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978-0-521-85783-3 - Making the Market: Victorian Origins of Corporate Capitalism

Paul Johnson

Excerpt

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1 Mammon's cradle

True, it must be owned, we for the present, with our Mammon-Gospel, have come to strange conclusions. We call it Society; and go about professing openly the totalest separation, isolation. Our life is not a mutual helpfulness; but rather, cloaked under due laws-of-war, named 'fair competition' and so forth, it is mutual hostility. We have profoundly forgotten everywhere that *Cash-payment* is not the sole relation of human beings; we think, nothing doubting, that it absolves and liquidates all engagements of man. 'My starving workers?' answers the rich mill-owner: 'Did I not hire them fairly in the market? Did I not pay them, to the last sixpence, the sum covenanted for? What have I to do with them more?' – Verily Mammon worship is a melancholy creed.

Thomas Carlyle, *Past and Present* (1843)

When the citadels of capitalism started to quake and crumble in September 2008, the race began to find someone or something to blame. The venal investment bankers who put personal gain before financial prudence, the complacent regulators who ceded to markets their fundamental responsibilities, the conceited hedge-fund managers who thought they could diversify all risk to the nth degree and beyond, the reckless traders whose short selling corroded value and rendered fragile that which should be secure – these were the characters who populated the dystopia of global financial crisis. A new lexicon emerged – of sub-primes and naked short selling, of CDOs and CDSs, though few beyond the financial markets understood the nature of collateralised debt obligations or credit default swaps, or could tell whether short selling was demurely covered or impudently exposed.

As the quest for agency came up against a cacophony of denial – not me, not me – from bankers, brokers and broken Icelandic bankers, the market became increasingly anthropomorphised. The problem was not the various actors, either individually or collectively, but the market itself. The market was over-confident or depressed, the market was strong or weak, the market was ailing or recovering. But above all, the market was unpredictable. Like a two-year old with tantrums, the

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market could switch from beatific calmness to screaming fury in the blink of an eye. If the market chose to misbehave, there was little the responsible carers – the bankers, regulators, hedge-fund managers and traders – could do except avert their gaze, cover their ears and wait for a return to equanimity.

How did the market come to be so febrile, so precarious, so incapable of providing the transparency and efficiency that are supposed to be its hallmarks? Ever since the publication of Adam Smith's *Wealth of Nations* in 1776, the dominant idea in economics has been that welfare will be maximised when markets are free and competition is intense. In the nineteenth century the British Empire grew on the back of a free-trade doctrine; in the twentieth century the *Pax Americana* spread across the globe, carried by faith in the greenback, and a commitment to deregulation. Yet after more than two centuries in which economists have analysed market relationships and practitioners have developed sophisticated market instruments and strategies, the market has been revealed as a much less familiar or predictable entity than almost anyone had thought.

The capacity of markets to flip from stability to collapse in a matter of days, though unexpectedly cruel to modern eyes, was disarmingly familiar to people in Victorian Britain. The nineteenth century witnessed the creation of many of the key institutions of the modern market economy, and Victorian society bore the cost of experimentation and failure as different forms of capitalist organisation and activity staked their claim for market domination. The most important institution of the modern market – the joint-stock limited liability company – was a disputed, legally suspect and morally dubious organisational form at the beginning of Victoria's reign, yet by the 1880s it had become the primary form of business organisation in Britain. In 1801, when the London Stock Exchange was founded, it was widely viewed as a locus for morally indefensible gambling, but by the end of the nineteenth century it had become the hub of a global investment market.¹ The process of institutional innovation and development was far from orderly; many by-ways were pursued, many dead-ends encountered. The market institutions that existed at the end of the nineteenth century, and which continue to underpin the structures of modern capitalism, were the result of a specific set of historical conjunctures rather than the outcome of an orderly process of optimal institutional selection.

The institutional structure of corporate capitalism in the early twenty-first century reflects both the winnowing effects of competitive evolution over many decades, and the formative impact of those

¹ Ranald Michie, *The London Stock Exchange* (Oxford, 1999), 45.

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commercial and political interests that became embedded in nineteenth century corporate legislation and practice. The historical legacy is profound, and the historical parallels striking. The hand-wringing that has accompanied the global financial crisis of 2008 would have been familiar to Victorians who lived through the 'Railway Mania' of 1845, or the credit crunch following the collapse of the finance house of Overend Gurney and Co. in 1866, or any one of the crises that punctuated the equilibrium of financial markets at least once a decade throughout the nineteenth century. Also familiar would have been the call for legislative intervention and tougher regulation to bring wayward market operators to heel and to prevent any future market frenzy. The historical experience is not encouraging. Each set of nineteenth-century market regulations produced new constraints but also a new array of opportunities for businessmen and financiers to develop innovative ways to operate and prosper. With unerring inevitability, innovation trumped regulation, and new ways of doing business promoted further rounds of boom and bust.

