TOWARDS CENTRAL BANKING

A CENTURY OF GROWTH

WHEN PALMSTRUCH'S BANK was founded in the mid-17th century, Sweden's economy was rather static and dominated by agriculture, with tens of thousands of small farms, many of them self-sufficient, run by the family together with one or two hired hands. An iron industry was emerging and goods that farms needed, but could not produce, were being manufactured but there was little economic activity in

THE CREDIT SYSTEM expands. The evolution of the Bank as a central bank is hampered by political conflicts but Sweden does acquire a well developed banking system. The international monetary policy debate is influential; interest rates are deregulated, the Riksbank starts to use the discount rate and in 1897 the Riksbank Act institutes a modern central bank. The Bank's management becomes more professional. The Riksbank continues to be an agency of the Riksdag, though the chairman of the board is to be appointed by the King-in-Council.

1820s The first savings banks in Sweden.
1824 Proclamation for private banks.
1831 Skånes Enskilda Bank is founded.
1830s Mortgage institutions are introduced.
1834 Currency reform. Silver standard.
1844 Oscar I succeeds Karl XIV Johan.
1855 Currency reform; in the new decimal system; the *riksdaler riksmynt* (*rmt*) is subdivided into 100 *öre*.
1856 A.O. Wallenberg founds Stockholms Enskilda Bank.
1857 Commercial crisis after the boom associated with the Crimean war.
1859 Karl XV succeeds Oscar I.
1861 General Mortgage Bank founded.
1863 Skandinaviska Kredit AB is established. A.W. Björck becomes the Estates' Bank's delegate for internal administration (the first governor in the modern sense).
1864 The Bank of England starts to use its discount rate as a monetary policy instrument. Sweden's interest rate ceiling is abolished for most kinds of loan.
1866 The Riksdag is replaced by a bicameral parliament.
1867 The Bank of the Estates of the Realm is renamed Sveriges Riksbank (National Bank of Sweden).
1868 A.W. Dufwa is appointed 'governor' of the Riksbank.
1871 Stockholms Handelsbank is founded.
1872 Oscar II succeeds Karl XV.
1873 Gold standard. Scandinavian monetary union. New currency unit, *krona*.
1875 Norway joins the Scandinavian monetary union.
1878–9 International financial crisis.
1883 Johan Wolter Arnberg is appointed 'governor' of the Riksbank.
1890 The Baring crisis. The Riksbank uses its discount rate for the first time.
1897 The Riksbank Act institutes the Bank as the central bank of Sweden with an exclusive right to issue bank notes.
1901 Karl Langenskiöld is appointed first delegate (governor) of the Riksbank.
1906 The Riksbank moves into its new building on Helgeandsholmen.
1907 Gustav V succeeds Oscar II.
1907–8 Financial crisis.
1912 Victor Moll is appointed first delegate (governor) of the Riksbank.

the modern sense. The 18th century was somewhat more dynamic but still just a beginning.

Industrialisation and a growing international division of labour in the 19th century generated a more decisive economic transformation. Various inventions contributed to this. New forms of transport helped to expand and diversify world trade, which also benefited from trade agreements that lowered tariffs and other barriers.

In Sweden, the 19th century marked a transition to economic expansion; it was the first century in which output consistently grew faster than the population. Annual per capita growth was quite modest in the first five decades – 0.3 to 0.5 per cent according to Schön (2000) – but sufficient to bring about major changes in agriculture, where much of the transformation began. Sweden, a somewhat backward, sparsely-populated country on the outskirts of Europe, experienced a strong catch-up effect. The economic upswing led to new conditions for industry and trade.

As to the Bank of the Estates of the Realm, an old-fashioned state enterprise was developed into an up-to-date central bank. The growth of foreign trade, accompanied by increased pecuniary flows, accentuated the importance of monetary matters. In particular, the credit market changed in response to greater demands from industry and commerce, accompanied by numerous new instruments and participants.

While Sweden's traditional iron exports continued much as before, in the early 19th century other industries had a growing need for investment and credit. In agriculture, the ongoing transition from strip farming to consolidated holdings initiated a development that required capital. Some farmers needed loans in order to buy more land; the dispersion of villages entailed the construction of many new buildings. Moreover, continuous holdings made it simpler and more profitable to use modern methods of cultivation and procure more expensive implements and machinery. At the same time, the growth of trade opened up a market for large-scale commercial crops. All this generated a rapidly growing demand for agricultural capital.

The first industrial enterprises in Sweden had been manufactories, mainly for textiles, in the 18th century. Factory production started to expand in the 1830s, not least in the consumer goods industries, including sugar refineries, paper mills and printing. Much of the growing demand came from the upswing in agriculture and a more prosperous rural population.

A further impulse came from industrialisation and construction in other countries. The new railways in Britain and elsewhere provided a market for Swedish inputs. Sawmills enjoyed a boom around the middle of the century, by which time manual or water-powered farm saws were being joined by big sawmills that produced for export; the latter had a larger capacity and many of them were powered by steam.

Shortly after 1850 the Riksdag approved the construction of main-line railways and, in order to speed things up, decided to finance this with loans. This was the most spectacular addition to infrastructure. The growth of towns and industrial estates also required large resources.

In the latter part of the 19th century, strong demand abroad boosted Swedish output. Prices for iron ore, iron and timber were firmer than those for many finished goods, which tended to fall in the 1870s and '80s. New production techniques revived the iron mills and the iron trade. Sweden's industrialisation prospered on favourable international conditions.

The daily farm wage fell in real terms in the 1830s and '40s but turned upwards in the next decade. After the disastrous 1860s, real farm wages then rose continuously up to the First World War. Besides an increase in farm productivity, the upward wage trend suggests that labour demand exceeded supply, in agriculture as well as manufacturing, partly as a result of the drain caused by emigration. Increased real earnings strengthened the domestic market. Important factors towards the end of the 19th century were residential construction and the need to provide infrastructure for urban growth.

For Sweden in the 19th century, the international capital market was far more important than it had been before. Dutch and British capital had admittedly helped to finance the iron industry in the 17th and 18th centuries and the Crown had raised large loans abroad, particularly in connection with wars. Now, however, the borrowing requirement was on an entirely different scale.

To meet the greater needs, the credit market became increasingly diversified, with additional institutions and more sophisticated instruments. For many years, however, the question of how the system ought to be developed and held together was stymied by political and constitutional conflicts concerning the Bank and credit in general.

Political forces and controversies changed in the course of the 19th century. The general trend affected banking policy and the status of the Bank.

The Fourth Estate was in the ascendancy. Previously, its most powerful functionary had been appointed by the government, in most cases from the administration. As the Age of Liberty drew to a close, however, the Peasants asserted their own opinions to a greater extent, at first in down-to-earth matters, not least aquavit and its ramifications, then over a wider range of interests. They saw Bank matters as an opportunity of obtaining favourable loans for the transformation of agriculture. There was a tradition of the Peasants being supported by a substantial proportion of the Clergy, whose members were wont to articulate the interests of their parishioners.

The Riksdag was a four-chamber diet of the Estates up to 1866. After the change to an elected, bicameral parliament, the influence of landed farmers was, if anything, greater. Their voting rights in the newly-formed Agrarian Party gave them a powerful position in both chambers. Agrarians dominated the lower chamber and mostly got their way there.

Prior to 1866, one of the arguments for electoral reform had been that new industries were not properly represented – ironworks, other industries and public officials had difficulty in exercising an influence. Their interests were closest to those of the Burghers, but some of them belonged to the Nobility and the occasional professor was to be found among the Clergy. Their views clashed with those of other groups. Officers and conservative officials were strong among the Nobility. Burghers elected to the Riksdag included mayors and councillors with a legal background, as well as representatives of more traditional crafts and businesses. In the bicameral parliament, many representatives of the new industries had seats in the upper chamber. In the latter half of the 19th century the two chambers repeatedly clashed over banking policy.

Then there were the conflicts between the Riksdag and the government. The sovereign's personal power was still a force to be reckoned with. Karl XIV Johan played an active political role and his successors withdrew only gradually. Besides the monarch's political ambitions, the Bernadottes had private financial interests, for example the silver value of the Guadeloupe income or the properties which Karl XIV Johan accumulated, with the Gällivare iron ore as the most enticing asset.

However, the government also included the king's advisers, the elite officials. Although Karl XIV Johan vigorously and stubbornly opposed the currency reform of 1834, it was in these circles that the progressive forces were at work. The government had conservative members as well as advocates of a modern economic policy. Foremost among the latter were Gustaf Fredrik Wirsén, Carl David Skogman and Johan August Gripenstedt.

It was the Bank that brought the conflict between the government and the Riksdag to a head. At this time, banks were being founded all over Europe, some of them out-and-out state banks, others privately owned under state control. In the latter cases, however, the state almost invariably meant the government, whereas Sweden's Instrument of Government sidelined the King-in-Council as regards the Bank and its accountability for monetary policy. This provision was anathema to the government. At the same time, the Instrument of Government assigned financial legislation to the Crown. The government took advantage of this to regulate the emergent banking system on its behalf, to the annoyance of many members of the Riksdag.

THE BANK OF ENGLAND'S EXAMPLE

Developments in the 19th century stimulated economic theory and debate. Schools of political economy were to be found in Britain, France and Germany. In Sweden, academic economics did not attract much attention but people with a political interest and engagement could follow the international discussion and make well-informed contributions. The Swedish Economic Society, formed in 1877, was for many decades a major forum for debate (Herin & Werin, eds., 1977).

Developments in monetary policy were often driven by people with practical experience. Lessons were learnt from the Bank of England, which led the way in developing the functions and methods of a central bank. The debate in Britain launched ideas and theories that left their mark in other countries, too.

The original purpose of the Bank of England was to mobilise capital for the British government. When Charles II caused the Treasury to confiscate the gold deposits of goldsmiths and others, people were reluctant to lend what was needed to finance the war with France. With the installation of William and Mary as constitutional rulers in 1689, parliament assumed direct control of the government finances. In 1694, a number of wealthy merchants founded the Bank of England, which guaranteed its deposits and provided the Crown with loans. The Bank was authorised to issue notes and for a long time was the only joint-stock bank in Britain.

In the next century, other banks and bankers were already depositing growing amounts with the Bank of England, both because its notes enjoyed most confidence and because it was the banker and agent of the government. During the mid-18th century's European and colonial wars with France, Britain had access to far cheaper loans than her opponents, just as the Netherlands had had in the Thirty Years War. The Napoleonic wars added immensely to Britain's national debt. In 1826, when other joint-stock banks were admitted, the Bank of England was already the recognised guardian of the private banks' cash reserves and thereby of the national gold reserve. In 1854, a system was introduced whereby the mutual accounts of other banks were cleared on a daily basis.

The next step was the Bank's acceptance of the function that Bagehot (1873) called lender of last resort. It was the Bank of England which ensured that in a crisis, every solvent bank could meet its commitments. In doing so it assumed responsibility not just for the exchange rate but also for liquidity and thereby for the stability of the country's credit system.

An Act of 1844 during Robert Peel's ministry divided the Bank of England into an Issue Department and a general Banking Department. The Bank's primary function was to ensure the convertibility of its notes by maintaining the ratio between them and the gold reserves. However, a series of economic crises (in 1847, 1857 and 1866) highlighted the relationship between currency and credit. The best way for the Bank to protect the gold reserves was therefore to counteract public fears about credit.

It was soon realised that such fears often concerned a suspension of credit and withdrawals – people rushed to obtain cash while it was still available. So it was up to the central bank to reassure people that credit would continue to be available, albeit perhaps at a higher price for the time being. Money was still available to those who were prepared to pay the required rate; that limited applicants, which calmed the market.

The practical innovations interacted with the theoretical and political discussion. *An Enquiry into the Nature and Effects of the Paper Credit of Great Britain*, published in 1802 by Henry Thornton, a banker and member of parliament, argued that the Bank of England should deploy the discount rate to influence demand for money. It took several decades for his thesis to win

Sweden's monetary system became more stable under Karl XIV Johan (b. 1763, Crown Prince 1810, King 1818–44). Portrait by Fredrik Westin.

adherents. During the crisis of 1839–40, the Bank did try to check the outflow of gold by raising the interest rate; however, the measure was ineffective (the increase was too small) and for a long time this was seen as a reason for not using the rate. Nevertheless, the discount rate did ultimately become an instrument for controlling credit.

Thornton also contributed to the debate on banknote convertibility. Rumours of a French invasion in 1797 had led to such a run on banks that parliament rescinded the obligation to exchange notes for gold. A discussion then arose about the pros and cons of a return to convertibility. James Mill, a Scottish economist, saw no need because banks issued notes only when merchants came to discount bills; as long as the bills were secured, the notes were, too (the real bills doctrine). His opponents (the bullionist school) saw the right to convertibility as a disciplinary measure that counters the temptation to print notes to excess. Sterling's convertibility was restored in 1821.

The 1844 Bank Act then prescribed a fixed ratio between the quantity of banknotes and the Bank of England's bullion. The banking school argued that economic activities took up as many or as few notes as were required; if more notes were issued, no one would need them and they would simply flow back to the banks; a fixed relationship between the stock and reserves was therefore unnecessary. The Bank should adjust the volume of notes to the economic situation; an analysis of exchange rates and interest rates would indicate whether more or fewer notes were called for. The currency school saw the reserve requirement as essential for preventing excessive note issues and thereby inflation. The disciplinarians gained the upper hand but the debate continued into the 20th century.[19]

According to Lobell (2006), those closest to the Bank wanted clear rules and therefore preferred the currency school's plea for a fixed relationship between notes and reserves. The line advocated by the banking school placed greater demands on the Bank and implied a greater risk of its managers being held to account for their assessments.

19 In Germany it was the banking school that prevailed. When fiscal policy there went awry in the early 1920s, the Reichsbank printed notes as fast as it could; in 1922 the bank boasted that it had 30 paper mills and 29 printing-plate factories which kept 7,500 workers employed in its own and 132 other printing shops that helped to satisfy the market's demand for notes. At the end of August 1923 the head of the bank, Rudolf Havenstein, declared that: 'No one denies that the central bank's credits increase the notes in circulation but in so far as the central bank approves economically desirable and necessary credits that support the production and sale of goods, it does not create artificial purchasing power.' Citing the Reichsbank's independence, Havenstein refused to resign; however, he suffered a heart-attack the day after making a speech in defence of independence and died in November 1923, by which time the stock of notes in circulation totalled 192,000,000,000,000,000,000 (quintillion) marks (James, 1999).

In the light of the Bank of England's record, the demands on a central bank were summarised by Walter Bagehot, editor of *The Economist*, in *Lombard Street* (1873), which made a deep impression on the international discussion and has gone through numerous editions. The earliest copy in the Royal Library in Stockholm belongs to the fourth edition but is still from 1873. Developments and the debate abroad left their mark on discussions in the Riksdag of 1834–5. At the Riksdag of 1844–5, just a few months after the British Bank Act, Skogman used that reform as a basis for questions to the bank committee. Much inspiration in these matters was obtained abroad, not least by businessmen, liberal politicians and officials.

SAVINGS BANKS, MORTGAGE INSTITUTIONS AND LIFE ASSURANCE

A fairly complete picture of Sweden's credit and capital markets is not available for periods before the 20th century. Various sources and flows can be discerned in earlier centuries but their relative size and importance have to be guessed.

Loans have almost always been available to those who were able and willing to pay for them. In the days of Palmstruch's Bank in the 1650s, interest rates ranged from 6 to 12 per cent (Heckscher, 1936). When alienated estates reverted to the Crown in 1680, the interest rate was set at 8 per cent, which was low according to some of those affected. Individuals in particular borrowed from each other, while the iron industry was already obtaining capital abroad.

The flows of funds were handled by brokers on the exchanges in Stockholm and Göteborg. Borrowers issued bonds backed by guarantees and mortgages in exchange for funds provided by investors. The brokers negotiated contracts at the interest rate which was acceptable to the parties concerned, sometimes with supplements and commissions to evade the legal limit.

The Estates' Bank was often closed to borrowers. The introduction of discount companies had enlarged the organised credit market, so their demise left a vacuum. This revived the importance of the unorganised and private credit market, even though the Estates instructed their Bank to lend more and establish branches in additional towns. The use of promissory notes was widespread; people with funds in trade, agriculture and public institutions lent their money to other individuals as well as to enterprises against guarantees or collateral.

The development of new institutions began with savings banks, which were established to help the poor help themselves. A widow who managed to put a bit aside, for example, could now deposit it as a buffer against even harder times. The first savings bank had been started in Scotland by Henry Duncan, a minister in Ruthwell, and the idea soon caught on. By 1819 Britain already had 319 savings banks and the movement had spread to France, Prussia and Denmark.

On 5 February 1818 the deputy speaker for the Burghers, Johan Westin, the tanners' alderman, submitted a memorandum to the Riksdag proposing a savings bank movement along the lines in England and Scotland to encourage thrift and consideration. The Riksdag requested the Crown to investigate the matter and the task was assigned to Carl David Skogman, then a young man. His report, 'Intelligence concerning so-called Savings Banks', completed in December 1819, was presented to the King-in-Council together with draft regulations 'which with satisfaction and in grace were approved'. Regulations based on the draft were issued for *Göteborgs Sparbank* (savings bank) in 1820 and *Stockholms Stads* (Urban) *Sparbank* in 1821.

The savings banks were a project for relieving the poor. County governors and bishops (Agardh of Karlstad, Wallenberg of Linköping) were often involved in their formation. In their reports for 1828, county governors were required to assess the situation for savings banks in their county. Many savings bank directors were public officials and burghers, sometimes recruited from poor relief boards.

In time the savings banks extended their operations. The Riksdag of 1828–30 authorised them to invest a part of their funds in the discount companies. Göteborgs Sparbank functioned as a commercial bank in the days before private banking; lending in the first two decades was mainly secured with commercial goods. In the troublesome 1820s, savings banks started to replace money brokers. Moreover, prudent budding capitalists soon saw that placing money in a savings bank was preferable to lending it in person.

Mortgage societies were founded from the 1830s onwards. The first, in

1832, was for foundry proprietors. Regulations for a 'Mortgage Society between Skånska Landowners' were approved by the government on 20 February 1839; five more societies appeared between 1845 and 1851. Capital investment had traditionally been arranged by lending directly to farmers and landed proprietors against property mortgages. The latter now placed their mortgages in a society, which raised capital for all its members. Investors did not have to assess borrowers individually, risk was diversified and by borrowing on a larger scale, a society could obtain better terms than a landowner on his own.

As long-term capital was difficult to come by in the Swedish market, the mortgage societies began to issue bonds abroad, where the practice was familiar and rates tended to be lower. The societies in southern Sweden placed large issues in the German capital market. The business became so extensive that in the 1850s and '60s mortgage institutions dominated the supply of credit. In 1872 the loan stock of the two largest societies – Smålands and Östgöta – still exceeded that of the two largest commercial banks, Skånes Enskilda Bank and Skandinaviska Kreditaktiebolaget.

