WILLIAM PITT, THE BANK OF ENGLAND, AND THE 1797 SUSPENSION OF SPECIE PAYMENTS: CENTRAL BANK WAR FINANCE DURING THE NAPOLEONIC WARS

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MODERN MILITARY ENGAGEMENTS are made possible by a state's ability to easily acquire revenue. Central banking and the circulation of fiat currency enable the state to control the money supply and to fund any national interest the government deems worthy. By either taking the money from its citizens via taxation, borrowing funds through bonds or loans from private financiers or other governments, or inflating the currency by issuing bank notes without the backing of specie or another commodity, Western governments wield enough power over money and banking to fund any venture. British involvement in the Napoleonic Wars was no exception to the rule. By manipulating the currency and controlling the supply of money through the policies of William Pitt the Younger, Parliament, and the Bank of England, the British were able to satisfy its military ambitions. The Suspension of Payments in 1797, moreover, played a central role in wartime financial policy. Suspending payments of specie enabled the British government to fund its engagements abroad by inflating the currency and expanding the public debt, which was ultimately paid by acquiring funds through taxation. This paper examines the role of the British government, including William Pitt and Parliament, and the Bank of England in manipulating the currency, by borrowing, taxing, and issuing Bank notes to fund the war with Napoleonic France in the late eighteenth and early nineteenth centuries.

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British Central Banking

Central banking in England rose out of the British government's demand for funds to continue King William's War in the 1690s, on the heels of the Glorious Revolution. Public confidence in the government reduced dramatically as a result of ongoing war and rising military expenditures. Private creditors became hesitant to loan money to the government in this time when revenue ran desperately low. In 1694, the British government accepted the proposal from William Paterson to establish the Bank of England; the government received its badly needed loans in return for granting special privileges to the Bank. Paterson further demanded that the government deem the new Bank's notes legal tender. The British government refused, but Parliament did grant the Bank the power to issue new notes to pay for government debt and the advantages of holding all government deposits. The Bank of England was thus created as a way to serve the military interests of the British Empire.[1]

Two years after its founding, the Bank experienced its first experiment with suspending payments, an act that foreshadowed the Bank's enormous influence in the future. To buy government debt, the Bank of England issued £760,000 in bank notes, which immediately caused inflationary effects on the British economy. A run on the Bank ensued, and the central bank became insolvent. In May 1696, Parliament allowed the Bank to suspend payments of specie. In other words, the Bank could refuse to pay its "contractual obligations of redeeming its notes in gold…yet in operation, issuing notes and enforcing payments upon its *own* debtors."[2] Accordingly, the Bank of England suspended specie payments, effecting a severe depreciation of bank notes in circulation because of the uncertainty of the Bank in the future to resume payments in gold. Specie payments resumed two years later, but the early history of the Bank continued to be plagued with a record of periodic suspensions of payment, and Parliament continued to grant special privileges to the Bank to serve the interests of government revenue. The Bank of England, thus, wielded impressive power over the supply of money that made it easier for Britain to engage in military conflict without having to persuade private investors for loans.[3]

In 1708, the Bank of England received a generous gift from the British government. During a war with Louis XIV, Parliament restricted associations and banks of more than six individuals from engaging in banking business in

[1] J. Lawrence Broz, "The Origins of Central Banking: Solutions to the Free-Rider Problem," *International Organization* 52, no. 2 (1998): 244–45, Murray N. Rothbard, *The Mystery of Banking* (Auburn, Alabama: Ludwig von Mises Institute, 2008), 177–79.

[2] Rothbard, *The Mystery of Banking*, 180.

[3] Ibid.

