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The "Old Lady of Threadneedle Street" – The Bank of England and the Development of the British Banking System*

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Richard D. Richards:
The Early History of Banking in England
P. S. King & Son Ltd., Orchard House, Westminster, London, 1929, 345 p.

The reference library of the Magyar Nemzeti Bank has a large number of old books that are difficult to find in both domestic and foreign libraries. In this review, I present one of these books, which is considered a seminal work in foreign economic and banking history literature. Published in 1929, the work describes the early days of banking in England. The author of this volume is Richard D. Richards (1881–1937), born 140 years ago this year, who served in the First World War and published extensively after the war, mainly on economic and banking history topics. His research focused on the history of the Bank of England and the development of the British banking system, and he published a number of articles on the subject in various periodicals. Although the present volume deals mainly with the English banking system of the 16th and 17th centuries, it also provides an insight into English banking before that time and in the 18th century as well.

In England, bills of exchange were in use as early as the 14th century, but became more widespread during the Tudor period (1485–1603) as trade expanded. The main trading partners for Britain at this time were France and Flanders, but the wide-ranging connections of English merchants are also shown by the fact that they also traded with African countries, among others, obviously in the context of colonialism. One of the first companies formed by the pooling of capital (joint-stock) was the Company of Adventurers of London Trading to the Ports of Africa, founded in 1553, or "The Guinea Company" as it was then called, which operated some 15 merchant ships and imported African larch from the continent, among many other commodities.

* The papers in this issue contain the views of the authors which are not necessarily the same as the official views of the Magyar Nemzeti Bank.

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In the time of Elizabeth I (1533–1603) and James I (1566–1625), the financial intermediaries in the major English cities were mainly merchants, vendors, money changers and goldsmiths, who were the first "bankers" in England and were then called by that name. In rural areas, it was mainly wool producers and cereal growers who were involved in the trade, so it was common practice for merchants to provide credit to wool producers as advance compensation for the subsequent supply of wool. In addition to the expansion of trade, another important factor that contributed to the proliferation of financial intermediaries was the relatively high level of interest rates that could be charged, which were regulated by law. Act VIII of 1545 allowed an interest rate of no more than 10 per cent to be charged, and although it was gradually reduced in later years (8 per cent in 1623, 6 per cent in 1660, and capped at 5 per cent in 1713), this initial 10-per cent interest rate, which could be considered significant, combined with the nascent insurance products, certainly encouraged entrepreneurship.

In terms of the importance of financial transactions, *Sir Thomas Gresham* (1519–1579) can be highlighted, a merchant who did business in the 1550s, mainly in Antwerp through the Fugger family's representative office there. Regarded also as the founder of the London Stock Exchange, *Gresham* also played an active role in brokering municipal loans as the "banker of the royal court". He was also able to provide London with substantial loans, which contributed to London's later rise to the rank of a financial centre. The city loans were initially granted in large part by English merchants on fairly favourable interest terms for them, as evidenced by records showing that on 24 December 1610 the City of London repaid six English merchants 30,000 pounds of loans at an interest rate of around 3,000 pounds. Later, in addition to merchants, pawnbrokers also became increasingly involved in lending, and in the 1660s and 1670s, especially in the context of unauthorised pawnbroking, usury and the sale of stolen pawned goods were common, posing significant regulatory challenges. "Deposit taking" in England was first started by money changers: there are references from 1616 to "deposits" being placed with the money changers for safekeeping (not for interest at that time), which the money changers could also use to provide loans.