There were clouds on the horizon, however. Societies placed loans abroad without much coordination. Moreover, they started to issue puttable bonds in the domestic market; an advantageous interest rate made this instrument attractive to many investors and it functioned in practice as a deposit account. The problem was that the money invested in these so called bonds could be withdrawn at short notice, whereas the societies' loans ran for many years. In other words, there was a hazardous imbalance between long-term loans and short-term claims. The crisis of 1857 made the situation untenable. The boom for agriculture ended together with the Crimean War and the mortgage institutions had difficulty in placing their bonds.

The government intervened. In a bill in 1861, finance minister Johan Gripenstedt organised the supply of long-term agricultural credit along the lines in France and Norway. Borrowing was concentrated to the General Mortgage Bank of Sweden (*Allmänna Hypoteksbank*), which channelled the capital to the individual mortgage institutions. The state guaranteed a reserve fund and appointed two of the five directors. The mortgage institutions were debarred from accepting deposits, which were transferred to the banking system.

The mortgage institutions were enmeshed with landowners, the nobility and the commercial banks; ordinary farmers were excluded until

1861. This was a problem when farms with funds to deposit from the export trade in oats were turned down by urban savings banks that lacked borrowers. At the same time, well-to-do farmers were displeased with the early savings banks' concern for the poor. As a result, another type of savings bank was established, based on an ancient jurisdictional district (härad) and promoted politically by members of the Riksdag who were otherwise critical of banks. These savings banks became small-scale agriculture's counterpart to the mortgage societies.

Economic growth and industrialisation in the second half of the 19th century entailed greatly increased construction. The first urban mortgage societies were formed in the 1860s. A general building society for Sweden's towns was established as a private enterprise in 1871. Following an inquiry initiated by the government, the Urban Mortgage Bank of the Kingdom of Sweden (*Konungariket Sveriges Stadshypotekskassa*) was founded in 1910, absorbed the earlier society and operated with twenty-one affiliated urban mortgage societies.

Life assurance was first sold in Sweden in the 1840s by agents of companies in Britain and Germany. Elsewhere in Europe, this way of securing old age with an annuity had started two centuries earlier. The Riksdag of 1844–5 instituted an inquiry into life assurance and endowment institutions in order to 'promote capital remaining in the Kingdom'. Statutes for an Annuity and Endowment Institution in the City and County of Stockholm (*Ränte- och Kapitalförsäkringsanstalten i Stockholms Stad och Län*) were approved by the government on 11 January 1850. Its operations were extended to county after county and covered the whole of Sweden by 1869. Most of the customers came from the growing middle class. Sommarin (1942) states that at the end of 1865 one inhabitant in seven had a savings bank account but only 1 in 724 had placed money in the annuity and endowment institutions.

The first Swedish life assurance company, Skandia, was founded in 1855 as a private initiative. Others followed in the 1860s. The pension system was in its infancy, so many people opted for assurance. A part of the premium income was invested in sizeable loans against property. By around 1910 assurance companies were providing credit on much the same scale as the savings banks had achieved fifteen years earlier and were one of the major investors in the bond market.

THE FIRST COMMERCIAL BANKS

The shortage of money and credit in the 1830s increased with the distance from the capital city. When neither the Estates' Bank nor the new savings banks managed to meet the demand, landowners and industrialists turned to other channels for credit.

The 1823 Riksdag addressed the government about the importance of establishing private companies for raising and lending funds. A government ordinance for private banks appeared the following year but had no immediate effect, which Skogman (1845) attributes to fears about the value of money. However, the 1830 currency reform dispelled the uncertainty and paved the way for the first private banks. Articles of association and lending regulations for Skånska Privatbank were approved that year and the bank opened its doors on 5 April 1831. In accordance with the 1881 bank committee's definition, loans by the bank were paid out in the form of 'printed and engraved debt instruments made out to the holder, bearing no interest and payable at call'. These were Sweden's first private banknotes.

The 1824 ordinance had not mentioned note issues. Issuing banknotes is profitable; provided notes are accepted and passed from hand to hand as a means of payment, for the issuer they represent an interest-free deposit. This has mostly been a source of government revenue known as seignorage (from the ruler's levy for minting precious metal) or inflation tax (the return increases with the rate of inflation); when a banknote is redeemed after a period of inflation, it is worth less than when it was issued.

In those days the issue of notes was not a prerogative of the state. Notes functioned if people accepted them. The reticence of the 1824 ordinance enabled Skånska Privatbank to disburse loans in its own notes. This was how private banks financed most of their loans up to the 1860s. Their 5 and 10 *rdr* notes were particularly popular because they equalled a farmworker's weekly wage. That displeased opponents of banking because it meant that the working class contributed much of the capital that generated handsome profits for bank-owners. It also deprived the state of seignorage.

Notes were used in Sweden probably more widely than anywhere else. People had grown accustomed to them in the 18th century, when money and a market economy spread more rapidly than would otherwise have been the case. Evidence from Vånga parish in Skåne (Perlinge, 2005) shows that if printed notes were hard to come by, people wrote them independently; in the mid 1800s, promissory notes between the parishioners made up between 50 and 70 per cent of the local credit market. Instead of being debt instruments in the modern sense, many of these notes were simply a form of payment – if the master of the house was short of cash, the maid or farmhand was given a note that then circulated in the community.

This practice worried the Bank's clergyman, Dean von Schwerin, who argued that it obstructed the circulation of silver: 'It is not in the Bank that the silver shall lie which the daily operations require; it shall lie in the *pockets of the people*, it shall pass from hand to hand if it is to contribute to improvement'. In time he arranged for petty cash to be minted in silver but that did not help, according to Skogman (1845): 'The mass of people continue in *their pockets* to prefer the filthiest 8 *skilling* note to the shiniest 1/16 *riksdaler* piece: and it is only gradually that this habit can be eradicated'. Thanks to this habit, issuing private notes was good business.

Many critical members of the Riksdag argued that the private notes contravened §72 of the Instrument of Government, which gave 'the Estates of the Realm the sole right through the Bank of issuing notes that may be recognised as legal tender in the kingdom'. Supporters of banks considered otherwise. Private notes were admittedly not accepted for tax and other official purposes but the law did not debar private individuals or companies from issuing debt instruments; that these then circulated as a means of payment was a matter for the market. Neither did the government object; Skogman was in fact the leading advocate of the first private banks. The licence for Vermlands Provincialbank in 1833 was likewise silent on the subject of notes. The first licence to explicitly permit the issue of printed or engraved notes was issued at the end of 1835 for Stora Kopparbergs Läns och Bergslags Enskilta Bank. The government had utilised its right to legislate economic matters without seeking the Riksdag's approval.

During the seventy years and more when private banknotes were issued in Sweden, no private bank failed to redeem its notes. Private bank failures occurred in Scotland and the United States, turning their notes into scraps of paper. In Sweden, private banks were required to maintain reserves that covered their note issues; another important factor was the structure of their ownership (Jonung, 2000). Their capital was subscribed in specific amounts but the holders of these shares were jointly accountable for the bank's commitments. If one of the banks had not been able to redeem its notes,

A 3-*riksdaler* note issued by Skånska Privatbank in Ystad (established in 1831 as the first private bank in Sweden) to finance its operations; 13×195 mm.

Fredrik Bogislaus von Schwerin (1764–1834), the leading member of the Bank's board in the 1820s and early 1830s. Medal engraved by Mauritz Frumerie; diam. 44 mm.

customers could in principle have demanded compensation from any of the shareholders. The owners and managers (often identical) therefore had a strong incentive to be prudent about note issues and lending. However, this did tend to discourage expansion; once notes for a certain amount had been put into circulation, further issues and lending were considered to entail unnecessary risks.

Note issues rather than deposits were used to finance lending because the law limited interest rates to 6 per cent. Private brokers found ways of charging one or two percentage points more than this, so money could be invested with them at 3 to 4 per cent. The interest margin was too narrow for the new banks, at least with the limited business they undertook in the early decades, which is why note issues were so crucial.

Licences were issued for Örebro Privatbank and Östgöta Bank in 1836, followed next year by Smålands Privatbank, after which a decade passed without any more private banks. Part of the reason may have been that Skogman resigned as under-secretary in September 1838. He had been heavily criticised in the press for the new, more liberal rules about occupations and residence for Jews.[20] In their opposition to royal power and the government, radicals did not hesitate to appeal to anti-Semitic tendencies. The campaign culminated in a riot in which Skogman's home was stoned. Sensing a lack of support from the king, Skogman resigned and was appointed president of the Board of Trade. He continued to feature in various banking questions but had less influence than before.

Opposition to the private banks grew and the king was less supportive. The licence for Skånska Privatbank was renewed a year after Skogman's resignation but only until 1847; the licences for all the other private banks were due for renewal in that year and the whole matter would be reconsidered. At the Riksdag of 1840–1, opposition to royal power was stronger than

20 Queen Kristina summoned a royal physician and a painter from abroad and some of the creditors who followed Karl XII from Turkey to Sweden were also Jews. In general, however, Jews were repeatedly forbidden to reside in Sweden in the 17th and 18th centuries, though under Gustav III a seal engraver, Aaron Isaac, was permitted to settle in Stockholm in 1774, Jews were allowed to live in a free port, Marstrand, and the first regulations for Jews were issued in 1782, entitling them to live in Stockholm, Göteborg and Norrköping to pursue trade and some specified occupations. Most of the restrictions on Jews' residence and occupations were finally abolished in 1870 but the general barriers to alien creeds closed the door for much longer to such posts as a minister of state and a primary school teacher.

previously in the reign of Karl XIV Johan and bank law was one of the disputed matters. The opposition saw to it that Skogman was impeached. The issue of Jews, the bank laws and the management of exchange dealings in the 1820s all featured in the case; Skogman was acquitted on every count. Still, the political winds were blowing against commercial banks.

FROM A SILVER CRISIS TO CONTRACTION

In the 1830s, the Riksdag continued to keep the Bank on a tight rein; the bank committee left the board of directors little room to manoeuvre in major monetary policy issues. In the aftermath of the currency reform, the Riksdag's banking regulations from 1835 spelled out the order in which the Bank was to take a series of measures in the event of a threat to convertibility.

In the United States, President Andrew Jackson had refused to renew the national bank's licence in 1832. Against the advice of his finance minister, he deposited federal revenue in local banks, thereby adding greatly to their liquid assets at the same time as their lending was no longer held in check by a national bank. The banks financed frenzied speculation for a number of years before the collapse came in 1837.[21] When the repercussions reached Europe, there was a run on the Bank of England's gold reserves, whereupon the Banque de France provided a gold loan to check the run and stabilise Europe's monetary system. When the crisis spread to Sweden, much silver left the Bank as people played safe and handed in notes for redemption.

A year or two later, Sweden experienced even greater strains when a variety of factors caused a drain on bullion. Crop failure in 1841, followed by two more poor harvests, entailed increased imports of grain, while exports of iron suffered from stronger international competition. When Hamburg was ravaged by fire in 1842, a number of bankers there called in loans, which obliged their Swedish connections to convert their credit into bullion. Moreover, the Bank sold off much of its stock of silver piastres to profit from the premium rate connected with the flourishing trade with China and India.

21 In his political autobiography from 1875, A.O. Wallenberg claims that bank failures in the United States during his stay in 1837 prompted him to consider how to organise a sound credit system, though Nilsson (1984) did not find any evidence of this in the contemporary sources.

Even more important were events in Finland, where Swedish notes continued to circulate after what had been one-third of Sweden passed to Russia in 1809. While the rouble was used in some parts of Finland, other parts had *riksdaler*, which meant that the market there was providing its former Bank with a long-term interest-free loan. Emperor Alexander I had ordained in 1811 for an Exchange, Loan and Deposit Office (*Wäxel-, Låne- och Depositions-Contoiret*) in Turku and this had moved to Helsinki in 1819. It was not until 1840, however, that what was to become Finlands Bank was authorised to issue notes that could be exchanged on demand for metal coin. In order to build up a metal reserve, the new bank collected the Swedish notes for redemption, which occasioned a heavy drain on the silver reserves of the Estates' Bank in Stockholm.

The consequences could have been troublesome. The 1845 bank regulations required the Bank to cut back lending if its bullion dwindled. Loan repayment would generate a flow of notes from borrowers to the Bank, thereby reducing the amount in circulation and helping to maintain the prescribed ratio between silver and notes. However, recalling loans would hit business at a time when the situation was already precarious on account of the crisis. The regulations from 1835 had stressed preventive action and been wary about lending. Now, however, the Riksdag saw restrictions on lending as the principal instrument for safeguarding the value of money.

A bountiful harvest in 1845 eased matters. Grain exports increased up to 1847 and a below-average harvest did not recur until 1851. Meanwhile, the first railway boom abroad called for increased exports of Swedish iron and timber. Soon after Britain had begun to cut import tariffs on wood products, Sweden removed export tariffs on boards and planks. Silver flowed into Sweden at a time when the 1845 bank regulations increased the Bank's right to issue notes to a ratio of 4:1 to bullion. When a bank crisis hit Britain in 1847, and other countries in Europe were disturbed by revolutionary movements, Sweden was comparatively unaffected.

AFFILIATED BANKS

The commercial banks came in for growing criticism. During the prosperous years the Crown had used its right to economic legislation to enact the 1846 banking laws. In 1848, however, the Riksdag called on the government to refrain from issuing licences for any new private banks; moreover, the

For many years, Sweden's foreign financial transactions were arranged via the Hamburg exchange; when a fire in 1842 led Hamburg bankers to withdraw credit, the Riksbank's stock of bullion was severely strained.

The Exchange building (left), from 1841, was protected from the fire. Later lithograph by Wilhelm Heuer after a drawing by Charles Fuchs.

existing banks should close when their ten-year licences expired in 1856–7. This actually favoured the established private banks because it put a stop to note-issuing newcomers.

Pending the closures, the opponents focused on how the private banks financed their operations. During the Riksdag of 1844–5 they wanted to ban small note denominations and have 20 *rdr* as the minimum. However, it was the 5 and 10 *rdr rgs* notes which circulated most and longest, thereby financing a large proportion of the banks' loans. The combined bank and law committee considered it was 'subject to doubt whether the private banks under such circumstances would want and be able to continue their operations' and recommended a compromise minimum of 6 *rdr* 32 *sk bco* (10 *rdr rgs*), which the Riksdag approved.

The government issued a proclamation to the effect that the 5 *rdr* notes would remain in circulation until the end of 1850, after which the 10 *rdr* note would be the lowest denomination. This deadline was then postponed by means of exemptions and deferments but the private banks had to live with the threat of losing the small notes.

The Estates' Bank had been opened for deposits in 1830 and its notes were given a more attractive design. Lending on a commercial basis had also been initiated in the 1830s: loans for up to 20,000 *rdr* at 6 per cent interest with a maturity of four to nine months. The opponents of private banking saw the Bank as an alternative and fitted it out to compete in that market.

Other considerations were at work, however. The separation of the Bank of England's note issue from its banking operations was seen as an attractive model. The call on the government not to renew the private bank licences was qualified with the statement that this should be done 'without inconvenience to the community at large'. How would industry and commerce obtain credit if provincial private banks ceased to exist?

The solution to this problem was remarkable. Even the opposition realised that the Bank in Stockholm could hardly cope with direct lending to the general public. The Riksdag of 1850–1 therefore decided to set up privately-owned affiliated banks with no right to issue notes; their lending would be financed with favourable loans and credit lines from the Bank in Stockholm. They were intended to spread the latter's notes to compete with private issues.

The bank committee saw the project as a way of relieving the Bank of its dual functions of providing loans and guarding the silver standard; the former function could be taken over by the affiliated banks. The Bank itself would be content with the interest on its advances to affiliates and focus on the silver value of the national currency.

The project got off to a modest start; the share of the Bank's profit the Riksdag assigned to the new operation was enough for only two affiliated banks. However, the Riksdags of 1853–4 and 1856–8 continued the work and ultimately there were as many as 22 of these banks. Calling them 'affiliated' (*filialer*) was actually misleading; the Bank in Stockholm took no part in their operations apart from providing funds. In practice the affiliated banks were just as independent as the private banks.

This situation was turned to good account by A.O. Wallenberg, a naval officer and merchant from Linköping, who had already subscribed to the newly established Östgötha Privat-Bank. During his naval career he had cultivated political and commercial interests in Sundsvall, which he represented at a series of Riksdags. He now recruited a sufficient number of interested parties to found affiliated banks in Sundsvall and Hudiksvall.

As an unofficial managing director, Wallenberg set about renewing Sweden's banking system. Lending by his affiliated banks was mainly arranged by discounting bills; matured bills were easier to collect than other debts and also made it possible to get round the 6 per cent interest rate ceiling. The affiliated banks' bills were sold to the Estates' Bank in Stockholm and to Östgöta Bank, which made it easier for customers to pay elsewhere. Another innovation in Swedish banking was Wallenberg's generous personal commission – one-fifth of the profit.

The competition with private banks turned out to be more costly and hazardous than the advocates of affiliated banks had foreseen. Instead of three per cent, the interest that accrued from affiliated banks amounted to little more than two per cent and the advances tied up a large part of the Bank's liquidity. To make matters worse, the affiliated banks failed to attract enough business; on average, they were only one-fifth as large as the private banks, which hampered effective competition.

Even so, the dénouement was a political sensation (Nilsson, 2006). In spring 1863 a virtually unanimous bank committee proposed an end to appropriations for additional affiliated banks, while all the existing entities should be wound up, starting in 1868. According to the 1881 bank committee, this decision was based on the low return on the Bank's capital. Nilsson cites a further explanation from A.O. Wallenberg. The key figure here was Anders Sandberg, rural dean in Madesjö and a long-standing opponent of private banks, who in the committee had shouldered the clergy's traditional role of helping the Fourth Estate to articulate its opinions. However, on learning that the affiliated banks in Sundsvall and Hudiksvall were aiding the circulation of the private banks' notes, Sandberg did an about turn – this assistance amounted to deceiving the Bank in Stockholm. Sandberg also asserted that lending by the affiliated banks was mainly arranged with pernicious personal guarantees. He managed to persuade the committee and the clergy before the peasants realised what was happening.

This pleased the finance minister, J.A. Gripenstedt. Addressing the Estates' joint discussion of banking issues, he welcomed a new type of bank that operated 'without any subvention, which they all to date have had, the affiliated banks in the advances from the Riksbank, the private banks in their profitable right to issue notes'. Sweden's most far-sighted finance minister presaged the future but it was far from imminent.

THE BANKING SYSTEM TAKES SHAPE

In the 1850s the international price level rose. The discovery of Californian and Australian goldfields in 1848 and 1851, respectively, boosted the extraction of gold and the price fell, which increased the money supply and led to inflation. In countries with a bimetallic standard, silver was crowded out by the cheap gold and flowed to countries with just a silver standard, bringing inflation in its wake. More plentiful gold meant that gold coins were worth less, whereupon prices for goods and services began to rise. Two and a half decades of rising world market prices stimulated the industrialisation and commercialisation of manufacturing and trade. This resulted in an upswing for banking and spread the gold standard around the world.