England. This act essentially granted the Bank a monopoly over the issuing of bank notes; its only competitors afterward were small country banks of fewer than seven partners. Creditors were thus limited to storing their money at these small banks or with the Bank of England. The Bank regarded this monopoly over paper currency as essential to profitability, making concessions to the government as a way to protect and expand its control. The government, thus, had no problem with continuing to enforce the monopoly, because the Bank was a central figure in financing foreign wars. [4]

In return for government support, the Bank continued to show *its* loyalty. In 1742, just before the Bank was due for rechartering, the Bank, not by coincidence, provided the government with an interest-free loan. The government expressed its gratitude by confirming its monopoly power, which reinforced the privilege of issuing bank notes, and extended its charter until 1764. In that year, when it came time to extend the charter again, the Bank presented the government with a £110,000 gift on top of a cheap subsidized loan. The government gladly received another subsidized loan in 1781 in return for another extension of the Bank's charter until 1812. The government, as it was seen, needed the Bank's financing as much as the Bank needed the government's power of rechartering, special privileges, and authorization of the monopoly over issuing bank notes.[5]

The Bank, in essence, operated in two spheres of influence. Privately, it exercised influence over foreign and domestic trade. Not by legal tender law but by common market agreement, its notes circulated within London to the exclusion of all other banks' paper. The Bank also operated beyond the limits of ordinary banking. It "issued the coin, managed the debt, took charge of government deposits, and made advances to the Exchequer and the Treasury, on security of Exchequer Bills."[6] The Bank similarly maintained the supply of gold and bought, at a fixed rate, all gold that arrived at its counters waiting to be redeemed. It, moreover, obtained the exclusive privilege of discounting government paper, of holding public balances, and of circulating its bills through government channels.[7]

As a result of Britain's involvement in numerous wars in the eighteenth century, including Queen Anne's War, the War of Jenkin's Ear, the French and Indian War, and the American Revolutionary War, a massive public debt accrued. In 1783, the national debt consisted of £243 million in government loan stock. William Pitt attempted to reduce this debt in 1786, by means of a

[4] Broz, "The Origins of Central Banking: Solutions to the Free-Rider Problem," 247.

[5] Ibid, Rothbard, *The Mystery of Banking*, 181.

[6] "The Bank of England Restriction, 1797–1821," *North American Review* 105, no. 217 (1867): 393–94.

[7] Ibid.: 394.

sinking fund. This financial instrument was fed by taxes formerly paid as interest on bonds redeemed by the government. In other words, it accumulated interest based on an original government deposit, and the fund constantly returned greater dividends as the original deposit grew. The fund was built on the words of Richard Price, "A Sinking Fund fed by interest is a fund constantly increasing."[8] Initially, it slowly reduced the public debt, as Pitt noted:

> By means of the sinking fund, we had advanced far in the reduction of the national debt…But…we shall have far to go before the operation of that fund, even under the influence of peace, can be expected to counteract the effects of the war…The principle I have in view is such that…we shall not owe more than at the beginning. I cannot, indeed, …say that the war will not stop the progress of the plan of liquidation; but if the means to which I look be adopted, it will leave us at least stationary—it will leave us where we were…Its effects…will go farther, it will go to the exoneration of the nation from increased burthens and to the relief of those who are to follow us…"[9]

As soon as the war began in 1793, though, the government accrued greater liabilities and added to the debt that Pitt attempted to alleviate; but, Pitt was forced into a war that he did not want to fight or fund.[10] Pitt kept taxes low in the first few years of the war by borrowing instead of taxing. Since borrowing accrued debt faster than the sinking fund's interest could accumulate, the national debt was increasing instead of slowly diminishing. The sinking fund, the Britons criticized, wasted public money and led to higher levels of taxation in the long term. By the end of the war in 1816, the accumulated nominal British public debt accumulated to £792 million, which equaled about 250 percent of Britain's national income.[11]

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[8] Patrick Karl O'Brien, "Mercantilist Institutions for the Pursuit of Power with Profit: The Management of Britain's National Debt, 1756–1815," in *Working Papers No. 95/06* (London School of Economics, 2006).

[9] Richard Cooper, "William Pitt, Taxation, and the Needs of War," *Journal of British Studies* 22, no. 1 (1982): 100.

[10] The Editor of the Diary, *A Corrected Detail of the Speech of the Right Honorable William Pitt, Chancellor of His Majesty's Court of Exchequer, Delivered in the House of Commons, on Tuesday the 12th Instant, Preparatory to His Motion for an Address on His Majesty's Message, Relative to the War with France. To Which Is Added, the Decree of the 19th of November, 1792.* (London: W. Woodfall, 1792).

