

The Origin of the Bank of England

Edward D. Duvall

9 Mar 2022

Note: This essay is extracted from section 1.12 of my book, *The Control and Manipulation of Money*, available for free download at <https://fremontvalleybooks.com>.

One of the lessons of history is that national debt tends to benefit the wealthy to the detriment of the common working people. The reason is that the wealthy can afford to invest in government debt and receive the annual interest payments, and are in no hurry to have the debt paid off. Meanwhile, those investments can still be sold on the open market for their current value. In other words, government debt becomes an asset if the holder thereof can find someone to buy it. It is instructive to examine the details by which the first great national debt with regular financing was developed, namely the example of England beginning with the reign of William III (a.k.a. William of Orange, Holland) and Mary II (Stuart) as related by Walker [1]:

"When William of Orange succeeded to the throne of England [1689], Louis XIV [of France], then at the zenith of his power, refused to acknowledge him as a legitimate monarch, and espoused the cause of the exiled Stuart [James II of England]. War, of course, followed. But fighting, in consequence of the invention of gunpowder, and the changes it gradually introduced into warfare, had become an expensive luxury; a game which kings, with their limited and uncertain revenues, could ill afford to play at, particularly for a great length of time. War with one so powerful as the *Grand Monarque* [Louis XIV] could not be safely commenced or successfully prosecuted, while every penny must be extorted from a reluctant and now independent Commons [Parliament], and the taxes immediately assessed on the large land or other property holders of the realm.

Such was the difficulty which King William encountered; but, fortunately for his fame, he was a shrewd financier, as well as an able soldier. Up to this time, England had never had a permanent organized national debt, a national bank, or any regular and reliable system of revenue. Grants and subsidies had been voted from time to time; duties and special taxes had been imposed, but these were not to be counted upon.

The monarch might and did borrow money from time to time, in great emergencies, but on the most disadvantageous terms. The credit of the government was always low, because there was no regularity or system in the public finances. Men had no confidence in the responsibility or punctuality of the government. William changed all this. He borrowed for a specified period, and promised the punctual payment of the interest semi-annually, and the principal when due; and pledged "the public funds" for the fulfillment of his promises. Hence the public securities [government bonds] were called "the funds".

He negotiated loans and issued stocks [government debt obligations]. He granted annuities upon the payment of specific sums. Interest and principal were secured by a pledge of the public funds, or revenues derived from various sources.

This put a new face upon the financial affairs of England: but something further was desirable; viz., an agency by which the national debt could be readily managed, and its semi-annual interest promptly paid.

This was accomplished by the incorporation of a national bank [Bank of England, 1697], consisting of the holders of the public stocks [government debt], to the amount of £1,200,000.

One thing more was wanting; viz., a permanent and sufficient income, to meet not only the interest on the accumulated debt, but the current expenses of the government, already large, and constantly increasing. To effect this, a land-tax was established; small, indeed, in amount, and upon a fixed valuation, so that it could not be increased with the increasing value of the land.

A system of duties on all imports was also enacted, and an excise upon all home manufactures and products. In short, a system of indirect taxation was adopted, far more general and effective than any which had before existed.

Thus was completed the grand triad of the system of finance, inaugurated by the English Revolution [1688]; viz. -- funding, banking, and indirect taxation. The immediate as well as ultimate, results of the new system are alike remarkable and worthy of our attention.

First, the credit of the government was firmly established. It could borrow more money, and at a lower rate of interest than ever before. Men of small means could now loan money to the government, and with entire confidence. The whole community could be laid under contribution [i.e., payment of taxes].

Second, government was enabled to carry on war by borrowing, instead of imposing taxes. War could be waged with credit, instead of cash. Parliament had only to vote a loan. No expenditure need be stopped for want of funds, while the national credit was unimpaired. This was a great change. Many a war had been abruptly closed for want of funds. There was no such necessity hereafter.

Third, this course removed the fear of immediate and pressing taxation from the rich, because the greater part was now to fall upon the masses of the people, who pay taxes, not in proportion to property, but to consumption [in the form of tariffs and excise taxes]. This was an agreeable consideration to the wealthy classes; and the more so, because, as the public stocks [debt] were multiplied, better opportunities were afforded for investments [in government debt].