This book investigates the legislative, organisational and behavioural foundations of corporate capitalism which were laid in nineteenth-century Britain, and which continue to exercise a profound influence on the manner in which modern markets operate. Despite the huge analytical effort of many generations of economists and historians, the ways in which market structures were consciously constructed in Victorian Britain is only indistinctly glimpsed in the literature. As will be shown below, economists have tended to reify and simplify the market, assuming away many of the contestable and conditional characteristics of exchange, thereby creating an orderly analytical model out of what is, in reality, a complex web of competing economic, legal, political and moral claims. Historians have largely ignored the institutional processes by which market structures were created in nineteenth-century Britain, satisfied perhaps that a general commitment to minimal regulation and free trade was enough to underpin a century of economic growth. This lack of historical and economic understanding of how markets have been constructed results in surprise and fury when markets fail to produce orderly and anticipated results. In truth, we have been there before; the historical parallels are legion, and disconcertingly familiar.

M & M

They could have been brothers, perhaps even twins. In looks and speech, in origins and actions, they were almost as one. They were

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the most famous capitalists of their time, they rose from obscure beginnings to giddy heights of wealth and power, and when their business empires failed, the fall was calamitous. Even their names were similar, and similarly invented. Yet they lived – if that is the right word – a century apart, one in the mind’s eye of an author, the other in the public gaze of the media. For, in a bizarre example of life imitating art, they were Augustus Melmotte, financier and railway promoter, the central character of Anthony Trollope’s 1875 novel *The Way We Live Now*, and Robert Maxwell, multi-millionaire and media mogul, whose body was found floating in the Atlantic in November 1991.²

Melmotte was ‘a large man with ... rough thick hair, with heavy eyebrows, and a wonderful look of power about his mouth and chin’.³ Maxwell was much the same, but larger. Quite where Melmotte hailed from was never discovered, though he certainly had central European, and possibly Jewish, origins, perhaps not dissimilar to those of Jan Lodvik Hoch, the son of an agricultural labourer from the Ruthenian village of Slatina-Selo on the Czech-Bulgarian border. Whether Melmotte was a family name or an acquired moniker is unclear, but when Jan Hoch arrived in Liverpool in June 1940 as a 17-year-old Free Czech soldier he quickly decided to reinvent himself, first as Leslie du Maurier, and by 1944 as (Ian) Robert Maxwell.⁴ They were both superb linguists, though Melmotte never quite lost a touch of his middle-European accent, which always undermined his claim to be a trueborn Englishman. Maxwell, on the other hand, morphed – in speech and demeanour – into an upper-middle-class English persona.

Perhaps there was some element in these personal histories of geographical, nominal and linguistic mutation that accounted for the domineering personalities and overpowering sense of self-belief that characterised these two great men. Descriptions of their behaviour are interchangeable:

² All details of Augustus Melmotte’s life, and all direct quotations from Anthony Trollope, *The Way We Live Now* (London, 1875) are taken from the Penguin Classics edition published in 1994. Further references appear as *TWWLN*. Details of Robert Maxwell’s life and business dealings are taken from critical biographies by Tom Bower, *Maxwell: The Outsider* (London, 1988), by Peter Thompson and Anthony Delano, *Maxwell: A Portrait of Power* (London, 1991), and from the despicably toadyish ‘official’ biography by Joe Haines, *Maxwell* (London, 1988). Additional details of the financial manoeuvres and misdemeanours which led to the final collapse of the Maxwell empire come from Tom Bower, *Maxwell: The Final Verdict* (London, 1995).

³ *TWWLN*, 31. ⁴ Haines, *Maxwell*, 73.

