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The Baring Financial Crisis

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in the *Times* of April 7th, and which were obtained by a much rougher method.

I have not said anything of the methods of estimating the populations of smaller areas, such as towns, by the number of births, or the number of inhabited houses, as these have been described by many writers. I would however suggest that the census of school children taken by the School Boards in many towns might afford a useful basis for estimating the total population.

A recent writer in the *St. James's Gazette* designated estimates as 'the most delusive of all forms of ignorance masquerading as knowledge.' If he be correct (and I am scarcely inclined to gainsay him), it only strengthens the case for a quinquennial census, for which I trust the Government may see its way to make arrangements before the Charles Street staff is dispersed.

What may be the value of my estimates will be shown by the Preliminary Reports of the Census, which will possibly appear before this article.

May, 1891.

G. B. LONGSTAFF

P.S.—Since the above was set up in type the preliminary report of the census of Ireland has been issued, and the populations of the twenty-eight great towns of England and Wales (as well as those of Edinburgh and Glasgow) have been published in the Registrar-General's weekly return. The population of Ireland is 4,706,162, a number exceeding that I have given by 11,373, so that my estimate is within $\frac{1}{4}$ per cent. of the truth. As regards England and Wales the population of the twenty-eight great towns (comprising a population of nearly ten millions) falls as much as 621,985 below the estimate, it may therefore be regarded as practically certain that the total population will turn out to be also very far short of the estimate. As for the various towns in many cases the discrepancies are so startling as to render all recently published vital statistics valueless. In Scotland there is less to go upon, Edinburgh falls short by 13,466, while Glasgow exceeds the estimate by 34,901.

June 13th.

G. B. L.

THE BARING FINANCIAL CRISIS

THERE are some aspects of what will always be known as the Baring financial crisis, which occurred in the middle of November of last year, that have not been dwelt upon, so far as I know, and which I think an early number of the *Economic Journal* may be asked to find room for, because those coming after us will expect to find it not only a storehouse of facts, but, what is of nearly as much importance, a record of comments on, and deductions from, these facts. What is the first thing that strikes us as a most dangerous element in the state of things out of which the Baring crisis arose? It is the uncontrolled one-man power! Prince Bismarck did his work, and then fortunately,

in due time, a man came who had character enough to see that he was spoiling with success, and that, if left to his own devices, he would probably do a good deal of harm. Events have shown that he could be done better without than with. The same rule applies to a house of business. No matter how clever a man is, he should neither be allowed to play with the destinies of an empire nor the millions of money of a great trading and banking firm. In both cases the head is apt to get turned with the belief in one's own infallibility, and the result often is ruin. The unfettered one-man power is, moreover, no longer suited to the times in which we live, and there could be no more emphatic condemnation of the system than the fall of Bismarck in Germany and of Baring in England in their respective spheres, and so close one upon the other. When the world was one or two hundred years younger, and there were no electric currents traversing the ocean-beds and continents of the earth, one man could find pigeon holes enough in his little brain to keep sorted and remembered the details of his business, whether political or commercial; but now it is quite otherwise. Unless there is well-ordered co-operation and properly divided command and responsibility in a large mercantile firm like that of Baring Brothers, the brain will get confused, the mind disordered, and, to descend a long flight for a parallel, like a man too long at a time in a railway signal-box, sooner or later there will be a crash. This evil is being slowly remedied by the joint-stock company principle. Two of our largest mercantile houses have been recently converted into companies, where the one-man management cannot err to the extent that it could in the conduct of the business as previously constituted. In all cases in which large private firms and private banks have been converted into joint-stock companies, it will generally be admitted, I think, that no such conduct of the business as that discovered to have been carried on in later years by the firm of Baring Brothers could possibly have been persisted in where there was a board of directors and responsible sub-managers, independent as regards emolument of their immediate superiors in office. We require to look no further for the proof that such a contention is well founded than in the fact that all London banks have kept their doors open through a crisis, the cause of which was the fall of the most widely-known commercial firm in the world. It is no exaggeration to say that until the middle of November 1890 the name of Baring Brothers was as good as a bank-note in every port in the civilized world. If the joint-stock principle could have stepped in in the month of October previously and put an end to that one-man power, a precious fragrance might have been saved to the commercial name of this great trading community, which, unhappily, was allowed to be brushed away like the bloom from the grape, to be known no more. There are still some survivors amongst us where more or less of the one-man power insufficiently controlled presides; but people respect each other's feelings so much that the management is allowed to jog along in the old groove, where there is no independent board with individual responsibility to the shareholders, until there is another crash and disappearance of an antiquated system of administration.

