

ON  
COMMERCIAL PANICS :

A P A P E R

READ BEFORE

THE DUBLIN STATISTICAL SOCIETY :

BY

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DUBLIN :

PUBLISHED FOR THE SOCIETY, BY HODGES AND SMITH,  
104, GRAFTON STREET.

1848.

# DUBLIN STATISTICAL SOCIETY.

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THIS society was established in November, 1847, for the purpose of promoting the study of Statistical and Economical Science. The meetings are held on the third Monday in each month, from November till June, inclusive, at 8, P. M. The business is transacted by members reading written communications on subjects of Statistical and Economical Science. No communication is read unless two members of the council certify that they consider it accordant with the rules and objects of the society. The reading of each paper, unless by express permission of the council previously obtained, is limited to half an hour.

Applications for leave to read papers should be made to the secretaries at least a *week* previous to the meeting.

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The subscription to the society is one pound entrance, and *ten shillings* per annum.

*On Commercial Panics.* By James A. Lawson, LL.B.

Amongst the many subjects of inquiry which present themselves in the wide field of Statistics, there is none, I think, more calculated to excite our interest, than the one which I am about to bring under the consideration of the Society, and which is so well known in the mercantile world under the name of Commercial Panic or Crisis. If it be difficult to ascertain the laws which regulate commercial matters under ordinary circumstances, surely the extraordinary or anomalous ones challenge our most careful consideration. Indolence and ignorance may, and indeed do, evade such inquiries altogether, by adopting the short and easy solution of saying that this is an extraordinary case, and not to be determined by ordinary rules; and thus we are taught that, though in ordinary circumstances we are to apply the results of our previous knowledge, yet when anything unusual occurs—that being the very time when we most urgently require guidance and assistance from settled principles—we are to throw aside all that we have learned, and either abandon the cure in despair, leaving all to chance; or become empirics for that occasion, and adopt a course which our previous experience altogether condemns. Thus, during the distress of the two last years, it was very common to say, “Oh, these are extraordinary times; we cannot apply the rules of Political Economy to them.” These persons thus readily cut the knot which they cannot disentangle, though, indeed, they say:—

“Nec Deus intersit, nisi dignus vindice nodus  
Inciderit.”

I need not dwell on the fallacy of such reasoning. If we have any faith in the truth or certainty of science, we must feel fully persuaded that the truths are of universal application; that they cannot be true at one moment and false at the next; that they are not to be taken up in smooth seasons, and laid aside in rough ones. It is when the storm rages highest that the mariner needs to put forth his utmost skill, and bring forth the fruits of his long training; it is at such junctures that superior skill has the opportunity and the power of displaying itself; and let me observe that they, and they only, will know how to guide us in the extraordinary state, who have made the ordinary state their study; as the physician can best meet and cope with disease, who is most intimately acquainted with the structure and functions of the healthy subject.

Commercial panics, then, are diseases to which the body politic is subject—not chronic diseases, but epidemics as regular in their recurrence as influenza itself, though at longer intervals. The existence of these and other evils incident to the body politic, has been one of the most powerful means of drawing attention to Political Economy, just as human ailments called medicine into existence: as long as the natural functions go on with their usual regularity, either in the individual or social state, there is not much to attract attention to the laws which govern them; thus we ate, and drank, and breathed, without knowing anything of our heart, lungs, or other organs, until some injury or derangement took place, and directed our attention to them; and so we produced, consumed, and distributed wealth, and coined money, and bought and sold, without knowing that there were any principles or laws which regulated operations apparently so simple, until some interference either from government or ourselves deranged the usual course of things, and set the mind of man upon inquiry; so apt are we to be anxious about matters of comparatively remote concern, and to remain contentedly ignorant of what is nearest home.

I shall now briefly call your attention to some leading facts connected with Commercial Panics, and make some suggestions as to their causes and proposed remedies. I observe, in the first place, that these are diseases which exhibit themselves only in a very civilized state of society, where trade and commerce flourish, where there is commercial enterprise and spirit; they occur in England, France, Holland, and the United States of America; but I do not find any account of such in Spain or Portugal. If we look at the modern history of England, we shall find these periods of commercial distress regularly and periodically recurring in cycles of from five to seven years. I now call your attention to the facts connected with some of them, because it will show that similar symptoms have always preceded and accompanied these periods of depression and panic.

