend to the company in smaller amounts and charge higher rates of interest under the same circumstances. The agency theorists' argument is that a company's administrators have an incentive to enter into any bonding and/or monitoring arrangement that consumes fewer resources than the residual loss it eliminates.

Alfred Chandler championed the virtues of professional management and the separation of ownership and control it entailed. Yet the agency problem barely featured in his work.[19] It is not as if he was unaware of the agency problem. America's business schools devoted a lot of energy to the agency problem during his

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"Agency problems, auditing, and the theory of the firm."; Kathleen M. Eisenhardt, "Agency theory: An assessment and review," *The Academy of Management Review* 14, no. 1 (1989).

[19] Alfred D. Chandler and Louis Galambos, "The development of large-scale economic organizations in modern America," *The Journal of Economic History* 30, no. 1 (1970); Alfred D. Chandler, *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, Massachusetts: Belknap Press, 1977); Alfred D. Chandler and Herman Daems, "Administrative coordination, allocation and monitoring: A comparative analysis of the emergence of accounting and organization in the U.S.A. and Europe," *Accounting, Organizations and Society* 4, no. 1-2 (1979); Alfred D. Chandler, "The growth of the transnational industrial firm in the United States and the United Kingdom: A comparative analysis," *The Economic History Review* New Series 33, no. 3 (1980); Alfred D. Chandler, "The emergence of managerial capitalism," *The Business History Review* 58, no. 4 (1984); Alfred D. Chandler, "The enduring logic of industrial success," *Harvard Business Review* 68, no. 2 (1990); Alfred D. Chandler and Takashi Hikino, *Scale and Scope: The Dynamics of Managerial Capitalism* (Cambridge, Massachusetts: Belknap Press, 1990); Alfred D. Chandler, "Organizational capabilities and the economic history of the industrial enterprise," *The Journal of Economic Perspectives* 6, no. 3 (1992).

lifetime. As early as 1932, Adolf Berle and Gardiner Means warned American shareholders "surrendered the right" to have a company "operated in their sole interest" when they entrusted its administration to others.[20] In the 1970s, agency theorists erected an entire research paradigm on the foundations of Michael Jensen and William Meckling's seminal analysis of the separation of ownership and control. These agency theorists went on to influence the curricula taught in America's business schools profoundly.[21] Chandler thought professional managers were the unsung heroes of American industrialisation. Chandler believed an owner-manager posed a far bigger risk to organisational effectiveness because they accounted to no one.[22] Besides, the evidence seemed irrefutable to Chandler. Large professionally managed firms acquired competitive advantages over their smaller owner-managed counterparts in so many cases.[23] The economies of scale and scope realised in a large firm must have compensated for any costs the agency problem imposed.

Chandler left others to worry about the agency problem, but this study of English and Welsh banking industry has to address this issue. The English and Welsh were aware that a separation of ownership and control in their joint stock banks created difficulties and they experimented with several corporate governance regimes to resolve those difficulties. As usual, the analysis begins in Scotland

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[20] Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* (New York: Macmillan, 1932), 355.

[21] Jensen and Meckling, "Theory of the firm." See also: Fama, "Agency problems and the theory of the firm."; Fama and Jensen, "Separation of ownership and control."; Watts and Zimmerman, "Agency problems, auditing, and the theory of the firm."; Eisenhardt, "Agency theory."; Sumantra Ghoshal, "Bad management theories are destroying good management practices," *Academy of Management Learning & Education* 4, no. 1 (2005); Jeffrey R Cohen and Lori L Holder-Webb, "Rethinking the influence of agency theory in the accounting academy," *Issues in Accounting Education* 21, no. 1 (2006).

[22] Chandler, "The emergence of managerial capitalism," 495-98; Chandler, "The enduring logic of industrial success," 138.

[23] Barry Supple, "Scale and scope: Alfred Chandler and the dynamics of industrial capitalism," *The Economic History Review* New Series 44, no. 3 (1991).

because the Scots supplied the corporate governance model adopted by the first generation of English and Welsh joint stock banks in 1826.

THE CORPORATE GOVERNANCE IN SCOTTISH JOINT STOCK BANKS

Scotland's unincorporated joint stock banks emerged in an environment subject to very little regulation. The industry's administrators, creditors and shareholders negotiated their corporate governance arrangements without the assistance of the state and they did so by entering into bonding and monitoring arrangements. The Banking Company in Aberdeen (established in 1767) was typical of many of the unincorporated Scottish joint stock banks.[24] It operated under the supervision of a Court of the Governor and Directors made up of a governor and 18 directors. The bank's shareholders elected the Court of the Governor and Directors and every one of them bonded with their constituents because they had to own shares in the bank.[25] The Banking Company in Aberdeen also employed a cashier and an accountant, neither of whom had to own shares although other arrangements compensated for share ownership's absence. A simple majority at a shareholders' general meeting could dismiss them. Opportunism would cost the cashier and an accountant more than their jobs. The cashier signed a bond of fidelity and honesty for £5,000 and the accountant signed one for £1,000.[26] These bonds of fidelity and honesty were a key feature of the Scottish banks' corporate governance model. As Thomas Joplin explained, the agents that administered a Scottish bank's branches signed bonds too. Joplin wrote:

[24] Graeme Acheson, Charles R. Hickson, and John D. Turner, "Organisational flexibility and governance in a civil-law regime: Scottish partnership banks during the Industrial Revolution," *Business History* 53, no. 4 (2011).
[25] Banking Company in Aberdeen, *The Contract of the Banking Company in Aberdeen* (Aberdeen: J. Chalmers, 1767), 11.
[26] Banking Company in Aberdeen, *The Contract of the Banking Company in Aberdeen:* 11-12.

> The Scotch Banks ... in the arrangements, which they make with their agents established in distant towns, assume that there is no risk whatever, and lay it down ... that if ... [agents] ... incur any loss, they are to suffer it themselves.... Securities are required of them ... to the extent, I understand, of not less than ten thousand pounds.... It is, I believe, generally calculated by the agent, that if he can make out a case of very unforeseen loss, it will be partly allowed him; but the assumed principle is, that there need be none at all.[27]

An accounting system supplied the primary means of monitoring. The Banking Company in Aberdeen brought its books of account to a "just and true Balance" every March in readiness for the shareholders' general meeting in April.[28] Furthermore, three shareholders acting in concert could inspect the bank's books at any time they wished.[29]

The Scottish banks' reputation for stability suggests they handled their agency problem well.[30] No Scottish bank of any real significance failed between 1772 and 1857.[31] The lessons learned by Scotland's provincial banks laid the foundations for a new generation of even larger institutions in the nineteenth century.[32] In 1810, the promoters of the Commercial Bank of Scotland set out to create a bank that would rival the Bank of Scotland, the Royal Bank of Scotland and the British Linen

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[27] Thomas Joplin, *An Essay on the General Principles and Present Practice of Banking in England and Scotland: With Observations Upon the Justice and Policy of an Immediate Alteration in the Charter of the Bank of England, and the Measures to be Pursued in Order to Effect It*, Second ed. (London: Ridgway & Company, 1822), 23-24.

[28] Banking Company in Aberdeen, *The Contract of the Banking Company in Aberdeen*: 7.

[29] Banking Company in Aberdeen, *The Contract of the Banking Company in Aberdeen*: 8.

[30] Joplin, *An Essay on the General Principles and Present Practice of Banking in England and Scotland*.

[31] Henry Hamilton, "The failure of the Ayr bank, 1772," *The Economic History Review* New Series 8, no. 3 (1956); S. G. Checkland, *Scottish Banking: A History, 1605-1973* (Glasgow: Collins, 1975), 127-31, 466-69; Roy H. Campbell, "Edinburgh bankers and the Western Bank of Scotland," *Scottish Journal of Political Economy* 2, no. 1 (2007).

[32] Commercial Bank of Scotland, *Articles of Copartnery of the Commercial Banking Company of Scotland* (Edinburgh: Alex Lawrie & Company, 1810); National Bank of Scotland, *Contract of Copartnership of the National Bank of Scotland* (Edinburgh: National Bank of Scotland, 1825); Glasgow Union Banking Company, *Abstract of the Articles of the Contract of Co-partnership of the Glasgow Union Banking Company* (Glasgow: Glasgow Union Banking Company, 1830); Edinburgh and Glasgow Bank, *Contract of Copartnership of the Edinburgh and Glasgow Bank* (Edinburgh: Edinburgh and Glasgow Bank, 1844).

Company in size. They followed precedents set by the provincial banking companies and the larger public banks to do it. The Commercial Bank of Scotland had a committee of ordinary directors to supervise its day-to-day operations and another committee made up of extraordinary directors who met less frequently to advise it.[33] Nevertheless, the Commercial Bank of Scotland remained different to the Bank of Scotland, the Royal Bank of Scotland and the British Linen Company in one fundamental respect. The law held an unincorporated bank like the Commercial Bank of Scotland's shareholders liable for its debts on an unlimited liability basis whereas the three public banks were banks of limited liability. The public bank's shareholders could lose no more than the amount they agreed to pay for their shares.[34]

An unusual feature of the Scottish banks' corporate governance model was the relative absence of safeguards accorded to their creditors. No Scottish bank made its balance sheet available to the public prior to 1865 for example.[35] The creditors of a Scottish bank of unlimited liability did not demand more because unlimited shareholder liability offered them all the protection they required. The creditors only needed an assurance that the shareholders remained wealthy enough to reimburse

[33] Commercial Bank of Scotland, *Articles of Copartnery of the Commercial Banking Company of Scotland*: 8-9. See also: Royal Bank of Scotland, *Warrant of the Charter Erecting the Royal Bank of Scotland* (Edinburgh: James Davidson and Company, 1729), 21-28; Hugo Arnot, *The History of Edinburgh* (Edinburgh: W. Creech, 1779), 533; William Hugh Logan, *The Scottish Banker; or, a Popular Exposition of the Practice of Banking in Scotland*, Second ed. (Edinburgh: Gallie and Bayley, 1844), 41-50; Richard Saville, *Bank of Scotland: A History, 1695-1995* (Edinburgh: Edinburgh University Press, 1996), 95.
[34] Jack Carr, Sherry Glied, and Frank Mathewson, "Unlimited liability and free banking in Scotland: A note," *The Journal of Economic History* 49, no. 4 (1989); Tyler Cowen and Randall Kroszner, "Scottish banking before 1845: A model for laissez-faire?," *Journal of Money, Credit and Banking* 21, no. 2 (1989).
[35] William John Lawson, *The History of Banking: With a Comprehensive Account of the Progress of the Banks of England, Ireland and Scotland* (London: Richard Bentley, 1850), 439-30; Andrew William Kerr, *Scottish Banking During the Period of Published Accounts, 1865-1896* (London: Effingham Wilson, 1898), 1-2; Checkland, *Scottish Banking*: 520.

them if the bank failed. The Scottish unincorporated banks did not publish balance sheets because they published the names of their proprietors instead.[36]

The creditors of a Scottish unlimited liability bank had allies who ensured its proprietors remained wealthy enough to compensate them if the bank failed. When a bank of unlimited liability collapsed, the difference between its debts and the realised value of its assets was borne in the first instance by all the shareholders in proportion to the number of shares owned. Unfortunately, once a shareholder exhausted his or her personal wealth, he or she had no more to give. This meant that the greatest obligation would always fall upon the wealthiest shareholders who could afford to pay their share of the loss and then make good any amounts not collected from their fellow shareholders. Consequently, wealthy shareholders had an incentive to ensure every other shareholder remained rich enough to meet their obligations to the creditors at the first time of asking.[37] At the Dundee Banking Company, the directors could reject a potential shareholder nominated in a will.[38] The Banking Company in Aberdeen took an even more draconian approach. Share transfers had to take place in the presence of at least two directors. The executors of a deceased shareholder's estate had to sell their shares to parties approved by the directors within six months. The directors even had the power to sell a deceased shareholder's shares, at a loss if necessary, should an executor fail to nominate an acceptable buyer

[36] Evans and Quigley, "Shareholders liability regimes," 499-500. See for example: Banking Company in Aberdeen, *A List of the Proprietors of the Banking Company in Aberdeen* (Aberdeen: Banking Company in Aberdeen, 1790); Western Bank of Scotland, *List of Partners of the Western Bank of Scotland: 28 June 1849* (Glasgow: Western Bank of Scotland, 1849).
[37] Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime."
[38] Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime," 514.

for them.[39] Scottish law reinforced the tendency to exclude the poor from a bank's shareholding constituency. The shareholders of a Scottish company of unlimited liability remained liable for their share of the debts incurred during their tenure.[40] Rich shareholders could not escape their obligations to the creditors by transferring their shares to an impoverished risk taker at the first sign of difficulty.

The Scottish corporate governance model proved so secure that it presented no hindrance to the growth of an unlimited liability bank. The Commercial Bank of Scotland, its younger sibling the National Bank of Scotland (established in 1825) and several other banks like them established before 1844 were all banks of unlimited liability. This generation of Scottish unincorporated joint stock banks demonstrated just how robust the Scottish banking industry's unlimited liability corporate governance model really was by becoming as big as Scotland's three banks of limited liability. Lawrence White noted that by 1845:

> (1) the Commercial Bank of Scotland had more branches than any of the public banks, a greater note circulation than two ... and more shareholders than one; (2) the National Bank of Scotland had more branches than two of the three public banks, a note circulation only one per cent smaller than that of the second largest public bank and more shareholders than any of the three; (3) the North of Scotland Banking Company and the Edinburgh and Glasgow Bank each had more shareholders than any of the three public banks; (4) the Union Bank of Scotland had a greater note circulation than two of the three public banks.[41]

This regime of unlimited liability also had an effect on a bank's financial structure. Joplin noted that banks of limited liability generally demanded their shareholders

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[39] Banking Company in Aberdeen, *The Contract of the Banking Company in Aberdeen*: 11; Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime," 514.

[40] George Joseph Bell and Patrick Shaw, *Commentaries on the Laws of Scotland: In Relation to Mercantile and Maritime Law, Moveable and Heritable Rights, and Bankruptcy* vol. 6 (Edinburgh: T. & T. Clark, 1858), 224.

[41] Lawrence H. White, "Scottish banking and the legal restrictions theory: A closer look: comment," *Journal of Money, Credit and Banking* 22, no. 4 (1990): 529-30.

supply more capital than a bank of unlimited liability did because shareholders subject to limited liability would contribute no more if the bank failed.[42] An unlimited liability bank like the Dundee Banking Company maintained a debt to asset ratio that fluctuated around 80 per cent between 1775 and 1810. During the same period, the debt to asset ratios of the limited liability Bank of Scotland and the Royal Bank of Scotland fluctuated around 50 per cent.[43]

The Scottish banking industry took pride in the fact that its creditors had little to fear. Scottish banks failed rarely and when they did fail, their creditors usually received full compensation.[44] The English and Welsh panicked during the financial crisis of 1825 because their small private banks put them at risk but the Scottish public felt little inclination to orchestrate a similar run on their joint stock banks. As Chapter Two explained, Liverpool's government abolished the six-partner rule in the English and Welsh provinces in 1826, which gave the English and Welsh banks the opportunity to adopt Scottish joint stock banking for the first time. However, the English and Welsh were embracing a corporate governance model that was new to them when they adopted joint stock banking in 1826. They would have to learn how to manage the agency problem as effectively as the Scottish banks to replicate Scotland's more stable banking system.

[42] Thomas Joplin, *The Principle of the Personal Liability of the Shareholders in Public Banks Examined* (London: W. J. Ruffey, 1830), 7-8.
[43] Checkland, *Scottish Banking*: 737-38.
[44] Andrew William Kerr, *History of Banking in Scotland* (Glasgow: David Bryce & Son, 1884), 508; Acheson, Hickson, and Turner, "Organisational flexibility and governance in a civil-law regime."

