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1 Introduction

Alice Teichova, Ginette Kurgan-van Hentenryk and Dieter Ziegler

This volume explores the symbiotic relationships between banking, trade and industry and the state during the rise and expansion of capitalism, and seeks to compare and assess the results in order to widen current perspectives. The chronological dimension of its twenty-one contributions spans eight centuries and the geographical dimension extends across four continents.

Banking and trade in the pre-industrial era

The cradle of modern banking stood in the northern Italian cities. In this context David Abulafia traces the protracted process of the emancipation of banking from long-distance trade. The scope of early banking operations ranged from the pawnbroker who concentrated on small loans, often aimed at peasants or artisans in need of short-term credit, to the collectors of papal taxes who transmitted funds from the northern outposts of Christian Europe to Rome. In order to circumvent the ecclesiastical prohibition of usury, which restrained the money-lender from living exclusively off the charging of interest, the business of banking was conducted in the context of trading. Such exchange transactions were tolerated by the Church as they were generally regarded as non-usurious. The primary objective of the larger banking businesses was therefore neither deposit taking nor the provision of local

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credit but exchanges and transfers. Abulafia, by concentrating on fourteenth- and fifteenth-century Florence, concluded that modern ideas of investing into production or of competitiveness cannot be fully applied to these early banking companies, whose success was built on a network of family connections and trust rather than on rules set by an anonymous market.

It may be doubted whether pre-industrial Europe was an economic entity but there can be little doubt that the commercial centres connecting the Mediterranean, the Baltic and the North Sea took shape along European trade routes from the late Middle Ages. As the 'first mover' in the development of banking the Italian cities fell behind, late medieval Italian banking techniques were successfully adapted to their local environment in other European cities. As the centre of gravity of commercial activity shifted from the Mediterranean to the Atlantic and north-western Europe, new banking techniques spread to those regions with which the commercial centres were connected by long-distance trade. Geneva lost its position as a leading financial centre to Lyons as early as the mid-fifteenth century, and Bruges to Antwerp about half a century later. Antwerp and Amsterdam in turn were unable to keep their leading position as they failed to develop a modern discount and issuing banking system. The decline of the Amsterdam financial market is not as yet fully understood; however, the hypothesis of 'institutional ponderousness' advanced by Herman Van der Wee in the case of Amsterdam might more generally explain the regional discontinuity in the development of banking.

Antwerp bankers developed the practice of endorsement and modern discount during the sixteenth century, which was an outstanding technical innovation and decisively stimulated the transferability and negotiability of commercial paper. This innovation was only fully exploited in Amsterdam, where many Antwerp bankers had immigrated. To limit the speculative activities of the immigrated bankers the Amsterdam authorities in 1609 founded a public deposit and clearing bank: the Amsterdamsche Wisselbank. This bank turned out to be an enormous success. Van der Wee stresses that it must not be regarded as a particular banking innovation as its business did not significantly differ from banking practices introduced by the Italian bankers and elaborated in Bruges and Antwerp. Nevertheless, the Wisselbank was a cornerstone of Amsterdam's position as the leading financial centre of the seventeenth and early eighteenth centuries: it refined the banking techniques, which it had copied, concentrating all

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accounts in a single bank; its own seemingly unshakeable solvency enhanced the trust in these accounts.

The spread of banking techniques along the established medieval trade routes is analysed in detail by Paola Avallone, Youssef Cassis, Michael North and Herman Van der Wee. In southern Italy and Naples public banks, descending from charitable institutions, became of overall importance as they functioned as main lenders to the governments of the Kingdom and of the City of Naples but also provided services to the public, such as opening saving accounts, lending money on collateral and issuing paper documents which were used both as credit and as means of payment. By accepting the public banks' *fedi di credito* for tax payments the government helped to ensure that these documents were widely accepted instead of metal currency.

A major innovation introduced by some of the public banks, such as the Neapolitan public banks and the Stockholms Banco, was paper money. Although the issuing of bank notes in Sweden had been prohibited after the failure of the Stockholms Banco, deposit receipts issued by the Riksbank soon became a substitute, and by 1726 the *transportsedlar* were accepted as legal tender by the state for tax payments. By the mid-century confidence in this medium of exchange had already become so great that neither suspension nor resumption of the notes' convertibility into coin seriously undermined monetary stability.