[11] "The Bank of England Restriction, 1797–1821," 396, Cooper, "William Pitt, Taxation, and the Needs of War," 94–95; O'Brien, "Mercantilist Institutions for the Pursuit of Power with Profit: The Management of Britain's National Debt, 1756–1815," 5; J.F. Wright, "The Contribution of Overseas Savings to the Funded National Debt of Great Britain, 1750–1815," *Economic History Review* 50, no. 4 (1997): 657; *idem*, "British

Drain of Specie and Suspension of Payments

England declared war on France in February 1793. After beginnings that were favorable to England and her allies, the tide of the war quickly turned for France's benefit. The next few years witnessed continual victories for the French. During this time, many of England's allies settled their grievances with France through peace treaties, leaving England to wrestle with France alone. By 1797, the economic and military situations looked bleak. In February of that year, fear of a French invasion caused a run on the banks, forcing the Bank of England to suspend payments. This move essentially took Britain off of the gold standard, further damaging the country's confidence in the financial sector. [12]

At the beginning of the war, in 1793, financial strains on the government were light. In the financial year of 1792–1793,[13] which included eight months of war, the British government borrowed only casually; Pitt desired to preserve the progress made from the sinking fund.[14] The next year, however, borrowing increased to about ten million pounds, the total revenue being approximately £18–19 million. Financial troubles began in 1794–1795, when the first heavy calls began to be made on the bank, and the deficit met by borrowing shot up to £20 million. From time to time, but occurring more frequently now, Pitt asked the Bank for advances to fund his military ambition. Traditionally, the Bank was prepared to go a long way to accommodate the government's requests, as it had done before in wartime. But in the spring of 1795, foreign exchanges, which were due to the Treasury's issuing of bills payable at the Bank, showed an injurious tendency. A continuous flow of bills with no reserve backing began arriving at the Bank demanding payment, causing a misgiving to the Bank. In 1795, the quantity

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Government Borrowing in Wartime, 1750–1815," *Economic History Review* 52, no. 2 (1999): 355.

[12] Cooper, "William Pitt, Taxation, and the Needs of War," 95–96, Albert Feavearyear, *The Pound Sterling: A History of English Money* (Oxford: Clarendon Press, 1963), 179–81, Frank Whitson Fetter, *Development of British Monetary Orthodoxy, 1797–1875* (Cambridge, Mass.: Harvard University Press, 1965), 19–21, R.G. Hawtrey, "The Bank Restriction of 1797," *Economic Journal* 28, no. 109 (1918): 53–54, Edwin Walter Kemmerer, *Gold and the Gold Standard: The Story of Gold Money, Past, Present and Future* (New York: McGraw-Hill, 1944), 41–42.

[13] The financial year at that time ended in October.

[14] The Editor of the Diary, *The Speech of the Right Honorable William Pitt, Chancellor of the Exchequer, on Friday, the 17th Day of February 1792, on Proposing the Application of an Additional Sum for the Reduction of the Public Debt, and the Repeal of Certain Duties on Malt, on Female Servants, on Carts and Waggons, on Houses, and on Candles.* (London: W. Woodfall, 1792).

of bills outstanding, which had never previously exceeded £9 million, rose to nearly £13 million and continued to grow.[15]

In August of that year, additionally, greater strain on reserves precipitated with the French restoration of its gold standard following the hyperinflation of the *assignat*. Any specie that flowed inward during the reign of the *assignat* flowed back to France as financial confidence in France returned. During the next two years, Bank circulation steadily diminished, as the supply of gold became smaller and smaller. But, the contraction policy did not bode well for Pitt, who insisted on advances.[16] The drain of gold continued, and reserves fell from £6,000,000 in 1795 to £2,000,000 in August 1796. During the same period, circulation of bank notes fell from £14,000,000 to £9,000,000.[17] The Bank tried to close the gap between the number of notes and the amount of reserves, but as "violent as this contraction was, it failed to counteract the causes of the drain. Foreign subsidies, the payment for large quantities of imported grain, and of articles the price of which had been enormously increased by the war demand, prevented the exchange from rising."[18]