CORPORATE GOVERNANCE IN ENGLAND AND WALES

The English and Welsh established 143 joint stock banks between 1826 and 1843. Only 25 banks left the industry during this period and 19 of those 25 failed, which yielded a failure rate of just 13.5 per cent.[45] This was a significant improvement on the rates of failure exhibited by the English and Welsh private banks, which suggests joint stock banks improved the stability of the English and Welsh banking system.[46] Nevertheless, there was disappointment because some of the first English and Welsh joint stock banks failed to live up to expectations. All too often, an English and Welsh joint stock bank entrusted its operations to those who had little or no banking experience.[47] The result was a banking industry in which administrative standards were poor.[48] In 1836, William Clay delivered a speech in parliament at the height of the joint stock banking boom.[49] In this speech, Clay questioned three elements of the Scottish corporate governance model imported into England and Wales in 1826. Clay objected to unlimited liability, the absence of regulation with respect to paid-up capital and the failure to publish balance sheets.

Clay warned a regime of unlimited liability threatened bank stability for two reasons. First, wealthy shareholders would avoid shares in a joint stock bank

[45] Philip L. Cottrell and Lucy Newton, "Banking liberalisation in England and Wales," in *The State, the Financial System and Economic Modernization*, ed. Richard Sylla, Richard Tilly, and Gabriel Tortella (Cambridge: Cambridge University Press, 1999), 83-84.
[46] Cottrell and Newton, "Banking liberalisation," 83-84.
[47] S. Evelyn Thomas, *The Rise and Growth of Joint Stock Banking*, vol. I (London: Sir Isaac Pitman & Sons, 1934), 296.
[48] Henry Dunning Macleod, *The Theory and Practice of Banking: With Elementary Principles of Currency; Prices; Credit; and Exchanges*, vol. II (London: Longman, Brown, Green and Longmans, 1856), 508.
[49] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks to Which are Added Reflections on Limited Liability, Paid-up Capital and Publicity of Accounts as Applied to Such Associations with Some Remarks on an Article on Joint-Stock Companies in the Last Number of the Edinburgh Review* (London: James Ridgway and Sons, 1836).

because the risks imposed on them were too great. The result, Clay feared, would be an industry administered by directors accountable to poor and ill-educated shareholders who would demand high returns and have little regard for the risks incurred because they had nothing to lose. "By the permission to establish banks of limited liability," Clay said, "we should acquire the most important securities for the good conduct of such establishments, namely a certainty that the most respectable persons in the community would become partners in them."[50] The second problem was that unlimited liability induced creditors to trust their banks too much. Clay argued:

> By permitting only joint stock banks with limited liability, I would crush at once the spurious credit ... enjoyed by these establishments from the responsibility of the individual shareholders, and reduce the credit ... obtained by a joint stock bank ... to the exact amount of its paid-up capital and available money resources.[51]

The absence of any controls over paid-up capital was the second failing of the Scottish corporate governance model in need of attention according to Clay. In too many cases, he said, a bank's promoters issued shares to themselves to establish the bank. Clay complained these promoters then issued more shares to the public at a premium and treated that premium as profit rather than capital. The promoters used the premium to pay a dividend, which meant money that ought to stay within the bank ended up in the promoters' pockets instead. Clay demanded, "The whole capital of a joint-stock bank should be paid-up by the time the bank opened its doors for business so there "could be no holding back of shares to be subsequently issued at

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[50] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks*: 37.
[51] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks*: 35-36.

a premium."[52] Finally, Clay noted the English and Welsh joint stock banks followed the Scottish example to the letter and withheld their balance sheets from the public. Clay wanted every joint stock bank to publish balance sheets "making clear to the apprehension of all ... the circumstances of the bank, both as to its assets and liabilities."[53]

Clay's call for reform in 1836 struck a chord because it resulted in a Secret Committee on Joint Stock Banks that began its deliberations in that year. However, his views on limited liability were too radical for the age. *The Times* expressed a general distrust of Clay's commitment to limited liability in the following terms:

> Let ... [shareholders] ... be pronounced only partially liable, and they will scarcely remember the existence of the bank, except when they occasionally receive some interest for their investment; and ... would suffer an establishment ... to fall into decay or ruin with as much indifference as they hear of a breakdown of an old carriage or an old cow house. No, it is to the wealthy shareholder that the public looks for security; destroy, or, which is the same thing, limit ... liability, and the bank becomes a delusion.[54]

Unlimited liability seemed essential to secure the creditors' interests. There was a risk that limited shareholder liability would promote shareholder neglect.[55] In 1836, the Secret Committee on Joint Stock Banks' interim report noted that shareholder vigilance remained the primary guarantor of sound bank administration.[56]

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[52] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks*: 37.
[53] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks*: 38.
[54] "Nothing that may have occurred to us on first hearing the discussion introduced by Mr Clay last Thursday," *The Times*, 14 May 1836. Also cited in Bishop C. Hunt, "The joint-stock company in England, 1830-1844," *Journal of Political Economy* 43, no. 3 (1935): 344.
[55] John D. Turner, "'The last acre and sixpence': Views on bank liability regimes in nineteenth-century Britain," *Financial History Review* 16, no. 2 (2009): 120-21.
[56] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks; Together With Minutes of Evidence and Appendix* (London: Parliament of the United Kingdom (House of Commons), 1836), x.

The Northern and Central Bank of England collapsed in the middle of the Secret Committee on Joint Stock Banks' deliberations, which gave the committee an opportunity to take evidence on a failed joint stock bank when it reconvened in 1837. The committee called the Northern and Central Bank of England's chair, its accountant, a bank director and its manager to give evidence.[57] The interrogation revealed a litany of managerial malpractice. The directors purchased shares from the bank, although their intention was not to bond with their proprietors. Instead, the directors traded in these shares on their own account and profited by selling the shares at a premium. The directors did not even pay the calls due on the shares traded, preferring instead to wait until they sold them to settle their obligations. The directors also recorded the amounts they owed on their shares in a secret ledger that they never divulged to their fellow shareholders.[58] The bank compounded this error by making loans on the security of the Northern and Central Bank's shares, which would offer no security at all if the bank got into difficulties because they would become worthless.[59] The bank also put its managerial hierarchy under stress by expanding too quickly.[60] In Leeds, an inexperienced and poorly supervised branch manager ran up £40,000 in bad debts. In Sheffield, a manager lost between £12,000 and £14,000 and the amount lost in Nottingham was £12,000. The bank tried to protect itself from the losses imposed. It made all of the managers involved sign Scottish-style bonds but the bonds proved worthless. The bank only made its

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[57] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks; Together With Minutes of Evidence, Appendix and Index* (London: Parliament of the United Kingdom (House of Commons), 1837), 1-94.
[58] Lawson, *The History of Banking*: 326.
[59] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks*: 7, 14-16.
[60] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks*: 40-41.

managers liable for acts of dishonesty. It did not make them liable for acts of negligence or incompetence.[61]

The Northern and Central Bank of England's collapse in 1836 reinforced a widespread prejudice against geographically dispersed branch networks in England and Wales.[62] Vincent Stuckey was as progressive a country banker as one could hope to find, having been one of the first private bankers to embrace joint stock banking in 1826.[63] Yet, his view was that a bank could only administer its branches effectively if it limited them to "one or at the most two counties" with no branches located more than 50 miles from head office.[64] A representative of the North of England Bank was even more cautious in his approach to branches. He told the Secret Committee on Joint Stock Banks that branches should be within 20 miles of head office so that a bank officer could visit it on horseback and return within a day.[65] The Secret Committee on Joint Stock Banks noted that the law did not "limit the number of branches or the distance of such branches" from head office before suggesting the oversight constituted a threat to "the future stability of the banks throughout the United Kingdom."[66]

The Secret Committee on Joint Stock Banks' claim that large branch networks constituted a threat to the industry angered a long-standing proponent of joint stock

[61] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks*: 40-41.
[62] Victoria Barnes and Lucy Newton, "How far does the apple fall from the tree? The size of English bank branch networks in the nineteenth century," *Business History* 60, no. 4 (2018).
[63] Cottrell and Newton, "Banking liberalisation," 90; Lucy Newton, "The birth of joint-stock banking: England and New England compared," *The Business History Review* 84, no. 1 (2010): 34.
[64] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks*: 81; Thomas, *The Rise and Growth of Joint Stock Banking*, I: 257; Cottrell and Newton, "Banking liberalisation," 90.
[65] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks*: 128.
[66] Secret Committee on Joint Stock Banks, *Report of the Secret Committee on Joint Stock Banks*: ix.

banks like Joplin. Joplin attacked the Secret Committee's findings, arguing the English and Welsh distrust of branches made no sense. Banks in Scotland and Ireland were supervising branches at far greater distances from their head offices than was the norm in England and Wales at no discernible risk. In addition, the impeccably managed National Provincial Bank of England administered English and Welsh branches located beyond the 65-mile radius from its head office in London.[67] Joplin asserted the arrangements imported from Scotland in 1826 could supervise large branch networks effectively if the bank applied them properly. Poor administration, not branches, constituted the industry's greatest threat in Joplin's mind.

The evidence taken by the Secret Committee did not yield an immediate legislative response. Nevertheless, the Bank of England's charter was due for renewal in 1844 and by then the United Kingdom had a Prime Minister who was suspicious of the joint stock banks erected under the auspices of the *Country Bankers Act*.[68] The findings of the Secret Committee on Joint Stock Banks reinforced Robert Peel's prejudices against the joint stock banks. In 1844, Peel and his government took advantage of a reform of the laws relating to joint stock companies in general to pass special legislation designed to improve corporate governance standards in the banking industry. That legislation was the *Joint Stock Banking Act* of 1844.[69]

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[67] Thomas Joplin, *An Examination of the Report of the Joint Stock Bank Committee To Which is Added an Account of the Late Pressure in the Money Market and Embarrassment of the Northern and Central Bank of England*, Third ed. (London: James Ridgway, 1837), 38-43; Charles W. Munn, "The emergence of joint-stock banking in the British Isles a comparative approach," *Business History* 30, no. 1 (1988): 78-79.
[68] Walter Bagehot, *Lombard Street: A Description of the Money Market* (London: Henry S. King & Co., 1873), 252.
[69] 7 & 8 Victoria c. 113.

THE *JOINT STOCK BANKING ACT*

Legal historians consider 1844 a watershed year in British corporate history.[70] The *Joint Stock Companies Act* of that year put a joint stock company's right to litigate in its own name on a secure foundation.[71] Every company registered under the *Joint Stock Companies Act* acquired a legal personality.[72] However, the *Country Bankers Act* of 1826 had already given a legal personality to every English and Welsh joint stock bank registered under it.[73] In 1844, only London's joint stock banks lacked the capacity to litigate in their own right because the Bank of England's belief that a legal personality constituted a privilege. The Bank of England argued bestowing any privilege on London's joint stock banks would breach an undertaking given to it by the government in 1833.[74] The Bank of England could hardly maintain a legal personality continued to constitute a privilege now parliament made it available to every other joint stock company in the land.[75] The *Joint Stock Banking Act* of 1844 gave London's joint stock banks the right to litigate in their own names for the first time. London's joint stock banks did not even have to register under the *Joint Stock Banking Act* to acquire this privilege.

Parliament denied the English and Welsh banks the right to register under the *Joint Stock Companies Act* because it intended them to register under the *Joint Stock Banking Act* of 1844 instead. Both acts exhibited one similarity by providing for the

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[70] Geoffrey Todd, "Some aspects of joint stock companies, 1844-1900," *The Economic History Review* 4, no. 1 (1932); Paddy Ireland, "Capitalism without the capitalist: The joint stock company share and the emergence of the modern doctrine of separate corporate personality," *The Journal of Legal History* 17, no. 1 (1996).
[71] 7 & 8 Victoria c. 110.
[72] Todd, "Some aspects of joint stock companies," 47.
[73] 7 George IV c. 46.
[74] T. E. Gregory and A. Henderson, *The Westminster Bank Through a Century*, vol. 1 (London: Oxford University Press, 1936), 139-48.
[75] Gregory and Henderson, *The Westminster Bank Through a Century*, I: 150.

incorporation of a joint stock company on an unlimited liability basis. However, the *Joint Stock Banking Act* imposed corporate governance obligations that were absent from the *Joint Stock Companies Act*. Consequently, the *Joint Stock Banking Act* singled the banking industry out for special treatment and as such, it constituted Peel's response to the evidence taken by the Secret Committee on Joint Stock Banks in the 1830s.[76] The *Joint Stock Banking Act* decreed a new joint stock bank would have to petition the Board of Trade for letters patent and append its proposed constitution to the application. That constitution had to accord with the requirements of the *Joint Stock Banking Act* and the bank's promoters would have to amend the constitution to accommodate any additional demands made by the Board of Trade. At the very least, an acceptable constitution would provide for monthly statements of assets and liabilities and annual financial statements audited by two or more parties chosen by the shareholders. The constitution should also provide for minimum capital of £100,000 divided into shares of a value no lower than £100. In addition, the bank must issue at least half its shares and collect a minimum of ten per cent of their value before the Board of Trade could entertain the application. If the Board of Trade granted letters patent, then the bank would have to issue all of its remaining shares and collect half of their value before it commenced trading. Finally, the bank would have to make an application to the Board of Trade if it wanted to issue more shares later. A subsequent act imposed the same regulations onto Ireland and Scotland.[77]

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[76] "House Of Commons, Friday, August 9," *The Times*, 10 August 1844; Macleod, *The Theory and Practice of Banking*, II: 508-14.
[77] 9 & 10 Victoria c. 75.

The *Joint Stock Banking Act* and its Irish and Scottish equivalent met all but one of Clay's objections to the joint stock bank's corporate governance model. These acts regulated a bank's paid-up capital and provided for greater publicity by demanding the bank produce balance sheets regularly. However, banks registered under these acts were to remain creatures of unlimited liability, which disappointed Clay. Clay intimated in parliament that he wanted to move an amendment to the English and Welsh legislation to provide for limited liability but he did not act on the threat. Peel made it clear to Clay that he would do all he could to ensure such an amendment's defeat.[78]

The *Joint Stock Banking Act* of 1844 and its Irish and Scottish equivalent possessed a significant defect that turned them into dead letters in their respective jurisdictions. These acts' regulations only applied to banks registered under them or formed after they became operational. Joint stock banks formed prior to the passage of the *Stock Banking Act* and its Irish and Scottish equivalent had a choice. They could apply for letters patent under their respective legalisation, although doing so would entail a rewrite of their constitutions. Alternatively, they could ignore the acts altogether and continue to operate under their old arrangements. By now, every established joint stock possessed a workable legal personality.[79] An established joint stock bank simply had nothing to gain from incorporation under the *Joint Stock Banking Act* or its sister legislation.[80] Consequently, the boom banks of the 1830s, the banks whose perceived failings motivated the passage of the *Joint Stock Banking*

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[78] "House Of Commons, Monday, July 22: Joint Stock Banks Regulation Bill," *The Times*, 23 July 1844; "London, Tuesday, July 23, 1844," *The Times*, 24 July 1844.
[79] Todd, "Some aspects of joint stock companies, 1844-1900," 49-50.
[80] Macleod, *The Theory and Practice of Banking*, II: 510.

Act in the first palace, avoided its regulations completely. They chose not to register under it.

The *Joint Stock Banking Act* may have been something of a dead letter but it influenced the English and Welsh banking industry nonetheless by discouraging the formation of new joint stock banks. Chapter Three explained that the *Bank Charter Act* denied new banks the right to issue bank notes after 1844.[81] This prohibition represented something of a barrier to entry to the industry in England and Wales but one could have surmounted it. A prohibition on new joint stock banks of issue in the Metropolis did not prevent the establishment of the London joint stock banks after 1833. Only the Bank of England issued bank notes in London.[82] In addition, some country banks had surrendered their rights to issue bank notes and were using bank notes issued by the Bank of England to conduct a deposit-taking business.[83] In theory, one could have erected a new joint stock bank of deposit in post-1844 England and Wales. The problem was that the promoters of such an enterprise would now have to register under the *Joint Stock Banking Act* and having jumped that hurdle, they would have to compete with established rivals that were not subject to the *Joint Stock Banking Act.* Those rivals could issue bank notes if they had been a bank of issue in 1844. In addition, those rivals hid their failings from public view because they were not obliged to publish their balance sheets. Finally, those rivals could increase their capital to issue more shares whenever their directors and shareholders deemed it necessary. Achieving success on a playing field as uneven as this seemed so unlikely that few even attempted it. One industry commentator

[81] 7 & 8 Victoria c. 32.
[82] Macleod, *The Theory and Practice of Banking*, II: 504.
[83] Schedule (C.) of 7 & 8 Victoria c. 32 identifies these banks.

complained, "The framers of the ... [*Joint Stock Banking Act*] … appear to have had in view the entire suppression of all attempts to establish future joint stock banks or they would not have passed such very stringent clauses."[84] Another wrote, "A more unfortunate specimen of legislation or one more entirely unsuitable to the nature of the business it related to has not emanated from parliament in recent times."[85] The flood of proposals to establish new joint stock banks turned into a trickle after 1844.[86] The *Joint Stock Banking Act* helped put an end to the joint stock banking boom by making it prohibitively difficult to establish a new bank.