Spain's history exemplifies a case of declining commercial and financial centres. In almost all the main commercial centres of the Kingdoms of Aragon and Castile bankers had been established by the late Middle Ages, and by the sixteenth century Spain had become the very centre of the emerging world market. Gabriel Tortella observes, in the seventeenth century, 'a sharp cleavage between the early modern and the modern periods in the field of banking'. The Sevillian bankers, in particular, who were closely linked to the chaotic finances of the Spanish crown were prevented from developing a banking system appropriate to the needs of the rising commercial capitalism of the seventeenth and eighteenth centuries. Persistent budget deficits and lack of respect for legal rules and the market mechanism stymied private business. This helps to explain why Spain was unable to keep its leading position in the emerging world market. The same is true for the demise of the bankers of southern Germany, who had been closely related to the Spanish crown and consequently were brought down by the Spanish state bankruptcies of 1557, 1575 and 1607.

The state did not always play a retarding role in the development of

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banking, as the Spanish case might suggest. Indeed, the public bank was created by governmental (or rather municipal) authorities. Although most of these deposit and clearing or note issuing agencies finally proved unable to adapt to the needs of modern industrial capitalism, they can be seen as the forerunners of the modern central bank.

One important exception is the Swedish Riksbank. Its predecessor, the Stockholms Banco had not only combined deposit and credit functions but also became the first note issuing bank in Europe. Although Håkan Lindgren rejects the term 'central bank' as an anachronism for the early Riksbank, which had been founded in 1668 by the Swedish Parliament when the Stockholms Banco had to close its doors; learning the lesson of its failed predecessor and dividing the giro from the credit function, it gradually took on embryonic central banking functions in the course of the eighteenth century. The fact that all Scandinavian countries had founded public and semi-public banks by the eighteenth and early nineteenth centuries can be attributed to the example of the Riksbank, in particular to its successful introduction of paper money in a specie-scarce economy.

The other major exception, the Bank of England, was in fact no public bank, but privately owned by the merchant elite of the City of London. However, the Bank was developed and protected by a state which became financially dependent upon it. The British national debt and the taxation system withstood the early modern wars and crises (including the French Revolutionary and Napoleonic Wars) so that the Bank was able to develop, by trial and error while fairly independent from state control, both its commercial activities and – closely related to the latter – its early central banking strategies. It was, however, the state which forced the Bank of England to extend its activities as the backbone of the London finance market to the English provinces, where the Industrial Revolution was taking place. This 'crisis-induced reaction by the state', as Huw Bowen and Philip Cottrell described it, paved the way to turn the Bank of London into a national central bank. The final step in the establishment of the modern banking system was the creation of a note issuing agency: in 1694 the Bank of England was founded and in 1707 it was granted the right to issue bank notes. Although the founding of the Bank was in the first place motivated by the state's demand for a government banker, it was relatively free to develop its commercial business of bullion purchases, note issuing and discounting, and with it the Bank became the backbone of the emerging financial centre of the world.

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Outside Europe – with the exception of North America – the development of banking techniques was connected with the European trading and financial network in early modern times. Montserrat Gárate analyses the development of payment and clearing transactions between Europe, Spain and the Spanish colonies in Latin America in the eighteenth century. The export of manufactured goods from different parts of Europe to the Latin American colonies created the demand for a means of payment which was not only payable in Spain, but in all major European commercial centres and the Atlantic ports. Drafts payable in Bordeaux, Paris, London or Amsterdam were successfully introduced and eased the development of the triangular export trade between Europe, Spain and the Latin American colonies.

These innovations hardly touched the domestic colonial economies. In the early period the abundance of precious metals in Latin America discouraged the development of more sophisticated means of payment. Some important merchant banking houses appeared in the colonial centres during the heyday of the triangular export trade with Europe, but they did not develop an intra-colonial banking infrastructure. When the colonies had become independent in the early nineteenth century and the strong links to the European economies were in danger of being cut a large majority of the Latin American merchant banking houses decided to transfer their businesses to one of the European centres with which they had already close contact, apart from Spain, mostly with Bordeaux, Paris and London.

From the viewpoint of world trade this Euro-centric approach has brought a greater understanding of banking in the imperialist period; however, it has tended to neglect indigenous economic development in former colonial areas. Recent research on banking in non-European countries has not primarily been concerned with its impact on industrialization but has emphasized its influence on political, social, national and institutional development. Thus Carlos Marichal characterizes the bank as a key institutional innovation not necessarily linked to industrialization but connected with the agro- and mineral-export economies of Latin America. From the second half of the nineteenth century the dominant role in political and administrative modernization and in the evolution of state structures was played by powerful government banks in Argentina, Brazil, Chile, Mexico and Peru. In these countries, he postulates, the banking revolution preceded the industrial revolution. This is borne out by Andrés Regalsky's account of

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Argentina when he also stresses that the banking system supported agrarian rather than industrial capitalism.