Demands on the bank became continually exhaustive to the Bank's specie. Alarm came at the end of 1796 with the threat of invasion. The small French force was put down upon landing, but it caused widespread panic. Britons, in a frantic attempt to secure their money, demanded their gold at their country banks, which in turn caused a demand on the Bank of England. In February 1797, reserves fell to a low of about one million pounds. The Bank could no longer meet the demand for specie, and an Order in Council was issued on 27 February to forbid the Bank to pay specie until the will of Parliament could be known.[19] But, this is not to say that the government did not use this crisis to its advantage. Preying on the fears of the British, the government printed, in the *Oracle and Public Advertiser*, "But as the resources of this country are immense, A FIRM RELIANCE ON GOVERNMENT in

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[15] Feavearyear, *The Pound Sterling: A History of English Money*, 179, J.H. Clapham, "The Private Business of the Bank of England, 1744–1800," *Economic History Review* 11, no. 1 (1941): 79.

[16] William Graham Sumner, *A History of American Currency, with Chapters on the English Bank Restriction and Austrian Paper Money, to Which Is Appended "The Bullion Report"* (New York: Greenwood Press, 1968), 231–33, Hawtrey, "The Bank Restriction of 1797," 53–54, Fetter, *Development of British Monetary Orthodoxy, 1797–1875*, 19.

[17] "The Bank of England Restriction, 1797–1821," 397.

[18] Ibid.

[19] Feavearyear, *The Pound Sterling: A History of English Money*, 181, Hawtrey, "The Bank Restriction of 1797," 56, Sumner, *A History of American Currency, with Chapters on the English Bank Restriction and Austrian Paper Money, to Which Is Appended "The Bullion Report"*, 232–33.

the day of danger, and an energetic support of PUBLIC CREDIT, will discomfit the enemy."[20]

In the end, the drain of specie from the Bank was attributed to three causes. First, the government made heavy demands for advances to meet wartime expenditures, which often included the transfer of large sums to the military in Europe. Second, the return of France to a gold-backed currency after Her years of trying to manage the disastrous hyperinflation of the *assignats*, moreover, pulled specie from Britain back to France. This bullion no longer flowed to Britain as a way of keeping it safe from devaluation by ill-advised French policy. And finally, the drain also resulted from an unstable and unpredictable political environment in Britain, which contributed to the heavy demands on the Bank for gold.[21] During the years 1794–96, bullion was still easily obtainable at the bank. Payments of specie caused a heavy drain of reserves without affecting its market price too much. It was this drain that subsequently precipitated the Bank suspension. The suspension, then, took the Bank off of the gold standard, enabled it to issue notes freely without specie backing, and retained for it the ability to accumulate treasure without dolling it out. [22]

War Expenditures

The British government committed to massive expenditures during the war, including loans and subsidies to other countries and military spending in general. Subsidies to aid allies began in 1793, when Britain offered funds to Hanover, Hesse-Cassel, and Sardinia. The next year, England gave £2,500,000 to the King of Prussia. Throughout the war, subsidies to Hesse D'Armstadt, Baden, Brunswick, Portugal, Austria, Russia, the prince of Orange, Sweden, Sicily, Morocco, and "Minor Powers under engagements with the Duke of Wellington" totaled close to £50,000,000. Remarkably, though, more than half of that total was paid in the last four years of the war.[23] This financing came predominantly out of strict payments rather than loans. The only loans that the British offered were:

1794–96: The Emperor of Germany, £4,600,000 (guaranteed loan).

[20] "The Bank," *Oracle and Public Advertiser* February 20, 1797.

[21] Kemmerer, *Gold and the Gold Standard: The Story of Gold Money, Past, Present and Future*, 42.

[22] Norman J. Silberling, "Financial and Monetary Policy of Great Britain During the Napoleonic Wars," *Quarterly Journal of Economics* 38, no. 2 (1924): 232.

[23] C.P.H., "War Loans Versus Subsidies: A Note on Great Britain's Advances to Her Continental Allies," *Foreign Affairs* 9, no. 4 (1931): 684, J.H. Clapham, "Loans and Subsidies in Time of War, 1793–1914," *Economic Journal* 27, no. 108 (1917): 495.

1796–97: The Emperor of Germany, £1,620,000 (of which £1,200,000 were sent by Pitt without Parliamentary authorization. The loan was not repaid. Much of it went to pay interest on the first loan).

1809: Portugal, £600,000 (payment maintained only to 1815).

1813: The House of Orange, £200,000 (not guaranteed; repaid).