The *Joint Stock Banking Act* imposed no constraints on the size or the geographic reach of a bank's branch network. In theory, banks remained at liberty to amalgamate with each other if they wished. However, Chapter Two explained the natural inclination of the English and Welsh banks granted rights to issue bank notes in 1844 was to retain their independence. The *Joint Stock Banking Act* of 1844 only made it easier for these banks to pursue such a course of action because a new joint stock competitor was not going to emerge in their districts to take business away from them. In *Lombard Street,* Walter Bagehot wrote of Sir Robert Peel, "Though he was exceedingly distrustful of the joint stock banks founded between 1826 and 1845, yet he was in fact their especial patron and he more than any other man encouraged and protected them."[87] The *Joint Stock Banking Act* kept the existing

[84] Lawson, *The History of Banking*: 331.
[85] Henry Dunning Macleod, *The Theory and Practice of Banking*, 4th ed., vol. II (London: Longmans, Green, Reader and Dyer, 1886), 388. This observation also appears in James William Gilbart, *The History, Principles and Practice of Banking*, vol. II (London: George Bell and Sons, 1907), 140.
[86] W. F. Crick and J. E. Wadsworth, *A Hundred Years of Joint Stock Banking* (London: Hodder and Stoughton Publishers, 1936), 27; Cottrell and Newton, "Banking liberalisation," 108.
[87] Walter Bagehot, *Lombard Street: A Description of the Money Market* (London: Henry S. King & Co., 1873), 252.

banks in business and the rate of bank amalgamations in England and Wales stalled after 1844.[88]

The *Joint Stock Banking Act* of 1844 did not improve the banking industry's corporate governance standards because most banks ignored it. To make matters worse, the banks that ignored it enjoyed the moratorium on the new competitors needed to drive a poorly administered bank out of business. Nevertheless, some bank promoters did manage to erect new joint stock banks under the auspices of the *Joint Stock Banking Act.* The failure of the Royal British Bank in 1856 dealt the *Joint Stock Banking Act* its final blow. Parliament repealed the *Joint Stock Banking Act* and its Irish and Scottish equivalent soon afterwards.

THE FAILURE OF THE ROYAL BRITISH BANK

Anyone studying English common law will encounter the 'indoor management rule,' a legal principle that states a party contracting with a joint stock company can assume its officers have complied with the company's constitution. The rule protects outsiders who cannot observe a company's inner workings. An outsider may assume a company's officers have done all it takes to acquire the legal authority needed to bind the company to a contract. The Court of Exchequer expressed the indoor management rule in *Royal British Bank v Turquand*, a case decided in the Royal British Bank's favour in 1856.[89] What a law student typically does not know is that this landmark decision did the Royal British Bank very little good. The bank collapsed soon afterwards.

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[88] Joseph Sykes, *The Amalgamation Movement in English Banking, 1825-1924* (London: P. S. King and Son, 1926), 18-29.

[89] (1856) 6 Ellis and Blackburn 327. See also: K. E. Lindgren, "History of the rule in *Royal British Bank v. Turquand*," *Monash University Law Review* 2, no. 1 (1975/76).

Established in 1849, the Royal British Bank was one of the few banks erected under the *Joint Stock Banking Act*.[90] It possessed the requisite capital of 1,000 shares valued at £100 each when it made its application to the Board of Trade. The bank issued all of its shares and collected half of their value before opening its headquarters at 52 Threadneedle Street in the City of London. In addition, the Royal British Bank reported its assets and liabilities every month and furnished audited accounts once a year. There was even a provision in the bank's constitution providing for its winding-up if a quarter of its capital were lost. Consequently, the Royal British Bank should have had a lot going for it. It had official recognition in the form of letters patent (hence the designation 'Royal' in its title), it reported on its operations to its creditors and shareholders diligently, it was well capitalised and its head office occupied a prestigious location in the City of London just a stone's throw from the Bank of England. None of this helped because the Royal British Bank stayed in business for just seven years. It suspended payments in September 1856.

Registration under the *Joint Stock Banking Act* of 1844 failed to render the Royal British Bank immune to poor management. The bank's promoters created it to fill a gap in the London banking market. Their intention was to use a deposit-taking business to fund overdraft lending. Unfortunately, the Royal accepted security on its

[90] For a review of the Royal British Bank and its collapse see: "The history as well as the affairs of the Royal British Bank," *The Times*, 13 March 1857; "The investigation into the affairs of the Royal British Bank," *The Times*, 29 April 1857; Anonymous, *The Curious and Remarkable History of the Royal British Bank Showing 'How He Got it Up' and 'How it Went Down' by One Behind the Scenes* (London: Effingham Wilson, 1857); Anonymous, "The trial of the directors of the Royal British Bank for conspiracy," in *The Annual Register or a View of the History and Politics of the Year 1858*, ed. Anonymous (London: F. & J. Rivington, 1859), 330-39; George Robb, *White-Collar Crime in Modern England: Financial Fraud and Business Morality, 1845-1929* (Cambridge: Cambridge University Press, 1992); James Taylor, "Company fraud in Victorian Britain: The Royal British Bank scandal of 1856," *The English Historical Review* 122, no. 497 (2007).

loans that no prudent banker would have deemed acceptable. Bad debts ate into the bank's paid-up capital. To make matters worse, the bank's administrators paid themselves generous wages that consumed paid-up capital too. The directors also helped themselves to the bank's funds, granting loans to themselves and their associates that they never disclosed to the shareholders. This failure to disclose exemplified the poor state of the Royal British Bank's financial reports. At the end of its life, the bank published fictitious accounts audited by two elected shareholders who lacked the experience needed to undertake the task. One of the auditors even had a conflict of interest because he ranked amongst those granted undisclosed loans. Consequently, the Royal British Bank's shareholders remained unaware of what was happening until it was too late to avert a disaster. The directors compounded the deceit by paying the shareholders generous dividends to create an illusion of profitability, which eroded the bank's capital further. The Royal British Bank had consumed all of its paid-up capital and more by the time it failed. Karl Marx (1818-1883) condemned the Royal British Bank's directors for "cheering on" their proprietors with "high dividends" and "fraudulent accounts."[91] The *Bankers Magazine* suggested "the Royal British Bank proves how utterly futile is the dependence upon … published and audited accounts … as the criterion of the prosperity or the solvency of a joint stock bank."[92]

The Royal British Bank's failure resulted in calls for its directors' conviction under the criminal law. *The Times* wrote, "In the annals of commercial fraud we have never heard or read of more outrageous acts of rascality than they have

[91] "What distinguished the present period of speculation in Europe is the universality of the rage," *New York Daily Tribune*, 9 October 1856.
[92] The Bankers' Magazine, "Rumoured banking difficulties," *The Bankers' Magazine and Journal of the Money Market* 1857, 6.

perpetrated against the customers and shareholders."[93] However, the directors' greatest failing was their exploitation of their positions to borrow from the bank. Consequently, those directors lacked the *mens rea* needed to secure convictions for larceny because they had intended to repay the funds borrowed. The authorities struggled to identify an appropriate charge upon which they might secure convictions. Eventually, the bank's falsified financial reports furnished a solution. The directors faced a charge of "conspiring to falsely represent the condition of the bank to the shareholders," a minor fraud offence that resulted in comparatively light sentences ranging from fines of one shilling to terms of imprisonment of up to a year.[94]

The Royal British Bank's failure showed that the *Joint Stock Banking Act* was no guarantor of sound banking practice. This bank failure also demonstrated that unlimited liability could rest upon uncertain foundations because this time the shareholders did not compensate the bank's creditors in full. The Royal British Bank's shareholders should have ranked amongst the directors' primary victims because it was a bank of unlimited liability. The directors deceived their shareholders to such an extent that they missed the opportunity to wind the bank up before it was too late to avoid significant loss. Some shareholders had even purchased new shares issued by the bank after it received approval from the Board of Trade to increase its capital.[95] None of those realities furnished a defence to the creditors' claim against the shareholders and the shareholders with the most to lose began to protect themselves. By May 1857, up to a third of the Royal British Bank's

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[93] "If a wretched shopboy filches a few shillings out of his master's till," *The Times*, 24 September 1856.
[94] Anonymous, "The trial of the directors of the Royal British Bank," 339.
[95] Taylor, "Company fraud in Victorian Britain," 703.

proprietors put their property beyond their creditors' reach by moving abroad.[96] The creditors faced a harsh reality. They could press their claims against the remaining shareholders, which would have entailed legal costs with no guarantee they would recover everything owed to them. Alternatively, the creditors could reach an agreement with the shareholders. The creditors took the latter course of action and accepted repayment of their debts at a rate of 15 shillings in the pound.[97]

The failure to compensate the Royal British Bank's creditors in full suggested those creditors might have been better off if Peel had followed Clay's advice in 1844 and permitted banks of limited liability basis. At the very least, limited liability would have put the creditors on notice that they might not recover the amounts owed to them. In 1857, the member for Newcastle-upon-Tyne, Thomas Emerson Headlam (1813-1875), observed that banks of unlimited liability failed. Banks of limited liability like the Bank of England, the three Scottish public banks and the Bank of Ireland appeared to stay in business no matter what.[98] Surely, their stability confirmed that banks of liability limited liability discouraged managerial malpractice because creditors exercised greater caution when they dealt with them. Headlam's opinion elicited no response initially although the Royal British Bank's failure did provoke two immediate legislative responses. First, the struggle to secure convictions against the bank's directors highlighted the criminal law's inability to deal with corporate fraud. Parliament created new offences designed to criminalise abuses of privilege like those perpetrated by the Royal British Bank's directors soon

[96] Taylor, "Company fraud in Victorian Britain," 708.
[97] Taylor, "Company fraud in Victorian Britain," 710.
[98] "House of Commons, Tuesday, July 21: Banking Bill," *The Times* 1857, 6.

afterwards.[99] Second, parliament repealed the *Joint Stock Banking Act* and its Irish and Scottish counterpart.[100] The legislation repealing the *Joint Stock Banking Act* ensured the banks remained a special case in one important respect. By now, companies in other industries could incorporate on a limited liability basis but joint stock banks were to remain creatures of unlimited liability for the time being.

LIMITED LIABILITY COMES TO BANKING

By the mid-1850s, some joint stock companies began to introduce limited shareholder liability by exploiting a legal back door. They inserted clauses into their contracts limiting their shareholders' liability for the debts incurred under those contracts and the courts started to recognise the validity of these clauses.[101] In addition, there was a view that unlimited liability disadvantaged the poor who needed some protection to encourage them to invest in joint stock companies and to form companies of their own.[102] A free trade argument also suggested that the market, not the parliament, should determine which form of liability was best. Britons should have the right to choose for themselves whether they wanted to contract with companies of limited or unlimited liability.[103] In 1855, parliament relented and embarked on a series of reforms that gave most British joint stock companies the right to adopt limited liability.[104] However, parliament remained steadfast in its determination to deny limited liability to the banking industry. The act repealing the

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[99] Taylor, "Company fraud in Victorian Britain."
[100] 20 & 21 Victoria c. 49.
[101] Gary M. Anderson and Robert D. Tollison, "The myth of the corporation as a creation of the state," *International Review of Law and Economics* 3, no. 2 (1983): 114.
[102] Donna Loftus, "Capital and community: Limited liability and attempts to democratize the market in mid-nineteenth-century England," *Victorian Studies* 45, no. 1 (2002).
[103] Robb, *White-Collar Crime in Modern England*: 25-26.
[104] Robb, *White-Collar Crime in Modern England*: 25-26. See also: 18 & 19 Victoria c 133, 19 & 20 Victoria c. 47, 20 & 21 Victoria c. 14, 20 & 21 Victoria c. 80.

Joint Stock Banking Act in 1857 denied banks the right to incorporate on a limited liability basis.[105] Within a year, that policy reversed.

Another financial crisis struck the banking system in 1857. This time the Western Bank of Scotland was one of the banks to succumb to the crisis. Thus, in 1858 a parliamentary Select Committee took evidence related to a major Scottish bank failure for the first time in living memory.[106] The degree of mismanagement uncovered at the Western Bank of Scotland only added to a growing sense that something had to change.[107] New legislation giving banks the right to incorporate on a limited liability basis soon passed into law.[108] This 1858 act imposed three obligations on a bank of limited liability. Its shareholders would remain liable on an unlimited liability basis for all bank notes issued, the minimum paid-up value of its shares would be £100 and the bank would publish a balance sheet at six monthly intervals. In 1862, parliament abolished the £100 minimum on limited liability bank shares.[109]

The editor of *The Economist,* Walter Bagehot, became one of the keenest advocates of the newly introduced regime of limited liability. Bagehot observed that no system of banking could be entirely safe.[110] There was an ever-present risk that

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[105] 20 & 21 Victoria c. 49.

[106] Sheffield Neave et al., *The Western Bank Failure and the Scottish Banking System: Being Evidence Thereon Given Before the Select Committee on the Bank Acts* (Glasgow: John Bain, 1858); Anonymous, *How to Mismanage a Bank: A Review of the Western Bank of Scotland* (Edinburgh: John & Charles Black and John Maclaren, 1859).

[107] "Mr Headlam returned with great ability and some success to the question of limited liability," *The Times*, 13 February 1858.

[108] 21 & 22 Victoria c. 91.

[109] 25 & 26 Victoria c. 89.

[110] Bagehot, "Sound banking."; Bagehot, "Unfettered Banking."; Bagehot, "The safest bank."; Bagehot, "Limited liability in banking I."; Walter Bagehot, "Limited liability in banking II," in *The Collected Works of Walter Bagehot*, ed. Norman St John-Stevas (London: The Economist, 1978). See

funds might be lost due to incompetence or fraud. The vital question was "what kind of bank is safest?"[111] Bagehot argued that in the small communities that typified Britain in the past, a small private banking partnership was safest. Those who dealt with a bank like this knew who owned it, how much property they had and could expect them to manage the bank diligently because they were responsible for its debts. In the urban environments that characterised post-Industrial Revolution Britain, a private banker acquired the capacity to deal with their property in relative anonymity. According to Bagehot, this was why joint stock banking became a necessity after 1826. The wealth supplied by the proprietors of a small bank might fluctuate but it was unlikely the collective wealth of a large number of shareholders could do the same. "Changes there will be," Bagehot wrote "but, in all probability, one will get richer, and another poorer."[112] A joint stock bank's great advantage was that its enlarged proprietorship secured the creditors' interests far better than a small common law partnership ever could.

A joint stock bank's enlarged proprietorship may have resolved one of the private bank's shortcomings. However, Bagehot thought joint stock banking created new opportunities for abuse. Bank officers could incur a loss and leave the shareholders to pick up the pieces. According to Bagehot, a joint stock bank's shareholders could employ two defences to alleviate the risks associated with this agency problem. The first was audited accounts, although Bagehot argued the failure

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also: Charles R. Hickson and John D. Turner, "Shareholder liability regimes in nineteenth-century English banking: the impact upon the market for shares," *European Review of Economic History* 7, no. 1 (2003); Charles R. Hickson and John D. Turner, "The trading of unlimited liability bank shares in nineteenth-century Ireland: The Bagehot hypothesis," *The Journal of Economic History* 63, no. 4 (2003).

