

Geneva and London: investments in the English funds

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Alongside French debt, Geneva's capitalists invest in British public funds. After the revolution of 1688, England put in place a system of public credit founded on the authority of Parliament, which votes the taxes intended to service the debt, and on the Bank of England, which manages part of the borrowing.¹ This system inspires growing confidence among European investors, who agree to lend to Great Britain at rates lower than those demanded of France.

Genevan investors gain access to the English funds through bankers established in London, often themselves of Huguenot or Genevan origin, and through Dutch houses. They buy shares in the Bank of England and the East India Company and, later, securities of the consolidated debt, the "consols", which in the middle of the eighteenth century become one of the principal investment instruments in Europe.²

Great Britain, too, had its speculative crisis. The South Sea Bubble, contemporaneous with Law's System, caused considerable losses in 1720.³ But the British system survived this crisis and consolidated itself, whereas the French system remained fragile. This difference in trajectory is due in large part to institutions: the parliamentary guarantee gave the creditors of the British state an assurance that the French absolute monarchy could not offer.

For the Genevans, the English funds offer a lower return than French annuities, but greater security. The most prudent capitalists place part of their fortune in them in order to diversify their risks. This diversification will prove invaluable when the Revolution strikes the creditors of France. The families that had spread their assets between Paris, London and Amsterdam withstood the shock better than those that had staked everything on French debt.

The comparison between France and Great Britain has nourished an abundant economic literature on the link between political institutions and public credit.⁴ The investors of the eighteenth century had a practical intuition of it: a state whose government is limited by a parliament and whose financial commitments are guaranteed by a credible institution borrows on better terms. The lesson remains topical. The yield spreads between sovereign debts still reflect, in part, the perceived quality of the institutions of the borrowing states.

Worked example. A Genevan capitalist places 50,000 livres in French annuities at 5 per cent and 50,000 livres in English funds yielding the equivalent of 3.5 per cent. His annual income amounts to 4,250 livres. If France reduces the value of its commitments by two thirds, the French part of his portfolio is worth only 16,667 livres, and his total capital falls to 66,667 livres, a loss of one third. A capitalist who had placed everything in French annuities would have lost two thirds of his fortune. The figures are fictitious and simplified.

1 Notes

1. Wikipedia (en), “Bank of England”: royal charter of 27 July 1694 (Tonnage Act); loan of £1.2 million to the government, serviced at 8 per cent per annum plus £4,000 in fees, subscribed in twelve days by 1,268 persons; context of the War of the League of Augsburg after the naval defeat of Beachy Head (1690) and of the government’s weak credit. ↩
2. Wikipedia (en), “Consol (bond)”: first consols issued in 1751; in 1752 the Chancellor of the Exchequer Henry Pelham converted the redeemable loans into a single security, the Consolidated 3½ % Annuities; the last consols were redeemed between February and July 2015. ↩
3. Wikipedia (en), “South Sea Company”: company created in 1711 to consolidate the public debt; debt conversion scheme presented in January 1720; share price rising from £128 in January to 175 in February, 330 in March, 550 at the end of May and about £1,000 at the beginning of August 1720, before falling back to £100 before the end of the year; Bubble Act (June 1720); Walpole had on average 82 per cent of the directors’ fortunes confiscated. ↩

4. Douglass C. North and Barry R. Weingast, “Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England”, *Journal of Economic History*, vol. 49, no. 4, December 1989, pp. 803–832: “the new institutions allowed the government to credibly commit to upholding property rights. The success of the originators of the Revolution is nothing short of remarkable, as the evidence from capital markets shows”. ↩

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