Economic activity in Sweden also benefited from the Crimean war. Russia invaded the principalities of Moldavia and Walachia, whereupon the Ottoman empire declared war on the Tsar on 4 October 1853. Britain and France tried to resolve the conflict; when that failed, they sided with the Sultan in 1854. Sardinia joined them in 1855 to ensure that the Italian question would get a hearing at the peace conference. Oscar I, who had succeeded his father Karl XIV Johan on 8 March 1844, likewise worked for an alliance with the western powers with a view to recovering Finland. According to

A.O. Wallenberg (1816–86), for decades the leading man in Swedish bank policy, both as a bank director and as a member of the Riksdag. Photograph by Bertha Valerius, 1864.

Nilsson (1984), ‘there are many indications that Sweden’s participation in the war was also expected to provide good opportunities for a royal coup d’état à la Napoleon III’. It was too late. After a year-long siege, the western allies took Sebastopol in September 1855 and scuttled the Russian fleet; the fighting ceased before Sweden could take part and the treaty of Paris was signed in March 1856.

The economic situation resembled the boom at the time of the Napoleonic wars. The belligerent nations were not in a position to compete with Swedish rivals in enemy territory. The earnings from Swedish exports of grain, wood products and iron were used to speculate in assets that would generate even more export goods. In the north of Sweden there was also the chance of illegal transit trade via Finland to evade the blockade of Russia. During the economic growth in 1851–5, lending by private banks rose by as much as 26 per cent, whereas the Bank’s lending was unchanged. The upward phase peaked in 1854 but a high level continued for as long as the war.

In the period 1850–70 annual export growth averaged over 7 per cent, compared with 0.7 per cent in the preceding half century. Exports of oats rose most spectacularly as urbanisation in Europe required more and more horses to draw carriages and carts. From a tenth of total Swedish exports in 1850, oats rose to almost a third around 1870. Exports of timber and sawn wood rose at an annual rate of 9 per cent in this period, from a share of just over a quarter to more than a third. The share for metal exports, iron in particular, fell, on the other hand, from 70 to 40 per cent. The products came from all over Sweden: oats from the south, iron from the central region and timber from the north.

As the economy expanded, the financial system’s shortcomings became increasingly clear. Nilsson (1981) cites the example of a merchant, J.L. Strindberg (uncle of the author August Strindberg), who had run a banking business with extensive deposits from the general public, only to be declared bankrupt in 1852. The evening paper *Aftonbladet* found that the bankruptcy documents indicated the need for a bank:

> Just the circumstance that a person who is not known to own any solid wealth can, when he opens a deposit business, be called on as much as Herr Strindberg has been, points to that extent to the great need of a real deposit bank; even without looking at the experience, one finds moreover that so must be the case.

The good times attracted new players. The most striking plan was for a ‘Belgian’ bank – an investment bank with far more share capital than any Swedish bank in those days. The Péreire brothers had founded the Société générale de crédit mobilier in Paris in 1852 and a similar Belgian institution had been operating ever since the 1830s. Instead of joint liability, these banks were based on the shareholders’ limited liability. They invested large amounts of capital in share and bond issues, lent against securities and traded on the stock exchange.

The Swedish version was to be called Svenska Handelsaktiebank (SHAB) and its share capital would be limited to 12 million *rdr bco* (18 million *rdr rgs*), with just a small fraction contributed in cash. The outline was vague; the would-be founders seem to have contemplated a crédit mobilier arrangement but played safe by including the possibility of running SHAB as a conventional commercial bank. They hoped to attract foreign capital, primarily British.

The men behind SHAB applied to the government for a licence on 21 February 1853. When the Bank’s directors examined the application a few days later, they were highly critical. Besides the bureaucrats’ numerous technical objections, the directors were most concerned about the consequences for the value of money. SHAB’s large capital and foreign loans would make Sweden more dependent on economic activity abroad. Frans Schartau, one of the leading figures in the Third Estate and the board of directors, saw a risk of the joint-stock bank practicing arbitrage and bill-jobbing in a way that would endanger the Bank’s small reserves of foreign exchange. Even more serious, however, was the fact that SHAB would need to invest its huge capital in the Swedish market, leading inevitably to undue speculation and an economic crisis. After a lengthy public debate the venture came to nothing, even when SHAB submitted new applications in June 1853 and February 1856.

By 1856 SHAB had a rival. Building on his experience of banking in Sundsvall, A.O. Wallenberg had assembled 72 participants in a new joint-stock bank in Stockholm. During the preparations, Wallenberg’s project was known as the ‘counter-bank’. Its two main opponents, SHAB and the Estates’ Bank, argued that there was absolutely no need for a private bank in the capital.

The counter-bank tried to avoid a dispute with the Estates’ Bank – Wallenberg would be content with an affiliated bank; and in any event, a local bank with a fairly modest capital base could hardly be a harmful competitor of the nation's Bank; in Göteborg, a private bank had operated alongside the Bank's loan office for eight years without harm to either party.

Matters were complicated by the royal family's private transactions. Karl XIV Johan had acquired the rich Gällivare ore-field but the cost of transporting ore made the venture unprofitable and the investment added to the strains on the royal household. In 1846, Oscar I tried to sell the field to English investors; in December the following year it was purchased by a consortium of Norwegian timber merchants who were after the forests and intended to dispose of the ore-field. The purchase price seems to have been high in relation to the returns (Qvist, 1964) but the deal included a political favour: a fortnight after the sale, Oscar I overruled the majority of his ministers and lifted the ban on exports of pig iron. By the time the deed of sale was issued in May 1857, the government had tabled a bill whereby iron ore would also be exportable. Nilsson (2006) finds it possible that Oscar I's support for SHAB was another aspect of the same 'scabby matter', as Wallenberg put it. The fact remains that making ore and pig iron available for export opened new markets for the Swedish iron industry.

When the Council considered SHAB's application on 16 May 1856, Oscar I was in favour of issuing a licence without delay but some of the most influential ministers disagreed. It was decided that the proposed regulations could not be approved 'in the state in which they have now been presented'. A setback, indeed, but also an opening for a new proposal. In the course of the discussion, two ministers, Gripenstedt and Wallensteen, mentioned the 'counter-bank' as a perfectly satisfactory alternative solution to the matter of banks in Stockholm.

Meanwhile, the King was preparing to reshuffle the cabinet prior to the autumn's Riksdag. On 22 May he offered Gripenstedt the post of finance minister and the latter stipulated 'that the question of SHAB is not to be dealt with again before the Estates have been able to express an opinion on the principles for such legislation'. The King gave way. On 1 July 1856 the government granted a 10-year licence for the note-issuing private bank Stockholms Enskilda Bank.

A.O. Wallenberg exploited the favourable economic situation. Montgomery (1947) notes that higher export income during international booms in the 19th century led to a capital surplus and lower interest rates. During

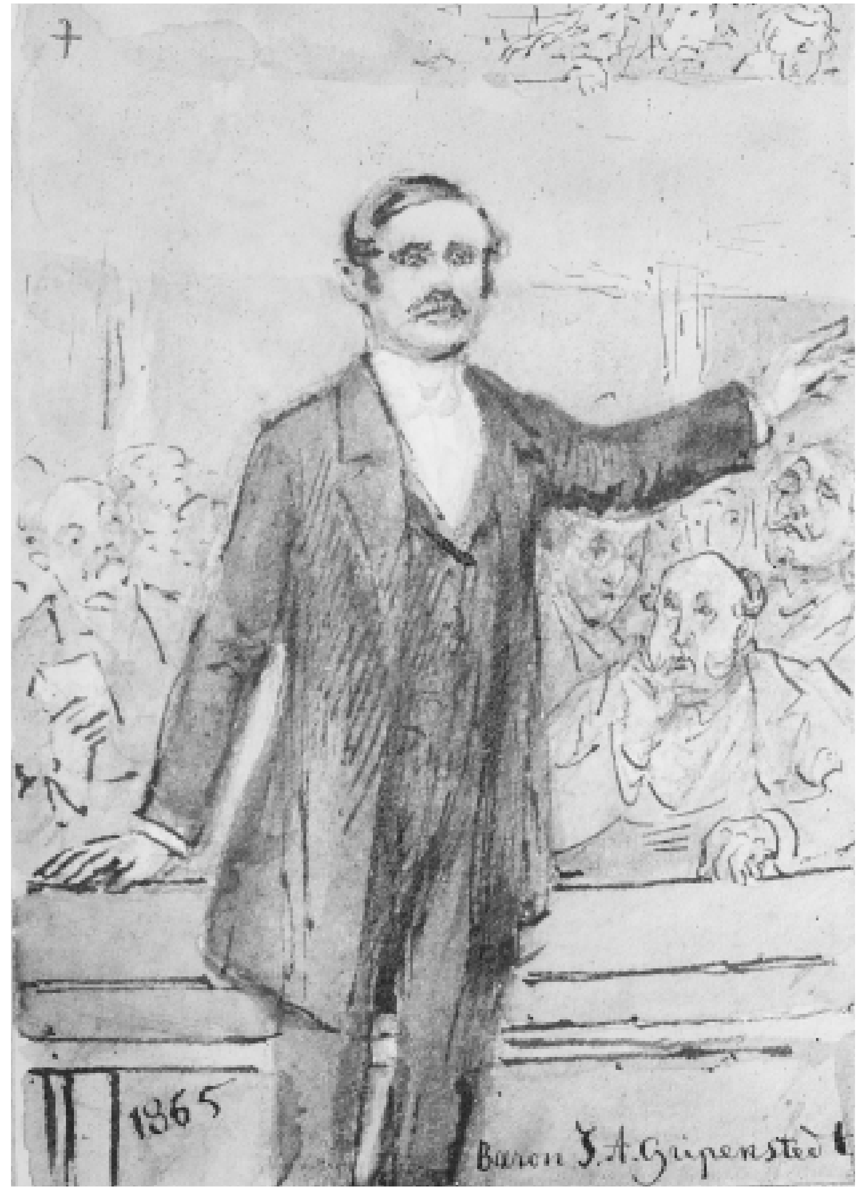
Oscar I (1799–1859).
Portrait by Fredrik Westin.

 the Crimean war, many liabilities had been settled with export earnings, so a large amount of capital was waiting to be invested. Stockholms Enskilda Bank was the first sizeable Swedish bank to fund a large part of its loans with deposits. It offered deposit accounts with a favourable interest rate but required some months' notice of withdrawals. This enhanced stability compared with the conventional sight accounts.

Sweden did finally acquire a crédit mobilier, Skandinaviska Kreditaktiebolag; the applicants for its licence in 1863 included A.O. Wallenberg. The backers intended this bank to channel foreign capital to industrial projects in Sweden, just as the General Mortgage Bank was doing for agriculture. Bond loans would be arranged and shares would be bought and sold to promote stability, 'particularly in a country where no stock market has come into existence'.

The original idea had been that most of the capital and shares would come from sources abroad. However, the continental money market weakened sharply in November and December 1863 and the Bank of England raised its discount rate from 4 to 8 per cent. Meanwhile, the conflict over Schleswig-Holstein became more acute when Denmark defied Prussia by proclaiming a new constitution that would include Schleswig. Oscar I's successor, Karl XV, wanted to side with Denmark with a view to uniting the Nordic countries under his crown but Gripenstedt argued against; the finance minister was receiving alarming reports (Gasslander, 1949): his father-in-law warned against borrowing abroad; in Paris the risk of war had made the Rothschilds doubtful about a government loan to Sweden; and a sharp drop in Swedish bond rates was reported from Hamburg. Market evidence and support from the Norwegian ministers enabled Gripenstedt to block Karl XV's plans. For the first time, civilians in the cabinet had managed to thwart a bellicose monarch.

When the German Union's troops marched into Holstein in December 1863, followed in January by Prussia's and Austria's declaration of war against Denmark, foreign investors were no longer interested in a Scandinavian bank. C.F. Tietgen, a Danish banker and industrialist, wanted to defer the matter but A.O. Wallenberg got his way: capital would be subscribed up to the minimum, the board would be slimmed and 9 of the 10 members would be from Sweden. The only foreigner was Tietgen, the initiator of the whole business. Skandinaviska Kreditaktiebolag started in 1864; under its first managing director, Theodor Mannheimer from



Johan August Gripenstedt (1813–74), cabinet minister and finance minister, laid the foundation for the role of government in the modernisation of Sweden's economy. Drawing by Fritz von Dardel, 1865.

Denmark, it soon became one of Sweden's largest banks. Its headquarters in Göteborg were joined later by establishments on an equal footing in Stockholm and Norrköping.

Skandinaviska Kreditaktiebolag differed from the private banks in that, instead of issuing notes for which the participants would be accountable, it obtained funds from deposits as well as by issuing shares; this limited liability to the amount of the share capital. In Sweden, privately-owned banks (*enskilda banker*) and joint-stock banks (*bankaktiebolag*) are referred to collectively as commercial banks (*affärsbanker*); state-owned commercial banks were established in the 20th century.

Banking in Sweden achieved a breakthrough in 1864. Finance minister Gripenstedt had pledged that instead of assessing the 'utility' of each application, the government would not obstruct freedom of establishment. Eight new private banks were licensed in that year and four in the following year, which doubled the number of note-issuing banks. The decision to close the affiliated banks gave rise to a series of mergers and transformations into conventional commercial banks. After 1871, when an internal conflict in Stockholms Enskilda Bank led to the establishment of Stockholms Handelsbank as a joint-stock bank, the banking system hardly changed for a couple of decades.

THE FIRST BANK CRISIS

Peace put an end to the Crimean boom. The commercial crisis of 1857 was the sharpest, though also the shortest, of its kind in the 19th century. A Cincinnati insurance company suspended payments in August and the crisis spread from the United States to Europe. At the same time, a good harvest pushed grain prices down. Many merchant and banking houses were in dire straits, particularly in Britain and Hamburg, some of them with sizeable claims on Nordic foreign trade. The crisis reached Sweden in the latter part of the year and a depression followed in 1858. World market prices fell 15 per cent, Swedish exports plummeted and terms of trade deteriorated.

These developments affected the credit market and banking. No one dared lend, even against good security. Trade and banking faltered and business circles called for government intervention. Finance minister Gripenstedt was sceptical. At a conference on 20 November 1857 between

the government and representatives of the boards of the Bank and the National Debt Office, the only person in favour of intervention was the Crown Prince, then acting as regent.

When the crisis hit Skåne Enskilda Bank in Ystad, however, Gripenstedt changed his mind. This bank's notes had spread across the Sound to Denmark, where two Swedish *riksdaler* were worth about as much as one Danish, which facilitated exchange. During the crisis, people in Sweden as well as Denmark rushed to the bank to convert notes into national currency and silver. The situation prevented the bank from replenishing its reserves by drawing on customary credit lines. In a telegram from Malmö on 7 December, the county governor described the situation as extremely alarming. Next day he reported that the bank would have to close if it did not obtain a loan of 650,000 *rdr* before the following evening.

Faced with this situation, Gripenstedt overcame the obstacles to state intervention and arranged for the State Office to lend 500,000 *rdr* against bonds issued by a provincial mortgage institution, Skånska Hypoteksförening. However, the bonds were in the safekeeping of Skåne Enskilda Bank's exchange agent in Stockholm[22] and he refused to furnish a personal supplementary guarantee for the loan, whereupon A.O. Wallenberg did so instead and then took over as exchange agent. The loan was placed at the bank's disposal on 11 December and warded off the immediate threat.

Meanwhile, Gripenstedt was preparing a broader approach. Sweden's representatives abroad were instructed to make soundings about a two-year government loan to ease the credit market. A reply from the embassy in London arrived next day: 'Dispatch of the 8th received. Rothschild will respond next week. Baring tomorrow morning. Poor prospects. Hambro considers it impossible to make the deal on the specified terms. He and those named see the proposal more as a 2-year bill than a loan, and money by bill currently gives 10%.'

The loan was obtained, at a cost. The government raised what it needed in Hamburg on worse terms than the National Debt Office had obtained

22 The provincial banks were obliged in practice (though not formally) to have an agent in Stockholm to exchange their notes for national currency. In many cases this was done by merchant houses or bankers; in 1857, however, Stockholms Enskilda Bank offered these banks a centralised exchange facility at its head office in the Old Town. A mixed collection of notes could then be exchanged all at once every weekday instead of calling on individual agents who were available only twice a week.

some days earlier in Frankfurt-am-Main. Gripenstedt took full responsibility, the government confirmed the terms and the money was placed in a state fund; those who needed credit could borrow from the fund, albeit at a high interest rate (9 per cent to begin with, later 8 per cent). The acute crisis had been resolved.

After some years the lesson had sunk in. Addressing the Nobility in September 1863, Gripenstedt stated that 'a banking institution stands unquestionably in a completely different relationship to the public than other industrial enterprises such as, for example, a cotton mill or a bath-house' (Nilsson, 1989). He was the first – but by no means the last – finance minister to realise that the state could not leave banks to their fate.

Contemporaries compared the terms for the two loans. Fredrik Åkerman, chairman of the board of the National Debt Office, had offered to coordinate borrowing but Gripenstedt had declined. Nilsson considers that Gripenstedt's unspoken reason may have been 'that the Bank needed the loan not only for Swedish industry and commerce but also for its own account'. With its sizeable commercial banking operations, the Estates' Bank was also shaken by the crisis.

CENTRAL BANK FUNCTIONS

As the credit market expanded and developed, the need for coordination, support and regulation became increasingly clear. The private banks had a surplus to invest, their customers' bills had to be re-discounted and credit lines were needed in times of crisis. The quest for foreign capital was not confined to agriculture and mortgage institutions; investment in industrial expansion also called for more capital than the domestic market could provide.

In other countries these functions ultimately resided in the national bank, which might be privately owned but even then was regulated by the state. The Bank of England handled the surpluses of other banks and the Banque de France discounted bills. In Sweden, however, interaction between the Estates' Bank and other financial institutions was blocked politically. After the failure of the discount companies, the government had been expressly forbidden to support private banks. The proclamation of 1824 stipulated that private banks 'neither now nor in the future shall be able to count on any support from public funds and under no pretext may the state

'Consequences of the so-called monetary crisis'. Many bankers and merchants were ruined by a brief but severe commercial crisis in 1857. Gripenstedt and Wallenberg came to the rescue of Skånes Enskilda Bank. Cartoon, artist unknown.

be involved in their or others' private enterprise or in any way contribute to their maintenance or support'.

This was interpreted rather strictly. Although it would have made things easier for Skåne Enskilda Bank, in December 1857 Gripenstedt was not prepared to accept private bank notes for tax payments; tax collectors were actually reminded that this was not allowed (Montgomery, 1947). Another consequence was the conclusion that the Estates' Bank could not serve private banks with functions that ultimately characterised a central bank.