[111] Bagehot, "Sound banking," 306.

[112] Bagehot, "Sound banking," 307.

of the Royal British Bank demonstrated that an audit would not prevent the manipulation of a bank's published reports.[113] The second defence was that shareholders only paid a portion of their wealth into the bank. The rest of the shareholders' wealth remained outside the bank where its administrators could not lose it.[114]

Bagehot's fundamental conviction was that the security unlimited liability accorded was beginning to unravel. The problem with unlimited liability was that no one could determine *a priori* exactly how much an individual shareholder would have to contribute when a bank failed. Everything depended on the size of a bank's losses in the first instance and then the amounts collected from all of the shareholders. According to Bagehot, wealthy shareholders had good reason to avoid shares in a joint stock bank under these circumstances because they had the most to lose. The observation was not new. Clay said much the same thing in 1836 and like him, Bagehot predicted bank shares would soon accumulate in the hands of poor shareholders who would demand their banks take risks. Bagehot wrote, "The system of *un*limited liability ... fosters the *most* speculative management. It is a system which makes bankers out of men ... who do not object to subject *all* their property to liability, because they have *no* property."[115] The key to establishing a secure basis for the banking system as far as Bagehot was concerned lay in enticing rich shareholders back into the industry. Unlimited liability could not do this as long as it drove the rich away but limited liability might because it offered certainty. "Rich

[113] Bagehot, "Sound banking," 308; Bagehot, "The safest bank," 347-48.
[114] Bagehot, "Sound banking," 308.
[115] Bagehot, "Limited liability in banking I," 397. Italics in original.

people would … see the *maximum* that they could lose and be able to estimate the worst," he wrote.[116]

Bagehot recognised that limited liability entailed risks too. Fully paid shares of limited liability rendered all the property available to secure the creditors' interests liable to loss. If the law held shareholders liable for partially paid shares instead, he reasoned, things would be different. The unpaid amount would remain with the shareholders where the bank's administrators could not lose it. Bagehot explained:

> It does not follow, because the liability of shareholders is defined, that the entire sum for which they are liable should be at the disposal of the directors. A man [sic] may be made liable for twice his investment capital or thrice: A shareholder may now invest £1,000 in a bank; the directors may call up the whole if they please and lose it if they so please; but the shareholder may now be answerable for another £1,000 or £2,000; the limit of the liability may be placed where we please; the essential point is that a limit should exist.[117]

Bagehot's belief was that an obligation to contribute uncalled capital under a regime of limited liability offered greater security than unlimited liability could. Unlimited liability encouraged poor shareholders with little to lose who would demand their banks take risks. Rich shareholders liable for uncalled capital, on the other hand, would demand conservative bank administration to limit the size of any contribution they would have to make if the bank failed. In addition, an obligation for uncalled capital imposed on rich shareholders would, Bagehot argued, make more property available to compensate the creditors because poor shareholders subject to unlimited liability had very little property to give.

[116] Bagehot, "The safest bank," 349. Italics in original.
[117] Bagehot, "The safest bank," 349.

The extraordinary feature of Bagehot's campaign in favour of limited liability in the banking industry was that it rested on a false premise. Rich shareholders were not abandoning the English and Welsh banking industry at the time. The Scottish corporate governance model adopted by the English and Welsh banks demanded bank directors monitor their shareholding constituencies to exclude the poor.[118] It seems English and Welsh bank directors fulfilled that obligation diligently because no evidence exists to suggest the wealth of an average shareholder declined when unlimited liability was the norm.[119] Very few English and Welsh banks saw a reason to take up limited liability after its introduction in 1858.[120] Similarly, none of the Scottish banks of unlimited liability felt any need to convert to limited liability under acts passed in 1858 or 1862.[121] Those who controlled most banks continued to believe subjecting wealthy shareholders to unlimited liability remained an indispensable source of competitive advantage. As late as 1880, the directors of the Liverpool Union Bank boasted their bank rested upon foundations supplied by "gentlemen of known wealth and standing who were … responsible to their last farthing."[122]

The industry's commitment to unlimited liability ran so deep that the few banks adopting limited liability attempted to replicate the advantages offered by unlimited liability by following Bagehot's advice in one important respect. In 1879, *The Times* noted that banks of limited liability generally called only a fraction of their shares'

[118] Anderson and Tollison, "The myth of the corporation as a creation of the state," 114-15.
[119] John D. Turner, "Wider share ownership? Investors in English and Welsh Bank shares in the nineteenth century," *The Economic History Review* New Series 62, no. S1 (2009).
[120] R. S. Sayers, *Lloyds Bank in the History of English Banking* (Oxford: Clarendon Press, 1957), 222; Turner, "Wider share ownership? Investors in English and Welsh Bank shares," 170.
[121] Carr, Glied, and Mathewson, "Unlimited liability and free banking in Scotland: A note," 975.
[122] Sayers, *Lloyds Bank in the History of English Banking*: 221.

value, which left their shareholders under an obligation to contribute significantly more if the bank failed.[123] The Birmingham Joint Stock Bank incorporated under the 1858 act. It issued shares with the requisite value of £100 value but they were paid to just £25. The Lloyds Banking Company adopted a similar arrangement in 1865. Lloyds incorporated under the 1862 act, which allowed it to divide its capital into shares of £50 called and paid to only £14/10/- per share. The arrangement put Lloyds' shareholders under an obligation to contribute another £35/10/- per share if the bank failed. The Bucks and Oxon Union Bank did essentially the same thing. Its shares had a nominal value of £25 paid to £5, which left the shareholders under an obligation to contribute another £20 per share if the bank failed.[124] All of these banks feared that a regime of limited liability would put them at a competitive disadvantage *vis-à-vis* a bank of unlimited liability. They followed Bagehot's advice to utilise the added security an obligation for a significant amount of uncalled capital offered.

The banking industry's reluctance to embrace limited liability persisted until the 1880s by which time the Amalgamation Movement was already underway. The Amalgamation Movement was yet to reach its peak, but a process of consolidation had begun nonetheless. Banks started to convert to limited liability in increasing numbers in the 1880s after another Scottish bank failure shook the industry's confidence in unlimited liability. The failure of the City of Glasgow Bank in 1878 exposed the dangers a regime of unlimited liability imposed. The City of Glasgow Bank's creditors received compensation in full but the security unlimited liability

[123] "It is understood that the leading directors of the joint-stock basks will hold a meeting to-day," *The Times*, 1 May 1879.
[124] Sayers, *Lloyds Bank in the History of English Banking*: 220-21.

accorded to them came at a high cost to the bank's shareholders. The City of Glasgow Bank ruined many of its shareholders.

THE FAILURE OF THE CITY OF GLASGOW BANK

Throughout its life, the City of Glasgow Bank adopted policies broadly similar to those utilised by the failed Western Bank of Scotland, another Glaswegian bank that collapsed in 1857.[125] Glasgow was Scotland's preeminent industrial city and as such, its merchants and manufacturers offered the Glaswegian banks many opportunities for growth. Banks like the Western Bank of Scotland and the City of Glasgow succumbed to the temptations on offer by tailoring their lending policies to the needs of their industrial and mercantile clientele. Unfortunately, the City of Glasgow Bank's lending also became increasingly concentrated until its capacity collect the amounts owed to it depended on the fortunes of a relatively small number of local borrowers. To make matters worse, the City of Glasgow Bank broke one of the cardinal rules of banking. It undertook long-term investments in faraway places that provided their returns slowly and proved difficult to sell at short notice even though most of the banks debts were payable at call. The bank's managerial hierarchy compounded the City of Glasgow Bank's difficulties by supplying falsified financial reports. They even misrepresented the state of City of Glasgow Bank's bullion reserve on the returns needed to comply with the currency legislation. The

[125]For a review of the City of Glasgow and its failure see: Anonymous, *Report of the Trial of the Directors of the City of Glasgow Bank Before the High Court of Judiciary Edinburgh* (Edinburgh: The Edinburgh Publishing Company, 1879); Kerr, *History of Banking in Scotland*: 217-26; Leo Rosenblum, "The failure of the City of Glasgow Bank," *The Accounting Review* 8, no. 4 (1933); Checkland, *Scottish Banking*: 469-77; Michael Collins, "The banking crisis of 1878," *The Economic History Review* New Series 42, no. 4 (1989); Greame G. Acheson and John D. Turner, "The death blow of unlimited liability in Victorian Britain: the City of Glasgow failure," *Explorations in Economic History* 45, no. 3 (2007); Thomas A. Lee, "'A helpless class of shareholder': Newspapers and the City of Glasgow Bank failure," *Accounting History Review* 22, no. 2 (2012).

City of Glasgow Bank eventually ran out of cash in October 1878 whereupon its 133 branches stopped making payments.

The City of Glasgow Bank was one of the largest banks of unlimited liability in Scotland. When the dust settled, its shareholders confronted a harsh reality. The City of Glasgow Bank's liquidator made a first call of £500 on shares with a nominal value of £100. Later, he made a second call of £2,250 per share. Only 250 shareholders out of 1,819 met both calls in full. The rest paid what they could and were ruined.[126] A report of a public meeting in November 1878 noted that the shareholders faced "destitution and bereavement" because the bank's debts would reduce many of them to "absolute and hopeless beggary."[127] One industry commentator claimed the loss of the City of Glasgow Bank "was a calamity so unlooked for, so huge and disastrous, that it riveted men's gaze and made their hearts stand still, and we shall all remember it to our dying day as a landmark in the history of our generation."[128] Those who held shares in the other joint stock banks throughout the United Kingdom and the directors who represented them saw the damage inflicted on the City of Glasgow Bank's shareholders and began to question whether unlimited liability was worth the risks it imposed.

The problem with conversion to limited liability under the limited liability legislation passed in 1862 was that nothing could stop a bank demanding its shareholders pay the unpaid amount on their shares after which the bank might lose

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[126] James William Gilbart and A. S. Michie, *The History, Principles and Practice of Banking*, vol. II (London: George Bell & Sons, 1893), 408; Checkland, *Scottish Banking*: 471; Lee, "'A helpless class of shareholder': Newspapers and the City of Glasgow Bank failure," 147.
[127] "The City of Glasgow Bank," *The Times*, 5 November 1878.
[128] Alexander Johnstone Wilson, *Banking Reform: An Essay on Prominent Banking Dangers and the Remedies they Demand* (London: Longmans, Green & Company, 1879), 46.

the all the capital available to secure the creditors interests. A bank could convert partially paid shares into fully paid shares by calling the unpaid amounts if it wished. Consequently, it seemed prudent to offer some sort of guarantee that a bank's directors could not call all of the capital available to secure its creditors' interests.[129] Parliament introduced legislation in 1879 that created a new form of limited liability known as 'reserved liability' tailored to the needs of the banking industry.[130] Parliament took a leaf out of Bagehot's book. The 1879 act attached two values to the shares issued by a bank of limited liability. The first was the share's nominal value, which represented the maximum the directors could demand from their shareholders during the bank's lifetime. This was the amount liable to loss. The second value remained with the shareholders because the bank could only call on it after it failed. The amount 'reserved' in this fashion was uncalled capital waiting for a liquidator to utilise it to reimburse a failed bank's creditors.

The fate of the City of Glasgow Bank's shareholders acted as a catalyst for change as joint stock banks throughout the British Isles converted to reserved liability. Most of London's joint stock banks converted to limited liability on a reserved basis in 1882.[131] Scotland's seven banks of unlimited liability converted in the same year.[132] By 1884, 80 of Britain's 138 joint stock banks had put a limit on their shareholders' liability to their creditors.[133] Initially, the added security reserved liability promised seemed so desirable that the Bank of Scotland, Royal Bank of

[129] The Economist, "Banks and limitation of liability (Article published 25 October 1879)," in *Select Statutes, Documents and Reports Relating To British Banking, 1832-1928*, ed. T. E. Gregory (London: Oxford University Press, 1929).
[130] 42 & 43 Victoria c. 76.
[131] Crick and Wadsworth, *A Hundred Years of Joint Stock Banking*: 34.
[132] Checkland, *Scottish Banking*: 481.
[133] Turner, "'The last acre and sixpence': Views on bank liability regimes in nineteenth-century Britain," 125.

Scotland and British Linen Company all tried to convert to it too.[134] These three banks owed their existence to special acts or royal charters that made no provision for a reserved amount on their shares whatsoever. Consequently, the three banks petitioned parliament for the legislation needed to reorganise their capital on a reserved liability basis only to discover that the government would insist they surrender one of their ancient privileges in return. All three would have to append the word 'Limited' to their names. More importantly, the Treasury asked the government to re-open the question of the Scottish bank note issue's regulation, whereupon the three public banks withdrew their request to reorganise their capital.[135] The three Scottish public banks need not have worried. Subsequent events showed that reserved liability bestowed far less of a competitive advantage than they feared. Subsequent events would show that shareholders resented the imposition of a reserved value on their shares.

The adoption of limited liability in the 1880s vindicated both Clay and Bagehot, although neither lived long enough to see it happen. Both anticipated that the composition of the bank industry's shareholder constituencies would change once limited liability became commonplace. They were right, although the change ran in the opposite direction to the one they predicted. The rich did not flood into the banks' shareholding constituencies as they predicted. Clearly, a shareholder's wealth mattered even under the regime of limited or reserved liability because shareholders had to be wealthy enough to meet the obligation for uncalled capital. However,

[134] "The Scotch banks," *The Times*, 19 November 1880; Gilbart and Michie, *The History, Principles and Practice of Banking*, II: 445-53; Checkland, *Scottish Banking*: 481; M. Gaskin, "Anglo-Scottish banking conflicts, 1874-1881," *The Economic History Review* New Series 12, no. 3 (1960): 444-45.
[135] "Scotch banking," *The Times*, 22 July 1881; Gilbart and Michie, *The History, Principles and Practice of Banking*, II: 445-55.

limited liability offered the richest shareholders protection by placing a limit on the maximum amount they would have to contribute if a bank failed. Consequently, limited liability gave bank directors the freedom to admit less wealthy middle class shareholders into their shareholding constituencies in increasing numbers. The total number of individuals deemed wealthy enough to own bank shares in England and Wales changed little under the regime of unlimited liability. It was 22,031 in 1849 and 22,980 in 1859. This figure rose after limited liability became available in 1858 and stood at 65,528 by 1879. The widespread adoption of limited liability saw it rise again to reach 125,859 by 1899. The vast majority of the newly admitted shareholders came from the middle classes.[136]

Both Joplin and Clay had promised that banks of limited liability would become more reliant on capital supplied by their shareholders to fund their operations.[137] However, an unexpected development accompanied the influx of capital from the middle classes because the banks admitting them economised on the amounts they raised from their shareholders. The banks of limited liability became more reliant on their creditors to fund their operations.[138] In the 1850s, an average English and Welsh joint stock bank borrowed £5 for every £1 invested in it by its shareholders although there was substantial variation amongst the banks.[139] Larger banks borrowed more heavily than smaller ones because their creditors thought they were safer. By the late nineteenth century, the largest banks' higher debt ratios

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[136] Turner, "Wider share ownership? Investors in English and Welsh Bank shares in the nineteenth century," 172-77.

[137] Joplin, *The Principle of the Personal Liability of the Shareholders in Public Banks Examined*; Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks*.

[138] Sykes, *The Amalgamation Movement in English Banking*: 100-15.