From the very beginning of European settlement the situation in North America was different, since it lacked the precious metals of the Spanish colonies. The British and French colonies relied on coin shipped from Europe, and as the colonial societies grew other forms of money had to be introduced. Already in the second half of the seventeenth century the British colonial legislature was empowered to print paper money in order to finance military expeditions against the French, and in the mid-eighteenth century the government of Nova Scotia – followed by other colonial governments – issued treasury notes for the same reason. The British government, however, was concerned and prohibited the issue of treasury bills and restricted colonial note issue. According to Larry Schweikart these restrictions 'provided one of several economic irritations that contributed to the American Revolution'. The impact of independence in North America furthered the development of banking. As early as 1782 the Continental Congress permitted the establishment of the first chartered bank in North America. Established in Philadelphia to support the credit of the young nation it issued paper money convertible in gold and silver, and despite the unfavourable circumstances it proved to be a success. Its example was soon followed by other banks, and by 1800 there were more than thirty commercial banks, among them the First Bank of the United States, chartered by the Congress of the United States in 1791. As in Britain the foundations had been laid for backing the early stages of industrialization in the US; in Schweikart's words, 'financial intermediaries played a key role in supplying credit to antebellum American industrial and commercial development'.

The role of banks in the process of industrialization

The growth of banking in England in the second half of the eighteenth century cannot be interpreted simply as a reaction to the needs of the first industrializing nation. In the nineteenth century London was still the world centre of commercial capitalism and its banking mechanism was only marginally attuned to industrialization. Banking in the English provinces and in Scotland developed as a reaction to the inadequate provision of means of payment by the Bank of England and of short-term credit by the London money market.

Historians agree that in the early period when industrialists relied

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mainly on their own resources the English banking system was permissive in the sense of neither actively promoting nor restricting new investment but accommodating all credit-worthy borrowers. With the quickening pace of economic and technological change and the increasing capital intensity of industry, however, the parochial character of banks in the provinces came into conflict with the rising demand for credit. Practically until the turn of the century, the banks supplied their local economy by refinancing through the London money market. Growing dependence on their London correspondents and the long-term effect of the crisis of 1878 led to the transformation of the independent provincial banks into branches of the London-based deposit banks.

In Belgium the Société Générale's investment in industry resulted from illiquidity of its short-term debtors during the 1830s crisis. To avoid a crash, the Société Générale required its customers to transform their firms into joint-stock companies and convert their bills into shares which were kept in its portfolio. Concurrently the new Belgian state's decision to build a railway system stimulated investment banking. Banks financed industry by short-term loans which mostly became revolving credits and were generally converted into stock. The crisis of 1848 revealed the weaknesses of the system: when the banks were unable to get capital from the market they were overwhelmed by non-liquid assets; in the crisis of 1848, they lost their issuing privilege and part of their discount business. During the following twenty years the Société Générale operated as a *banque d'affaires*. From the 1870s it started commercial banking and at the end of the century mixed banking was the dominant feature of the Belgian financial market.

The centralized French state developed a centralized banking system with Paris at its centre only slowly, as described by Eric Bussière. Apart from the fact that the Banque de France had already been created in 1800, the breakthrough for a modern banking system only came with the building of the railway network in the mid-nineteenth century and was facilitated by the Saint-Simonian belief of the banking pioneers. Around 1860 a new generation of banks was created, among them the famous Crédit Mobilier. Although this bank was a model for a whole generation of banking, it finally failed, because it proved unable to cope with the illiquid nature of long-term engagements in industry and transport. Investment banking was abandoned and from the 1880s the banking system *à la française* was established with two types of banks: the deposit banks specialized in collecting public savings and lending

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short-term to industry and commerce; and the *banques d'affaire* which applied the resources of the *haute banque* to capital market operations, such as foreign government loans and public utilities.

The third quarter of the nineteenth century was the decisive period when the structure of the German banking system was shaped. Unlike France, however, investment banking in Germany did not fail, but was successfully extended by the first joint-stock banks, which had been modelled on the Crédit Mobilier. During these decades the banks gradually moved from funding railways to financing industry. This was facilitated by their current account and overdraft business best attuned to the financial needs of industry and commerce. In this context Dieter Ziegler points out that the relative success of the German universal banking system before 1914 depended on the holding of a relatively large guarantee capital and, also, on the central bank's *de facto* liquidity guarantee for fundamentally sound banking houses whose assets were temporarily unavailable. When in the 1920s the banks operated on a much smaller capital basis and when in 1931 the Reichsbank was not prepared to step in as a lender of last resort, the whole system collapsed and was rebuilt only by massive state intervention. A similar pattern can be observed in the revival of Italian banking. As Luigi De Rosa argues, banking reappeared in Italy during the catching-up process of industrialization in the nineteenth century. It was largely modelled on an adaptation of the Crédit Mobilier system, strongly influenced by German and, to a lesser extent, by Swiss banks. Italian banking in the first half of the twentieth century followed the path from universal banking to total state control of the financial system under Mussolini's Fascist dictatorship.