Other solutions had to be found. In the crisis of 1857–8 the government did finally step in and organise a state fund for loans. When bankers refused to place Swedish bills in Hamburg, Frans Schartau organised a credit association for this purpose by using his dual role as exchange delegate in the Bank and leader of one of the major merchant houses. The bills were sent to an office in Hamburg and a merchant, C.D. Jederholm, spent the winter there and ran the business. When the bills from Jederholm's office were accepted by the Bank, they could be included in its balance sheet, because bills on Hamburg were eligible for this. The Bank could then exchange silver with Swedish trading houses, which used it to pay foreign debt when the credit market dried up and loans were recalled during the crisis.

In the latter part of the 19th century, the commercial banks arranged a supply of foreign capital and so did the National Debt Office and the General Mortgage Bank. This was done in the first place on behalf of Swedish industry and commerce; access to foreign funds also enabled these institutions to come to the aid of banks in distress as lenders of last resort.

This led to peculiar situations for the Bank in relation to the National Debt Office. Both of them were agencies of the Riksdag; in the early 19th century Gustav IV Adolf had proposed they should have a joint board of directors but that did not happen. At times their actions had contrary effects. When exports slackened and credit was scarce after the boom in the 1840s, for instance, the government saw to it that the National Debt Office stimulated the economy by purchasing and mortgaging bonds, while the Bank called in loans in order to restrict imports and demand. The Office based its action on a decision by the 1840–1 Riksdag that required it to invest idle funds in the credit market. It was these funds the Office used to assist distressed banks. In the 1870s the Office even issued bonds abroad rather than call in loans.

Opponents of commercial banks discerned a chink in the Riksdag's armour and called for greater coordination of the Bank and the Office. At the 1874 Riksdag the auditors recommended transferring the Office's lending operations to the Bank and the combined bank and finance committee concurred. The matter went to and fro for some time but in summer 1876 the Bank's board saw to it that the National Debt Office would place a large part of its surplus funds in the Bank. After that, lending to banks by the Office dwindled; besides the political element, this was because a diminishing government borrowing requirement in the 1880s reduced the Office's resources.

It was superseded by the General Mortgage Bank, which from 1877 onwards was more important than the National Debt Office as a source of credit to the rest of the banking system. Its chairman was appointed by the government, which therefore exerted more influence than it could over the two agencies of the Riksdag, for instance as regards the size and timing of issues abroad.

The National Debt Office made a comeback as a source of funds for commercial banks, not least in connection with the Baring crisis in 1890, but this was controversial. A board member, Johan Johansson of Noraskog, who represented the Agrarian party, argued against placing surplus funds at the disposal of general business because that could interfere with the Bank's control of the money supply.

Quite a few central bank functions were performed by private banks. Banking operations were hampered by the fact that all transfers between their own accounts, their exchange agents and other banks had to be made in notes and coins, which was costly and clearly hazardous. It was common practice for board members or other trustworthy persons to take parcels of notes with them on regular journeys. In the 1850s, steamboats began to be used for transporting money in the captain's personal care.

When A.O. Wallenberg founded Stockholms Enskilda Bank, one of his principal ideas was to relieve banks of this constraint. His bank would assist its provincial cousins by settling their mutual claims, arranging their customers' distant payments and meeting the need to exchange notes for other notes as well as with the national currency. Stockholms Enskilda Bank became increasingly popular as an exchange agent. Previously, in Sundsvall, Wallenberg had introduced postal money orders, which made transfers simpler and less risky. Moreover, for the bank of origin, the order provided an interest-free deposit until it was redeemed. Wallenberg's bank was also the first private bank to trade bills abroad, which aided the expanding export industries.

Another newcomer, Skandinaviska Kreditaktiebolag, also played the part of a central bank in many respects. It did not compete with the provincial banks because it did not issue notes (Söderlund, 1964) and actually undertook to use their notes in its own operations. Furthermore, its interest rates were more favourable than those of Stockholms Enskilda Bank and it bought and sold foreign currency in Stockholm and Göteborg on behalf of the provincial banks. It was partly by becoming a bankers' bank that Skandinaviska Kreditaktiebolag took only a decade to become one of the two largest banks in Sweden.

It was with such improvisations that institutions and the government provided what have come to be regarded as functions of a central bank. Private banking expanded rapidly, even compared with other countries, but in central banking the Swedish system lagged behind.

The Bank's Resuscitation

By the mid 19th century the Estates' Bank was out-dated. In an account to the clergy of the Bank's round-about processes (cited in Nilsson, 1981), J. Mortimer Agardh, professor of astronomy, described how people had to go from room to room in the pair of buildings in the Old Town to complete a transaction that involved about ten officials:

> Say that I have a payment to the Crown, amounting to 10 *rdr*; with a deposit note written solely for this purpose I have first to go to one of the four tellers located on the lower floor of the old bank building, who, having counted the money, presents the cash receipt for this to me, with which I go to the special cash accountant located in the same premises who makes a note of the receipt and furnishes it with his initials and annotation.
>
> Then I must write a separate note for the deposit department, attaching the related documents if there are several of these, and then proceed before 11 a.m. two floors up in the new bank building, to the deposit department's counter-window and there hand over my note and my documents, receive a token for them

Theodor Mannheimer (1833–1900), first managing director of Skandinaviska Kredit AB, which superseded Stockholms Enskilda Bank as the 'central bank' for privately-owned banks.

with which I must again present myself at 1.30 p.m., when in exchange for the token I obtain my deposit receipt.

[. . .]

Now for what reason can it be that in the deposit department I cannot be attended to immediately instead of having to return after 2½ hours to get my service? To understand the reason one must take into consideration the multifaceted and time-consuming treatment my little cash receipt shall undergo in this department before it has been dealt with here. When the *book-keeper* in the window has accepted my note with the accompanying one or more documents and provided me with the token, he hands the note over, after entering the amount of the deposit in his day-book, to the *office clerk* standing by the same desk, who in a so-called itemised day-book enters a description of the content of each of the accompanying documents, after which he hands the documents to a *porter*, who takes them to an *office clerk* located in another room whose sole deed consists in providing each document with a form for the deposit receipt. The clerk then hands the documents with the forms attached to be actually expedited by a *book-keeper* and three *clerks*, who fill in and countersign the forms. The matter is then taken over again by a *porter* who brings it to the two *commissioners* [managers] in another room who hand over the documents to a *cancellation marker* located there who obliterates the same, whereupon one of the *commissioners* applies his name to the receipt, which only now is completed. Finally the receipt is fetched by the *book-keeper* in the window, who marks it off in his day-book and hands it out at 1.30 p.m. to the depositor; the obliterated documents are fetched by the *office clerk* with the itemised day-book, who marks them off there.

The Bank's routines were also laborious in other ways. People in Stockholm could manage on their own but customers elsewhere needed a commissioner to look after the documents and their money. Most of the commissioners were Bank officials, for whom this was a sideline. It supplemented their regular pay but entailed a risk for them as well as for the customer. If a commissioner ran off with a customer's money, the Bank was not accountable. At 11 a.m. one Saturday in 1867 a porter from Stockholms Enskilda

Front of the southern Bank building in 1867, seen from Järntorget.
Svenska familj-journalen 1869.

Bank came to the Bank to exchange a large sum of money; when he returned just before closing time at 1.30 p.m. (just as Mortimer Agardh had recounted) he was told that the transaction had not been completed. On Monday it transpired that the teller had disappeared with 38,860 *rdr* – more than the senior managers earned in several years. Arguing that the teller had accepted the money as a private individual, the Bank refused to compensate the loss and won the case in the courts.

It was the impact of the new institutions that forced the Bank to put its house in order. The first private banks had not been able to change things; the competition from Stockholms Enskilda was more serious. A.O. Wallenberg had a new head office constructed a block or so away from the Bank, which had to compete with the commercial banks for note issues as well as lending. The commercial banks found various ways of spreading their own notes far beyond the place of issue; the further away, the longer the notes circulated before being redeemed and the greater the profit. A corollary of this was less demand for the Bank's notes and thereby lower earnings. In the latter 19th century the greater part of the note stock came from private banks. The Fourth Estate's and later the second chamber's opposition to private banks was one issue; another was the commercial threat.

Attempts to reform the Bank led to further conflicts. The Bank's supporters on the bank committee and the board of directors tended to become mired in the Bank's bureaucracy, and the management opposed changes in its collective procedures. The intractable nature of this resistance was personified by C.H.O. Ossbahr, whom Nilsson (1981) dubs 'the foremost of the Bank's bureaucracy'. Ossbahr was appointed secretary to the board in 1844 and held this post until his death in 1873. During the Bank's attempts to undermine the SHAB project, director Hartmansdorff warned supporters that Ossbahr was one of their main opponents.

A modest change occurred when the Riksdag of 1840–1 divided the Bank into seven main departments whose heads constituted a managerial board that took over the day-today operations from the 21 commissioners. When a committee that would include the aging Skogman was mooted in 1852 for a further review of the organisation, the managerial board was up in arms, whereupon the directors retreated and everything continued as before.

By 1854 the bank committee had had enough; it revived the proposal

from 1852 and moved that the Riksdag largely adopt the recommendations. Most of the tellers were brought together in a single room and the processing of loans was speeded up. There were fewer staff and they were better paid. A postal order service was introduced between the Bank's offices in Stockholm, Göteborg, Malmö and Visby, with instructions to the board to commence negotiations for an extension to all private and affiliated banks. Besides simplifying matters for the Bank's customers, this amounted to an initial approach to the commercial banks (Nilsson, 1981).

The crisis of 1857–8 led to the appointment of a large committee to review the entire banking system, including the Estates' Bank and the commercial banks. To get round §72 of the Instrument of Government, in 1860 the committee proposed that the Bank be divided into a Bank of the Estates of the Realm (*Riksens Ständers Bank*), with the right to issue notes and the task of backing the entire stock with silver, and a General Swedish Bank (*Allmänna Svenska Bank*), which would undertake the remaining operations. This ingenious plan did not appeal to the 1862–3 Riksdag; three of the Estates rejected the committee chairman's motion, which sealed its fate.

However, the same Riksdag did call for a modernisation of the Bank's internal organisation. The commercial banks were held up as an example. The commissioners did what they could to oppose the bank committee's intention of replacing the managerial board with three directors from the senior board. However, the Riksdag largely approved the proposal; instead of three directors, the senior board's exchange delegates were retained, with responsibility for the Bank as a secondary occupation, and a third delegate was added to focus full-time on the internal administration at an annual salary of 8,000 kronor, more than twice what the other two delegates earned (an exchequer councillor got 5,000 kronor, a senior schoolmaster 3,000 kronor).

A.W. Björck, a Göteborg magistrate, was appointed delegate for internal administration and was thus the Bank's first governor in a modern sense. He had combined a career in the judiciary with that of a commercial law consultant and been involved in the birth of Göteborg's banking system. In the Riksdag he was a leader of the burghers and had joined the Bank's board of directors in 1860.

With a single person in charge and present, the work of reform started. An office was set up for all the commissioners' business, the regulations were cut from 158 pages to 63 and the number of officials and porters was reduced from 87 and 31, respectively, in 1860 to 49 and 20 in 1875. The provision of services on commission died out, partly because in 1872 the Riksdag ordered the Bank to stop charging fees for its services.

One of the most noteworthy statements from this period concerned the board's reasons for introducing an annual holiday for staff: year-round attendance 'occasions an exhaustion and dulling of mental strength that soon enough is evident in an aversion, usually bred of an inability, to even the most insignificant change in the way of handling matters, and hereby arise difficulties for management in the implementation of new instructions, those that aim for a speedier service to the people who have business with the Bank'. The Bank smoothed the rationalisation with higher wages and better social conditions; even so, the wording says something about feelings among the staff.

When the Riksdag as the Diet of the Estates decided to replace itself with a bicameral parliament in 1866, the Bank could no longer be called the Bank of the Estates of the Realm, though banknotes continued to display the symbols of the four estates, one in each corner, up to 1879. In 1867 the bank committee proposed National Bank of Sweden (*Sveriges Riksbank*) as the new name; A.O. Wallenberg countered with Bank of Sweden (*Sveriges Bank*). The upper chamber supported Wallenberg, the lower chamber the committee. In the subsequent joint vote, 147 members were for Sveriges Riksbank and 135 for Sveriges Bank, so Sveriges Riksbank won the day.

During the decade of reform, management of the Riksbank changed hands. Björck retired in 1868 in the middle of the reorganisation and was succeeded by another lawyer, A.W. Dufwa, who had left the judiciary in favour of the world of insurance. Dufwa had joined the newly formed Skandia insurance company as a clerk in 1855 and risen to become managing director in 1861. In autumn 1869, however, Skandia's board, acting on a proposal by one of its number, A.O. Wallenberg, decided to grant assistance to an employee whom Dufwa had dismissed for misconduct. A fortnight later Dufwa took leave of absence to be editor of the evening paper *Aftonbladet*; he left the paper six months later and on 4 May 1879 was appointed delegate for the Riksbank's internal administration, a post he occupied until his death on 10 August 1883. The bitter atmosphere between him and Wallenberg added to the antagonism between the Riksbank and the commercial banks.

Dufwa continued the reform. The Bank's premises had been recon-

Albert Wilhelm Björck (1812–85), the first head of the Bank to preside as a governor in the modern sense. Portrait by an unknown artist.

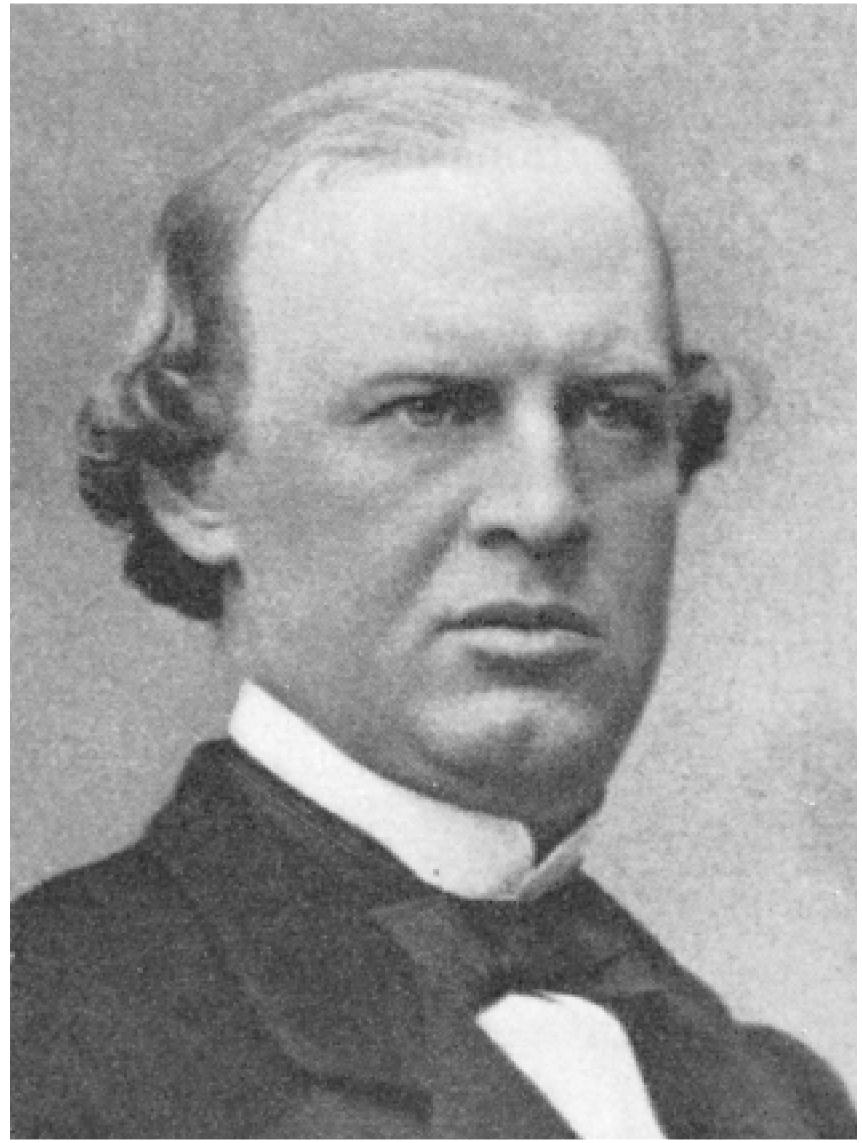
 structed in 1873 but were still a problem. As the board had declared in 1872, the location was at fault: 'The position of the present bank buildings in the southeastern part of the city must already be considered unsuitable and undoubtedly will become even more so in a not too distant future as the major business operations have their premises mainly in the more western parts of the city between the bridges and probably in time will gravitate northwards.' This raised the question of a completely new building; the final solution on Helgeandsholmen (the small island between the Old Town and what is now the city centre) was mentioned but for the time being a large annex even further north, on Malmtorgsgatan, had to suffice; it was opened in 1876.

The internal reforms gave the board more discretion, which cut both ways. The changes connected with the adoption of a bicameral parliament had made the composition of the board more arbitrary and subject to political fortunes (Nilsson, 1994). In the late 19th century, the Bank's organisation and operations were increasingly a bone of contention in the political struggle.

Interest-bearing cheque accounts had been introduced in the 1850s. From time to time, other banks were allowed to use their accounts with the Riksbank to earn interest on surplus funds. Meanwhile, the Bank expanded its commercial lending in connection with a breakthrough for bill discounting and increased advances against bonds and shares. Neither did the Bank refrain from sharp practice; when Stockholms Enskilda Bank requisitioned silver for export in the 1860s, the Riksbank provided its competitor with debased 50 *öre* coins.

The allocation of the Riksbank's profits caused controversy. The farmers in the lower chamber argued that the profit should be used for a further extension of the Bank's operations; agricultural credit should be provided to counterbalance the commercial banks. The upper chamber favoured an allocation to the government budget. The bank committee and the directors supported the farmers. For two decades, starting in 1872, approximately half of the profit went towards reinforcing the Bank's funds.

The Riksbank found it hard to compete with Stockholms Enskilda and other commercial banks. Interest rates and periods of notice were used to attract private customers but in the absence of a differential it was the Riksbank that lost. Around 1870 the Riksbank was having difficulty in lending all the funds at its disposal. According to Brisman (1931b), 'men in



Alfred Wilhelm Dufwa (1825–83),
Bank 'governor' who repeatedly clashed
with private banker A.O. Wallenberg.

the business world [...] preferred to deal with a private bank, even if it charged half of a percentage point more. There are no indications that this attitude was due to an aversion in principle to the Riksbank as such; the reason was quite certainly that they had not found the same support and the same compliance there as from the other banks.'

THE BRANCH OFFICE CONTROVERSY

In order to fill the gap when the discount companies disappeared, the Bank had opened branch offices in Malmö and Göteborg in 1823; another branch had been established in Visby in 1851. A long struggle began in the 1870s when the Agrarian party in the Riksdag called for additional branches.

The board of directors opposed the idea at first in order to protect their influence. It was the Riksdag that appointed all members of branch boards except the director, who was the Bank's agent. This was a legacy from the era of the National Discount Office. The Bank's board refused to agree to additional branches as long as their control was split. In 1872 the Riksdag left it to the Bank to appoint the board of a new branch in Luleå and in the following year all the branches were fully integrated with the Bank. The provincial loan offices were renamed branch offices and the Bank in Stockholm was called the head office.