[139] Michael Collins, "The business of banking: English bank balance sheets, 1840–80," *Business History* 26, no. 1 (1984): 48-49.

became the norm as the Amalgamation Movement fostered an increase in average bank size.[140] In 1909, the chair of the London and Westminster Bank made a startling admission to his shareholders. He claimed the London and Westminster was disadvantaging them because it had taken too much capital from them. Walter Leaf told his shareholders:

> Some of you may remember, as I well do, the downfall of the City of Glasgow Bank in 1876 [a voice: 1878, Sir], and the disastrous ruin which it brought upon hundreds of innocent shareholders…. At that time, limitation of liability was a thing unheard of in bank shares; but in the panic of that year … made it evident that a change was imperative. The lead was taken, as was right and proper, by the Westminster, which was the first to venture into putting the word "Limited" at the end of its name. The Board of the day very properly made the credit of the bank their first consideration, and, not knowing how the public would view a step of such startling novelty, coupled it with an increase in paid-up capital, from £2,000,000 to £2,800,000. There was no corresponding increase in business, and the result is that since that time our capital has stood at a figure of from 10 to 12 per cent of our liabilities….
>
> This was a very cautious figure … but events have proved that it was over-caution, which has hampered us ever since…. Other banks followed our lead; but, profiting by our experience, they fixed their capital at much lower proportionate figures and if you will go through the list, you will find that our competitors generally have paid-up capital ranging from about 4 per cent to 7 per cent of their liabilities to the public. …I will quote only the case of the [London and] County. While in our last statement, our paid-up capital represented 11 per cent of our liabilities that of the County was under 5 per cent….
>
> Now consider the effect of our disproportionately large capital … it means a lower rate of dividends; and this means a smaller premium on our shares. Whilst a County share is today worth over four and a half times its nominal value, ours are worth only two and a half times.[141]

The London and Westminster Bank's directors overestimated the importance of paid-up capital when the bank converted to limited liability in the 1880s. An amalgamation in 1909 with the London and County Bank corrected the mistake. The

[140] Collins, "The business of banking," 48-49.
[141] London and Westminster Bank, "Report on the proceedings at the extraordinary general meeting held at the bank, Lothbury, London E.C. on Friday August 6th 1909 Walter Leaf esquire in the chair," (Royal Bank of Scotland Archive (LWB/113), 1909), 5-7.

London and Westminster Bank's shareholders exchanged their shares for shares issued by the London and County Bank because the latter bank's capital was "more favourably arranged" according to Leaf.[142]

The English and Welsh banks' increasing reliance on debt is a paradox. The industry's depositors and its other creditors allowed their banks to become increasingly indebted to them at a time when the industry limited its shareholders' obligations to them. Perhaps Bagehot was right on one point after all. Maybe an obligation for reserved and uncalled capital imposed on an enlarged shareholding constituency really did make more property available to secure the creditors' interests than a regime of unlimited liability ever could have done. However, such an argument is hard to sustain. Shares carrying liability for uncalled capital or reserved capital proved unpopular with shareholders who already stood to lose what they paid for their shares and did not relish the prospect of having to contribute more. In 1912, Barclay and Company rearranged its share capital to issue fully paid shares with no uncalled or reserved value attached to them whatsoever. The new shares proved an instant success.[143] The obligation for uncalled and/or reserved capital on a typical bank share ran as high as three times the amount paid for it when the banks converted to limited liability in the 1880s. That obligation had dwindled to virtually nothing by 1920s.[144]

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[142] London and Westminster Bank, "Report on the proceedings at the extraordinary general meeting," 7.
[143] "Barclay's Bank capital rearrangement," *The Times*, 21 November 1912; "Banking in 1913," *The Times*, 16 January 1913.
[144] Walter Leaf and Ernest Sykes, *Banking*, Third ed. (London: Thornton Butterworth, 1937), 113-14; Turner, "'The last acre and sixpence': Views on bank liability regimes in nineteenth-century Britain," 125-27.

A share swap negotiated as the purchase consideration in a bank amalgamation was all it took to relieve disgruntled shareholders of their obligation for uncalled and reserved capital. Consequently, the Amalgamation Movement resulted in a progressive withdrawal of the obligation for uncalled and reserved capital. The development went largely unnoticed until the Treasury Committee on Bank Amalgamations drew attention to it in 1918.[145] When the National Provincial Bank acquired the Union of London and Smiths Bank in 1918, for example, the liability to contribute additional capital imposed on the Union's shareholders fell by "over 48 per cent."[146] In the same year, the London County and Westminster Bank's amalgamation with Parr's Bank reduced the "uncalled liability" imposed on Parr's shareholders by "17 per cent."[147] An amalgamation between the London City and Midland Bank and the London Joint Stock Bank more than halved "the uncalled liability of [London] Joint Stock Bank shareholders."[148] The obligation for uncalled and reserved capital suffered a similar fate to the London and Westminster's cautious debt to equity ratio. Uncalled and reserved capital were reminders of a time when the banks feared the conversion to limited liability and demanded too much of their shareholders. The Treasury Committee on Bank Amalgamations pointed to the withdrawal of paid-up, uncalled capital and reserved capital to accuse the

[145] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," in *Select Statutes, Documents & Reports Relating to British Banking, 1832-1928*, ed. T. E. Gregory (London: Oxford University Press, 1929), 329.
[146] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 329.
[147] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 329.
[148] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 329.

Amalgamation Movement of having created “substantial benefits to shareholders at the expense of ... security” for their creditors.[149]

The banking industry’s creditors should have boycotted the banks imposing the risks alluded to by the Treasury Committee on Bank Amalgamations. Creditors could have given a competitive advantage to the banks with the lowest debt to equity ratios and whose shareholders carried the highest obligations for uncalled and reserved capital by transferring their business to them. Instead, most of the industry’s creditors patronised a small number of large English and Welsh banks that became increasingly indebted to them and withdrew the security accorded by uncalled and reserved capital.[150] It is possible that these creditors had no choice and had to accept the changes the Amalgamation Movement imposed. After all, the banks with lowest debt ratios and the highest liability for uncalled and reserved capital were the ones that disappeared. However, it is also possible that the Treasury Committee on Bank Amalgamations overestimated the risks the Amalgamation Movement imposed because no one lost so much as a penny as the result of the failure of one of the Big Five English and Welsh banks after 1918.[151] The next section argues the banking industry’s creditors tolerated the rising debt ratios and the reduction in liability for uncalled and reserved capital because bank amalgamations yielded inherently safer banks.

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[149] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations," 329-30.

[150] Forrest Capie and Ghila Rodrik-Bali, "Concentration in British banking, 1870-1920," *Business History* 24, no. 3 (1982): 287.

[151] Richard S. Grossman, "The shoe that didn't drop: Explaining banking stability during the Great Depression," *The Journal of Economic History* 54, no. 03 (1994).

HOW AMALGAMATIONS MADE BANKS SAFER

The banks of limited liability borrowed more heavily from their creditors at a time when they had released their shareholders from the obligation to secure their creditors' interests. These developments would have imposed greater risk on those creditors, but the banks compensated for the changes by redirecting a larger proportion of their resources into liquid assets.[152] Lending on bills of exchange, short-term loans and overdrafts accounted for approximately three quarters of all English and Welsh bank assets in the 1860s and 1870s. By the outbreak of World War I, that ratio had fallen to approximately 55 per cent.[153] This reduction in the rate of commercial lending released funds for investment elsewhere and a significant portion of the funds liberated financed an increase in cash, deposits with the Bank of England, money deposited at call with the London money market and government securities. Liquid assets like these constituted 30 per cent the English and Welsh banks' total assets in the 1870s. By 1914, that ratio had risen to 40 per cent.[154] These liquid assets enhanced the banking system's capacity to weather any financial crisis.[155]

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[152] Mae Baker and Michael Collins, "Financial crises and structural change in English commercial bank assets, 1860–1913," *Explorations in Economic History* 36, no. 4 (1999); Michael Collins and Mae Baker, "Sectoral differences in English bank asset structures and the impact of mergers, 1860-1913," *Business History* 43, no. 4 (2001); Michael Collins and Mae Baker, "English commercial bank liquidity, 1860–1913," *Accounting, Business & Financial History* 11, no. 2 (2001); Michael Collins and Mae Baker, *Commercial Banks and Industrial Finance in England and Wales, 1860-1913* (Oxford: Oxford University Press, 2003).

[153] Baker and Collins, "Financial crises and structural change in English commercial bank assets."; Collins and Baker, "Sectoral differences in English bank asset structures and the impact of mergers."; Collins and Baker, "English commercial bank liquidity."

[154] Baker and Collins, "Financial crises and structural change in English commercial bank assets," 435-38. See also Charles Albert Eric Goodhart, *The Business of Banking, 1891-1914* (London: Weidenfeld and Nicolson, 1972), 95-117; Forrest Capie and Michael Collins, "Industrial lending by English commercial banks, 1860s–1914: Why did banks refuse loans?," *Business History* 38, no. 1 (1996); Collins and Baker, "Sectoral differences in English bank asset structures and the impact of mergers."

[155] "Sir Edward Holden on banking," *The Times*, 4 November 1913.

The Amalgamation Movement encouraged the trend towards greater security by removing those that could not adapt to a new corporate governance realities imposed by the conversion to limited liability. An article published in the *Bankers Magazine* written by a Fellow of the Institute of Bankers noted that bank amalgamations nearly always promoted lending practices that were more conservative.[156] Those who were used to negotiating loans with a small institution that depended upon their patronage were often shocked to discover that a larger bank with more customers to lend to could demand greater security from them. Borrowers who complied with the demand for greater security received financial accommodation commensurate with the extra security they provided. Those who did not provide sufficient security soon discovered that an enlarged bank could deny them credit.[157] More telling was Collins and Baker's discovery that the Amalgamation Movement's predators generally possessed higher liquid asset ratios than their targets.[158] In other words, a greater commitment to liquid assets differentiated the banks taking other banks over from the banks taken over during the Amalgamation Movement. London's joint stock banks possessed the highest liquid asset ratios in England and Wales. Unsurprisingly, London's banks ranked amongst the most Amalgamations Movement's most active predators.[159]

Unlimited shareholder liability was no barrier to bank amalgamations. Amalgamations undertaken under conditions of the old regime of unlimited liability

[156] The article is reproduced in Francis E. Steele, *Present Day Banking: Its Methods, Tendencies and Practices* (London: Butterworth, 1909), 27-35.
[157] Steele, *Present Day Banking*: 34-35.
[158] Collins and Baker, "Sectoral differences in English bank asset structures and the impact of mergers," 11-19.
[159] Collins and Baker, "Sectoral differences in English bank asset structures and the impact of mergers," 18-19.

were a common feature of Scottish banking practice during the nineteenth century.[160] In England and Wales, the Amalgamation Movement was about to embark on its second decade when the banks converted to limited liability in greater numbers.[161] Banks of unlimited liability could and did amalgamate with each other. However, the regime of unlimited liability secured their creditors' interests.[162] The regime disappeared because unlimited liability became unpopular with the proprietors who were guaranteeing the banking industry's debts. When a bank converted to a regime of limited liability therefore, it relieved its proprietors of an unwanted burden whilst putting its creditors at greater risk. A newly converted bank of limited liability had to accumulate liquid assets to maintain its creditors' confidence under these circumstances. A bank that could not do both (convert to limited liability and accumulate adequate reserves) operated at a competitive disadvantage. Either it imposed unwanted risks on its proprietors by remaining a creature of unlimited liability or it put its creditors at risk by becoming an under-resourced bank of limited liability. Many banks resolved this agency problem by amalgamating with a better-resourced rival. Such an amalgamation gave the target's proprietors the protection they craved because they emerged from the amalgamation with shares in a predator that had converted to limited liability. In addition, the predator's liquid assets offered the target's creditors the security they demanded. This was why the Amalgamation Movement accelerated following the industry's conversion to limited liability.

[160] Checkland, *Scottish Banking.*
[161] Sykes, *The Amalgamation Movement in English Banking.*
[162] John D. Turner, *Banking in Crisis: The Rise and Fall of British Banking Stability, 1800 to the Present* (Cambridge Cambridge Univeristy Press, 2014).

Changes in financial reporting practices enhanced the tendency to remove from the industry weak banks that failed to invest in liquid assets. Banks began to publish their balance sheets, which exposed their potential failings to their rivals and to the public. The banks registered under the reserved liability act of 1879 were subject to an obligation to produce audited accounts.[163] Of course, the demand banks produce audited financial statements was nothing new although audited accounts had proven virtually worthless in the 1850s when the Royal British Bank failed.[164] However, joint stock companies were now far more common in Britain than at any time in the past and their reporting obligations to their shareholders created a growing demand for professional auditors.[165] The Scots led the way by forming their first professional accounting body as early as 1854.[166] In 1870, the Institute of Chartered Accountants in England and Wales also came into being.[167] After that, financial statements audited by an independent, qualified and experienced accounting professional became increasingly common. The published accounts demanded by the 1879 act proved so useful that banks not registered under the act came under pressure to furnish them too after the merchant banking house of Bearing Brothers came close to collapse in 1890.[168] The Chancellor of the Exch equer, George Goschen (1831-

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[163] Stephen P. Walker, "More sherry and sandwiches? Incrementalism and the regulation of late Victorian bank auditing," *Accounting History* 3, no. 1 (1998).
[164] The Bankers' Magazine, "Rumoured banking difficulties," 6.
[165] Watts and Zimmerman, "Agency problems, auditing, and the theory of the firm," 630-31; Robert Henry Parker, "Regulating British corporate financial reporting in the late nineteenth century," *Accounting, Business & Financial History* 1, no. 1 (1990); Brian P. West, "The professionalisation of accounting: A review of recent historical research and its implications," *Accounting History* 1, no. 1 (1996).
[166] Stephen P. Walker, "The defence of professional monopoly: Scottish chartered accountants and “satellites in the accountancy firmament” 1854–1914," *Accounting, Organizations and Society* 16, no. 3 (1991).
[167] Harold Howitt, *The History of the Institute of Chartered Accountants in England and Wales, 1870-1965* (Garland, 1984).
[168] Alec Ford, "Argentina and the Baring Crisis of 1890," *Oxford Economic Papers* New Series 8, no. 2 (1956).

1907), responded with a call for greater transparency in the banking industry.[169] The private banks heeded Goschen's warning and started to supply balance sheets voluntarily before he and the government intervened. By 1892, *The Economist*'s half-yearly banking supplements displayed the balance sheet statistics of almost every bank (both private and joint stock) in the county.[170]

The Amalgamation Movement had one last card to play in its pursuit of greater security by subjecting the English and Welsh bank employees to controls designed to eliminate the risk of loss caused by fraud, misconduct or incompetence. The risks imposed by the industry's employees diminished of their own accord as the English and Welsh banks became more familiar with the realities of joint stock banking.[171] Employee conduct became an insurable risk as bank employees stopped relying on relatives and associates to guarantee their good conduct and began to enlist the services of a guarantee and suretyship association to perform the same function. Some banks found the new arrangement so useful that they established guarantee and suretyship funds of their own.[172] Greater professionalism reduced the supervisory burdens employees imposed on the banks even further. The Scots established the Scottish Institute of Bankers in 1875 and its English and Welsh counterpart emerged soon afterwards in 1879. Both organisations adopted an educational role by instituting a system of examinations and awarding qualifications to those who passed

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[169] "Mr Goschen at Leeds," *The Times*, 29 January 1891; "Mr Goschen's ideas on currency," *The Spectator*, 31 January 1891; George Joachim Goschen, "Our cash reserves and central stock of gold: Speech delivered at a banquet of the Leeds Chamber of Commerce, 28 January 1891," in *Essays and Addresses on Economic Questions (1865-1893) With Introductory Notes (1905) by the Right Honourable Viscount Goschen*, ed. George Joachim Goschen (London: Edward Arnold, 1905).

[170] Goodhart, *The Business of Banking, 1891-1914*: 13.

[171] Steele, *Present Day Banking*: 30-32.

[172] Guarantee and suretyship amounted to employee insurance. The association received a periodic payment from the employee. In return, it undertook to compensate the employer for any liable for compensation imposed by the employee. See: Gilbart and Michie, *The History, Principles and Practice of Banking*, II: 16-18, 99-101.

them.[173] The risks posed by a large geographically dispersed branch network diminished as employees became less prone to error.