Fourth, especially was the new policy acceptable to the aristocracy, who, at that time, even more perhaps than now [1867], monopolized the public offices, and whose revenues and patronage were increased by governmental expenditures."

The American patriot Thomas Paine [2] of *Common Sense* fame and some additional details by Walker [3] give an accounting of how the national debt in Great Britain grew with each war from 1688 (under William III and Mary II) to 1867 (under Victoria), starting with the initial debt (investors in the £1.2 M of government debt administered by the newly formed Bank of England):

- a. War vs. France from 1688 to 1697: cost = £20.3 M; total debt in 1697 = £21.5 M
- b. War of Spanish Succession, 1702 to 1713: cost = £32.25 M; total debt = £53.75 M
- c. Approximately £7.5 M paid off between 1727 and 1739; total debt in 1739 = £46.25 M
- d. War of Austrian Succession, 1739 to 1748: cost = £31.75 M; total debt in 1748 = £78.0 M
- e. Then came eight years of peace, during which £3.0 M of the debt was repaid; the debt in 1756 was £75.0 M
- f. Seven Years War, known in America as the French and Indian War, 1756 to 1763: cost = £72.5 M, total debt in 1763 = £147.5 M
- g. Then came peace for twelve years, and in that time £10.5 M was paid off; the debt in 1775 was about £136.0 M
- h. The American War [American Revolution], 1775 to 1783: cost = £103 M; total debt in 1783 was £239 M
- i. Ten years of peace, and the debt was reduced by £5.0 M; total debt in 1793 was £234 M
- j. The Jacobin War, 1793 up to 1796, when Paine wrote: additional debt to that time was £44.0 M; total debt in 1796 was about £278 M
- k. The total cost of the Jacobin War that ended in 1802 turned out to be £248 M; and the debt in 1803 was £526 M.

l. Then came the final Napoleonic War, from 1803 to 1815, which cost £339 M; the debt in 1815 was £865 M

m. From 1815 to 1835 a total of £87 M was paid off; and the debt in 1835 was £778 M

n. Then 800,000 slaves were emancipated in the West Indies at a cost of about £22 M; and the debt as of 1867 was about £800 M or so

Paine's great contribution was to notice that each war cost about 50% more than the preceding one. He was correct except for the War of Austrian Succession (£31.75 M vs. his projection of £48 M) and the Jacobin War (£248 M vs. his estimate of £162 M). Walker [4] informs us why repayments were so slow during time of peace:

"Because it was no object with the ruling class to pay off the debt, since the national stocks [national debt] had become the most eligible investments [interest paid to the holders of the debt by the government but actually paid by the people]; so the resources of the nation were squandered upon the court [aristocratic class]."

Walker informs us that this convergence of debt and taxation in England resulted in the impoverishment of the working class [5]:

"This is especially apparent in England. What has become of the yeomanry [small independent landowners], once the pride of the country? Their little estates have disappeared; have been swallowed up by the terrible system of taxation to which they have been subjected. The pleasant hedges which still surround the small enclosures, once constituting the freeholds of her yeomanry, may yet be seen in all parts of the country. They are the monuments of an industrious, brave, and independent class of men, now extinct. These lands are indeed tilled by the hands of their descendants, no longer yeomanry, but peasants, almost the paupers of the nation. ...

The economy of a national debt, under the modern financial system, must always impoverish the productive classes. Its entire influence on them is oppressive. It deprives them of their honest reward, by a false currency [i.e., a fiat money], which robs them of a large share of their nominal wages; it imposes upon them, through indirect taxation, an undue proportion of the public burdens, and is in fact, a stupendous engine for depressing them, though perhaps not so intended. Hitherto we have known little of its effects in the United States. Until the present time we have felt little pressure from public indebtedness and consequent taxation; but the case is now [1866] altered. We have an immense debt, and a larger amount of annual interest than any other people on the face of the earth."

References

- [1] Amasa Walker, *The Science of Wealth: A Manual of Political Economy*, Boston, MA: Little, Brown & Co., 1867, pp. 363-365
- [2] Thomas Paine, *The Decline and Fall of the English System of Finance*, an essay dated 6 Apr 1797. It was banned in England for over 20 years, so that should tell you something.
- [3] op. cit., Amasa Walker, pp. 366, 367
- [4] op. cit., Amasa Walker, p. 366
- [5] op. cit., Amasa Walker, pp. 369-371