The pressure to expand came from the lower chamber. Increased exports from the United States, Canada, Argentina, the Ukraine and Australia weakened agricultural prices in the 1880s, while farm wages were rising, partly to counter competition for labour from manufacturing. The Agrarians had split into a traditional fraction that favoured free trade and a 'new' protectionist group for whom higher import tariffs were not enough. A larger number of provincial branches of the Riksbank would exert downward pressure on local interest rates and ease farmers' financial burden. A reservation to the bank committee included the following argument: 'I consider cheap money to be the most effective aid for our depressed industries and agriculture and I am convinced that by establishing branch offices of the Riksbank in the provinces, it shall be possible in time to push the interest rate down because the Riksbank should not to such a great extent pay consideration to a profit which for the private banks constitutes the mainspring of their operations.'

The board of directors and the upper chamber based their case on

Palatial branch offices of the Riksbank, like this one in Halmstad, were erected in the county capitals from 1823 onwards. Architect, Jakob Martin Borgstedt.

business economics: the branches generated a poor return on the invested capital. Moreover, the branches and the increased lending came up against demands connected with central bank functions. The more capital the Riksbank tied up in its loan stock, the greater would be the difficulty in mobilising the necessary resources for coping with monetary policy crises.

The opponents did manage to slow things down. The Riksdag insisted on one new branch after the other and in 1889 the board of directors relented. It was tacitly accepted that each county town would get a Riksbank branch, though the pace was reduced to one new establishment every other year.

The board had retaliated by emasculating the branches over the years. Their lending was restricted to instalment credit and secured loans; all other advances were to be handled by head office. The branches had to report their lending activities to head office and their directors were summoned to Stockholm to coordinate operations. Branch independence never went as far as in Norges Bank, where each branch was free to implement its own interest rate policy; it was not until 1892 that Norway's official discount rate was decided by the board of the national bank (Jahn et al., 1966).

THE INTEREST RATE

Many years passed before Henry Thornton's ideas about using the interest rate to manage the economy were applied in practice. An important impetus to the development of monetary policy came from Lord Goschen's *The Theory of the Foreign Exchanges*, published in 1861. It analysed how the interest rate could attract and repel cross-border capital flows, as well as its ability to check imports and subdue prices. The earlier method of withdrawing notes and credit had admittedly acted by pushing the interest rate up but it had also squeezed industry and commerce. Goschen recommended preventive interest rate increases; '... it is clear that there is no corrective of a drain on gold, and all its attendant consequences, more powerful and effectual than a rapid advance in the rates of discount. It is the only mode by which that which is on the point of being lost may be retained, or that which is actually gone may be replaced'.

International economic activity was listless in the 1860s; crises and failed harvests made things worse. The authorities still saw the defence of convertibility as their primary task; commitments to depositors and holders of notes had precedence over the squeeze's consequences for borrowers and the business community.

The importance of continuous access to a liquid credit market was underscored by Walter Bagehot, from 1860 editor of *The Economist*, which incidentally the Riksbank first subscribed to five years later. Bagehot argued that it was up to the central bank to ensure that credit was always obtainable; the best means of balancing demand for credit and the available liquidity was the interest rate. By making sizeable discount rate adjustments early on, the central bank could see to it that loans were available for those who were able and willing to pay the current rate. The adjustments provide potential creditors with the return they required for advancing their money.

The crisis and the theoretical studies led to what Brisman (1931b) describes as an 'international breakthrough for the ideas behind modern discount policy'. In 1864 the Bank of England adjusted its discount rate 15 times and the Banque de France 11. When cotton exports from the southern states dried up because of the American civil war, the Lancashire textile industry was in dire straits; cotton from Egypt and India helped fill the gap but cost more and had to be paid for in gold or silver. In order to stem the outflow of gold, the Bank of England raised the discount rate; in the following years this instrument was used again and again, reaching a peak with 24 adjustments in 1873.

The new approach soon spread to Denmark, where the National Bank had been founded in 1818 to restore convertibility when the currency had collapsed in the aftermath of the Napoleonic wars and the state bank had been declared bankrupt. The National Bank first deployed the discount rate to influence borrowing in 1856; in the early years the rate was generally too low to keep liquidity fully under control but when Moritz Levy had been appointed director in 1861, a modern discount policy was developed along British lines and gained the support of the commercial banks.

Things took longer in Sweden. The Riksbank's hands were tied by the usury laws from 1734, which limited the lending rate to 6 per cent, though the informal credit market took no notice of this. The crisis of 1857–8 meant that even the government had to charge more. The statutory ceiling was observed by treating the surcharge as a commission, just as private money brokers did.

After the crisis of 1857, six countries, led by France, abandoned or modified their limits on interest rates. The legitimacy of Sweden's ceiling was also in tatters – it had not prevented the interest rate from rising at times towards 12 per cent.

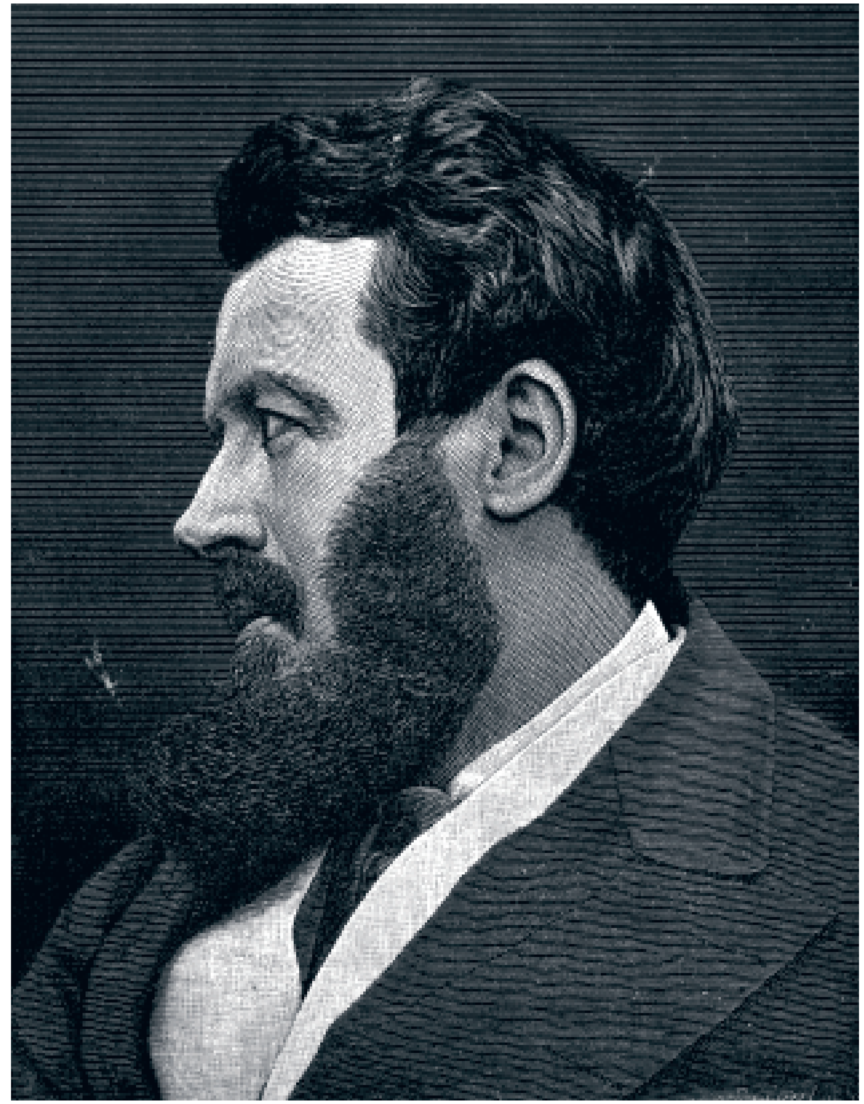
The 1862–3 Riksdag's arguments in favour of removing the ceiling were based on freedom of trade. Labour was not restricted, so why was capital? The combined bank and law committee also pointed out that free interest rates would make it easier to discern economic tendencies. Above all, a high interest rate was less harmful than a credit squeeze:

> When on account of a scarcity of money the interest rate rises, even to a considerable height, for a businessman who absolutely must either procure money to meet his commitments or under unfavourable circumstances realise his assets and often moreover wind up his operations, it is a far smaller loss to have to bear a high interest rate than to be subjected to the latter necessity.

The committee proposed that interest rates should not be deregulated completely, only for loans up to six months. The Fourth Estate was pacified by exempting loans against property. The government would decide when the time had come. The Riksdag approved the proposal but the Agrarians took the unusual step of presenting a joint protest to the government; the ingrained distrust of flexible – at times high – interest rates still applied and would continue for a long time to come.

When the Riksdag's writ concerning interest rates had been approved by the Supreme Court, the Cabinet considered it on 13 September 1864. There was a consensus but some ministers questioned the timing. The cotton crisis was at its height and in Scandinavia the situation was made more uncertain by the war between Denmark and Germany. However, Louis De Geer, minister of justice, insisted that the ordinance be issued immediately: he argued that a free interest rate was most needed just in times of crisis.

At first the change made little difference to the Riksbank's relationship with the rest of the banking system. The commercial banks set their lending rates regardless of the Riksbank; they adjusted to the free market: Stockholms Enskilda Bank raised its rate to 7 per cent, many provincial banks to 8 per cent because the level was higher outside the capital. The Riksbank announced an increase but followed this six months later with a cut to 5½ per cent even though money was still scarce; commercial considera-



Walter Bagehot (1826–77), editor of *The Economist*, presented theories about a central bank's role in *Lombard Street*, published in 1873.
After a photograph by Adolphe Beau, 1864.

tions gained the upper hand because even with a low rate the Riksbank had difficulty in attracting enough borrowers.

The next crisis was not long in coming. In Britain, where a charter had been required to establish a company with limited liability, incorporation with limited liability was made open to anyone in August 1862. The innovation proved extremely popular and led to a wave of speculation that lasted some years. In February 1866, however, the number of corporate failures began to rise and panic broke out when a prominent discount house, Overend, Gurney & Co., defaulted on 10 May. The 1844 Bank Charter Act was suspended and Bank rate exceeded 10 per cent for a good three months.

The uncertainty spread like wildfire. In Sweden, the newly established Skandinaviska Kreditaktiebolag had difficulty in obtaining funds. The strain on liquidity made it necessary to refuse an unusually large number of credit applications. Some approved loans carried the qualification that they would not be paid out until funds permitted. Stockholms Enskilda Bank was in a quandary when Vereinbank in Hamburg withdrew its promise of a large advance.

A fortnight or so after the Overend crisis erupted, the Riksbank's directors considered an interest rate increase but doubted whether it would 'to any essential degree reduce demand for loans'. Moreover, an increase would 'give the private banks cause for a further rise in the interest rate on top of what has already occurred, which would not only exceedingly burden operations but also in places outside the country arouse distrust of the monetary position here'. The board still believed that withdrawing notes was the safest way of stabilising the situation. A fortnight later the board found an increase more acceptable but still rejected it. As interest rates abroad were so high, the increase in Sweden would need to be unduly large in order to attract an inflow of capital.

On 2 December 1864, Johan Holm, a city broker and the spider in the traditional credit market's web, left Sweden for Switzerland, leaving behind a huge estate in bankruptcy. Among the private banks, Östgötabank and Smålandsbank not only incurred large losses (Holm had been their exchange agent) but also found their transactions with Stockholm in jeopardy. Public confidence in the banking system was shaken. Without being asked, A.O. Wallenberg immediately arranged for his bank to take over the conversion of these banks' notes into national currency, a commission which his bank then retained.

Besides likening this crisis to events in 1857–8, Wallenberg compared it with what had happened abroad. Acting on an understanding with the British government, the Bank of England had functioned as lender of last resort in order to stabilise industry and commerce. The Riksbank had done the opposite: withdrawn notes from circulation and squeezed the supply of credit. Writing in the evening paper *Aftonbladet* at the end of 1867, Wallenberg called for a modern central bank, accountable for the money market throughout the country. Neither Stockholms Enskilda nor Skandinaviska Kreditaktiebolag could shoulder such a responsibility.

He was kept waiting. In the 1870s the Riksbank did become more alert to the importance of liquidity and made an effort, possibly influenced by Bagehot, to find alternatives to a monetary squeeze. It removed the automatic link between fluctuations in foreign exchange reserves and the volume of domestic lending. Foreign bills were purchased to be used as a regulator of changes in demand for foreign exchange; the stock of bullion would then be unaffected and so, accordingly, would the loan stock. In 1875 the Bank parried an outflow by obtaining large advances in London. Foreign credit and foreign bills became monetary policy's primary instruments and the approach to interest rates remained passive.

The first time the Riksbank attempted to manage the interest rate, it had its sights on Stockholms Enskilda Bank. When the major banks, on the Riksbank's initiative, agreed in March 1880 to widen their interest margins by lowering the rate for cheque accounts, A.O. Wallenberg was not informed; he read about it afterwards in the press. He responded by narrowing his bank's margins instead, with the result that Dufwa's attempt at exclusion led to an increased market share for Stockholms Enskilda.

Times were changing, however. Johan Wolter Arnberg joined the board of directors in 1874, with responsibility for operations in foreign bills. He had studied politics and political science, still a novel discipline, at Uppsala University, spent almost a decade on the board of Uppsala Enskilda Bank and been on the board of Stockholms Enskilda Bank from 1871. He was better equipped to direct the Riksbank than any of his predecessors and colleagues. The Wallenbergs clearly respected his competence even when the Riksbank's interests conflicted with those of the commercial banks.

Arnberg made his mark in 1881 by proposing an increase in the discount rate to check a currency outflow. The board turned a deaf ear, however, which Brisman (1931b) sees as an indication of the importance the board still attached to the Bank's own business and interest rate competition. When Dufwa died in 1883, Arnberg succeeded him as head of the Riksbank.

Falling prices and a weak economic development in the 1880s made the interest rate less of an issue. Rates were generally low, the Riksbank's and those of the commercial banks converged. It was not until the Baring crisis in 1890 that the discount rate again became a serious concern.

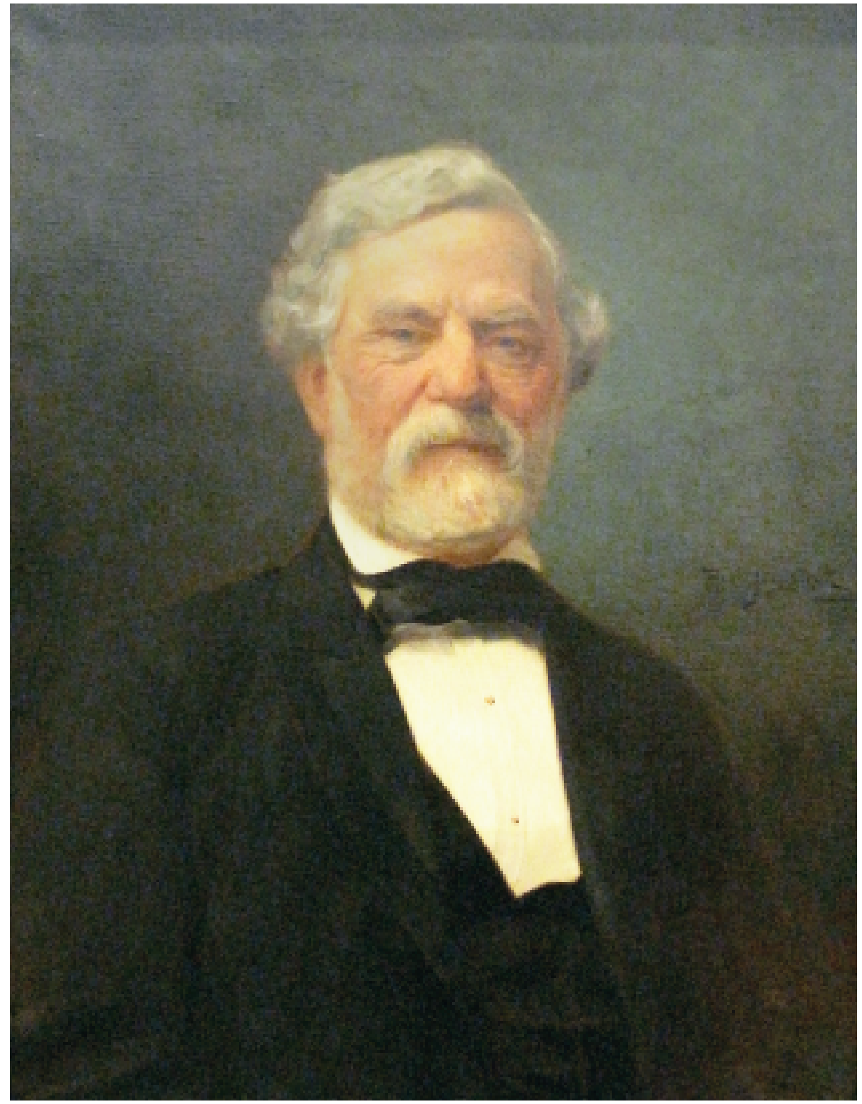
Argentina was a country that invested a great deal and imported capital in the late 19th century. When servicing the loans became difficult and the price of the bonds began to fall, the London banking firm Baring Brothers speculated that Argentina would manage to meet its commitments, just as other banks – among them Stockholms Enskilda – had taken a risk with cheap French securities after the war of 1870–1. Barings purchased Argentine bonds and borrowed from other British banks in order to buy still more. When Argentina, after a brief boom in 1889–90, suspended payments on its national debt, Barings was forced into liquidation but was rescued by a consortium headed by the governor of the Bank of England.[23] The losses and tighter credit spread to other countries, causing trouble for many indebted companies.

If the Bank of England had failed to manage the crisis, things could have been much worse. It arranged the guarantees Barings needed for survival, raised the discount rate and borrowed large quantities of gold from the Banque de France and Russia's state bank. Gold was available to any anxious depositor and the market gradually calmed down.

Sweden managed better than many other countries. Some debt-burdened ironworks failed on account of the credit restrictions but liquidity was boosted when the National Debt Office provided loans for 11 million kronor. The increased discount rates in Britain and Germany made it difficult for Stockholms Enskilda Bank to place its first major Swedish government loan but the matter helped to improve the bank's relationship with the Riksbank and Arnberg.

The greatest change occurred in the Riksbank's management of the

23 After more than a century, Barings hit the headlines again on 23 February 1995 when it was revealed that the chief broker in Singapore, Nick Leeson, had lost £852 million on trading in derivatives. When a rescue action failed, Barings was declared insolvent on 26 February; its operations were broken up and sold to other financial institutions.



Johan Wolter Arnberg (1832–1900), the first head of the Riksbank who had studied economics. It was under him that the Bank was transformed into a central bank. Portrait by an unknown artist.

 crisis. A credit squeeze was no longer on the cards; on the contrary, the Riksbank aided the commercial banks' liquidity by purchasing their bills at a discount.