The Amalgamation Movement contributed to the tendency towards greater professionalism by putting country bank employees under the control of an efficient bureaucracy. As the *Bankers' Magazine* observed in 1903, the banking industry's control systems became increasingly impersonal and bureaucratic as banks grew in size during the Amalgamation Movement:

> In the old days of banking ... an energetic bank would be content with a head office and ten or a dozen branches, Under these conditions the board [of directors] and general manager were able to maintain direct control over the whole business of the bank, without any elaborate system for such supervision. When, however, one bank has over 400 offices, it is easy to see that the old rough-and-ready systems of management would fall short of the necessities of the case. A general manager might look closely into ... the business conducted in ten or a dozen offices, but ... he cannot have the same intimate personal acquaintance with the transactions proceeding in hundreds of offices.[174]

Regional bank employees used to a small bank's informal control systems employees found themselves subject to the expectation that they compile returns and reports for head office. These employees encountered an expanding bureaucracy's "red tape" for the first time.[175] Rulebooks introduced during the early twentieth century added yet another layer of bureaucratic control. Lloyds Bank put all of its employees under an obligation to report "any fraud, error or underhand practice" that came to their

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[173] Edwin Green, *Debtors to Their Profession: A History of the Institute of Bankers, 1879-1979* (London: Routledge, 1979), 49-73; Youssef Cassis, "Bankers in English society in the late nineteenth century," *The Economic History Review* New Series 38, n o. 2 (1985): 227; Youssef Cassis, "The banking community of London, 1890–1914: A survey," *The Journal of Imperial and Commonwealth History* 13, no. 3 (1985): 119.

[174] The Bankers' Magazine, "The London City and Midland Bank Limited," *The Bankers' Magazine and Journal of the Money Market* 1903, 9-10.

[175] Steele, *Present Day Banking*: 31.

"knowledge or of which" they "may have suspicions."[176] Lloyds also forbade its employees the right to marry before their income reached a level that could support a family, the right to guarantee another person's debts without the directors' approval and the right to gamble or engage in any other "speculative dealings."[177] Non-compliance with these rules would result in dismal.[178] Impositions on the employees' private lives like these removed the temptation to engage in fraud by denying them the option of getting into financial difficulties.

Scottish experience suggested the banking industry had always constituted a congenial host for large firms subject to bureaucratic control. Adam Smith distrusted joint stock enterprises implicitly because those who established them under a special act or royal charter usually demanded monopolistic privileges to compensate for the agency problems imposed by a separation of ownership and control.[179] However, Smith noted that joint stock enterprises needed few privileges in industries like banking where "operations are capable of being reduced ... to a routine or ... uniformity of method."[180] Smith wrote:

> Though the principles of the banking trade may appear somewhat obtuse, the practice is capable of being reduced to strict rules. To depart on any occasion from those rules ... is ... extremely dangerous, and frequently fatal.... The principle banking companies in Europe, accordingly, are joint stock companies, many of which manage their trade very successfully without any exclusive privilege. The Bank of England has no other exclusive privilege, except that no other banking

[176] Lloyds Bank Limited, "Book of Rules Approved by the Board of Directors," (Lloyds Bank Archive (Ho/1/Rul/2.0), 1906), 13; Lloyds Bank Limited, "Book of Rules Approved by the Board of Directors," (Lloyds Bank Archive (Ho/1/Rul/3.0), 1908), 14.
[177] Lloyds Bank Limited, "Book of Rules Approved by the Board of Directors," 14-16; Lloyds Bank Limited, "Book of Rules Approved by the Board of Directors," 14. The Midland Bank imposed similar rules. See: Youssef Cassis, *City Bankers, 1890-1914* (Cambridge: Cambridge University Press, 1994), 136.
[178] Lloyds Bank Limited, "Book of Rules Approved by the Board of Directors," 14-16; Lloyds Bank Limited, "Book of Rules Approved by the Board of Directors," 14.
[179] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, II: 245-82.
[180] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, II : 279.

> company in England [and Wales] shall consist of more than six persons. The two banks of Edinburgh[181] are joint stock companies without any exclusive privilege.[182]

Smith thought bureaucracy made a joint stock banking company inherently safe by constraining its emplyees' freedom of action. According to Smith, banks could utilise bureaucratic controls to eliminate self-interested behaviour because the exercise of employee discretion in this industry was both unnecessary and dangerous.

The organisational structures adopted by the Big Five enforced the rules imposed on a bank's employees. The London City and Midland Bank's organisational structure demanded branch managers report to district superintendents, who reported to regional joint general managers, who reported to the managing director and the chair of the board of directors.[183] In 1903, the London City and Midland Bank deployed three regional joint general managers to supervise the South of England, the North of England and London.[184] The workload imposed upon these regional joint general managers must have increased as the Amalgamation Movement progressed and number of branches under their jurisdiction increased. By the late 1920s, the number of regional joint general managers at the Midland Bank had doubled to six, although in all other respects the bank's organisation structure remained unchanged.[185] Every branch manager at the Midland Bank possessed limited authority to grant credit and needed the approval from the district superintendent to exceed those limits. These superintendents had limits as to how

[181] The two banks of Edinburgh were the Bank of Scotland and the Royal Bank of Scotland.
[182] Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, II: 279.
[183] Yoshiro Kamitake, "Some notes on the life and works of Sir Edward Holden," *Hitotsubashi Journal of Economics* 23, no. 3 (1983): 50.
[184] The Bankers' Magazine, "The London City and Midland Bank Limited," 13.
[185] Luther A. Harr, *Branch Banking in England* (Philadelphia: University of Pennsylvania Press, 1929), 84. The six regions were London City, London, Lancashire and Liverpool, the Midlands, Yorkshire and Wales.

much additional credit they could approve and could only exceed them with the approval of their regional joint general manager. Regional joint general managers operated under lending limits too and could only exceed them with the consent of the managing director and chair of the board of directors.[186] The result was an organisational structure in which the authority for the one of the most important operational decision made (how much the bank lent) 'pyramided' as one moved up the organisational hierarchy. The arrangement ensured the bank retained enough funds in reserve to accumulate the liquid assets needed to placate its creditors.[187] An accounting system subject to random internal audits undertaken by branch inspectors provided all the information the Midland Bank's head office needed to coordinate its activities. Branches reported their cash balances, deposits, advances, overdrafts, other assets and liabilities at intervals ranging from daily to yearly depending upon how critical they were to the bank's success.[188]

CONCLUDING REMARKS

The Amalgamation Movement resolved the agency problems that dogged the English and Welsh banking industry since the introduction of joint stock banking in 1826. Prior to the Amalgamation Movement, a regime of unlimited liability put the industry's shareholders at risk by making them the guarantors of the good conduct of those who administered the industry. A bank's shareholders had to compensate their bank's creditors when it failed. However, the failure of the City of Glasgow Bank in

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[186] Harr, *Branch Banking in England*: 88; Board of Governors of the Federal Reserve System (United States), "Branch banking in England," (Fraser Federal Reserve Archive (oclc: 10702515), 1932), 24-27.

[187] Harr, *Branch Banking in England*: 110-13; Board of Governors of the Federal Reserve System (United States), "Branch banking in England," 26.

[188] The Bankers' Magazine, "The London City and Midland Bank Limited," 10-12; Harr, *Branch Banking in England*: 91-92, 95-96,110-13; Board of Governors of the Federal Reserve System (United States), "Branch banking in England," 27.

1878 demonstrated that shareholders could no longer bear the burdens imposed upon them. The industry subsequently converted to limited liability, which made the security of a bank an even more important source of competitive advantage.

The Amalgamation Movement facilitated a withdrawal of the burdens imposed on shareholders by reducing their obligation to supply paid-up and uncalled capital. The banks that asked too much of their shareholders disappeared. This development should have put creditors at risk but the Amalgamation Movement facilitated an investment in liquid reserves that ultimately secured the interests of the industry's creditors. The banks that made the greatest investment in reserves became the Amalgamation Movement's predators. In addition, bank amalgamations put the industry's employees under a system of bureaucratic control that eliminated the risk of fraud and error by constraining their freedom of action.

The next chapter considers whether the need to build the banking system on a secure foundation turned British banking into a natural oligopoly in which new entrants and small banks had no chance of survival.

CHAPTER SIX

IS BRITISH BANKING A NATURAL OLIGOPOLY?

> In Scotland, the growth of banking has been extremely gradual.... At present, there are but 17 distinct establishments in the country, but these have 460 branches extending into every village in the kingdom.... To suppose the English system of joint stock banking bore any similarity to this would be the most egregious fallacy, and it was this difference chiefly which led to those disastrous consequences which are too well-known to need repeating.[1]

> If you apply from North of the Tweed, don't say that having discharged … all of the duties of a branch in a Scotch village, you feel competent to undertake *any* duties at the head office of a London bank.[2]

Scotland conducted an experiment in banking that set a precedent for the rest of mainland Britain. Scotland's parliament established the Bank of Scotland in 1695 with the intention that it would be a commercial venture that performed few favours for the state.[3] The Bank of Scotland lent none of its capital to the crown, which meant that when Scotland joined the union with England and Wales the authorities in Westminster had little reason to protect it. Consequently, the Hanoverian regime granted a royal charter in 1727 that incorporated the Royal Bank of Scotland.[4] Within two decades, a third incorporated joint stock institution emerged as the British Linen Company began to exploit an industrial charter to conduct a banking business of its own.[5] In addition, Scottish law took a permissive attitude to large

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[1] Henry Dunning Macleod, *The Theory and Practice of Banking: With Elementary Principles of Currency; Prices; Credit; and Exchanges*, vol. II (London: Longman, Brown, Green and Longmans, 1856), 516.
[2] Francis E. Steele, *Present Day Banking: Its Methods, Tendencies and Practices* (London: Butterworth, 1909), 202. Italics in original.
[3] S. G. Checkland, *Scottish Banking: A History, 1605-1973* (Glasgow: Collins, 1975), 24-33.
[4] Andrew William Kerr, *History of Banking in Scotland* (Glasgow: David Bryce & Son, 1884), 34-43.
[5] Checkland, *Scottish Banking*: 92-97.

unincorporated businesses founded on the joint stock principle.[6] These unincorporated businesses possessed a workable legal personality and could issue transferrable shares. The result was a generation of provincial joint stock banking companies erected during the eighteenth century followed by the establishment of the Commercial Bank of Scotland in 1810. This latter institution that had genuinely national aspirations and the Commercial Bank of Scotland's success furnished a precedent that the National Bank of Scotland followed in 1825, as did several other newly established large banks in the 1830s.[7]

Scotland never really experienced an outbreak of bank mergers and acquisitions as dramatic as the English and Welsh Amalgamation Movement because a tendency to amalgamate had always been an inherent feature of joint stock banking as practiced in Scotland.[8] The Scottish banking industry became increasingly concentrated over a prolonged period. By 1850, Scotland only had 17 joint stock banks left open for business. Fifteen years later, that number of had fallen to just 12.[9] No legal restriction or prohibition intervened to inhibit this gradual process of consolidation in Scotland. Scottish banks were not subject to a six-partner limit that shielded the Bank of England from competition in England and Wales prior to 1826

[6] Graeme G. Acheson, Charles R. Hickson, and John D. Turner, "Organisational flexibility and governance in a civil-law regime: Scottish partnership banks during the Industrial Revolution," *Business History* 53, no. 4 (2011).
[7] S. G. Checkland, "Banking history and economic development: Seven systems," *Scottish Journal of Political Economy* 16, no. 1 (1969): 144-54; Charles W. Munn, "Scottish provincial banking companies: An assessment," *Business History* 23, no. 1 (1981); Charles W. Munn, *The Scottish Provincial Banking Companies, 1747-1864* (Edinburgh: John Donald, 1981); Charles W. Munn, "The emergence of joint-stock banking in the British Isles a comparative approach," *Business History* 30, no. 1 (1988).
[8] The Bankers' Magazine, "The union of English banking companies prevented by the Bank Act of 1844," *The Bankers' Magazine and Journal of the Money Market*, November 1849, 625-28.
[9] Checkland, *Scottish Banking*: 372-73, 524.

for example.[10] Furthermore, two amalgamating Scottish banks could aggregate their rights to issue bank notes granted under the currency legislation introduced after 1845.[11]

The English and Welsh banking industry could not have replicated the larger banks found in Scotland prior to the Amalgamation Movement. The six-partner limit imposed to protect the Bank of England was an obvious inhibitor of bank size prior to 1826. However, it is doubtful whether the English and Welsh banks could have been much larger than they were during this period even if the six-partner rule had not applied. English common law demanded that every bank other than the Bank of England litigate in the names of all of their proprietors. The only way around this inconvenience was to obtain a special act that bestowed a legal personality.[12] In addition, clause 18 of the *Bubble Act* of 1720 could have rendered the promoters of large English and Welsh banks liable to criminal prosecution had they chosen to issue transferable shares.[13] Consequently, the repeal of the six-partner rule in 1826 was not the only facilitator of joint stock banking in provincial England and Wales. The repeal of clause 18 of *Bubble Act* in 1825 made it lawful to issue transferable shares whilst the *Country Bankers Act* gave every bank erected under it a legal personality. Both developments played their part in making joint stock banking possible in the English and Welsh provinces.

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[10] Macleod, *The Theory and Practice of Banking*, II: 519; Henry Dunning Macleod, *The Theory and Practice of Banking*, 4th ed., vol. II (London: Longmans, Green, Reader and Dyer, 1886), 394.

[11] The Bankers' Magazine, "The union of English banking companies prevented by the Bank Act of 1844."

[12] Henry N. Butler, "General incorporation in nineteenth century England: Interaction of common law and legislative processes," *International Review of Law and Economics* 6, no. 2 (1986): 173-74.

[13] Armand Budington DuBois, *The English Business Company after the Bubble Act, 1720-1800* (New York: Octagon, 1971); Margaret Patterson and David Reiffen, "The effect of the Bubble Act on the market for joint stock shares," *The Journal of Economic History* 50, no. 1 (1990).

The *Country Bankers Act* of 1826 effectively excluded unincorporated joint stock banks from London by erecting a 65-mile radius around the Metropolis. This exclusion remained in force until 1833. The *Country Bankers Act* also initiated a tentative process of consolidation in provincial England and Wales. Between 1826 and 1843, 96 English and Welsh private banks took advantage of the six-partner limit's repeal either to convert to the joint stock form or to allow one of the newly established joint stock banks to take them over.[14] This process of consolidation came to an abrupt halt due after 1844 due to the combined effect of the *Bank Charter Act* and the *Joint Stock Banking Act* of 1844.[15] The *Bank Charter Act* forbade new banks of issue whilst the *Joint Stock Banking Act* made it difficult to erect a new joint stock bank of deposit. Consequently, existing banks enjoyed a moratorium on competition from newly established joint stock rivals, which made it easier for them to stay in business.[16] In addition, the *Bank Charter Act* demanded that in most cases at least one and sometimes both of the banks involved in an amalgamation would have to surrender the right to issue bank notes when they joined forces.[17] The English and Welsh Amalgamation Movement could not begin in earnest until the regulations imposed in 1844 ceased to act as a disincentive to amalgamation. When the Amalgamation Movement began, the process of consolidation it unleashed was already a long-overdue development. Two additional factors accelerated the pace at which the Amalgamation Movement progressed once the process got underway. The

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[14] Joseph Sykes, *The Amalgamation Movement in English Banking, 1825-1924* (London: P. S. King and Son, 1926), 1-17.

[15] 7 & 8 Victoria c. 32; 7 & 8 Victoria c. 113.

[16] William John Lawson, *The History of Banking: With a Comprehensive Account of the Progress of the Banks of England, Ireland and Scotland* (London: Richard Bentley, 1850), 331; Walter Bagehot, *Lombard Street: A Description of the Money Market* (London: Henry S. King & Company, 1873), 252.

[17] The Bankers' Magazine, "The union of English banking companies prevented by the Bank Act of 1844."

first was the decline of the inland bill of exchange. The second was the banking industry's conversion to a regime of limited liability.

The inland bill of exchange represented more than a convenient vehicle for industrial lending and a means of payment. Bills of exchange gave the banks that discounted them an inherently liquid asset that matured at short notice.[18] In addition, an industrial bank could obtain funds when it needed them by rediscounting bills of exchange in London to access the funds accumulated by the agricultural banks.[19] The demise of the inland bill and the growing dependency on overdraft lending it created presented a problem for an English and Welsh banking industry populated by small regional banks that relied on the market exchanges to sustain their operations.[20] Most banks no longer needed outside help to fund their lending because the amounts they collected on deposits had grown. Nevertheless, some did need additional funds to maintain the reserves needed to assure their depositors that their banks were safe whilst others needed safe outlets for the funds they accumulated. Bank amalgamations solved the problems imposed by the inland bill's demise by putting these banks under the control of an administrative hierarchy that could allocate the industry's financial resources rationally. The result was an increase in bank size as industrial and agricultural banks merged with a bank domiciled in London.