Whatever happens in the future, there is already sufficient evidence before us, in the fact I have already referred to, viz., that all the London banks kept their doors open until Baring's acceptances had run off, to show how enormously the system of managing banks and great commercial firms has improved of late years. One of the aspects of 'the Baring crisis' is that which relates more particularly to the circum-

stances which have been the indirect means of preventing the banks and great financial houses from getting themselves into difficulties. Someone has exclaimed, 'Why did not my partners prevent me from entering into such excessive commitments?' Had those partners been members of a board, each independent in a pecuniary sense of the other, and each responsible to the shareholders for allowing mismanagement to continue unchecked, what we now deplore might never, and need never, have happened. A great joint-stock bank is compelled to keep a close daily watch upon the proportion of cash held to the liabilities, and the manager—he he ever so strong-headed and venture-some—is not allowed to reduce the total below a fixed proportionate limit. Someone has exclaimed, '—————! I never conceived it possible I could be short of cash!' The conception would have been easy enough, had not the wrong principle of uncontrolled one-man power been allowed to govern the conduct of the business until all became such confusion that it was thought that even full speed a-head could not bring the ship to grief in the densest fog. In the case of the banks in London which are not joint-stock banks, there is probably not one where the engagements entered into depend upon the unaided judgment of one individual. The nature of the business is in these times too complicated for any one man to continue for any length of time to conduct it successfully. The great banks and the financial houses as a body have shown themselves to be sound through this crisis owing to the facilities they have enjoyed which were not at their disposal in the years prior to the Overend and Gurney crisis. The managers of these institutions can now better inform themselves as to the character, standing, and, what is of great importance, the latest engagements of those who propose business to them, than they could twenty years ago. Such is the rapidity with which rumour flies about in these times, that the weakness of a firm hardly makes itself felt in South America or even in remote Eastern cities, but the news flashes from one European centre to another, and the commercial paper bearing the name or names whispered about passes from one bank or discount house to another without finding any one willing to take it. There is, besides, not only a sort of free-masonry between dealers in money, who live more or less upon each other, but an itching to communicate bad news, which ensures the spread of the evil tidings with the utmost rapidity. What is the result? The detection of any financial weakness, which may be manifested in a variety of ways, so instantaneously reacts upon the bank or financial house that has entered into rash commitments, that engagements are undertaken with a degree of caution and care in our day which was quite unknown before electricity could ring bells and tell tales thousands of miles away. In our day every leading man of business sits opposite a set of buttons which communicates with his clerks. He has a telephone in a cupboard hard by; a boy or boys ready to run for his life with telegrams; and a machine too near to be pleasant which tells him on a strip of paper what horse has won the Derby almost as soon as he has passed the winning-post; what the Prime Minister has just said about the Russian intrigues in Bulgaria; how much lower the Bank reserve is, and what is the state of the stock markets two minutes ago. He has no sooner taken in these various small items than another bell rings, and his wife, who is in a shop in Bond Street, asks for another fifty-pound note as she has run short of cash.

The life-blood of commerce is credit. The difficulty of successfully utilizing credit has increased enormously owing to the greater competition. There is less profit, and the expenses of gaining it have not diminished in the same proportion. The London banks trust more in these days to gathering in their gains over a wider area than they used to. Branches of the great banks are to be seen everywhere in London. Kite-flying of the kind that Alexander Collie flew with the aid of his 'drawing-posts' is unknown to-day. The banks have very sensibly set themselves to tap the small tradesmen everywhere. A few pounds made upon each small account is safer business in the long run than discounting large acceptances of a firm whose failure will sweep away half the reserve fund at a blow. The making of profits in small amounts fosters greater care, and does not bring with it the kind of demoralization which follows upon large and quick gains. This is an aspect of the Baring crisis which is a very satisfactory one. The banks have all kept their doors open during a short time of great suppressed apprehension. Had any one of them been known to be seriously locked up, the chances are there would have been, between last December and March, a run upon that bank.