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[He] intimidated visitors as much by his gestures as his words, his gargantuan performance humbling those physically and financially less well endowed. The theatricality, the egocentricity and the vanity of the man were unsurpassed.⁵

[He] was becoming greater and greater in every direction – mightier and mightier every day. He was learning to despise mere lords, and to feel that he might almost domineer over a duke.⁶

The immutable sense of self-worth of both Melmotte and Maxwell was sustained and reinforced by the ostentatious and idolatrous residences they established for themselves in the heart of London, in Holborn and in Grosvenor Square:

The atmosphere in the citadel of his empire ... was suffocatingly imperious. Polished, double doors led across marble floors into a high-ceilinged hall supported by brown marble Doric columns and lit by glass chandeliers. Beyond, the spectacle of a huge living area decked out with expensive mock-Renaissance tapestry covered furniture and with carpets patterned in a vast 'M' design cautioned any visitor who might be contemplating criticism or challenge.⁷

There was the house. There was the furniture. There were the carriages, the horses, the servants with the livery coats and powdered heads, and the servants with the black coats and unpowdered heads. There were the gems, and the presents, and all the nice things that money can buy.⁸

Their homes were theatres for extravagant performance where the worlds of royalty, aristocracy, diplomacy, politics, finance and commerce could sit in attendance and pay homage.

Yet neither man was content with the trappings of wealth gained from commercial activity; they both sought, and achieved, political position. Neither of them had a deep emotional or intellectual commitment to any particular party or political ideology. For them, politics was a way to get closer to the centre of power, rather than to advance a nobler cause. Maxwell appears to have dallied with the Conservative party before becoming a Labour party member and candidate for the constituency of Buckingham at the 1959 election.⁹ Melmotte was courted by both Liberals and Tories to stand for the vacant parliamentary seat of Westminster, and finally deigned to offer his commercial expertise to the latter. As busy men of finance and commerce, they had little time for the quaint customs and manners of the House of Commons. Maxwell had been advised by his friend Richard Crossman to 'lie low for six months' before subjecting his parliamentary colleagues to his oratorical skills but patience was as much a Maxwellian trait as humility. Immediately after the Queen's speech which opened the new session

⁵ Bower, *Maxwell: The Final Verdict*, 17.

⁶ *TWWLN*, 267. ⁷ Bower, *Maxwell: The Final Verdict*, 16.

⁸ *TWWLN*, 33. ⁹ *Ibid.*, 106.

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of Parliament in 1864, Maxwell stood up and delivered an over-long peroration, thus becoming the first backbencher to address the new parliament, and the first new member to make a maiden speech.¹⁰ It was as if he was acting out a script penned by Trollope. In the House of Commons of the 1870s 'it was probably not in the remembrance of any gentleman there that a member had got up to make a speech within two or three hours of his first entry into the House', but that did not deter Melmotte from delivering to the House his opinion on commercial affairs. The House was not appreciative, but nor was Melmotte of his reception: 'It seems to me to be a stupid sort of place.'¹¹ Richard Crossman's judgement might equally well apply to either performance: 'It was absolutely disastrous. There he was trying to bash his way to fame in the first twenty-four hours.'¹²

The political campaigns and the conspicuous consumption of both Melmotte and Maxwell were paid for from the proceeds of large and complex businesses. Complexity and opacity was an ever-present element – almost an organising principle – of their commercial ventures. They pushed the flexibility of accounting practices to the limit and beyond, and they linked their personal financial affairs to those of the public companies they headed in such obscure and multifarious ways that it was practically impossible to determine what was owned by whom and what was owed to whom. It took the receivers years to untangle the links between the public companies chaired by Maxwell and the more than 400 private companies with which they were associated.

Maxwell had laid snares for any auditor in pursuit of financial revelation. The cross-cutting ownership network of his private companies was baroque in structure, and positively rococo in terms of the profusion of near-identical names which he bestowed on these businesses and then incrementally amended. Blessed with a photographic memory, Maxwell had no need to commit the details of this spider's web to paper. For Melmotte also 'it was one of his gifts to remember with accuracy all money transactions, whether great or small, and to keep an account book in his head, which was always totted up and balanced with accuracy'.¹³

But where, exactly, did the wealth come from? Melmotte was a financier and company promoter, Maxwell a publisher, but they both had an extensive range of other business interests. Just how extensive was impossible to determine, because their private business empires were

¹⁰ Bower, *Maxwell: The Outsider*, 100.¹¹ *TWWLN*, 530, 532.¹² Bower, *Maxwell: The Outsider*, 100.¹³ *TWWLN*, 404.