The earliest to which I shall advert took place in 1793. In that year we find great commercial discredit, and many failures—especially amongst country bankers. It had been preceded, as Mr. Tooke observes, and as we shall find in almost all similar cases, by a great extension of the system of credit and paper circulation; not only in the internal trade and banking of the country, but in the commercial transactions of the principal cities of the continent of Europe, and in the United States of America. We find also a great fall in prices to have taken place in 1792 and 1793 (a remarkable contrast with a rise of prices for two or three years before), in consequence of speculations, produced partly by paper circulation, and partly by an apprehended scarcity of some staple articles; and, superadded to all these, we have the breaking out of the war in 1793, which was the proximate cause of the pressure.

The next remarkable period of commercial distress occurred in 1809–10, and we shall see that it was preceded by similar circum-

stances. In consequence of our exclusion from intercourse with nearly all Europe, there was a prospect of a scarcity of most articles, which gave rise to a spirit of speculation, and a great advance of prices took place: for instance, hemp advanced within a short time from £58 to £118 per ton; flax from £68 to £142 per ton; wool from 6s. to 26s. per lb. There was also a new market opened for our exports, namely Brazil, and it was supplied with articles of a most extravagant and unsuitable kind. We also find that this was a favourable period for new projects in shares, so that in one year forty-two public companies were set on foot, with a capital of many millions. I will not attempt to enumerate them, but amongst them I find a United Public Dairy for the sale of Milk, and a new Medical Laboratory for the sale of genuine medicines, with a capital of £50,000; and during all this period the amount of the circulation was moderate and equable. In 1809 the depression commenced. Prices became ruinously low, and failures of half the traders in the kingdom followed. In one month there were 273 bankruptcies. In 1811 trade became brisk again, and from 1814 to 1816 commercial distress again prevailed. I find the number of bankruptcies to have been—

In 1809	...	...	..	...	1,089
1810	...	...	...	...	2,314
1811	...	...	...	...	2,500

We now come to the mercantile panic of 1825. Towards the close of the year 1824 it was observed that the rate of consumption of some of the leading articles was outrunning the supply—and thus an incentive was afforded to the spirit of speculation. Cotton, silk, wool, flax became the subjects of speculation, and the price advanced beyond all reasonable bounds. Coffee, though the stock was increased compared with former years, advanced 70 to 80 per cent., and spices in some instances 100 to 200 per cent.: in fact, there was scarcely any article of merchandise which did not participate in the general rise—every one bought; speculations in foreign loans and shares took place to an extent never before known; joint-stock companies were formed for every conceivable project; three companies were formed for working the Mexican mines, and similar companies for working the mines of Chili, Brazil, Peru, and the provinces of the Rio de la Plata, and for prosecuting the pearl fishery on the coast of Columbia. In the month of March, 1825, thirty bills were brought before the House of Commons for establishing companies. A writer of the day describes the mania in words which might be stereotyped as applicable to all similar occasions—“In all these speculations, only a small instalment, seldom exceeding 5 per cent. was paid at first, so that a very moderate rise in the prices of the shares produced a large profit on the sum actually invested. This possibility of enormous profit, by risking a small sum, was a bait too tempting to be resisted; all the gambling propensities of human nature

were constantly solicited into action ; and crowds of individuals of every description—the credulous and the suspicious, the crafty and the bold, the raw and the experienced, the intelligent and the ignorant, princes, nobles, politicians, placemen, patriots, lawyers, physicians, divines, philosophers, poets, intermingled with women of all ranks and degrees, spinsters, wives, and widows, hastened to venture some of their property in schemes of which scarcely anything was known but the name.” Commercial discredit and pressure followed in the month of December, 1825, to an extent never known up to that time. Five London and seventy country banks stopped payment. It became impossible to raise money upon any security ; and the mercantile embarrassments began to display themselves shortly after the failure of the banks. I should only weary you were I to specify the other instances of commercial panic from that time down to the memorable one of the last year, recurring as they did at intervals of from five to seven years. Suffice it to say, that all will be found to possess the same features, and to have been preceded by similar events.