1814: French Bourbons, £200,000 (not guaranteed; repaid).[24]

In addition to England's massive military spending, moreover, they handed out subsidies to every European nation except Turkey.[25]

Military spending included "ordinary" and "extraordinary" expenditures. Ordinary expenses comprised of sums specifically granted by Parliament, and extraordinary expenses included expenditure for which ways and means were not previously provided but which were funded when it became necessary.[26] British armies abroad acquired their support from officers, known as deputy-paymasters, who drew bills of exchange on the two paymasters-general of the forces in London. The paymasters-general paid the notes from accounts kept with the Bank of England. The extraordinary expenses were financed by officers called commissaries-general, who drew bills directly on the Treasury. Naturally, these bills were always payable by and at the Bank. Much of the government financing at the time by the Bank through purchases of Exchequer bills was for the purpose of meeting these expenditures as well as the funding of the subsidies to foreign governments. Initially, the bank was prohibited from lending to the government, except by permission of Parliament. But, Pitt took advantage of the act of indemnity from 1793, which repealed the restriction on the amount that the government could borrow. [27]

British fiscal policy before 1789 followed a pattern of tax smoothing—borrowing during wartime and paying back the debt by taxing during peacetime. Wartime expenditures were primarily financed by the issue of unfunded debt in the form of various "short-term obligations that included army, navy, ordnance [*sic*], and, increasingly, exchequer bills. The 'funded

[24] Silberling, "Financial and Monetary Policy of Great Britain During the Napoleonic Wars," 225.

[25] Clapham, "Loans and Subsidies in Time of War, 1793–1914," 495.

[26] Silberling, "Financial and Monetary Policy of Great Britain During the Napoleonic Wars," 222.

[27] Ibid.: 222–23, Sumner, *A History of American Currency, with Chapters on the English Bank Restriction and Austrian Paper Money, to Which Is Appended "The Bullion Report"*, 231, Glyn Davies, *A History of Money* (Cardiff: University of Wales Press, 1994), 298.

debt' or long-term securities, secured by specially earmarked indirect taxes, were mostly used during and after the war to retired the more costly unfunded debt."[28] After servicing costs and paying down the debt, the government could then borrow even larger amounts in succeeding military conflicts.

From the beginning of the war until the suspension of payments, 90 percent of expenditures were financed through traditional borrowing. In this period alone, the national debt doubled. The Napoleonic Wars required a much greater amount of funding than any engagement previously. Declining public confidence in fiscal management and increasing pressure on the government to continue to find ways to fund the war led to the suspension of payments and the introduction of an income tax in 1799. Traditionally, the gold standard kept the Bank of England and the British government honest in their war financing. But, as Bordo and White note, these circumstances were different: "The sale of government securities which otherwise would have been absorbed by the Bank competed with private securities, forcing up interest rates to unprecedented levels. Private borrowers then turned to the Bank, which responded by rationing credit in December 1795."[29] Direct government lending to the City helped to loosen credit, but the Bank's response to the diminishing reserves tightened the government's war financing. The eventual massive external drain and a run on country banks forced the government to allow the Bank to suspend specie payments in 1797.[30]

War Finance: Borrowing, Taking, and Making

The British government financed the war in three ways: borrowing, taxing, and printing notes. The government borrowed through the sale of paper securities to private capital markets. This complex operation involved the British Chancellor of the Exchequer and his advisors in the business of managing the national debt. Depending on the level of expenditure, the higher the level of taxes levied on the population, the lower the government needed to borrow. Given that the state usually repaid the debt in peacetime that accrued from borrowing during wartime, only the net amount of money borrowed could be used for the purchase of commodities and services by public agencies and to meet interest payments on the national debt. As O'Brien explained,

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[28] Michael D. Bordo, "A Tale of Two Currencies: British and French Finance During the Napoleonic Wars," *Journal of Economic History* 51, no. 2 (1991): 304–05.

[29] Ibid.: 310–11.

[30] Ibid.: 311.