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never exposed to public view or accountability. Thus the public perception of these empires might expand or contract as the public standing of their proprietor rose or fell. It was said of Melmotte that:

He was the head and front of the railway which was to regenerate Mexico. It was presumed that the contemplated line from ocean to ocean across British America would become fact in his hands. It was he who was to enter into terms with the Emperor of China for farming the tea-fields of that vast country. He was already in treaty with Russia for a railway from Moscow to Khiva. He had a fleet – or soon would have a fleet of emigrant ships – ready to carry every discontented Irishman out of Ireland ... It was known that he had already floated a company for laying down a submarine wire from Penzance ... round the Cape of Good Hope – so that, in the event of general wars, England need be dependent on no other country for its communication with India ... It may have been the case that some of these things were as yet only matters of conversation – speculations as to which Mr Melmotte's mind and imagination had been at work, rather than his pocket or even his credit; but they were all sufficiently matured to find their way into the public press.¹⁴

Maxwell, through his privately-owned publishing company, Pergamon Press, also had extensive dealings with Russia and other East European countries, a business which involved both serious scientific publishing and the production of extremely profitable and unreadable hagiographies of various communist political leaders. Maxwell's fluency in Russian, Hungarian, Czech and German, as well as French and Yiddish, eased his path into these East European and Soviet trades, as did connections he had made in Berlin in 1946 when, as a captain in the British army, he was involved in intelligence work. Rumours of an MI5/6 connection followed Maxwell to his grave.

Yet despite the grandeur and global outreach of their business ventures, there was always a shadow hanging over the names of Melmotte and Maxwell. Were they really credit-worthy? Could they really be trusted? With their wealth went rumour of how that wealth had been made. Melmotte apparently had made his money in France through company promotion – indeed it was said that he could 'make or mar any company by buying or selling stock, and could make money dear or cheap as he pleased.' Yet it was also said that he was 'regarded in Paris as the most gigantic swindler that had ever lived; that he had made that city too hot to hold him; that he had endeavoured to establish himself in Vienna, but had been warned away by the police'. According to Trollope's notes, Melmotte had been in prison in Hamburg, though as with so many other aspects of Melmotte's career, this point of detail

¹⁴ *TWWLN*, 337–8.

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remained unconfirmed.¹⁵ What was apparent, however, was Melmotte's way of operating companies. He packed the board with ineffectual directors who were indebted to him, in awe of him, or content to remain passive in exchange for their remuneration, he modified board minutes to reflect his own wishes rather than the true course of discussion, and he raced through business to prevent proper consideration of commercial developments. In effect he ran the public companies of which he was chairman as extensions of his private financial affairs.¹⁶

The origins of Maxwell's fortune lay in book wholesaling. He was a born salesman, with a phenomenal ability to convince sceptical purchasers that they had a burning desire for whatever book, encyclopaedia, business, bond or share he happened to want to dispose of at the time. But, as with Melmotte, his career was littered with cases of financial irregularity. As early as 1954 he had been censured by the official receiver for trading as a book wholesaler while insolvent, but it was not until an investigation by the Department of Trade and Industry in 1971 that the manner and scale of his commercial impropriety was revealed. In 1969 he sold the scientific publisher Pergamon Press to a US company. Within weeks of the takeover the new owners claimed that Pergamon's accounts had been contrived to project high profits and conceal losses; that they were, in short, fraudulent.¹⁷ The opaque management processes within the Maxwell corporate empire meant that no charges of wrongdoing could be laid against Robert Maxwell in person. Nevertheless, the DTI report on him was damning:

He is a man of great energy, drive and imagination, but unfortunately an apparent fixation as to his own abilities causes him to ignore the views of others if these are not compatible ... The concept of a Board being responsible for policy was alien to him ... We regret having to conclude that, notwithstanding Mr Maxwell's acknowledged abilities and energy, his is not in our opinion a person who can be relied upon to exercise proper stewardship of a publicly quoted company.¹⁸

Since so much was known, and so much more rumoured, about the financial probity of Melmotte and Maxwell, it seems scarcely credible that people would choose to invest resources in companies that they controlled. Yet they repeatedly managed to launder their commercial reputations through further speculative ventures which made money, and made profits for those who invested in them. When a potential investor, speaking to Melmotte's co-promoter of the South Central

¹⁵ Richard Mullen, *Anthony Trollope: A Victorian and His World* (London, 1990), 558.

¹⁶ *TWWLN*, 280–3. ¹⁷ Thompson and Delano, *Maxwell*, 124.

¹⁸ DTI report quoted in Bower, *Maxwell: The Final Verdict*, 21–2.