The banking industry's adoption of limited liability in the 1880s made the need to maintain an adequate reserve of liquid assets even more pressing. Thomas Joplin

[18] Alexander Johnstone Wilson, *Banking Reform: An Essay on Prominent Banking Dangers and the Remedies they Demand* (London: Longmans, Green & Company, 1879), 32-33.
[19] James William Gilbart, *A Practical Treatise on Banking*, Fifth ed., vol. II (London: Longman, Brown, Green and Longmans, 1849), 556.
[20] Shizuya Nishimura, *The Decline of Inland Bills of Exchange in the London Money Market, 1855-1913* (Cambridge: Cambridge University Press, 1971).

and William Clay promised that banks of limited liability would demand an increase in the amounts of paid-up capital supplied by their shareholders relative to the amounts borrowed from the public. Walter Bagehot argued that the banks would rely on uncalled capital to secure their creditors' interests.[21] All three were wrong. The banks of limited liability economised on the amount of paid-up capital they demanded from their shareholders whilst relieving them of the burden of having to supply more capital if the bank failed.[22] These developments should have put the industry's creditors at greater risk but the amalgamating banks compensated by making a greater investment in their reserves of liquid assets.[23] Liquid assets offered the public an assurance that the bank holding them in reserve would always meet its obligations when the fell due.[24] The banks that made the requisite investment in liquid assets held the upper hand during the Amalgamation Movement because they took their rivals over. Banks that could not make that investment operated at a disadvantage and merged with a better-resourced rival.[25]

[21] William Clay, *Speech of William Clay, Esq. M.P. on Moving for the Appointment of a Committee to Inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks to Which are Added Reflections on Limited Liability, Paid-up Capital and Publicity of Accounts as Applied to Such Associations with Some Remarks on an Article on Joint-Stock Companies in the Last Number of the Edinburgh Review* (London: James Ridgway and Sons, 1836); Walter Bagehot, "Limited liability in banking I," in *The Collected Works of Walter Bagehot*, ed. Norman St John-Stevas (London: The Economist, 1978); Walter Bagehot, "Limited liability in banking II," in *The Collected Works of Walter Bagehot*, ed. Norman St John-Stevas (London: The Economist, 1978); Bagehot, "The safest bank."; Bagehot, "Sound banking."
[22] London and Westminster Bank, "Report on the proceedings at the extraordinary general meeting held at the bank, Lothbury, London E.C. on Friday August 6th 1909 Walter Leaf esquire in the chair," (Royal Bank of Scotland Archive (LWB/113), 1909), 5-7; Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations (1918)," in *Select Statutes, Documents & Reports Relating to British Banking, 1832-1928*, ed. T. E. Gregory (1929), 329-30; Sykes, *The Amalgamation Movement in English Banking, 1825-1924*: 141-43.
[23] Michael Collins and Mae Baker, *Commercial Banks and Industrial Finance in England and Wales, 1860-1913* (Oxford: Oxford University Press, 2003), 97.
[24] "Sir Edward Holden on banking," *The Times*, 4 November 1913.
[25] Michael Collins and Mae Baker, "Sectoral differences in English bank asset structures and the impact of mergers, 1860-1913," *Business History* 43, no. 4 (2001).

The amalgamating banks did not rely on reserves alone to offer greater security. Administrative standards were improving of their own accord as the English and Welsh became increasingly familiar with joint stock banking. By the 1880s, the English and Welsh banks were making a concerted effort to raise professional standards under the auspices of the Institute of Bankers.[26] Rulebooks introduced by the largest banks at the turn of the century played their part in eliminating the risk of employed error and fraud. Bureaucratic control regulated the amounts lent to ensure the banks maintained sufficient reserves.[27]

The Amalgamation Movement's most obvious consequence was that it succeeded in making the English and Welsh banking industry safer. No English and Welsh bank of any significance succumbed to a run after 1878. The run of good fortune lasted until 2007 when a relative newcomer to the industry (a former building society called Northern Rock) fell victim to the Global Financial Crisis.[28] Apparent immunity from financial collapse like this was important. A growing post-Industrial Revolution economy needed an expanding monetary base and nineteenth-century Britain did not have access to enough gold and silver to sustain the transactions needed keep its resources fully employed.[29] Bank notes could not have filled the

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[26] Edwin Green, *Debtors to Their Profession: A History of the Institute of Bankers, 1879-1979* (London: Routledge, 1979).

[27] Luther A. Harr, *Branch Banking in England* (Philadelphia: University of Pennsylvania Press, 1929), 110-13; Board of Governors of the Federal Reserve System (United States), "Branch banking in England," (Fraser Federal Reserve Archive (oclc: 10702515), 1932), 26.

[28] Michael Collins, "The banking crisis of 1878," *The Economic History Review* New Series 42, no. 4 (1989); Richard S. Grossman, "The shoe that didn't drop: Explaining banking stability during the Great Depression," *The Journal of Economic History* 54, no. 03 (1994); House of Commons Treasury Committtee, *The Run on the Rock: Fifth Report of Session 2007–08*, vol. I (London: Her Majesty's Stationary Office, 2008); Hyun Song Shin, "Reflections on Northern Rock: The bank run that heralded the global financial crisis," *The Journal of Economic Perspectives* 23, no. 1 (2009); Paul Goldsmith-Pinkham and Tanju Yorulmazer, "Liquidity, bank runs, and bailouts: Spillover effects during the Northern Rock episode," *Journal of Financial Services Research* 37, no. 2 (2010).

[29] Thomas Attwood, *The Remedy, or Thoughts on the Present Distress in a Letter to a Public Editor* (London: Whittingham and Arlis, 1816); Thomas Attwood, *Prosperity Restored, Reflections on the*

gap. Abandoning the gold standard to issue fiat currency under peacetime conditions was out of the question because it would have jeopardised London's place at the epicentre of a growing global payments system.[30] The *Bank Charter* Act demanded Bank of England's bank note circulation expand and contract to accord exactly with changes in its bullion reserves.[31] In contrast, the Scottish banks supplied Scotland with its bank notes and they did so under less stringent restrictions than those imposed on the Bank of England. Nevertheless, the Scottish banks confronted a limit the amount of bank notes they could put into circulation also.[32] The British had no choice but to adopt cheques to create an increasingly deposit-based monetary stock to meet their needs.[33] The currency reforms introduced in the 1840s ensured that banks other than the Bank of England would furnish a growing proportion of the British money supply just as the banking school predicted they would.[34]

The British public's willingness to use and accept cheques as means of payment depended on the account balances they mobilised and their capacity to act

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Causes of the Present Distress and on the Only Means of Relieving Them (London: Baldwin, Cradock and Joy, 1817); Thomas Attwood, *A Letter to the Rt. Hon. Nicholas Vansittart, on the Creation of Money and on its Action Upon National Prosperity* (Birmingham: R. Rightson, 1817); Thomas Attwood, *Observations on Currency, Population, and Pauperism in Two Letters to Arthur Young, Esq.* (Birmingham: R. Rightson, 1818); Thomas Attwood, *Causes of the Present Distress: Speech of Thomas Attwood, Esq. at the Public Meeting, Held in Birmingham, on the 8th of May 1829 for the Purpose of Considering the Distressed State of the Country* (Birmingham: W. M. Hodgetts, 1829).

[30] Michael D. Bordo and Finn E. Kydland, "The gold standard as a rule: An essay in exploration," *Explorations in Economic History* 32, no. 4 (1995); Michael D. Bordo and Hugh Rockoff, "The gold standard as a "good housekeeping seal of approval"," *The Journal of Economic History* 56, no. 02 (1996).

[31] Robert Torrens, *The Principles and Practical Operation of Sir Robert Peel's Act of 1844, Explained and Defended*, 3rd ed. (London: Longmans, 1858).

[32] Frank W. Fetter, *Developmement of British Monetary Orthodoxy* (Cambridge, Mass: Harvard University Press, 1965), 194-97.

[33] Michael Collins, "Long-term growth of the English banking sector and money stock, 1844-80," *The Economic History Review* New Series 36, no. 3 (1983).

[34] Thomas Tooke, *An Inquiry into the Currency Principle: The Connection of the Currency with Prices and the Expediency of a Separation of Issue from Banking*, 2nd ed. (Longman, Brown, Green, and Longmans, 1844), 122; James William Gilbart, *The Letters of Nehemiah: Relating to the Laws Affecting Joint Stock Banks, the Effects Likely to be Produced by the Measures of Sir Robert Peel on the System of Banking in London and Throughout the Country* (London: London and Westminster Bank, 1845), 15; Collins, "Long-term growth of the English banking sector and money stock."

as a store of value, which in turn depended upon the banks' capacity to meet their obligations when they fell due. It is unsurprising that bank safety became an increasingly important consideration under these circumstances. As such, the Amalgamation Movement was the final step in a century-long quest for monetary stability. The process began with the recoinage and the adoption of the gold standard in 1816, included the resumption of cash payments in 1819-21, the introduction of joint stock banking into provincial England and Wales in 1826 and London in 1833 and the passage of the *Bank Charter Act* in 1844.[35] The ideas promulgated by Bagehot in *Lombard Street* also made their contribution by turning the Bank of England into the banking system's lender of last resort.[36] The Bank of England, Treasury and successive governments may have done little to initiate or encourage the Amalgamation Movement, but once the process of consolidation got underway they gave it their tacit approval. The Amalgamation Movement proceeded unhindered by any regulatory interventions until finally the degree of concentration it fostered seemed a threat to competition.[37] The authorities did not intervene in the Amalgamation Movement because it yielded safer banks. Safer banks diminished the burdens imposed on the Bank of England by its obligation to act as lender of last resort and reduced Britain's vulnerability to financial crises.

[35] Fetter, *Developmement of British Monetary Orthodoxy*.
[36] Bagehot, *Lombard Street: A Description of the Money Market*; Michael Collins, "The Bank of England as lender of last resort, 1857-1878," *The Economic History Review* New Series 45, no. 1 (1992).
[37] Treasury Committee on Bank Amalgamations, "Report of the Treasury Committee on Bank Amalgamations (1918)."

No system of banking is entirely safe; and yet, the British banking industry proved safer than most.[38] Britain's banks enjoyed an extraordinary run of good fortune after the Amalgamation Movement that lasted until the Global Financial Crisis of 2007/08. Caution lay at the heart of this remarkable record of stability. Britain's banks maintained their reserves, restricted their lending and managed their affairs diligently. By the 1930s, those who wanted to turn British manufacturing's fortunes around began to tire of this conservatism. In 1931, a parliamentary committee chaired by the Scottish lawyer Hugh Patterson Macmillan (1873-1952) that included John Maynard Keynes amongst its membership accused the banks of having failed British industry. The committee identified what became known as the 'Macmillan Gap,' an alleged shortfall in the banks' industrial lending that denied British industry the funds it needed to invest in new and emerging technologies.[39] After that, the idea that Britain's banks failed British industry became a widely accepted conventional wisdom. However, the banks were in a difficult situation after the Amalgamation Movement. Their proprietors demanded the protection of limited liability and were not prepared to guarantee the industry's debts as they had done in the past. In addition, most of the banking system's assets had fixed or indeterminable maturity dates and the vast majority of its liabilities were payable at call or short notice. The banks had little choice but to exercise caution under these circumstances to balance the interests of their stakeholders. Britain's banks would

[38] Richard S. Grossman, "The shoe that didn't drop: Explaining banking stability during the Great Depression," *The Journal of Economic History* 54, no. 03 (1994); John D. Turner, *Banking in Crisis: The Rise and Fall of British Banking Stability, 1800 to the Present* (Cambridge Cambridge Univeristy Press, 2014).

[39] Committee on Finance and Industry, *Committee on Finance and Industry Report* (London: His Majesty's Stationary Office, 1931); S. Evelyn Thomas, *The Macmillan Report: A Short Summary of its Main Points Prepared for Students* (St. Albans: Metropolitan College, 1931); J. C. Stamp, "The report of the Macmillan Committee," *The Economic Journal* 41, no. 163 (1931); Peter Scott and Lucy Newton, "Jealous monopolists? British banks and responses to the Macmillan Gap during the 1930s," *Enterprise and Society* 8, no. 4 (2007).

not have served the national interest if they prioritised profitability to lend so generously that they put Britain's monetary and financial stability at risk. The Global Financial Crisis of 2007/08 highlighted the dangers imposed when British banks abandon the aversion to risk that served them so well for much of the twentieth century.[40]

The apparent ease with which the English and Welsh banks joined forces to create large firms during the Amalgamation Movement coupled with the apparent stability the Big Five English and Welsh banks enjoyed after World War One stands in marked contrast to the experiences of Britain's manufacturing industries after 1918. Bernard Elbaum and William Lazonick argued that Britain's manufacturers struggled to come to terms with the administrative realities imposed by large-scale production and distribution during the twentieth century.[41] They explained that what British industry needed to compete on the global market during the twentieth century was an increase in average firm size so "the visible hand of coordinated control" could replace "the invisible hand of the self-regulating market."[42] Unfortunately, those who administered British industry lacked the experience, education, training, and expertise needed to manage a large manufacturing combination effectively. Elbaum and Lazonick claimed the "absence of leadership from within private industry" put "increasing pressure upon the state to try to fill the gap."[43] *Dirigism*e, economic planning modelled on policies adopted in post-war France, came into

[40] Turner, *Banking in Crisis: The Rise and Fall of British Banking Stability*.
[41] Bernard Elbaum and William Lazonick, eds., *The Decline of the British Economy* (Oxford: Oxford University Press, 1986). See also: Bernard Elbaum and William Lazonick, "The decline of the British economy: An institutional perspective," *The Journal of Economic History* 44, no. 2 (1984); Bernard Elbaum and William Lazonick, "An institutional perspective on British decline," in *The Decline of the British Economy*, ed. Bernard Elbaum and William Lazonick (Oxford: Oxford University Press, 1986).
[42] Elbaum and Lazonick, *The Decline of the British Economy*, 10-11.
[43] Elbaum and Lazonick, *The Decline of the British Economy*, 10-11.

fashion during the 1960s as a Labour government sought the collaboration of privately owned manufacturing firms to resolve the nation's economic problems.[44] In the 1970s, the state's commitment to the manufacturing economy increased even further. Businesses like the aero-engine division of Rolls Royce, British Leyland, British Shipbuilders and British Aerospace came under public ownership.[45]

Successive post-World War II governments intervened in Britain's manufacturing economy to arrest relative economic decline only to see their efforts fail.[46] By 1975, the Conservative Party was under the control of a party faction that believed state interventionism was the cause of relative economic decline rather than a cure. In 1978, Margaret Thatcher made her economic intentions clear. She declared, "The long night of collectivism must come to an end. The time has come to move to a new common ground."[47] Andrew Gamble explained her government's underlying economic assumptions in the following terms:

> The cause of Britain's economic decline … [was] … the wholesale perversion of the market order…. [Decline] involved the supplanting of individualism with collectivism and it led … to the proliferation of obstacles to the working of free markets throughout British society, so that Britain was … transformed from a country with some of the most

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[44] Astrid Ringe and Neil Rollings, "Responding to relative decline: The creation of the National Economic Development Council," *The Economic History Review* New Series 53, no. 2 (2000); Stewart Wood, "Why 'indicative planning' failed: British industry and the formation of the National Economic Development Council (1960–64)," *Twentieth Century British History* 11, no. 4 (2000).
[45] Ellen M. Pint, "Nationalization and privatization: A rational-choice perspective on efficiency," *Journal of Public Policy* 10, no. 3 (1990); Karel Williams et al., "Accounting for failure in the nationalised enterprises—coal, steel and cars since 1970," *Economy and Society* 15, no. 2 (1986); Robert Millward, "State enterprise in Britain in the twentieth century," in *The Rise and Fall of State-owned Enterprise in the Western World*, ed. Pier Angelo Toninelli (Cambridge: Cambridge University Press, 2000); Jim Tomlinson, "A 'failed experiment'? Public ownership and the narratives of post-war Britain," *Labour History Review* 73, no. 2 (2008).
[46] Wood, "Why 'indicative planning' failed: British industry and the formation of the National Economic Development Council (1960–64)."; Leslie Hannah, "A failed experiment: The state ownership of industry," in *The Cambridge Economic History of Modern Britain*, ed. Roderick Floud and Paul Johnson (Cambridge: Cambridge University Press, 2004).
[47] Margaret Thatcher, "Speech to Young Conservative Conference (12 February 1978)," (Thatcher Archive (CCOPR 194/78), 1978).