In Switzerland the banking system was also influenced by the Crédit Mobilier model. By the mid-nineteenth century it was dominated by small local and cantonal banks, on the one hand, and by influential, internationally oriented private banking dynasties in Geneva and Basle, on the other. When this banking structure proved inadequate to cope with the new demands of large investment projects, such as railways, joint-stock banks were founded. This is discussed by Youssef Cassis who mentions the non-economic reason for the establishment of the Crédit Suisse partly as a nationalist reaction to prevent foreign control of the country's railway network; the spectacular success of this bank finally induced the Basle bankers to overcome their institutional ponderousness. When the Basler Handelsbank and the Basler Bankverein were founded Zurich had already overtaken Basle as the predominant

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financial centre of Switzerland. As in all universal banking systems current account credit became prominent as a means of financing domestic industry and the Swiss banks were, at the same time, prepared to undertake capital market transactions. The great banks were engaged in Swiss-based finance companies which made direct investments in both domestic and foreign capital intensive ventures of the so-called Second Industrial Revolution, particularly the electrical industry and electricity supply.

According to Alice Teichova it was in the Habsburg Monarchy where the symbiosis of banking and industry was to be found in its purest form. Most typically this was expressed by the foundation in 1855 of the K.k. privilegierte Österreichische Credit-Anstalt für Handel und Gewerbe as a joint-stock bank on the pattern of the Paris Pereire brothers' Crédit Mobilier but adapted to Austrian conditions. Before the Great War eight leading Vienna banks had secured strategic positions in most branches of industry and their influence reached to all the empire's territories. After the break-up of the Habsburg Monarchy they found themselves suddenly standing at the head of multinational diversified concerns. Their efforts in defending their leadership in central Europe were eventually unsuccessful. The tradition of universal banking continued unbroken in the successor states. However, except for Czechoslovakia, insufficient domestic resources, liquidity problems and debt crises characterized the interwar period. Without a 'lender of the last resort' universal banks were unable to cope with the world economic crisis of the 1930s. It marked an end to the form of mixed banking that had functioned in central Europe since the 1880s.

An example of the long-term success of the Crédit Mobilier model in banking is Sweden. Unlike the other continental European investment banks, which were not authorized to issue bank notes, commercial banking in Sweden was started by note issuing banks. After the turn of the century when the major institutional obstacle, the prohibition of share ownership, was removed the full adoption of universal banking was completed. Lindgren concluded that, although the Swedish banks had been *de jure* deposit banks, by the turn of the century they had become *de facto* universal banks which took on the 'missionary role' which Alexander Gerschenkron had attributed to latecomer economies of the first generation. The comparison between the patterns of industrialization of the four Scandinavian countries – Finland, Sweden, Denmark and Norway – can be seen as an acid test for the role and importance of banking for industrialization in general. Diverse legal

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and institutional environments had created differently structured financial systems. Lindgren argues that each Scandinavian country developed the financial system most suitable to its economy.

By the turn of the century the leading European banks, above all of Britain, France and Germany, were a powerful force in developing capitalism in relatively economically backward countries. Elena Frangakis-Syrett emphasizes the involvement of the leading European banks in the Ottoman Empire's finances, in the construction of its railways and in investment in public utilities. Foreign influence was decisive in the Imperial Ottoman Bank and a cluster of foreign, especially French and German, banks dominated the Empire's banking sector at the same time as the domestic disorganized financial sector consisted mainly of merchants lending to small-scale enterprise and to rural borrowers.

The prevalent assumption of the unequal relationship between indigenous and foreign banks is tested and disputed by Shizuya Nishimura in the case of China. He substantiates that there existed a true division of labour between the operations of international and native banks: the former specialized in foreign exchange business and services to European and Japanese residents in China and they were also the bankers of the Chinese government until 1905 when the Bank of China was founded; the latter, the *chien chuangs*, were closely connected with their Chinese clients. These native banks were protected by barriers of language and traditional techniques from foreign penetration. This raises the question how far China's traditional economy was penetrated by Western and Japanese imperialist business.

Mature banking systems

A market-oriented financial system is characterized by a high degree of division of functions through specialized financial institutions – including banks, financial markets and market intermediaries. In a bank-oriented financial system savings are largely directly transferred from those who generate them to those wishing to use them by the intermediation of banks. Thus Britain, with her functional specialization, is seen as representing a market-oriented financial system and Germany, with her tradition of universal banking, as a bank-oriented financial system. The merits as well as the 'purity' of the respective systems which matured in the late nineteenth century are controversial.

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