Now what strikes one in looking at all these panics is this, that the circumstance which immediately gave rise to the pressure is always wholly inadequate to account for its long continuance, and for the loss sustained by it. For instance, the breaking out of the war in 1793 never could of itself have occasioned much commercial embarrassment, if commercial affairs had been in a sound state up to that time ; it might have limited the future operations of trade, or checked its advance, but it could not have entailed the universal ruin which ensued. In like manner, the fall of the prices of leading articles, which immediately preceded the panic of 1809, never alone could have caused it : nor could the circumstance of a deficient harvest alone ; that would generally only entail a loss of one or two millions : but where the panic takes place, failures to many times more than that amount ensue ; for instance, the general deficiency of food in 1846 never could of itself have occasioned the panic which ensued. We must, therefore, look beyond the proximate cause or the occasion of the panic to find its true cause ; and I think from the details I have given, you will be prepared to anticipate the conclusion to which I have arrived—namely, that it is to be attributed to *a sudden check given to an extensive and long continued trading upon credit*. This check may proceed from any of the various causes which, we have seen, gave occasion to the panic, or by any other circumstances which cause a revulsion in the public mind, or cause a disinclination to continue to give credit ; and it will be found that when this system of trading on credit has been extensively pursued, a very slight obstacle is sufficient to overturn the entire system.

Let us see, now, how this system of trading on credit is carried on, and how it accounts for these disastrous reverses in the commercial world. If there were no credit, the transactions of a country would be strictly limited by the amount of its capital, just

as the purchases of an individual who had no credit would be by the quantity of money he had ; and if we follow out this comparison between the individual and the whole mercantile community, we shall find that it throws light upon the subject. The individual case is generally easy of solution, and yet that of the community is only an agglomeration of individual results. If an individual deals on credit, it is obvious that he cannot go on for any time incurring liabilities beyond the amount of his annual income, without ruin. Suppose he merely anticipates his yearly income, and does not spend at a greater rate, the only result is, that his creditors are kept out of their money for a year ; but if he goes beyond this, he must ultimately break down : this is the limit in the case of unproductive expenditure. But it is very different if the money obtained on credit is employed productively ; he may then borrow to any amount that he can procure ; and if his speculations turn out to be successful, he will be able to repay his creditors, and have a profit, and this is *trading upon credit*. A man who has no capital is able, we will say, to get credit for £10,000 for six months or a year ; with it he buys cotton ; if the market is a rising one, he is sure to be able to re-sell it at a profit, and thus meet his engagement at the end of six or twelve months ; and if he is able to turn the money two or three times within that period, his profits will be doubled or trebled. On the contrary, if he has miscalculated, and the market turns against him, the speculation fails, and his creditor loses, he himself having nothing to lose. Now, this is always carried on to a great extent, not by persons having no capital, as I have supposed, but by capitalists trading beyond their capital. They find no difficulty in doing this, but, on the contrary, great facility and a constant temptation to do so. The money market is easy ; a merchant with a large capital then finds it easy to get discount ; no one knows whether his trading is speculative or not, and he is constantly in the way of seeing opportunities for a profitable speculation, which he is not able to resist. The probability therefore is, that almost every merchant, under ordinary circumstances, trades somewhat beyond his capital. To what an extent, and for what time, a person with good credit may carry on trade, though actually possessing no capital, nor assets enough to meet his liabilities, has been shewn by an exposure of the affairs of many mercantile houses of high repute ; and even to banks, after their failure, we find appended this note, ‘ Has been insolvent for many years.’\* Now, if there be such a tendency to trading on credit under ordinary circumstances, what must it be when the spirit of speculation is afloat. When the prices begin to rise under its influence, the early purchasers are sure to realise a profit ; they sell to another who sells again, producing additional rise of price ; and so the torch, passed from hand to hand, is sure to burn the last holder. This spirit of speculation

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\* See Sir Robert Peel's Speeches on the Currency, p. 73.