> the wider the gap between total receipts from the sales of bonds and bills and expenditures upon their redemption, the higher the proportion of borrowed money available for the finance of 'real' expenditure would become. At the same time the national debt would accumulate more rapidly. As the volume of debt redeemed grew the amount of current loans available for other forms of expenditure became comparably smaller. When the repayments of debt exceeded funds borrowed over the year, the Government in effect allocated taxes to meet obligations to its creditors, and the amount of debt outstanding and the interest bill then declined…[O]nly if the Government possessed a surplus of tax income over expenditure on resources could effective reductions be made in the size of the national debt.[31]

Debt management in the eighteenth century dealt with the sale and redemption of bonds and bills. The government's primary focus was to facilitate the flow of revenue into the Exchequer at the lowest possible cost to the public and without the public's knowledge of precisely how much was being spent on military expenditures.[32] Adam Smith explained this tendency of government regarding wartime finance:

> The ordinary expense of the greater part of modern governments in time of peace being equal or nearly equal to their ordinary revenue, when war comes they are both unwilling and unable to increase their revenue in proportion to the increase of their expense. They are unwilling for fear of offending the people, who, by so great and so sudden an increase of taxes, would soon be disgusted with the war; and they are unable from no well knowing what taxes would be sufficient to produce the revenue wanted… The facility of borrowing delivers them from the embarrassment which this fear and inability would otherwise occasion. By means of borrowing they are enabled, with a very moderate increase of taxes, to raise, from year to year, money sufficient for carrying on the war, and by practice of perpetually funding they are enabled with the smallest possible increase of taxes, to raise annually the largest possible sum of money.[33]

Of the three phases of the war,[34] government borrowing as a percentage of national income was highest in the first, between 1793 and 1801. During this period, Britain borrowed 11.6 percent as opposed to 4.3

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[31] O'Brien, "Mercantilist Institutions for the Pursuit of Power with Profit: The Management of Britain's National Debt, 1756–1815," 7.

[32] Ibid., 11.

[33] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, 5th ed. (London: Methuen & Co., 1904), Book V, Chapter 3.

[34] Phase 1 (1793–1801); Phase 2 (1802–1810); Phase 3 (1811–1815)

percent in 1802–1810, and 9 percent in 1811–1815. Aggregate government borrowing per annum, though, was highest in the third phase with £25.3 million per year. Just over 20 million pounds per year were borrowed in the first phase and about 11 million in the second. Although these funds were almost exclusively borrowed domestically, the national debt accumulated accordingly.[35]

The raising of funds by taxation was tenuous and less successful in the first half of the war than in the second.[36] Pitt decided, then, that "if there ever can be a moment in which necessity calls for a change of system, that moment is now arrived."[37] His plan passed the House of Commons in January 1798 in the form of a "triple assessment" tax. This method of taxation was a "kind of jury-rigged income tax based on past payment of assessed taxes. If a person had paid a certain amount in assessed taxes, that was taken as proof of a certain level of income, and he was taxed accordingly on a graduated scale. Thus someone who had paid £20 in assessed taxes paid three time the amount, or an additional £60, under the triple assessment, while someone who had paid £100 in assessed taxes paid four times that, or £400."[38] The implementation of the tax did not last long, as it did not meet the financial projections that Pitt hoped it would.

As a result and because of concern over the rapidly increasing size of the national debt, Pitt implemented an income tax in 1799. The Income Tax Act repealed the triple assessment and charged a graduated levy on all incomes above £60, not just on payers of the assessed taxes.[39] The tax, along with a property tax, succeeded in raising almost 20 percent of the total tax revenue by the war's end.[40] In the first three years, the income tax raised £6 million per year. The range of indirect taxes, additionally, widened as far as possible. Sidney Smith, in the *Edinburgh Review* in January 1820, complained about these taxes:

> Taxes upon every article that enters the mouth, or covers the back, or is placed under the foot—taxes upon everything which is pleasant to see, hear, feel, smell, or taste—taxes upon warmth, light, locomotion—taxes on everything on earth—on everything that comes from abroad or is grown at home—taxes on the raw

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35 Wright, "British Government Borrowing in Wartime, 1750–1815," 356, 59.

36 Silberling, "Financial and Monetary Policy of Great Britain During the Napoleonic Wars," 216–18.

37 Cooper, "William Pitt, Taxation, and the Needs of War," 99.

38 Ibid.: 100–101.

39 Ibid.: 102.

40 Bordo, "A Tale of Two Currencies: British and French Finance During the Napoleonic Wars," 312, E. Victor Morgan, *The Theory and Practice of Central Banking, 1797–1913* (New York Augustus M. Kelley, 1965), 2–3.