Private banking by goldsmiths also contributed significantly to the economic development of England in the late Stuart period. London's goldsmiths' shops were almost like banks during the Stuart Restoration period after the 1660s, as they paid interest on deposits, lent money, discounted bills of exchange in large numbers, exchanged gold bars in their shops, were active in the exchange of money, and recorded all these in ledgers. Several goldsmiths (who in many cases also engaged in pawnbroking) had not only domestic but also foreign clientele, and were involved in financing the royal court and the army. The latter was particularly prevalent during the Cromwellian period, mainly during the First Anglo-Dutch War (1651–1654), but was also prevalent earlier, in the years of the Civil War (1642–1649). One goldsmith carrying out such complex activity was *Sir Charles Duncombe* (1648–1711), who was later elected to the British House of Commons and mayor of London between 1708 and 1709. Duncombe amassed a fortune of around 400,000 pounds from his business activities, making him the richest member of the House of Commons at the time. Some goldsmiths were commissioned to provide banking services to other goldsmith bankers. They also issued promissory notes, initially guaranteeing the repayment of deposits at all times. Goldsmiths, on the other hand, could later outsource their deposits, and the promissory note they issued was not necessarily backed by money. Thus, it is fair to say that the goldsmiths also performed some of the functions of the later Bank of England by performing banking activity, issuing promissory notes i.e. actual negotiable "paper money", and acting as creditors. The promissory notes issued were also more widely accepted, subject to certain conditions, first under the Commercial Code, and then, after their incorporation into the civil law system, they became transferable by statute from 1704. The issue of promissory notes was not yet regulated by a central body, and it was precisely this unregulated financial activity that highlighted the need for a central body to carry out the "paper money issue" in an organised, regulated and supervised manner. This circumstance thus contributed in large part to the creation of the Bank of England in 1694. Such goldsmiths exercising banking activities as well were among others the Smiths of Nottingham, the Backhouses and Peases of Darlington and the Vaughans of Bristol who were able to continue their private banking business successfully even after the 1672 Treasury moratorium.[1] Several modern banking houses grew out of the goldsmiths' earlier private banking businesses, such as the Child's Bank – mentioned by *Charles Dickens* in his book A Tale of Two Cities – which was still in operation in 1923, but the National Provincial Bank, founded in 1692, and the iconic Lloyds Bank also have a similar goldsmith background.

Proposals for the creation of a national bank appeared in great numbers in England in the second half of the 1550s; they sought to organise the institution mainly on the basis of examples of Amsterdam and Venice. In general, the creation of a national bank was proposed at this time to meet credit needs (especially in the cities of London, York, Coventry, Bristol and Exeter), to "subsidise" less well-off citizens, to finance the army and the expenses of the monarchy as well as to expand trade following the Venetian example. In this context, Attorney General *John Cooke* (1608–1660) proposed that the poor should be allowed to receive small loans from the bank without interest. Several proposals were made for the payment of the capital necessary for the establishment of the bank, notable among them a so-called collective payment initiative, under which it was proposed to provide the funds

[1] The temporary one-year moratorium (*"Stop" of the Exchequer*) of 1672 was introduced by Charles I (1600–1649) to enable the Treasury to use its revenues to prepare for the coming war rather than to pay off public debts.

necessary for the establishment and continued operation of the national bank by a weekly payment of halfpenny per member of households (except the poor and minors), 4 pounds for the wealthy and a regular special tax to be paid by companies and office clerks (since they rarely or never took part in military service).

But it was *Francis Cradock*'s (?–1667?) pamphlets "Expedient", published in 1660, and "Wealth Discovered", published in 1661, that made the biggest impact. *Cradock* proposed to divide England into 100 districts, with a national bank (or "Royal" Bank as *Cradock* named it) and a branch bank in each district, replacing the private banking activity of the goldsmiths. He proposed a uniform interest rate ceiling of 3 per cent, that the loan should be secured mainly by real estate, and that the branch banks should also provide loans upon pledges, as Cradock envisaged. This idea of creating a regionally based provincial banking network ("land" or "country" bank) was also raised in later years by several writers, such as *Hugh Chamberlen* (1632?–1721?), physician and financial expert, in his "Dr. Hugh Chamberlen's Proposal to make England Rich and Happy", published in 1690, and *Daniel Defoe* in his "An Essay Upon Projects", published in 1697. It is worth mentioning that, in addition to his literary work, *Defoe* was also a frequent commentator on economic issues, and he advocated the Orphans' Fund[2] (or Orphans' Bank as he called it). However, the idea of creating a rural banking network was not widely accepted by the professional community, but these opinions contributed to the creation of the Asgill and Barbon's Land Bank in 1695 and the National Land Bank a year later. However, land bank–type institutions were less successful, probably due to a lack of public confidence and the extensive and successful lending activities of goldsmiths. Their expansion was further hampered by the fact that in many cases these banks were undercapitalised and found it difficult to raise capital in the face of existing and worsening currency problems.