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Pacific and Mexican Railway, noted that 'many people speak very badly of Mr Melmotte's honesty', he was told that 'There is always a want of charity when a man is successful.'¹⁹ When the sobriquet 'the bouncing Czech' was applied to Robert Maxwell, he could respond by showing how, within two years of taking over the near-bankrupt British Printing Corporation in 1980, he had transformed it into a profitable and efficient enterprise which laid the foundation for his purchase of the Mirror newspaper group in 1984. In fact, so credulous or craven were City investors that in 1987 they provided £630 million to purchase a huge issue of shares in the (now slightly renamed) British Printing and Communication Corporation, which Maxwell used to embark on a spree of acquisitions in an attempt to construct a multi-billion-pound global media empire. The brokerage house of Alexanders, Laing and Cruickshank was well rewarded for placing such a huge rights issue.²⁰

Yet Maxwell was still dogged by the damning DTI report, and needed to strengthen his personal credibility in commercial and financial circles, prior to his planned change of name of BPCC into Maxwell Communication Corporation. Who better to assist in this than the literary-minded Henry Poole, a partner in Alexanders, Laing and Cruickshank, who produced a glowing 48-page analysis of BPCC's business prospects entitled 'Unravelling the Melmotte Skein.' Poole argued that BPCC's stock was undervalued for a number of reasons, one of which was 'a feeling of unease, even hostility, towards the Group's chairman' which was akin to the sentiment surrounding Melmotte. Poole quoted from Trollope: 'But still there was a feeling of doubt and a consciousness that Melmotte, though a tower of strength, was thought by many to have been built upon the sands,' but went on to state that 'it is clear that in contrast to Mr Melmotte, Robert Maxwell has built on secure foundations'.²¹

Just four years after this encomium to commercial rectitude, Maxwell Communication Corporation had collapsed. In a desperate attempt to save his corporate empire from sinking in a quagmire of debt, Maxwell plundered hundreds of millions of pounds from the pension funds of the companies he owned and ran, using his sons Kevin and Ian to participate in and cover up the fraud. He died, possibly by his own hand, through falling off his yacht in seas near the Canary Islands. The foundations of his empire were revealed as being just as insubstantial as those of Augustus Melmotte who, as his money and credit ran out, first attempted to persuade his daughter to assign her property to him;

¹⁹ *TWWLN*, 67. ²⁰ Bower, *Maxwell: The Outsider*, 344.

²¹ Thompson and Delano, *Maxwell*, 31.

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then, when this failed, forged her signature on title deeds; and, when this action was about to be made public, took his own life by drinking a dose of prussic acid.

This comparison of the careers and lives of Augustus Melmotte and Robert Maxwell is, at one level, nothing more than an exercise in coincidence between literature and life. They were both such exceptional characters that at first sight it seems impossible to infer anything from their personal histories about the general nature and tenor of the commercial worlds in which they operated. In fact it would be wrong to read *The Way We Live Now* as a work of social realism.²² It was a satire on – or in the opinion of many contemporary reviewers, an overblown caricature of – the commercial morality of the 1870s. *The Times* was almost alone among the journals of the day in complimenting the novel for presenting ‘only too faithful a portraiture’ of modern manners.²³ On the other hand, Trollope had no shortage of models for the character of Melmotte. There was George Hudson (1800–71), the ‘railway king’, a banker turned railway promoter, MP for Sunderland, and reputedly one of the richest men in England until the revelation of accounting fraud in his railway empire led to the collapse of share prices and his financial and reputational ruin. There was ‘Baron’ Albert Grant (1830–99). Both the Grant and the Baron were acquired: he was born Albert Gottheimer, and received the title ‘Baron’ from Leopold 13th of Italy. Grant made a fortune for himself, and lost a fortune for shareholders, by promoting speculative mining companies. He served as an MP, but was ejected from his seat for electoral malpractice, spent much of his money building a palatial mansion in Kensington which was used only once, for a society ball, and he was eventually reduced to relative poverty after being forced by his creditors into bankruptcy. And there was John Sadleir (1814–56), solicitor, railway speculator, MP and director of the Tipperary Bank, from which he embezzled huge sums by forging title deeds as collateral for loans. He committed suicide on Hampstead Heath by drinking prussic acid.

These and other Victorian financiers and businessmen pushed their speculations to the limits of legality and beyond. For a time they reaped the rewards, and then they bore the personal costs of their deception and deceit. Yet no multi-millionaire businessman, whether a scion of moral rectitude or a duplicitous cheat, could operate a complex commercial

²² J. A. Banks, ‘The way they lived then: Anthony Trollope and the 1870s’, *Victorian Studies*, 12 (1968), 177–200.

²³ N. John Hall, *Trollope: A Biography* (Oxford, 1991), 388.