> sensible and efficient social and political arrangements … to sink into collectivism, bureaucracy and inefficiency.[48]

On March 26 1980, Geoffrey Howe (1923-2015) (Margaret Thatcher's first Chancellor of the Exchequer) delivered the his second budget speech. That speech contained the following committment:

> For many years, the fashion both in government and industry was to favour mergers and amalgamations. No doubt, mergers have brought advantages in some cases, but now it is quite clear that the fashion for industrial elephantism was greatly exaggerated. I believe that there are cases where business are grouped together inefficiently under a single common umbrella. They could in practice be run more dynamically and effectively if they 'demerged' … to pursue their own separate way under independent management.[49]

Britain's attempt to invoke Alfred Chandler's managerial revolution from above through a state-sponsored increase in average firm size was at an end.

Industrial elephantism may have been out of favour in the 1980s but the Amalgamation Movement began over a century earlier in the 1870s. In 1980, the Midland Bank, Lloyds Bank, Barclays Bank and NatWest dominated the English and Welsh market for banking service. The Bank of Scotland, the Royal Bank of Scotland and a Midland Bank subsidiary (the Clydesdale Bank) did the same in Scotland.[50] These seven banks came under little pressure to 'demerge' during the 1980s. Nevertheless, these banks were not immune to the Thatcher government's reformist agenda.

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[48] Andrew Gamble, *Britain in Decline: Economic Policy, Political Strategy and the British State* (London: Macmillan, 1981), 153.
[49] "Tory strategy for a Parliament," *The Times*, 27 March 1980, 6.
[50] Checkland, *Scottish Banking*: 677-78; Roger David, *The Big Four British Banks: Organisation, Strategy and the Future* (Basingstoke: MacMillan, 1999).

The 'Big Bang' of 27 October 1986 liberalised the London Stock Exchange by abolishing fixed commissions, removed the distinction between stockjobbers and stockbrokers and replaced an open-outcry trading system with a system based on electronic screens.[51] Another deregulatory effort undertaken in financial services in 1986 was the *Building Societies Act,* which allowed building societies (mutual organisations owned by their members) to compete with the banks on a level playing field. Traditionally, building societies only offered a limited range of banking-related services to their members. They collected deposits but unlike the banks, they used the funds raised to offer their residential mortgages and to accumulate their reserves. The *Building Societies Act* of 1986 allowed these building societies to expand the range of financial services they offered their members to match those provided by the banks. In addition, a building society could 'demutualise' to raise capital by issuing shares to the public. Demutualisation effectively turned a building society into a publically listed bank.[52]

Ten building societies took advantage of the *Building Societies Act* (1986) to convert into banks between 1989 and 2000. The ten demutualised building societies were Abbey National, Cheltenham & Gloucester, National & Provincial, Alliance & Leicester, Bristol and West, Halifax, Northern Rock, Woolwich, Birmingham

[51] For more on the Big Bank see: Nigel Lawson, "The Big Bang 20 Years on: New Challenges Facing the Financial Services Sector," ed. Centre for Policy Studies (London: Centre for Policy Studies, 2006).

[52] Jacqueline Cook, Simon Deakin, and Alan Hughes, "Mutuality and corporate governance: The evolution of UK building societies following deregulation," *Journal of Corporate Law Studies* 2, no. 1 (2002); Graham Tayler, "UK building society demutualisation motives," *Business Ethics: A European Review* 12, no. 4 (2003); Shelagh Heffernan, "The effect of UK building society conversion on pricing behaviour," *Journal of Banking & Finance* 29, no. 3 (2005); Robin Klimecki and Hugh Willmott, "From demutualisation to meltdown: A tale of two wannabe banks," *Critical Perspectives on International Business* 5, no. 1/2 (2009); Andrew Campbell and Judith M. Dahlgreen, "Demutualisation and risk: The rise and fall of the British building society," in *Complexity and Crisis in the Financial System: Critical Perspectives on the Evolution of American and British Banking*, ed. Matthew Hollow, Folarin Akinbami, and Ranald Michie (Cheltenham: Edward Elgar, 2016).

Midshires and Bradford & Bingley. Ultimately, these new entrants to the banking industry did little to disrupt the pre-existing oligopoly. Every one of the demutualised building societies either failed or fell under the control of another bank or some other financial services institution.[53] Today, the banking industry in mainland Britain remains as much a concentrated oligopoly as it was in 1980. NatWest became a subsidiary of the Royal Bank of Scotland Group in 2000.[54] HBOS (an amalgam of the demutualised Halifax and the Bank of Scotland created in 2001) became a subsidiary of the Lloyds Banking Group in 2009.[55] The Midland Bank merged with the Hongkong and Shanghai Banking Corporation in 1992 and subsequently changed its name to HSBC Bank to comply with the Hongkong and Shanghai Banking Corporation's global branding strategy.[56] Barclays Bank continues to trade as an independent publically listed company.[57] Finally, Scotland's Clydesdale Bank has regained its independence.[58] The Midland Bank acquired the Clydesdale Bank at the end of the Amalgamation Movement only to sell it to the National Australia Bank in 1987.[59] In 2015, the National Australia Bank sold the Clydesdale Bank along with its other British banking interests to the public.[60]

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[53] Campbell and Dahlgreen, "Demutualisation and risk."
[54] Graham Kennedy, David Boddy, and Robert Paton, "Managing the aftermath: Lessons from The Royal Bank of Scotland's acquisition of NatWest," *European Management Journal* 24, no. 5 (2006).
[55] Robert Cole, "Look on the HBOS bright side," *The Times*, 17 January 2009; The Financial Conduct Authority and the Prudential Regulation Authority, *The Failure of HBOS PLC (HBOS)* (London: Bank of England, 2015).
[56] Neil Bennett, "Midland and HK Bank to merge," *The Times*, 18 March 1992; Richard Miles, "HSBC to drop Midland Bank name," *The Times*, 28 November 1998.
[57] Barclays PLC, "Annual Report: Building the Bank of the Future," (London: Barclays PLC, 2016).
[58] Clydesdale and Yorkshire Banking Group PLC, *Annual Report & Accounts: Our First Year as an Independent Company* (Glasgow: Clydesdale and Yorkshire Banking Group PLC, 2016).
[59] "The Midland and Clydesdale Bank fusion," *The Times*, 23 December 1919; "Go ahead for acquisitions," *The Times*, 13 August 1987.
[60] National Australia Bank, *Scheme Booklet for the Demerger of CYBG PLC from National Australia Bank Limited* (Melbourne: National Australia Bank, 2015).

The British banking industry now stands at a crossroads. In 2008, the Global Financial Crisis exposed the dangers inherent in Britain's dependence on a domestic banking oligopoly made up of banks deemed too big to fail. On 8 October 2008, the Chancellor of the Exchequer announced a bank rescue package that would eventually see the government make a capital investment in the domestic banks.[61] The Royal Bank of Scotland Group raised funds through the sale shares to government's Bank Recapitalisation Fund. Both HBOS and Lloyds utilised the Bank Recapitalisation Fund too to raise money prior to their merger in 2009. The government's ownership stake in the Royal Bank of Scotland Group and the Lloyds Banking Group eventually peaked at 83 per cent and 41 per cent respectively.[62] Partial nationalisation was supposed to be a temporary measure designed to stave off the crisis and the Lloyds Banking Group has subsequently returned to public ownership.[63] In contrast, the British state remains the Royal Bank of Scotland Group's largest shareholder to this day.

The Global Financial Crisis and steps taken to mitigate its effects on the domestic banks had a profound effect on the Labour Party that was in power at the time. The notion that the banking oligopoly retards Britain's regional economic development by denying native industries the funds they need now informs official Labour Party policy. Labour's 2015 election manifesto promised, "We will increase competition on the high street.... [We] want a market share test and at least two new

[61] Francis Elliott, Patrick Hosking, and Philip Webster, "Darling's longest night: From mass takeaway to massive giveaway," *The Times*, 9 October 2008.
[62] Emiliano Grossman and Cornelia Woll, "Saving the banks," *Comparative Political Studies* 47, no. 4 (2014): 591.
[63] Philip Webster, Gráinne Gilmore, and Gary Duncan, "Banks nationalised," *The Times*, 13 October 2008; H. M. Treasury, "Lloyds Banking Group has been fully returned to private ownership," (London: H. M. Treasury, 2017).

challenger banks."[64] Two years later, the Labour Party's 2017 election manifesto stated:

> We will take a new approach to the publicly owned Royal Bank of Scotland and launch a consultation on breaking up the bank to create new local public banks that are better matched to their customers' needs…. [We] need a strong, safe and socially useful banking system to meet the needs of our own regional economies and communities. We will commit to creating a more diverse banking system, backed up by legislation.[65]

Labour is committed to winding back the process of concentration in the banking industry that began in Scotland and encompassed the Amalgamation Movement.

Whether the new entrants to the banking industry the Labour Party hopes to coax into existence will retain their independence is open to question. The fate of the demutualised building societies suggests that British banking is a natural oligopoly in which new entrants have little hope of long-term survival. Nevertheless, Labour's determination to restructure the industry reflects a conflict that always lay at the heart of the Amalgamation Movement. The creation of a banking oligopoly entailed a loss of competition and regional autonomy that seemed justifiable if the large banks created offered stability. The largest banks fulfilled their side of the bargain during the twentieth century by proving immune to failure. The bargain seemed a good one until 2008 when confidence in Britain's biggest banks collapsed during the Global Financial Crisis. A resurgent Labour Party now opposes a minority Conservative

[64] Labour Party, *Britain can be Better: The Labour Party Manifesto 2015* (London: The Labour Party, 2015), 22.

[65] Labour Party, *For the Many not the Few: The Labour Party Manifesto 2017* (London: The Labour Party, 2017), 16.

government in the House of Commons.[66] If the Brexit negotiations go badly for the government, the Labour Party might obtain the mandate needed to restructure the banking industry at the next general election.

[66] Oliver Heath and Matthew Goodwin, "The 2017 general election, Brexit and the return to two party politics: An aggregate level analysis of the result," *The Political Quarterly* 88, no. 3 (2017); Will Jennings and Gerry Stoker, "Tilting towards the cosmopolitan axis? Political change in England and the 2017 general election," *The Political Quarterly* 88, no. 3 (2017).

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24 Henry VIII c. 12, An Act that Appeals to the See of Rome shall not from henceforth be used, but within this Realme.

13 Charles II c. 1, An Act for the Safety and Preservation of his Majesty's Person and Government against treasonable and seditious Practices and Attempts.

18 Charles II c. 5, An Act for encouraging Coinage.

7 & 8 William III c. 31, An Act for continuing to his Majesty certain Duties upon Salt, Glass Wares, Stone and Earthen Wares, and for granting Several Duties upon Tobacco Pipes and Earthen Wares for carrying on the war against France, and establishing the National Land Bank, and for taking off the Duties upon Tonnage and Ships and upon Coals.

8 & 9 William III c. 20, An Act for making good the Deficiencies of several Funds therein mentioned, and for enlarging the Capital Stock of the Bank of England, and for the Publick Credit.

6 Anne c. 22, An Act for continuing several Duties therein mentioned upon Coffee, Chocolate, Spices, Pictures and Muffins and additional Duties upon Calicoes, China Wares and Drugs and for continuing Duties called two third subsidies of Tonnage and Poundage; for preserving the Publick Credit; for ascertaining the Duties of Coals exported for foreign parts; and securing the credit of the Bank of England; and for passing several Accounts and Taxes raised in the County of Monmouth; and for promoting the Consumption of such Tobacco as shall have paid her Majesty's Duties.

6 Anne c. 41, An Act for the Security of her Majesty's Person and Government, and for the Succession to the Crown of *Great Britain* in the Protestant Line.

7 Anne c. 7, An Act for enlarging the Capital stock of the Bank of England, and for raising a further supply for her Majesty for the Year 1709.

12 Anne c. 11, An act to raise twelve hundred thousand Pounds for public uses, by circulating a further sum of Exchequer Bills; and for enabling her Majesty to raise five hundred thousand Pounds on the Revenues appointed for Uses of the Civil Government, to be applied for or towards Payment of such debts and Arrears owing to her Servants, Tradesmen, and others as they are mentioned.

12 Anne c. 16, An Act to reduce the Rate of Interest, without any Prejudice to Parliamentary Securities.

6 George I c. 18, An Act for better securing certain Powers and Privileges, intended to be granted by His Majesty by Two Charters, for Assurance of Ships and

Merchandise at Sea, and for lending Money upon Bottomry, and for restraining several extravagant and unwarrantable Practices therein mentioned.

4 George III c. 25, An Act for establishing an Agreement with the Governor and company of the Bank of England for raising certain sums of Money towards the Supply for service in the year one thousand seven hundred and sissy-four and for effectually preventing the forgiving Powers to transfer such Stock, or receive such Dividends.

5 George III c.49, An Act to prevent the Inconveniences arising from the Present Method of issuing Notes and Bills by the Banks, Banking Companies, and Bankers in the Part of *Great Britain* called *Scotland.*

15 George III c; 13, An Act for establishing an Agreement with the Governor and Company of the Bank of England, for advancing the sum of one million six hundred thousand Pounds, towards the supply and Service for the Year 1742.

21 George III c. 60 An Act for establishing and Agreement with the Governor and Company of the Bank of England, for advancing the sum of two Millions, towards the supply for services of the year one thousand seven hundred and eighty-one.

37 George III c. 45, An Act for continuing, for a limited Time, the Restriction contained in the Minute of Council of the twenty-sixth of *February* one thousand seven hundred and ninety-seven, on Payments of Cash by the Bank.

39 & 40 George III c. 28, An Act for establishing an Agreement with the Governor and Company of the Bank of England, for advancing the Sum of three millions towards the Supply for the Service of the year one thousand eight hundred.

51 George III c. 127, An Act for making more effectual Provision for preventing the current Gold Coin of the Realm from being paid or accepted for a greater Value than the current Value of such coin; for preventing any Note or Bill of the Governor and Company of the Bank of *England* from being received for any smaller Sum than the Sum therein specified; and for staying Proceedings upon any Distress by Tender of such Notes.

52 George III c. 50, An Act to continue until Three Months after the commencement of the last Session of Parliament, for making more effectual Provision for preventing the current Gold Coin of the Realm from being paid or accepted for a greater Value than the current Value of such coin; for preventing any Note or Bill of the Governor and Company of the Bank of *England* from being received for any smaller Sum than the Sum therein specified; and for staying Proceedings upon and Distress by Tender of such Notes; and to extend the same to *Ireland*.

56 George III c.68, An Act to provide for a New Silver Coinage, and to regulate the Currency of the Gold and Silver Coin of the Realm.

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59 George III c. 49, An Act to continue the Restriction contained in several Acts on Payments in Cash by the Bank of *England*, until the First Day of *May* one thousand eight hundred and twenty-three, and to provide for a gradual Resumption of Such Payments; and to permit the Exportation of Gold and Silver.

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2 & 3 Victoria c. 37, An Act to amend, and extend until the First Day of *January* One thousand eight hundred and forty-two, the Provisions of an Act of the First Year of Her present Majesty for exempting certain Bills of Exchange and Promissory Notes from the Operation of the Laws relating to Usury.

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