An even more important innovation concerned the interest rate. In order to counter the strong demand for foreign currency, the Riksbank raised the discount rate to 4½ per cent on 1 July 1890 and then to 5 per cent on 16 October. On 6 November Arnberg proposed a further increase but could not convince the other directors. A week later, when foreign buyers could no longer be found for Swedish bonds, Arnberg called on the board to reconsider the issue:

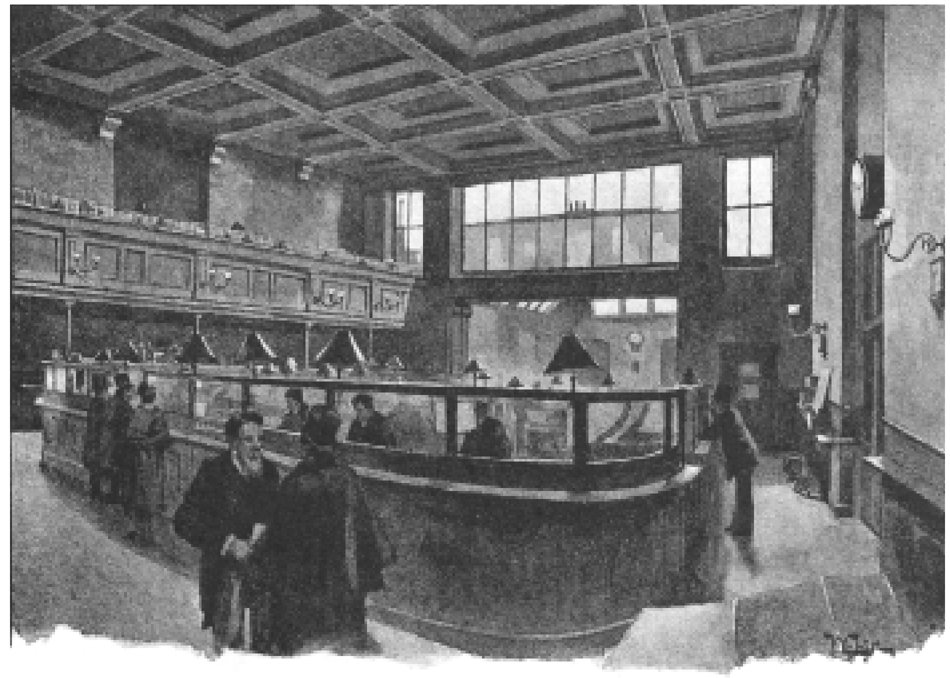
> Since therefore every measure for directly increasing the Riksbank's liquid assets abroad encountered difficulties, it seemed that for the Board all that remained was to attempt to work with more gravity to reduce the attack on the Riksbank's severely depleted foreign funds by curtailing the lending operations. For such a purpose the exchange delegate [Arnberg] considered it more appropriate to try to deter applications for larger discounting by substantially raising the Riksbank's discount and interest rates than by simply turning such applications down and proposed an increase of both the one and the other to 6%.

The board approved Arnberg's proposal – the Riksbank had become an adherent of modern discount policy. The interest rate clearly had precedence, particularly over the credit squeeze.

GOLD STANDARD

Sequences, statistics and standardisation were an obsession in the 19th century. Liberalism set great store by the decimal system – shared weights and measures would simplify international trade. The campaign included the monetary system; a universal currency was no less self-evident as a goal than the metre or the kilogram.

The first move concerned the currency's units. At the Riksdag of 1844–5 the bank committee had tried to abolish the dual system of *riksdaler banco* and *riksdaler riksgälds*, the units used by the Bank and the National Debt Office, respectively. As most people counted in the latter, it should form



Barings Bank. The bank's misplaced speculation in Argentine bonds triggered an international financial crisis in 1890. Rather more than a century later, losses on derivatives in the Asian market led to Barings' downfall.

the basis of a common unit that would be known as *riksdaler*, with a subdivision into 100 cents. However, the Estates preferred to retain the existing division of the *riksdaler* into 48 *skillingar*, with each *skilling* consisting in turn of 12 *runstycken*.

By the time of the 1850–1 Riksdag, the decimal system had become more acceptable. On 28 August 1851 the Estates called on the Council to propose a simpler currency, 'founded on the decimal division's consistent and scientific application'. The next Riksdag received the government's proposal that the currency unit was to be equal in value to 1 *rdr rgs*, be called r*iksdaler riksmynt* (*rmt*, '*riksdaler* national currency') and be 'subdivided into one hundred equal parts, called *öre*'. The Estates approved the bill and the government issued an 'ordinance concerning the national currency' on 3 February 1855.

This did not satisfy the advocates of reform. At the 1862–3 Riksdag, when Scandinavianism was all the rage, A.O. Wallenberg persuaded the Riksdag to call for a government inquiry into the possibility of introducing a common Nordic currency and measurement system.[24] A.W. Björck proposed a Nordic silver currency on a par with the North German system. One Danish *riksdaler* was worth slightly less than half a Norwegian *speciedaler* and the latter contained somewhat less silver than two Swedish *riksdaler*; all three currencies circulated in all three countries and those who lost out were disgruntled.

At this time, however, silver was giving way to gold. France, together with Belgium, Italy, the Netherlands and Switzerland, formed the Latin monetary union in December 1865 and many people saw this as a step on the road to an international monetary union with the French 10-franc coin as a universal currency. In connection with the Paris World Fair in 1867, Napoleon III convened an international monetary conference at which experts from the United States and nineteen countries in Europe spoke in favour of a gold standard with a French basis. They included Wallenberg, whom De Geer's government had appointed to represent Sweden.

On his return, Wallenberg initiated a campaign for Sweden to spearhead a major international reform instead of waiting until there was no

24 The combination was important; Wallenberg and his Norwegian ally, Ole Jacob Broch, considered that a Nordic monetary union without a common system of weights and measures would be perceived as 'incongruous'.

The *caroline*, introduced in 1868, was intended to be the Swedish version of a universal ten-franc gold coin; diam. 32 mm.

Contemporary caricature of A.O. Wallenberg as a Caroline soldier guarding Enskilda Bank, the family enterprise in Stockholm.

alternative. Joining later would be costly because the value of silver would fall as more and more countries moved to a gold standard and flooded the market with their surplus silver.

In 1868 Wallenberg persuaded the government to mint a new Swedish gold coin, *carolinen*, with a denomination of ten francs. It would be of little practical use but finance minister af Ugglas saw it as a preparatory measure whereby people 'would in time become accustomed to a coin that in all probability will become a universal coin'.

The following year the Riksdag called for a government inquiry into a new currency arrangement and a changeover to a gold standard. A committee of five advocates of reform was promptly appointed and published its report, in French as well as Swedish, in August 1870. It was unanimously in favour of moving from silver to gold and of using the gold weights in France's coinage. The *riksdaler* and the *öre* would be replaced by the franc and the centime.

A government bill in the matter was planned for the Riksdag of 1871 but was forestalled by France's disastrous defeat by Germany in the war of 1870–1. The collapse of France brought Britain's gold standard to the fore. As master of the London mint in 1717, Isaac Newton had fixed the value of one ounce of gold at £3 17s. 10½d. This remained the par value of gold for as long as the gold standard lasted.

The pound sterling had been a silver currency unit until the 1790s, when it became inconvertible on account of a shortage of silver. After the Napoleonic wars, Parliament voted for a return to convertibility in 1819 but by then the British system had adopted gold as the dominant metal. Convertibility was scheduled for 1823 but actually started two years earlier. In 1871 the new German empire adopted the reichsmark, with a gold content that differed from that of the French franc. After extracting a war indemnity from France, Germany also opted for a gold standard. Many other countries followed suit in the 1870s, while Russia, Japan and India did so in the 1890s.

A gold standard was a more modest project than the international monetary union. Each country or monetary union had its own currency and calculated in its own way but as the value of each currency was expressed in terms of gold, their mutual exchange rates were fixed.

The gold standard was a useful instrument for the first wave of 'globalisation'. The mid-19th century saw an extension and elaboration of the

international division of labour. Industrialisation took off, commerce expanded, more and more countries were drawn into the global economy, free trade was built up and capital flows increased. As trade and capital movements grew in the decades up to the First World War, the gold standard played an important role in the process of internationalisation that helped to make the countries concerned more prosperous.

With a gold standard, central banking issues differed from today's. The regulatory system was to some extent automatic. Most countries linked the note issue to the stock of bullion, so an outflow of the latter entailed a reduction of the note issue and tighter credit. In time, central banks managed to avoid the credit squeeze by using the discount rate to influence economic activity. Still, the principle was the same. Countries with a large influx of gold lowered their interest rate, whereupon rising prices led to an increased demand for imports from countries where an outflow of gold was having the opposite effect on interest rates and prices.

Gold shipments were avoided in practice; imbalances between countries were largely handled with credit (the system is sometimes described as a credit standard). A major driving force behind the development of the financial system was the increasingly large capital flows that accompanied the expansion of investment and foreign trade.

THE SCANDINAVIAN MONETARY UNION

Reflecting on France's defeat, the former secretary to the currency inquiry, Hans Forssell, renounced a universal currency and proposed a less ambitious monetary union between Norway, Sweden and Denmark. Besides promoting Nordic trade, such a union would 'forestall a harmful and dangerous split between the three countries'.

The three Nordic governments signed the Stockholm currency convention on 18 December 1872. The unit of account, the Scandinavian krona, was set equal to 1/2480 kilograms (0.44803 grams) of gold. However, the convention required parliamentary approval and both A.O. Wallenberg and Broch considered that a Nordic union stood in the way of the bigger idea. They joined forces with the traditionalist agrarian left and Broch played a part in Norway's initial rejection of the proposal. However, Wallenberg's attacks in *Dagens Nyheter*, the leading newspaper behind the Agrarian party, failed to prevent Sweden and Denmark from agreeing on a common currency system on 27 May 1873; Norway joined the union two years later. In 1877 Finland opted instead for the French franc's gold standard, on which the Latin monetary union was based.[25]

The time was ripe for a Scandinavian monetary union. Notes issued in Skåne, Sweden's southernmost province, had been circulating in Denmark since the 1850s. A.O. Wallenberg did complain that the union enabled Danes to flood the other countries' monetary systems with debased small silver and copper coins but this was checked by a legal right to refuse small change for payments of more than 20 kronor.

To begin with, the union was consolidated in a series of steps. In 1885 it was agreed that no commission would be charged on the central banks' mutual money transactions. Cross-border trade was facilitated by mutual undertakings to provide unlimited credit. In 1894 the Riksbank and Norges Bank agreed to redeem each other's notes at face value; Denmark waited until 1901.

The tide turned when Norway dissolved the union with Sweden on 7 June 1905. One week later the Riksbank cancelled its agreements with the other Scandinavian central banks; unlimited credit was replaced by limited accounts and credit lines. The new arrangement contained nothing about the right to redeem notes at par with one of the other countries' central bank; the Riksbank explained that it intended to go on doing so but was not prepared to include this in the agreement (Jahn et al., 1966).

FINANCIAL GROWING PAINS

Diversification was as much a characteristic of the 19th century as development. With the growth of international trade, price movements and business cycles spread across national borders; Sweden's economy was increasingly affected by conditions abroad. New institutions were accompanied by new industries that helped to diversify production and invigorate manufacturing

25 Finland's choice was complicated by its status as a grand duchy in the Russian empire. Pipping (1961, 1969) sees the gold standard as a way for Finland to distance itself as far as possible from Russia's chaotic monetary system. The committee of inquiry considered the German and British units of account but preferred the gold franc. Pipping notes that 'There was no mention of the Scandinavian krona … As an alternative the idea was perhaps not alien to the committee but the merest hint in that direction would have aroused political horror in Petersburg, in the same way as a proposal in 1860 to revive former Swedish names of coins had been described by governor-general Berg as "offensive".'

and trade. For a long time, cooperation was based on trial and error, not least in the banking system.

The first breakthrough occurred in the 1870s for industry but hardly at all for the commercial banks. Other sources, such as commercial houses, individual bankers and merchants, continued to be more important as providers of capital for new ventures (Samuelsson, 1968). Funds were also obtained from owner contributions and reinvested profits.

Developments in the financial system included a series of new investment opportunities. In the early 19th century money had been lent against personal guarantees or security, either directly or via brokers. In time there were banks that accepted deposits, on sight accounts to begin with and later for longer terms with a higher yield. Bonds were introduced by mortgage institutions in the second half of the century and became more widespread through issues by railway companies. Shareholding also featured in the funding of new projects and as a form of investment.

The proliferation of financial instruments catered for the growing demand for credit and investment. Early in the century, assets had been acquired in a straightforward manner by borrowing and buying. The fair price of a property or enterprise had been determined by its annual return. Industrialisation made things more difficult; it required investments that were larger and more uncertain. Who could tell what the market for completely new products would be? Who would be prepared to invest in the development of a patent that just might be a commercial success five to ten years ahead? At the same time, some things turned out to be more valuable than anyone had fully foreseen. The Atlas railway workshops in Stockholm, for instance, were an industrial failure but the site became extremely valuable when the city expanded.

A further complication was that economic development could be too rapid for a country's own investors and entrepreneurs; additional capital was needed from abroad. The opposite could also apply, for instance in France, where a saturated market in the late 19th century had too few sound projects to satisfy all the small investors. Moreover, institutions found it hard to assess the potential of a wide variety of projects in foreign countries.

The financial system gradually acquired appropriate instruments for managing all the new tasks and requirements but progress came in fits and starts, with many pitfalls. The strains sometimes proved too great for individual agents to cope with unassisted; it was under such circumstances that questions of accountability, regulation and support had to be addressed.

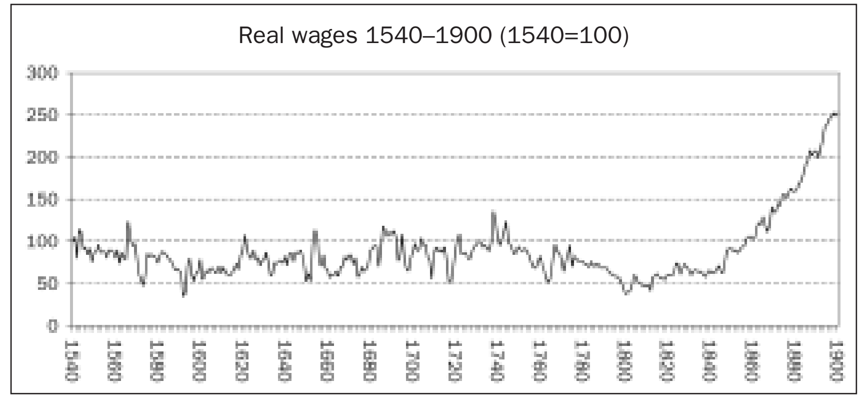
This was evident in the 1870s, when economic development in Sweden differed from that in North America and most of Europe. After several boom years, financial panic started in Vienna in 1873 and spread from there with renewed force to the United States in the early autumn and then throughout the world. The attendant price fall lasted until the mid or late 1890s; prior to the 1930s it was known in Britain as the great depression.

In Sweden, the boom continued more or less unbroken until the latter part of 1874. The first signs of a crisis appeared in 1875 but the problems did not become serious until 1877, when some railway companies defaulted on coupon payments. The price of iron started to fall that year and the price of wood products in 1878; this spread to many consumer goods and even wages were reduced.

Schön (2000) describes this as the first financial crisis in Sweden which originated in industry. Too much had been invested in activities that had not become profitable quickly enough. Difficulties in liquidating fixed assets were compounded by the strains that declining profitability imposed even on established enterprises.

It was the merchant houses and banks in Stockholm that suffered most. Population growth in Stockholm was below the urban average. Economic development in the 19th century had been stronger further south and west. Göteborg thrived, partly thanks to its proximity to British capital and markets; the town was the principal seat of one of Sweden's leading banks, Skandinaviska Kreditaktiebolag. Stockholm's mercantile establishments and banks had become more involved in the expansion of heavy industry and railways in central Sweden, activities that were hit by the crisis in the 1870s. The bank that got into worst trouble was Stockholms Enskilda; Handelsbank managed better because, after a shortage of funds in 1875, its lending policy had been cautious.

Stockholm's largest iron merchant, N.M. Höglund & Co, was already in difficulty in January 1878. A.O. Wallenberg's son, Knut Agathon, sounded the alarm from Paris but his father argued that a larger commitment was needed to prevent a failure: 'In the latter case it would have been not just one iron merchant; a score of ironworks would have kept it company.' When the hard times for the iron trade continued, A.O. Wallenberg attempted to reconstruct Höglund in November. By the 27th he thought he had succeeded, only to be told next day that additional guarantee undertakings



Wages rose faster than prices in the second half of the 19th century and this contributed to greatly increased bank deposits.

for 1.7 million kronor had come to light. When Höglund suspended payments on 2 December, the newspapers made much of the affair and people rushed to Enskilda Bank; in the course of just three days, one million kronor was withdrawn from the short deposit accounts.

The deposits on longer terms gave the bank a breathing space but even these decreased in six months from almost 20 million kronor to little more than 15 million. The bank was stuck with large holdings of railway bonds at 40–50 per cent of their face value. About forty companies and individuals with whom the bank had arrangements were forced to default. Personal visits by Knut Wallenberg failed to prevent credit withdrawals by a number of foreign connections. The acute crisis lasted eight months.

Other forces were at work, however. Oscar II counteracted the general tendency by adding 10,000 kronor to his cheque account on 7 December, followed by an equally large input to his deposit account on 14 January. A mortgage institution deposited 1.5 million kronor. Hambros in London provided credit for almost 1 million kronor. Shareholders were invited to subscribe a new issue that added 1 million kronor to the bank's capital. The stock of loans was reduced by 12 million kronor.

The government then took the decisive step. Hans Forsell, who had been appointed secretary to the Riksbank in September 1874, joined Louis De Geer's government as finance minister on 11 May the following year. His relationship with Wallenberg was somewhat frosty; they had clashed over the monetary union and did so again in 1877 when Forssell threatened to withdraw the private banks' five-kronor notes, a manoeuvre that elicited a sarcastic comment from Wallenberg: 'Chatterbox Forssell has gone to seek his fortune in favours from the farmers in the lower house'.

At first Forssell intended to do as little as possible about the railway crisis; he saw the problem as a matter for the banks. They should form a joint guarantee association that would mortgage the bonds; the government would contribute to the association's capital but that was all. However, when Forssell discussed the matter with Jules Stiernblad, a leading figure in Skånes Enskilda Bank, Stjernblad would not hear of it: 'The banks in general are not in any kind of distress. As to our friend A.O.W., more of that when we meet.'

By February 1879 Forsell was more prepared for the state to mortgage railway bonds but combined this with a proposal to end the private banks' right to issue five- and ten-kronor notes. The government proposed that the

Work on the line in Stockholm that linked up the railways from the south and north. Problems with funding the construction of railways contributed to the financial crisis in 1878–9. View near Björngårdsgatan, Södermalm, *Ny Illustrerad Tidning*, 1 February 1868.