> material—taxes on every fresh value that is added to it by the industry of man—taxes on the sauce which pampers a man's appetite, and the drug that restores him to health—on the ermine which decorates the judge, and the rope which hangs nails of the coffin, and the ribands of the bride—at bed or board, couchant or levant, we must pay.[41]

Unlike previous wars, total revenue gained by taxation made up a far greater portion of government expenditure than borrowing, peaking at 30 percent.[42] Through long-term borrowing and heavy taxation, the government acquired so much money during the war that the national debt increased from £273 million in 1783 to £816 million in 1816.[43]

As a result of the suspension of payments, the Bank acquired new privileges. The Bank was now permitted to issue notes in increments of less than five pounds. One and two pound notes began to be printed, driving gold from ordinary use and being deposited in return for paper. The Bank restricted payments in specie, but gladly received treasure.[44] The Bank also, with its accumulated privileges, obtained the power to affect general credit conditions. The Bank, moreover, played a central role in the supply of credit during the restriction period of 1797–1821. And, because most of the reserves of the country banks were Bank of England notes, it is easy to see that the influence of the Bank over the monetary setting in London as well as Britain as a whole increased dramatically after 1797.[45]

Since the Bank's founding, monetary manipulation was relatively restrained by the gold standard. On the gold standard, when the Bank over-issued its notes causing their market price in terms of gold to fall, people would simply trade their gold for notes at the low price and then re-exchange them at the Bank for gold at the higher price. The convertibility of specie, in other words, limited the Bank's issuing of paper. Until the suspension of specie, the rate of inflation was negligible. During the suspension of payments, which lasted until 1821, the Bank essentially became little more than the monetary arm of the Exchequer. Inflation ensued, and the value of sterling depreciated significantly against other European currencies. The value of money as a commodity plummeted, as the total quantity of cash

[41] Davies, *A History of Money*, 298.

[42] Bordo, "A Tale of Two Currencies: British and French Finance During the Napoleonic Wars," 312, Morgan, *The Theory and Practice of Central Banking, 1797–1913*, 2–3.

[43] Davies, *A History of Money*, 299.

[44] "The Bank of England Restriction, 1797–1821," 402–03.

[45] Ian P.H. Duffy, "The Discount Policy of the Bank of England During the Suspension of Cash Payments, 1797–1821," *Economic History Review* 35, no. 1 (1982).

notes was now determined by the will of the Bank of England and the government.[46]

Political ramifications because of the inflation and depreciation of notes caused by the suspension

> brought about a redistribution of wealth from all creditors and producers of nontradable goods to all debtors and tradables producers. No longer was the Bank controversial because its legal monopolies privileged one group of creditors against all others. Since its notes were now fiat currency and the government financed much of the war through inflation, two large intersectoral coalitions formed. The key beneficiaries of suspension were farmers and manufacturers. Tenant farmers found strong incentives to support the existing state of monetary affairs, since 'the price of the farmers' crops was rising whilst they were continuing to pay the same rents in depreciated notes…' Farmers and debtors of all classes gained from suspension, since they made interest and principal payments in a currency worth about 17 percent less in gold than when their debts were contracted.[47]

Under France's *ancien régime*, the National Assembly inflated the *assignat* to no return. Even though the French did not establish a central bank until 1800, the creation of the *assignat*—which was initially implemented to confiscate church lands and retire the national debt—led to the same inflationary disaster. Following the collapse of the *assignat* and the suspension of payments, it was the British who gave inflationary monetary policy a try.[48] Government wartime expenditures abroad strained the currency. Wartime spending rose from £400,000 in 1797–1798 to £2,400,000 in 1799–1800. The Bank's short term advances to the government rose from £6 million in 1797 to £11 million in 1800. The Bank's issue of paper, more importantly, expanded from £10–11 million in 1796 to nearly £16 million in 1800. The price of sterling silver, in addition, rose dramatically, and commodity prices rose 20 percent. The price of food also rose sharply in 1799. The effects of this inflationary crisis took another two years to fade.[49] Throughout the restriction period, the depreciation of the bank notes accelerated, as the

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[46] Ibid.: 248–49, The Select Committee on the High Price of Bullion, *The Paper Pound of 1797–1821: The Bullion Report*, ed. Edwin Cannan (New York: Augustus M. Kelley, 1925), xix.