soon extends itself to every species of commodity ; and as if nature did not produce food enough for the supply of the gambling mania, new commodities are invented for trafficking in, denominated shares in companies ; and this draws into its vortex, not the mercantile classes merely, but all those of every class who have either money or credit. When this system of fictitious trading has been extensively carried on, we can appreciate the results of any check to it ; a general rise of price has been produced, affecting the *bonâ fide* dealer ; the shares and other articles purchased, as soon as the bubble bursts, become utterly worthless, and the capital which has been advanced upon them is lost ; goods fall so rapidly in price, that they are unsaleable save at a ruinous sacrifice, and credit receives such a shock that no man trusts his neighbour. Even the least speculative houses are liable to be involved in the common calamity, because they have bills with the names of parties on them who have failed. The consignment of goods, on the faith of which they have accepted bills in the usual course of business, fails to realize the freight and charges ; and they cannot procure the discount of *bonâ fide* bills except at a ruinous rate of interest. Thus, the ramifications of mercantile dealings are so great, and the credit of houses so much depending on each other, that if one suffers, the shock is felt by many ; while those whose trading has been fictitious at once fall to the ground, just as in a house of cards, if one is removed, all the rest tumble. Thus it is that a loss, in itself insignificant, when it supervenes upon overtrading and speculation, produces failures to an enormous amount. The last panic, which followed upon the failure of the potato crop, and of food generally, and was ushered in by a railroad mania, was occasioned by a loss more extensive than any other of which we have a record ; but the amount of the failures far exceeded even that loss, while the loss itself was not represented by those failures, but was sustained by the non-trading public in their diminished consumption of food and every other article.

Such I conceive to be the true explanation of the periodically recurring calamities which visit our mercantile world ; and we find here something like the law in physics, that "action and reaction are equal and in opposite directions."

The subject of commercial distress is so generally connected in men's minds with the Currency, that I cannot conclude without saying a few words with respect to the theory, that it is caused by a defect in the currency system, and by the want of liberality in the banks in not giving discounts. If our circulating medium were purely metallic, the commercial transactions of the country would be nearly limited by its capital ; it is true that credit might be obtained by bills of exchange ; but unless there were the facility of getting these bills discounted—that is, of getting notes that would circulate for them, it would check operations very much ; but when there is a paper currency, the bank can discount these bills and issue their notes, which gives a great assistance to credit ; now



in the period of speculation antecedent to the panic, credit is high, the value of money is low, and discount is procured on ready terms; and this gives the means of carrying on the speculations, because, as long as trade is in that state, the notes will not be returned to the bank for gold. As soon, however, as the reaction comes, the bank must begin to protect itself, for a drain of bullion will immediately take place, to meet foreign and other engagements; the bank must, therefore, raise its rate of discount, or all its gold will be drained away; because there is a general fall in the value of all commodities except gold; every thing else is unsaleable, and therefore the gold will go out. Now, this operation of raising the rate of discount on all bills, and declining to discount many, is what is called "putting on the screw," and the distress is often attributed to this very harsh and unnecessary proceeding; but it is, in truth, a measure of necessity, as long as the bank is bound to give gold for their notes; and it is rendered necessary by the previous liberality or imprudence of the bank in discounting too largely. It is said that it is a pity that the bank should be tied down by this inconvenient restriction of paying in gold; in other words, that any limit should be put to these speculations. Now let us see what effect the removal of the convertibility of the notes would have upon speculation, and whether such a result is desirable. There would then be no motive of prudence to check these speculations on the part of the merchant, or to limit the discounts on the part of the bank; and a redundant issue of paper, and consequent depreciation would be the consequence; so that the merchant who had entered into these engagements would be able to discharge them in the depreciated currency, and all the creditors in the country and all the non-productive classes would be losers to the extent of that depreciation; and, therefore, what is sought by the merchant when he requires the rule to be relaxed, which requires the bank to give gold for its notes on demand, is, to make the public partners in the losses that may result from his speculation, although they derive, and can derive no gain from them. For I assert that the public derives no benefit from speculative trading; the speculator does not call any new capital into existence, but merely borrows some of that already existing, and applies it in purchasing what he thinks will rise in price; if the price does rise, the public lose by having to pay the higher price, if the price has been raised by this speculative dealing; if the price falls, the public do not lose, only the person who has given the speculator credit. In all these cases, the capital was in existence before, and we have every reason to think it would have been applied as much for the public benefit by the persons who had it, as by the speculator who has borrowed it. We have seen what disasters this spirit of speculation entails without conferring any solid advantage, and yet these men claim the credit of being public benefactors, and ask the public to become sharers in their losses; but they have no more right to the name, than those individuals, who deal on

credit, have to be considered patrons of the tradesmen or manufacturers, whose goods they condescend to take without paying for them. Credit to a moderate extent is good, but speculative dealing is not to be encouraged; and those who embark in it must expect to meet the usual reverse which attends those whose expenditure exceeds their income.