Riksdag should raise a 'predominantly' domestic loan of 30 million kronor for a railway mortgage fund that would be wound up without loss to the state no later than 1893. A separate government bill proposed the withdrawal of the private banks' five-kronor notes and presaged a withdrawal of the ten-kronor notes in 1882, moves that Forsell hoped would win support from the Agrarian party.

A.O. Wallenberg objected strongly; a domestic loan would simply mean that Stockholms Enskilda Bank's depositors withdrew their money to buy more attractive government bonds – transferring capital would not solve the problem of internal liquidity.

The National Debt Office was also critical. Domestic borrowing was ineffective, costly and detrimental to the government's credit at home as well as abroad. Raising a government loan abroad, on the other hand, was entirely advantageous; it could be arranged by disposing of residual parts of earlier government loans from 1872 onwards. The Office got its way.

The railway mortgage fund saved Stockholms Enskilda Bank. In 1879–80 the National Debt Office lent a total of 7.8 million kronor from the fund, of which 4 million went to Stockholms Enskilda Bank; that was equivalent to one-third of the bank's loan stock.

By the beginning of August 1879, A.O. Wallenberg could breathe more easily. The loan became increasingly favourable and the bank held on to it for as long as possible. As time passed, however, the tension between Forssell and Wallenberg grew; the former felt free to talk about how grave the situation had been, while the latter was inclined to downplay its importance (Nilsson, 1994).

The government's management of the crisis promoted a reorganisation of the financial system. Banks received support but bankers and merchants had to save themselves. The way was now more open for commercial banks and credit market innovations. By the end of the 1870s, Sweden had a more extensive banking system than any other country in Europe apart from England (Lundström, 1999).

The Riksbank was torn between its commercial operations and the need to coordinate and regulate the country's credit system. It contributed by purchasing the foreign bills which Stockholms Enskilda Bank drew on its foreign correspondents to supply wavering depositors, 'But that help was by no means provided in a trustful manner' (Nilsson, 1994); the Riksbank required collateral in the form of General Mortgage Bank bonds in case the

As finance minister, Hans Forssell (1843–1901) was forced to intervene and use 'state aid' in the form of the railway mortgage fund to rescue Stockholms Enskilda Bank. Caricature in *Fäderneslandet*, 28 February 1879.

foreign correspondents defaulted on Stockholms Enskilda Bank's bills.

The consequences of the crisis were also troublesome. The Riksbank had incurred substantial losses on its commercial loans; bad debts peaked in August 1879 at over 3 million kronor. This aroused the Agrarians' concern and displeasure; it also involved the Bank in the management of distressed enterprises.

The task of reconstructing industrial estates on the brink of bankruptcy was a major dilemma. The Bank wanted to act as a commercial bank but was prevented from doing so when its borrowers defaulted.[26] In bankruptcy proceedings concerning a number of merchant houses, the Riksbank was adamant about getting as much as possible from its claims.

The crisis prompted some enterprising men to explore new avenues. Soon after the failure of a leading merchant house in Stockholm, Guillemot & Weylandt, one of the owners, Ludvig Fredholm, started Elektriska AB; the company was transformed into ASEA in 1890 and played a key role in the industrial revolution that took off in that decade. In another world, the author August Strindberg had mortgaged the shares which his wife, Siri von Essen, held in the merchant house and was declared bankrupt in 1879; shortly afterwards, his novel *Röda rummet* (*The Red Room*) was published and restored him financially.

Exports of oats declined and became less profitable in the 1880s but exports of butter rose rapidly. This contributed to a second reorganisation of agriculture, with a switch to cattle and dairy farming. New industrial goods also left their mark; paper and safety-matches, for example, increased their shares in Sweden's foreign trade.

THE 1881 BANKING COMMITTEE

It took time to arrive at the banking system which is now considered normal: a variety of more or less specialised financial institutions grouped around a central bank. Private banks were first in some countries, in others a state bank that combined commercial operations with the functions of a central

26 A similar conflict arose in 1897 when Stockholms Enskilda Bank issued bonds in France for a loan to Norway's capital city, Christiania. The original plan had been for the bond consortium to include the Riksbank; however, when Stockholms Enskilda Bank needed to purchase bills in Norway, the Bank opposed the transfer with reference to the foreign exchange reserves and withdrew (Gasslander, 1956).

bank. The tendency in Sweden, as well as elsewhere, was to tackle the banking problem by having a state bank with a nationwide network of branch offices. In time there was a move towards transforming the state bank into a central bank with a note issuing monopoly.

For Sweden, an important influence was what happened abroad. Prussia announced the minting of an imperial gold coin on 4 December 1871 but did not consider that this required a central bank. Pressure for a solution grew after the 1873 *Gründerkrach*, when some years of speculation ended in numerous bank failures. When bank legislation was tabled in 1874 without provisions for a central bank, a liberal politician insisted on the establishment of a Prussian State Bank (incorporated two years later in the Reichsbank). Switzerland managed without a central bank in the 19th century by relying when necessary on the Banque de France. However, war or the threat of war put a stop to this and during the crises in 1870 and 1886 each Swiss bank saw to its own interest by restricting credit, which only made matters worse. This helped clarify the need for a Swiss central bank, which was established in 1905.

The United States was the major exception; the Federal Reserve System was not set up until 1913. 'In sum, the experience of the United States with rapid economic growth and a changing, somewhat chaotic banking system seems to show that, though banks are necessary for economic growth in complex industrial societies, a rational banking system is not' (Cameron & Neal, 2006).

In Sweden, the crisis of 1878–9 highlighted the drawbacks of financial disorder. In the days of the Diet of the Estates, the chairman of the Bank's board of directors had been appointed by the Nobility and was often an ally of the government. In the bicameral Riksdag, however, rivalry between the two chambers complicated matters; support for their nominees was regularly split equally, so the matter had to be settled by drawing lots. Meanwhile, the Agrarians in the lower chamber did what they could to strengthen the Riksbank, while the upper chamber favoured the private banks. It was an exhausting struggle – when the chambers decided differently and the matter was put to a joint vote, the second chamber generally won.

In 1881 the lower chamber called for an inquiry into the banking system and threatened to assign the task to the Bank's directors, which overcame the upper chamber's earlier opposition. A compromise was reached whereby the Riksdag requested the government to inquire into new legislation for the private banks. A ten-man committee was appointed in November 1881 with instructions to submit proposals before the bank permits expired in 1883. The committee included representatives of the Riksbank, the Agrarian party, the joint-stock banks and the private banks. A.O. Wallenberg was marginalised; the events of 1878–9 had severely weakened his authority. It was a bitter man who wrote of the committee's composition:

> When I contemplate Dufwa's committee in tranquillity and accordingly foresee how Dufwa, Lyttkens, Mannheimer and Heckscher would improve the banking system, I sense the same shudder I imagine Phidias and Praxiteles would have experienced if those in power had ordered apprentice masons to 'improve' their works of art.

Two years later, the banking committee's report took a clear stand for a more structured banking system. It praised a note-issuing monopoly while declaring that commercial operations were best left to private banks. The profits from commercial banking belonged to the commercial banks, while the Riksbank's profit should come from its note monopoly and from short-term lending to the commercial banks, which safeguarded their liquidity. The committee wrote as follows about the relationship between commercial banks and the central bank:

> During periods of undisturbed enterprise and unshaken confidence, such a [central] bank usually adopts a more withdrawn attitude and takes little part in other banking institutions' competition whereby each extends its business operations to the maximum its assets permit. But when the financial world's horizon clouds over and other banks promptly scale down their possibly unduly extended operations, the central bank then expands its and when the storm finally breaks, steps forward with the full might of its large, accumulated resources and its credit, recognised throughout the world.

The most controversial issue was ownership. There were other countries where the central bank was privately owned and from time to time this solution had been suggested for Sweden. The committee was sympathetic in

principle but went only so far as to propose that private interests would own a third of the bank and appoint a third of its directors, while the government would appoint the chairman and the Riksdag the others. The King-in-Council refused to give the Riksbank the sole right to issue notes without having a say in its management, a condition that went back to the time of Karl XIV Johan (Gasslander, 1956).

The proposal was doomed from the start and it may be asked why politically experienced people had backed it. Nilsson (1994) sees the influence of the King. Writing to A.O. Wallenberg, Oscar II confided that he had agreed to the committee in the 'grounded hope it would come up with a real reorganisation of the Riksbank, its nature and board'. On Christmas Day 1885 he took up the matter again:

> I must, however, *in accordance with the facts* correct a misunderstanding expressed in your letter. It is truly not stated by my 'political entourage' that the Riksbank ought to have a monopoly of 'ownership' [of the right to issue notes] as long as the Riksdag is to manage it. Neither has this ever been nor certainly ever will be my opinion. But a national limited partnership bank, with the monarch's real participation on the board and private capitalists' co-controlling assistance, *that* has been, is and will be my ideal. Though I doubt whether I shall experience the day when such a bank establishment can in our dear fatherland see the light of day.

The reform process was in the doldrums. The government renewed the private banks' permits, the Agrarians continued to snipe at them and the upper chamber stood firm.

At the Riksbank, however, a change was on the way. The Bank realised it was losing its influence in the money market and wanted to counter this by ending the issue of private notes. It began to lend to the commercial banks against government bonds, which gave it more influence over liquidity; in return, it was prepared to relinquish much of its commercial operations.

The man behind this was Arnberg. As a member of the 1881 banking committee he had persuaded the representatives of both the commercial and the private banks. The committee proposed that if the nation had a streamlined central bank, this would be 'a strong centre around which all economic life can gravitate and by which it is strongly borne and held together when other support fails, other cohesive forces are paralysed'. When banking was discussed in the Swedish Economic Society in 1884–5, the committee's secretary, Claes Westman, argued that the interest rate ought to be decided by a central bank that did not have to base its profit on transactions with the general public.

THE DECISIVE STEP

Another banking committee was appointed by the government in 1889 and presented its proposals the following year. It reiterated much of what the 1881 committee had found and proposed that private banks would have access to credit on favourable terms to make up for the withdrawal of private notes.

Note issues had become less important. Credit institutions could now provide credit in the form of certificates of deposit, money orders and bonds; this offset the effect of not issuing notes. Joint-stock banks that did not issue notes, headed by Skandinaviska Kreditaktiebolag and Stockholms Handelsbank, were carrying more weight among the commercial banks. As a central bank, the Riksbank would be able to control the credit market more effectively by rediscounting bank bills and thereby influencing the price of money via the discount rate.

Power over the Bank continued to block progress. As a concession to the King-in-Council, the committee proposed a larger board consisting of nine directors, of whom the government would appoint one third; this was unacceptable to the lower chamber, which feared that the upper chamber would join forces with the government's men and secure a stable majority. The matter was to have been settled before the private banks' permits expired in 1893 but this deadline also passed.

The lower chamber began to flex its muscles. If a note monopoly was not acceptable, private notes could at least be made unprofitable by means of the tax on issues. The lower chamber saw to it that the note tax was raised in two steps from 0.3 to 1 per cent and was prepared to go further. This had an effect on bank margins. The government and the private banks were in danger of seeing the right to issue notes taxed away without gaining either a law, compensation to note-issuing banks, or government influence over the Riksbank.

Faced with this threat, the leaders in the upper chamber sought a compromise. In 1894 both chambers approved a request for a government

A 10-kronor note issued by Stockholms Enskilda, a private bank; 120×75 mm.

bill based on the report from 1890. A proposal drafted in the finance ministry was presented by the government in 1896, whereupon the Riksdag approved the constitutional amendments for the first time; the following year the newly elected Riksdag approved both the dormant Riksbank Act and the law that terminated private note issues.

The lower chamber's concessions were not substantial. The chairman of the board would be a government appointee. The Bank's regulations would be decided in the same way as other legislation, not by a joint vote but by the two chambers arriving at the same decision; in that way the upper chamber did not risk being out-voted.

In exchange for its note monopoly and the role of central bank, the private banks wanted the Riksbank to abstain from offering interest-bearing deposits. The 1897 committee had proposed that the Bank would continue to provide cheque accounts and accept deposits. Current accounts would enable the Bank to keep in touch with the business community, and interest-bearing deposit accounts could influence bank interest margins. The upper chamber was opposed to deposit accounts and this provision was deleted when the decisions were harmonised. The note monopoly was to be in force no later than 1903.

While the private banks had earned income on note issues, they had also been obliged to hold interest-free funds in Riksbank notes and gold for the redemption of notes. Then there was the successively higher note tax. Instead, they now obtained credit from the Riksbank on favourable terms in the transitional years.

The slow changeover gave opponents a chance. A.O. Wallenberg argued that the note monopoly would favour joint-stock banks at the expense of private banks and pointed to the risk for small banks and thereby for rural credit. After A.O.'s death in 1886, his son Knut took up the cudgels: the note monopoly was hazardous outside the hands of a private institution, independent of political interests. In October 1900, a Danish colleague received a gloomy view of the future:

> Wise from experience in recent years, one begins to be generally concerned about the time when the Riksbank, still controlled by school-teachers and politicians, will be in sole control of the country's liquid assets. Since Arnberg left this world there are no professional insights there and even less courage.

THE MODERN CENTRAL BANK

The Riksbank Act of 1897 largely established a modern central bank, albeit with two persistent Swedish singularities: the Bank as an agency of the Riksdag and the separation of the central bank from the national debt office (likewise a parliamentary agency).

The Bank's new management structure was clearer and more professional. The government appointed the chairman of the seven-man board and the day-to-day operations were directed by a first delegate assisted by two second delegates. The Riksbank was to concentrate on being the banks' bank but was still not solely a central bank. It continued to arrange some residual lending and was banker to the state, though the National Debt Office was primarily responsible for government borrowing. The note monopoly applied formally from 1903; the private banks nullified their issues somewhat ahead of schedule.

When Arnberg died on 20 June 1900, the annual salary for his post as exchange delegate was increased from 12,000 to 20,000 kronor to attract a competent successor. The delegate for internal administration was paid 15,000 kronor. The banking committee changed their titles to first and second delegate, respectively, and raised the salary for a deputy delegate to 12,000 kronor to make this a full-time occupation.

The post of first delegate went to Karl Langenskiöld, who had read mathematics and law in Helsinki before presenting a doctoral thesis in political economy. He had then joined one of Finland's largest banks and become its head before Skandinaviska Kreditaktiebolag recruited him to its Stockholm office in 1892 and appointed him managing director in 1895. In the latter capacity he organised the first clearing between banks in Stockholm in 1896. This procedure, whereby banks settle their mutual payments, is a central bank function and the Riksbank took it over in 1899.

The politicians did not relinquish their hold over the monetary system but made greater use of professionals (Gasslander, 1956). They came, not from circles connected with Stockholms Enskilda Bank, but from joint-stock banks. Besides Langenskiöld, there was the banker Carl Weber, who was appointed deputy delegate. He had taken over the firm of L.R. Weylandt after his uncle and been offered a seat on the board of Stockholms Enskilda Bank in 1898 but declined on the grounds that he could never be a director of a joint-liability bank. Instead he had joined the board of Stockholms Inteckningsgaranti AB, a bank that specialised in property.

Under Langenskiöld, the Riksbank was modernised. A department for monitoring statistics and reporting the Bank's foreign exchange and credit positions was set up in 1906. His papers in the Bank's archives include regular market information from Warburg in Hamburg and Lazard Brothers in London and his correspondence was a forerunner of today's international surveillance.

The Riksbank was also on the way to having premises that were more suitable than the ancient buildings in the Old Town and the makeshift annexe in Malmtorgsgatan. The committee for a new building for the bicameral Riksdag had been given this matter to consider in the 1880s and the ensuing discussion, planning and construction had taken their time. The new premises on Helgeandsholmen, the small island between the Old Town and what was becoming Stockholm's centre, were finally ready in 1906; after closing time on Saturday 20 October the Riksbank left its old buildings and opened its new doors to the public two days later. One can say that it moved with the times; in the early 20th century the commercial banks were relocating their head offices from the Old Town to the area around Gustav Adolfs Torg and Kungsträdgården. They were following a general trend in the business community but still needed to be close to the Riksbank. Transport had become easier but cash holdings and documents continued to pass to and fro on a daily basis.

The Bank had 379 employees at the end of 1904. Somewhat belatedly, the first women were taken on as assistants in 1907. The board of Stockholms Enskilda Bank had decided to employ women 'after some discussion' as long ago as 1864; the matter had been backed by no less a person than A.O. Wallenberg under the influence of his second wife, Anna von Sydow. The savings bank for the city of Lund and its environs had in the same year appointed a woman to sit on its board; when the male director retired soon after, it was she and a female assistant who ran what soon came to be known as the 'womenfolk's bank'.

Such examples carried weight. The chairman of the Riksbank's board observed that 'Experience in the private banks has, however, plainly evinced that a great deal of the work in these banks can be done by women just as well as by men'. The Board did not find 'any hindrance to accepting women as temporary staff in the Bank'. The first four women were

Karl Langenskiöld (1857–1925), the first Riksbank governor to be in charge of the management of a financial crisis, in 1907.

The Note Office in the Bank's premises at Järntorget in the Old Town, 1904.

employed from 17 October 1907; the minutes of the board meeting show that none of them had a common surname. By 1924 the staff of 437 included 50 women.

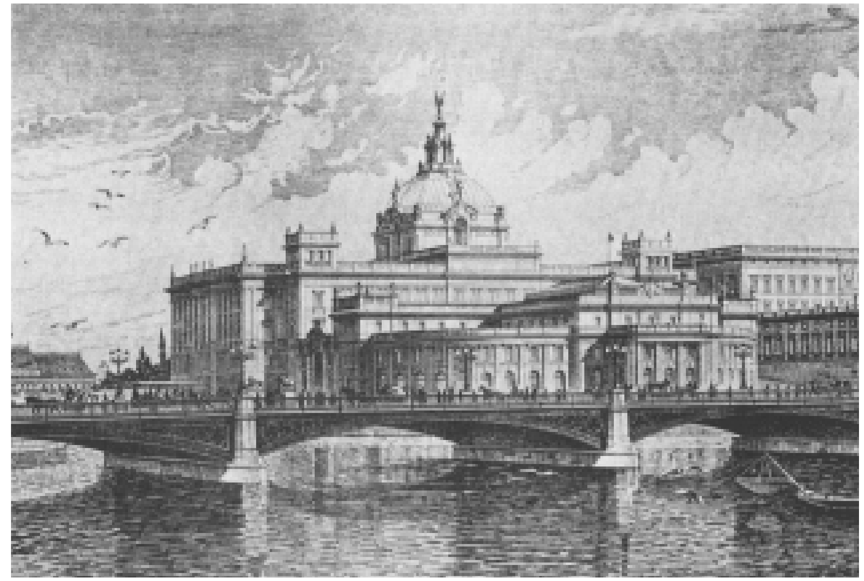
Other changes came from technological developments. On the day the board decided to employ women, the head porter complained about the cost of lighting in his accommodation in the new building and wanted to replace the electric fittings with paraffin lamps. 'Delegate Berg pointed out that, in view of its greater inflammability, paraffin lighting in the Bank building seemed inappropriate and therefore requested that, in order to avoid it, the Riksbank would contribute half of the cost of the electric lighting in the head porter's quarters.'