[47] Broz, "The Origins of Central Banking: Solutions to the Free-Rider Problem," 249.

[48] Bordo, "A Tale of Two Currencies: British and French Finance During the Napoleonic Wars," 303.

[49] Feavearyear, *The Pound Sterling: A History of English Money*, 191–92, Fetter, *Development of British Monetary Orthodoxy, 1797–1875*, 30.

quantity of paper continuously grew. As one observer of the inflation noted, prices rose in "every thing that is bought and sold, and an ever-craving, never-satisfied itch of speculation and gambling, in the place of wholesome and natural trade."[50]

Despite the potential disastrous consequences of temporarily moving to an incontrovertible and fiat currency, the British faired well when compared to the French model. The mistakes of the policies surrounding the French *assignat* did not translate into the same disastrous results for the British because the Bank of England always intended to resume specie payments. Although payments were suspended and the Bank enacted inflationary measures, complete devastation via hyperinflation never occurred because the Bank still collected specie during the restriction with hopes of soon returning to gold-backed notes. For the time being, the public had enough confidence in British money as a reserve currency, so long as the possibility of resuming payments existed. If the Bank knew from the beginning that the suspension would last all the way until 1821, policies in the first few years of the restriction may have been more radical, for no end was in sight. Instead, the Bank anxiously kept on its toes throughout the restriction period, making urgent pleas to Parliament to restore specie payments, which also translated into a hopeful confidence in the currency.[51]

The French created the *assignat* to pay the deficit remaining from the collapse of the monarchy and to reduce part of the public debt. The state used this paper money to pay its creditors, who then turned and bought the nationalized properties of the church. The outbreak of war in April 1792, created a growing deficit paid for by the creation of *assignats*. In the following years, the French revolutionary Terror government attempted to control inflation by implementing price controls and forced loans, but it failed miserably. Hyperinflation of the *assignats* ensued and the French abandoned them for a new paper money, the *mandats*. The *mandats* similarly inflated to the point of no return and served as the final example of France's eighteenth-century failed stint with fiat currency; the French, consequently, then returned to a currency backed by specie and made convertible.[52]

The British story followed a different blueprint. Following the suspension of payments, the government sold much of its short-term debt to the Bank. Until the government could slow expenditures once the war came to a halt, the "share of unfunded loans increased dramatically from a low of

[50] Thomas Doubleday, *A Financial, Monetary and Statistical History of England, from the Revolution of 1688 to the Present Time* (New York: Greenwood Press, 1968), 185.

[51] Bordo, "A Tale of Two Currencies: British and French Finance During the Napoleonic Wars," 310.

[52] Ibid.

19.3 percent in 1797 to a peak of 76 percent in 1808… Measured as the increase in bank notes divided by the average price level, *seigniorage* only exceeded 10 percent of the deficit in 1810 and never rose above 5 percent of war revenue."[53] Ultimately, that the Bank planned on ending the suspension of specie payments prevented the government, and the Bank, from enacting more inflationary policies as it might have under a pure fiat currency.

Easy access to money is the best friend of governments in the state of war. The Bank of England, created to aid in the funding of war, gradually accumulated greater exclusive privileges from the British government to continue the monopolization over the creation, circulation, and loaning of currency to the government. The British government used the Bank of England to its optimal ability to help finance its war with Napoleonic France. The government, by itself, borrowed from and taxed the British people to acquire revenue, and the Bank added another dimension to war financing. Once the Bank suspended payments of gold, the obligation of the Bank to hold reserves diminished, enabling it, essentially, to be able to issue notes at the government's discretion. By removing itself from the gold standard, the Bank of England toiled with the dangers of fiat currency from 1797 to 1821. The action that saved the Bank, and restored public confidence in the currency, was the resuming of specie payments in 1821. By helping to finance the war, the Bank of England served as an early example of central bank war finance.

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[53] Ibid.: 311.

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