Another aspect of the Baring crisis is, that there exist now so many comparatively new powerful financial companies of various kinds allied with Trust and kindred corporations, that the total disappearance of two large mercantile banking houses leaves no more trace upon the great surface of London's capacity to finance large undertakings as soon as confidence is restored, than is to be seen on the water a minute after a stone has been cast into a pond. This remark must be qualified with one important reservation relating to the Bank of England, which I shall deal with later on. Again, instead of large masses of securities being held in small quantities by individuals to be flung upon the Stock Exchange for anything they will fetch in unreasoning and unthinking haste when a crisis occurs, they are now in the possession of Trust companies, who, although they may in their collective management occasionally make mistakes, yet keep their heads cool in times of danger, and thus are the means and have been the direct cause upon this occasion of preventing the enormous losses to individual investors, which produced so much ruin and distress after 1866. We thus see that the area over which the effects of the breakdown of one or two large firms make themselves felt has been greatly extended, and there is in consequence an increase of resistance which, as I have said, almost nullifies the material loss sustained by the commercial community in which it occurs. The foreign business which for a number of years has been transacted in an office in one street of a city now migrates to other streets. The same facilities are granted by other houses, the purchasing power changes hands, and in a short time all goes on as before, with the important exception that revenues in the aggregate yearly increasing are diverted from one set of people to another set.

There is, however, one great and far-reaching change which the Baring crisis has introduced, and that is a kind of commercial salvage which has been sanctioned and approved of as it never was before. Not only here but on the Continent it is now and probably will continue to be the fashion to endeavour to save from destruction by prompt measures rather than to look on while commercial houses flounder in their difficulties in the future. What is this change of disposition to be traced to? It is a trite saying in a great city in speaking of different

banking houses, discount houses, and a good deal in the case of mercantile houses also, that 'they hate each other.' At all events they used to, and to a great extent do so still; but the spirit of rivalry is in a sense less bitter. There is more disposition to let live, and why? because profits are cut much finer, and business conducted on that system teaches people to show a kindlier spirit even to rivals. There are too many doing the same thing—offering the same facilities—to make a bank feel sure of keeping its customers unless they are treated well. The smaller profits involve a much greater number of transactions—a large increase in the risks which may all the same be sound trading risks. The more a single individual's engagements in any branch of business are spread out, the more anxious is he to prevent another man in the same line from coming down for fear of the loss of confidence generally it may cause. Each and all depend more than they did upon mutual support. So it is with institutions whose risks have to be run in all quarters of the world. Fear of the possible results to the general body induces them even to support a rival, if the position is not too bad, rather than face the unforeseeable effects of the collapse of one of their number whose position had for years been believed to be perfectly sound.

Previous to the Baring crisis the system of 'underwriting' new issues of capital was not known upon the scale practised of late years. This, although directly conducive to the financial trouble through which we have been passing by reason of the rapid appearance of new companies before the capital of the old ones had been absorbed by the public, at the same time introduced a certain element of safety into the business. Underwriters are not of much use to the promoters of new companies unless they are people of substance. Hence a great deal of the money expended in preliminary expenses connected with the formation of new undertakings has not been lost as it would have been in the absence of the underwriting system. On this system the necessary capital to float the new undertaking is assured, while in its absence frequent failure through the subscriptions from the public being too small is prevented. Besides, the larger houses being engaged as underwriters gives them an interest in upholding credit generally, and in doing their utmost to foster and encourage a feeling of confidence in times of disturbance, instead of darkly hinting at all sorts of possible troubles looming in the distance, which we know only too well is the line that has been taken earlier in our financial history, when more was to be got by destroying a rival in trade than is the case in the present day. But this underwriting system has its drawbacks, as is seen when those engaged in it are caught full of commitments when a crisis occurs. The tardy response of the public to the invitation to purchase offered by the lower prices is due very much to the large operators who go in the van of such movements being so fully engaged that they are unable themselves to buy.

The great and important new departure which has been introduced by the Baring crisis is what I have referred to as the system of commercial salvage. I think there will be no difference of opinion that as a question of strict principle no great public bank, or financial institution whose managers are responsible to stock or shareholders in that institution, is justified in going to the rescue of another large bank, financial institution, or trading firm which cannot meet its engagements, unless it can do so without incurring more risk than it would do in the transaction of its ordinary business.