With the Tunnage Act of 1694, passed during the reign of William III (1650–1702), the Bank of England (or as it was then referred to: "the Bank", and later, from 1797, after *James Gillray*'s notorious caricature, "The Old Lady of Threadneedle Street") was created to perform what could be considered primarily traditional central banking functions. Unlike, for instance, the Bank of Amsterdam, which has also had a significant influence on the operation of the stock exchange, for example. The Bank of England was founded in a rather unfavourable economic environment: the wars with France and the defeat suffered meant that not a single year between 1690 and 1699 was a prosperous one for the English economy. This is probably why, in the early years after its creation, the Bank of England was already lending

[2] Unfortunately, the purpose of the Orphans' Fund changed in later years. In 1766, Parliament decided that the fund could be used for public improvements, so it was renamed the Orphans' and Improvement Fund, and, as orphan relief gradually faded into the background, its name was changed to the London Bridge Approaches Fund. However, the Orphans' Fund was the most reputable "institution" after the Bank of England at the time.

substantial sums (1.2 million pounds at 8 per cent interest) to the government. Alongside the economy, the English currency was in a very poor state, the silver coins in circulation had been heavily worn and their value (weight) had declined significantly making it difficult for them to be widely accepted, especially abroad, and by 1696, around 10 per cent of the coins in circulation were counterfeit. This led to the Great Recoinage, which took place between 1696 and 1699, at a cost of not less than 2.7 million pounds involving the Royal Mint, led by *Isaac Newton*. Branches were also set up to mint coins in the cities of Bristol, Chester, Exeter, Norwich and York. However, the coin exchange did not go smoothly, the process was preceded by a number of professional debates, minor panic on the part of the public and considerable volatility in the value of the precious metal and the exchange rate. Before the recoinage was completed, there was a chronic shortage of money, which was addressed by the decision of *Charles Montagu* (1661–1715), Earl of Halifax, Chancellor of the Exchequer, to issue treasury bills to replace the coins. The recovery of the economy, the stabilisation of the currency situation and the establishment of the Bank of England were therefore the result of a rather lengthy and resource-intensive process; *Richards* summarised the overall situation as follows: "Avoiding national bankruptcy was a remarkable achievement. That the Bank of England did not immediately collapse was even still more remarkable." *Defoe*, in his aforementioned work "An Essay Upon Projects", expressed similar praise for the creation of the Bank of England under these circumstances, calling it a "particular glory" of the English nation.

The challenges did not disappear in the years following the establishment of the Bank of England as the volume of new coins put into circulation through the recoinage was initially insufficient and the cash shortage intensified in later years. These circumstances led to a bank run and a partial suspension of cash payments in May 1696, as a result of which the price of the central bank's shares gradually fell. This tendency intensified on the eve of the forthcoming War of the Spanish Succession (1701–1714), and the fall in the exchange rate was exacerbated by the fact that several shareholders were unable to pay their contributions to the capital of the central bank, forcing them to sell all or part of their parcels of shares. As a result, no dividends could be paid in the years following the Bank of England's creation in order to consolidate the capital position. However, the following period was more favourable, leading to a strengthening of the Bank of England's status (for example, through the capital increase implemented or the restriction on the rights of rural banks to issue banknotes). It is worth noting that until 1826, the Bank of England was the only English joint-stock bank. The central bank was finally granted the exclusive right to issue banknotes in 1844.

Although book reviews are typically given on recently published books, we think that it may be useful to pick up literature such as this and similar must-read books from time to time. It can also be observed that there has been a growing interest in textbooks on banking history, presumably as economic crises have become more frequent. Thanks to this book, which was published more than 90 years ago, it is possible to find much new information, as it is unfortunately difficult to find a book published in Hungarian, not only this volume, but also in this field. Finally, as we approach the centenary of the founding of the Magyar Nemzeti Bank, it is worth remembering that the circumstances of the Bank of England's foundation were not the only crisis in the history of European banking systems: the Magyar Nemzeti Bank was also established under extremely difficult circumstances, as the defeat suffered in the First World War, the human, material and territorial losses suffered by the country, and the problems of currency stabilisation also posed significant challenges for Hungarian economic policy. It can be mentioned as a further parallel that Hungarian currency stabilisation was strongly facilitated by a loan from the Bank of England, which was made possible to a large extent by the dynamic boom in foreign relations between the United Kingdom and Hungary during this period, not least thanks to the personal prestige and widely accepted professional recognition of Hungary's first central bank governor, Sándor Popovics.