The future head of Skandinaviska Kreditaktiebolag, Oscar Rydbeck, is said to have seen a 'reckoning machine' at the Stockholm Exhibition in 1897 (Thunholm, 1991), whereupon he got the bank executives' permission to buy one, according to him the first in Sweden's banking system. In 1893 the auditors of Östgöta Enskilda Bank had been less enlightened when they found the procurement of a typewriter 'unnecessary and useless'. It was Langenskiöld who headed Skandinaviska Kreditaktiebolag when Rydbeck bought his machine; at the Riksbank, things moved more slowly. Typed pages did begin to be pasted into the folios with handwritten minutes of board meetings but banks in general did not adopt the new technique in earnest until the 1920s, when speed typing competitions were arranged to popularise the skill.

As the central bank, the Riksbank was more explicitly but not solely responsible for the stability of financial systems. The events of 1878–9 had made the government and the Riksdag more aware of the risks. Bank legislation was tightened to protect depositors. A number of large industrial and investment banks had failed in France and Germany; in Sweden, the law prohibited banks from doing business in shares and property.

The Bank Inspection Board led the way. The decree that establishing a bank required permission from the King-in-Council dated from 1824, but it was not until 18 June 1868 that the government called for an official who would be specifically responsible for bank matters. A banking division, headed by a bank inspector, was set up in the finance ministry in 1876.

The work became stable and stringent under Robert Benckert, who left the post of ombudsman in Stockholms Enskilda Bank to become bank inspector in 1888 and enlarged the staff in the following years. The division



The Riksbank moved from the Old Town to its new building on Helgeandsholmen in 1906. Proposal by the architect, Aron Johansson (the dome was rejected).

The Bank first employed women in 1907. In time, the staff at branch offices, such as this one in Malmö, also included women.

was transformed into an independent administrative board in 1907, with resources for a close examination of banks' accounts that often led to sharp comments. The Bank Inspection Board developed a preventive role in relation to payment system stability.

This was just as well because economic developments kept the Board busy. International economic activity picked up in the 1890s. With the discovery of gold in South Africa, Alaska, Canada and Siberia, prices turned slightly upwards until the outbreak of the First World War.

In the years around 1890, Sweden had the highest growth rate among industrialising countries. This continued to be the case in the next six decades. At the same time, the commercial banks took the lead in industrial finance, relegating private bankers and merchant houses to a secondary role.

Swedish companies such as AGA, ASEA, L.M. Ericsson, Separator and SKF spearheaded some of the global economy's innovations. A number of these firms dated from the 1880s; their growth began in earnest in the early 1890s. They were specialised enterprises, associated with Sweden's foremost contemporary innovators. For many of them it was the new major banks that acted as financial midwife. The Wallenberg dynasty, with 'district judge' (*häradshövding*) Marcus Wallenberg as the leading industrialist, used Stockholms Enskilda Bank to build up a powerful industrial complex.

One aspect of the economic upswing was a marked change in the composition of Swedish exports. Pulp and paper expanded from 5 per cent of total exports of goods in 1890 to 30 per cent in 1930, while machinery and instruments grew from one or two per cent to over 10 per cent and exports of iron ore did much the same, to the benefit of the mines in central and northern Sweden.

The sustained growth made heavy demands on the financial system. 'Big business deals, such as the merger in 1896 of the Grängesberg mining company and the Grängesberg-Oxelösund railway company to form Sweden's largest company, TrafikAB Grängesberg-Oxelösund (TGOJ), the exploitation of the ore fields around Luossavaara-Kirunavaara in the LKAB mining company, the development of hydroelectric power and the pulp industry, the consolidation of domestic-market manufacturing into larger units – all this generated financial transactions on a far greater scale than before' (Schön, 2000).

The first big industrial companies had largely financed their growth from profits. Towards the turn of the century they needed more capital and became increasingly reliant on the banks. The Riksbank started to rediscount bank bills, which made provincial banks less dependent on the major commercial banks. Wider opportunities arose for new banks, 56 of which were established in the period 1896–1908. There were also a good many mergers (the most spectacular, in 1910, involved the two largest banks, Skandinaviska Kreditaktiebolag and Skånes Enskilda Bank) but the number of banks supervised by the Bank Inspection Board still increased from 47 to 85. This was accompanied by the expansion of savings banks and insurance companies.

After the Russo-Japanese war in 1904–5, the international economic situation became even more favourable. Share and property prices rose during the boom of 1905–7 and share dealing became more widespread. The Stockholm stock exchange had been reorganised in 1901 and was open as of 1907 to 16 banks in addition to the five established stockbrokers. This provided a functional secondary market in securities.

Rising share prices led many speculators to pledge their holdings for bank loans. A major driving force behind this was shares in Grängesberg, which in 1913 accounted for more than half of stock market turnover. The starting-point had been the company's purchase of the Lappland ore field in 1903. In these years, loans against shares made up 30 per cent of total commercial bank lending, more than half of Handelsbank's loans and an even larger share of Stockholms Enskilda Bank's.

To cover lending with capital, the banks competed for deposits, particularly before the boom ended in 1907. The commercial banks used a syndicate they had formed in 1880 to agree on interest rates; however, these arrangements were looser than they were after the syndicate had been converted into the Swedish Bankers Association in 1910.

Sydsvenska Kreditaktiebolag competed most aggressively. Its branch managers earned a commission on deposits and were authorised to accept other banks' certificates of deposit as an input of cash; in exchange, customers received the bank's certificates at a higher rate. The bank also used agents to recruit other banks' customers and openly advertised higher interest rates than those the syndicate had agreed on. In some cases the agreement was honoured formally and the rate to the customer was noted in the margin. The other banks did not respond with proper countermeasures until 1907, by which time Sydsvenska Kreditaktiebolag was strong enough to dispense with unorthodox methods.

Domestic funds were insufficient. In the years around 1910 Sweden's foreign debt per capita was probably the highest in the world (Schön, 2000). The current account had mostly been in the red since the mid-19th century and external debt was equivalent to 75 per cent of the gross national product. That was not unnatural for a rapidly expanding economy with large and profitable investment opportunities but it did call for efficient financial mediation.

K.A. Wallenberg in Stockholms Enskilda Bank and Louis Frænckel in Stockholms Handelsbank were instrumental in placing large bond loans abroad. For a long time the Riksbank's commercial operations enabled it to participate in the bank consortia behind the loans. Another procedure involved 'retiring' packages of Swedish bills abroad, which amounted to borrowing against the bills. It paid banks to 'retire' bills instead of rediscounting in the Riksbank because market interest rates in France tended to be below the Swedish discount rate. (A more developed form of this technique was involved when the collapse of the American subprime mortgage market triggered a financial crisis in 2007–8.)

Growth was not continuous, however. In mid-October 1907 a number of New York banks applied for and obtained support from their joint Clearing House. On 21 October their problems spread to the Knickerbocker Trust Company, which was not a member of the Clearing House; next day a run on Knickerbocker forced it to suspend payments. The panic spread to other trusts and banks until the Treasury Secretary, George Cortelyou, deposited $25 million in the leading New York reserve banks on 24 October and J.P. Morgan organised support together with some leading banks and financiers. By the time the situation in New York was under control, the disturbance had spread to other parts of the United States. It was this crisis that initiated the reforms which resulted in the Federal Reserve System.

The panic then spread from the United States to Europe and stock exchanges plummeted towards the end of 1907. Banks that had financed speculation in shares found themselves in difficulties when the value of collateral fell. The economic boom had been aided by massive borrowing abroad; when the economy slackened, many short-term loans were recalled. Speculation against Sweden's currency increased. Discount rates abroad went up, to 7 per cent in England, 7½ in Germany and as much as 8 per cent in

Denmark. The Riksbank raised its discount rate to 6½ per cent on 9 November and to 7 per cent on 12 December, which added to the pressure on Swedish banks and enterprises.

Loan repayment entailed a large demand for foreign exchange from the Riksbank. The Bank took over part of a foreign loan from the National Debt Office, sold some of its holding of foreign bonds and in November and December exported gold from the reserves. At the beginning of 1908 the City of Stockholm placed a foreign loan at the disposal of the Riksbank in exchange for the latter becoming accountable for the City's bills. All this greatly reinforced the Bank's external reserves.

The general public reacted to the crisis by redeeming notes and borrowing less. With fewer notes in circulation and decreased domestic lending, the Riksbank decided to lower the discount rate by half a percentage point on 28 January. When discount rates abroad fell during the spring, the Riksbank followed suit.

The crisis also spread to property. Falling prices and less access to credit proved too much for many building contractors, whereupon the banks had a great deal of property on their hands. A separate company was set up by Handelsbank to manage the holdings it had taken over, some of them still under construction. Stadshypotekskassa, an urban mortgage bank, was established in 1907. The financial problems left their mark on the closing years of the great transformation from 1890 to 1910. Banks and other companies that had remained solvent took advantage of the situation by acquiring other enterprises and concentrating operations.

For the first time, the Riksbank acted as a modern central bank. Langenskiöld focused on maintaining liquidity and sought assistance abroad. While the recovery was fairly rapid in other countries, in Sweden it was delayed by the general strike of 1909. Moreover, some banks were so hard pressed that they had to be either reconstructed or taken over.

Contemporary assessments of what the Riksbank had done were generally positive. Langenskiöld was judged to have handled the strains in the way Bagehot found appropriate for a modern central bank. Frænckel and K.A. Wallenberg both expressed their appreciation in the business journal *Affärsvärlden*. When Langenskiöld retired, he was praised in particular for his efforts during the crisis.

One dissenter was the political economist Gustav Cassel; in a critical paper (Cassel, 1908) he described the Bank as passive and incompetent. The discount rate had not been increased sufficiently to dampen the economy in 1906 and 1907. He also accused the Bank of divided loyalties: as the government's bank it preferred a low interest rate, while the economic situation called for an increase. The leadership of the Riksbank had not been sufficiently professional:

> The first condition for a better direction of the Riksbank is that we free ourselves from ways of thinking we have inherited from the days of the Secret Committee and learn to appreciate the value of competent criticism, based on a generally informed interest in the country's business community.
>
> The second condition concerns the individuals of whom the Bank's board is composed. *That the leaders of the country's central bank are appointed by the Riksdag is in itself an abnormal arrangement* [emphasis in Langenskiöld's copy] that does not possess a great probability of turning out well. Far from satisfactory, even from the Riksdag's point of view, is the way in which this arrangement actually functions.

Langenskiöld (1908) responded in a matter of weeks, refuting the 'abnormality' by referring to Cassel's own statement that the crisis had not caused any sizeable disruption in Sweden. Langenskiöld also asserted that on average the discount rate had been higher in Sweden than abroad. He had personally advocated a larger note issue but failed to get this accepted, and he cited the private banks' deposits as an example of cooperation during the crisis.

Writing about his time as bank inspector, Robert Benckert (1911 [1976]) repeatedly mentioned Langenskiöld. As head of the Riksbank, the latter had been more active in relation to other banks than any of his predecessors. He had intervened in the banking system's transformation, drawing on experience and contacts since his time with Skandinaviska Kreditaktiebolag. He had arranged support for struggling institutions. It was he who had put forward Oscar Rydbeck as managing director when Hernösands Enskilda Bank was reconstructed. As bank inspector, Benckert had consulted Langenskiöld in tricky cases; 'that the Riksbank is a powerful executor, when it wishes to don that mantle, is most evident in the matter of Stenberg'.[27]

Possibly mindful of Cassel's criticism, Benckert also discussed what

As bank inspector from 1888 to 1913, Robert Benckert (1846–1938) did much to stabilise the payment system. Medal engraved by Erik Lindberg,diam. 60 mm.

Langenskiöld had done during the crisis of 1907–8. He emphasised the ability to find solutions whereby hard-pressed banks and other enterprises could survive:

> Now I will admit that in retrospect it seemed that in individual cases Langenskiöld's 'mediation' went somewhat too far but anyone who impartially followed the events during the crisis of 1907–8 must recognise – with a salute for the hard, burdensome tasks L. voluntarily shouldered – that his activities on the whole were of very great value for our country. If instead the Riksbank had been headed by Frænckel[28] – he who managed his own bank in such exemplary fashion (!) – then many companies which were in danger during the crisis but are now viable once more would certainly have been dashed to pieces.

LANGENSKIÖLD'S BANK COUNCIL

Langenskiöld decided to retire in 1912 at the age of 55, tired (as he put it) of the bank committee harping on trivialities. He devoted his time instead to various public duties and the management of his fortune. On the eve of his departure, he raised the questions of the Riksbank as the agency of the Riksdag and responsibility for the Bank's operations.

The criticism from 1908 had not been forgotten. Langenskiöld, Cassel and many others saw the danger of a conflict between the Riksbank's political master and its increasingly complicated functions as a central bank. In order to bridge the gap, Langenskiöld proposed a 30-strong bank council, made up of 'men experienced in bank matters' with a three-year mandate; the upper and lower chambers would each appoint twelve members and the government would nominate the remaining six. The council would receive the Bank board's report on the state of the Bank, its operations and administration, as well as the auditors' report. It would appoint the regular and alternate members of the board and decide whether or not to grant discharge from liability. Only council decisions in purely economic matters would be subject to the Riksdag's approval.

The proposal was based on fears of the consequences of parliamentarianism. How could expert knowledge hold its own if politics reigned supreme? The Riksdag would still exert power over the Bank but the power would be mediated by competent, experienced men. The trade-off between a political foundation on the one hand and the need for monetary policy competence on the other was one of the ingredients of 19th century bank policy, just as it reappeared in the discussion of central bank independence in the late 20th century.

The issue was the subject of a survey by the evening paper *Aftonbladet*. Motions were tabled in the upper chamber by K.A. Wallenberg and A. Hedenlund, in the lower chamber by the Liberal A. Rune. Wallenberg and his allies used the matter as an opportunity to revive the question of privatising the Bank. This widened the issue to include ownership, an aspect Langenskiöld had been careful to avoid.

The Swedish Economic Society arranged a meeting on 23 April 1912 about 'The organisation of a note-issuing central bank, with special reference to Sveriges Riksbank'. Professor Sven Brisman welcomed the bank council as a sensible proposal; the Riksdag would receive expert assistance from an organisation that was formally independent but would appoint most of its members. Another speaker hoped that the Chamber of Commerce and other corporations would also be represented.

Marcus Wallenberg argued along the same lines as his half-brother Knut. They wanted an inquiry into 'depriving the Riksdag of its current influence on the Riksbank'; otherwise, a bank council would be a practical alternative. 'It would be appropriate for this bank council to consist of representatives of the nation's ten largest banks and for it to meet at regular intervals, for instance once a fortnight. In this way the business community

27 Director Stenberg had involved Gäfle Handelsbank in risky business but was backed by the board. Benckert arranged a meeting between the chairman of the board and Langenskiöld, who submitted a report. The chairman had referred to the board's written explanation of its actions; '– Yes, the baron [Langenskiöld] had also read it but found it unsatisfactory. – Well, what did the baron want? – Yes, since the Riksbank could not have confidence in the bank's leadership, it was no doubt best that Stenberg resigned. – At the next general meeting? – No, without delay. – When Stenberg remarked that resigning between general meetings was unpleasant, it was observed that *being dismissed* against one's will was still more unpleasant.' Stenberg had vacated his post on the appointed day but the chairman wondered whom should be chosen as director. Langenskiöld had proposed a Riksbank official, who was accepted. 'The choice seems to have turned out very well,' Benckert concludes.

28 Louis Frænckel, who began his career as a merchant and banker, became managing director of Stockholms Handelsbank in 1893. He was highly successful in the latter capacity but Benckert considered he was too prone to allow other banks and companies to fail even when temporary support would have enabled them to survive.

would be constantly in touch with the management of the Bank.'

The head of the General Mortgage Bank, Victor Moll, remained undecided about the question of a state or a private bank. All central banks had performed their tasks in a largely satisfactory way notwithstanding the differences in their organisation. The outcome depended on who ran the bank. Moll was not convinced that Langenskiöld's bank council would be better. According to him, political influence had diminished, if anything, in recent years. 'Herr Wallenberg has put forward the idea that one might be able to achieve an advisory bank council without having to curtail the Riksdag's current influence on the Riksbank. It is an idea that is worth considering.'

Langenskiöld had the last word. One of the principal objections was that there would be too many government appointees. Langenskiöld admitted to having believed that when the chambers nominated members for the council, they would in the first place look to their own. 'I had then thought that the King-in-Council would probably look more impersonally at the tasks of the council and restrict the search primarily to prominent men in the world of banking, trade and industry. From this angle I therefore consider it desirable that the government appoint some members of the council. I do not, as I said, consider that what matters most is to retain unchanged the present division of power between the government and the Riksdag; the main thing instead is to solve the question in the way that is most advantageous for the Bank.'

Noting that several proposals had been put forward for a reorganisation of the Riksbank, the Riksdag's bank committee made a courteous gesture to the head of the Riksbank: 'In this respect, one proposal, submitted from a competent quarter, has attracted a certain attention.' The committee refrained from deciding about the proposal for a bank council but did recommend that the matter be investigated.

When the issue was debated in the two chambers, however, there was more to come. Support from the Wallenbergs was counterproductive. Professor Gustaf Steffen attacked Knut Wallenberg for aiming to use privatisation as a means of removing an awkward competitor, to which Wallenberg replied: 'My reason for introducing the bill is that I am keenly convinced that the organisation of the Riksbank can be improved. I thought Herr Steffen was a political economist. He seems to have abandoned that path and devoted himself exclusively to sociological, not to say social democratic,

endeavours.' Another member explained that he had nothing against an inquiry with the emphasis on Langenskiöld's proposal but as the committee had not opposed the idea of private ownership he moved that the bill be rejected. Speaking last in the lower chamber, Hjalmar Branting, the future prime minister in the first Social Democratic government, argued against the Riksdag's influence on the Bank being limited by the government appointing a fifth of the council compared with a seventh of the board of directors.

By the time the committee's statement was voted down, Langenskiöld had retired. When it came to appointing his successor and a new second delegate, the Riksdag was divided; right-wing politicians nominated Richard Lindgren from Bank AB Södra Sverige (Southern Sweden) and Adolf Hallin från Bank AB Norra Sverige (Northern Sweden), while left-wingers put forward Victor Moll (the man who had refrained from deciding about the bank council) from the General Mortgage Bank and John Swartling from Nordiska Kreditbank. The voting resulted in a tie and the lot fell to Moll's advantage, with Lindgren as his second-in-command.

According to press reports, the fact that such an important post was decided by drawing lots was embarrassing abroad, as well as in Sweden. 'Moreover, according to contemporary opinion as well as the judgement of posterity, the result of the draw was a great calamity' (Thunholm, 1991).