Now that the severity of the Baring crisis has passed, there can be no impropriety in discussing the principle of the Bank's action, or in saying that nothing short of some threatened great national calamity would justify the Bank of England being placed in the position of having nearly one-half of its capital locked up in unsaleable foreign securities. To emphasize the importance of that position into which the Bank of England was brought through the decision to save the house of Baring Brothers from failure to meet its engagements, we will imagine the occurrence, even some time after the Baring difficulties were public property, of similar troubles overtaking another large house and an appeal being made to the Bank of England for help. The Bank would have been powerless—in fact was powerless, as was proved. This fact alone demonstrates that nothing, as I have said, short of the imminence of some great national calamity could justify such a lock-up of the liquid funds of a great public bank, and I very much doubt if the directors, realizing as they do now what has been their responsibility, would ever place themselves in such a position again. That responsibility, it is true, was in a sense shared by the other banks and by some of the more important public financial institutions, but inasmuch as the reserve of the Bank of England was at the same time the collective reserves of the London banks, the sharing of the responsibility by the other London banks as regards any immediate pressure that might arise was more imaginary than real. If the Barings were to be helped at all, I think each bank acting as a guarantor should in turn have liquidated some portion of the firm's acceptances as if the bills had borne their own name. On that system provision must have been made in case of need by the sale to some foreign market, if necessary, of securities, the proceeds of which would have furnished any increase in the gold that might be required. Some people may remark that that would have been a roundabout way of achieving the same result; but I repeat that the great central bank, holding the ultimate reserve of the country for immediate pressing needs, ought under no conceivable circumstances to be locked up to the extent of nearly one-half its capital with unsaleable foreign securities, and I think time and reflection will show that that opinion is a sound one. To reply that there was no alternative is not true. I say advisedly that the Barings could have been prevented from stopping payment without the necessity of the Bank of England placing itself in the position it did. The liability assumed by the Bank of England could have been more spread out without any greater danger of loss to the community than has been incurred. There was the alternative of a limited liability company, which was perfectly feasible if the right people had been called in in time.

There is still another point with reference to the policy pursued by the Bank in that matter. If the point be conceded that the leading bank in the country was not justified in fettering itself as it did even under such very grave circumstances, it must be conceded also that, being in that dangerous position, not a moment was to be lost in getting out of it, for I take it that there can be no difference of opinion upon the point that, the moment the Bank was in possession of a fair bid for the residuum securities of the Baring estate, they were bound to take it. Offers were made to them even before the last of the acceptances had run off, but nothing was done; perhaps there are reasons why nothing in this direction could be done. If so, we should all like to know what they were. Meanwhile affairs both political and

financial in the Argentine Republic were, not only not visibly improving, but at times threatened to relapse into still greater confusion than had been witnessed. By waiting the Bank of England might perhaps benefit considerably the Baring estate ; but by waiting the shareholders of the London joint-stock banks might on the other hand have to forego a dividend.

It will appear, no doubt, to some people ungrateful and uncharitable to endeavour to weaken the position which the prompt and energetic action of the Bank of England has placed them in in the public estimation. It can very easily happen that in such grave and exciting circumstances as those in which they found themselves when that momentous decision had to be taken, the judgment might be somewhat unhinged, and besides it could not perhaps have been foreseen that the Bank would have to come under such heavy advances. But in treating matters of this sort, sentiment ought not to be allowed to stand in the way of an outspoken opinion on the course pursued because susceptibilities may be ruffled. The duty of those who are in a better position than the generality of observers to form a judgment in such matters, is to force the discussion of a principle such as that in question, even at the risk of that judgment being afterwards pronounced to be wrong. The question I have raised is : Should the Bank of England under similar, or nearly similar circumstances, take such a responsibility upon itself again ? So far all has gone fairly well ; but no one could foresee that, and such being the case, I think the conclusion must be arrived at, that the first Bank in the empire should not, to prevent the fall of one firm, no matter how big, place itself in such a position that, in the event of similar disasters following, it would have to confess itself unable to afford any assistance.

ARTHUR CRUMP

THE PORTUGUESE CRISIS

IT is always impossible to dissociate politics from national finance. In the case of Portugal finance is not a section of politics ; it is the chief part, and almost the whole. Accordingly, political trouble has ensued upon trouble in Portuguese finance. A Ministry has been overthrown ; revolution is still looked for as the possible offspring of social discontent. The country, deprived of the help of the financiers, and short of the usual inflow of foreign capital, is distressed. Finance, and nothing else, is at the root of the whole crisis ; finance, and nothing else, needs to be considered.

For many years past Portugal has been accumulating fresh debt, while making no attempt to pay off old. The amount of Portuguese 3 per cents. was, in 1872, 66 millions sterling ; the amount is now considerably over 100 millions, and bonds of other denominations exist. How, then, has this increase been brought about ? The answer is : by corruption among the official classes ; by the aid of eager financiers, who undertook to find the ever-growing floating-debt from time to time, and made large profits on the transactions : by the feebleness of the Portuguese Government, which was throughout too ready to borrow afresh rather than impose taxes for the purpose of meeting national liabilities ;