Investment Banking History

National and Comparative Issues (19th-21st centuries)

Hubert Bonin & Carlo Brambilla (eds.)

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The recent financial and banking crisis revealed a discrepancy between internal management rules and the demand for stability within the divisions of corporate and investment banking in universal banks or within pure investment banks. Their mastership of risks did not balance the variety and breadth of their operations, at the expense of transparent and well-structured balance sheets.

This book intends to fuel comparisons between historical national case studies and present the evolution of investment banking. It will foster arguments about the management of risks, investment bankers' portfolios of skills and the role of senior bankers. Two chapters concerning issues and presenting assessments will help make sense of banking history through the mobilisation of concepts spanning decades until the present day. It will engender deeper thinking about the very nature and good practices of investment banking.

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P.I.E. Peter Lang
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Part I

Introductive Issues

Chapter 1

Varieties in Investment Banking Evolutions and Functions

Hubert Bonin & Carlo Brambilla

Our book is the concrete expression of issues raised during a session on investment banking history held in Utrecht in August 2009 at the congress of the World Economic History Association; but it prolonged a middle-term research programme which Hubert Bonin, Carlo Brambilla and Giandomenico Piluso had set up as soon as a Ebha (European Business History Association) congress in Copenhagen (2007) and developed afterwards (Geneva: 2007; Bergen: 2008). Since then, our informal academic "club" deepened its analysis and moreover; it could confront its analysis about the past to the arguments among academics fuelled by the present crisis, where investment banks were suspected to play altogether as triggers to the krash (Bear Stearns, Lehman Brothers) and the greedy sharks swallowing the fundamentals of capitalism and even market economy. But the final version of the collective process which gave birth to this book was completed under the Franco-Italian guidance of professors Bonin and Brambilla.

1. Varieties of investment banking: How to unify our prospects?

Sure, one might pretend that everything has already been told about investment banking history, models, strategy, and even prospects… A few books brought rich materials and arguments to this topics, line those of Vincent Carosso, in his time one of the founders of such investigations about US investment banks (1970),[1] Samuel Hayes and Philip Hubbard

[1] Vincent Carosso, *Investment Banking in America: A History*, Cambridge, Mass., Harvard University Press, 1970. Also see: Vincent Carosso, *More than a Century of Investment Banking: the Kidder, Peabody & Co. Story*, New York, McGraw Hill, 1979. Vincent Carosso, *The Morgan's: Private International Bankers, 1854-1913*, Cambridge, Mass., Harvard University Press, 1987.

(1990),[2] Alan Morrison and William Wilhelm, a perfect handbook (2007),[3] like that of Richard Roberts (1988).[4] Anyway, banking and business historians can enrich the analysis of banking and economic experts, of researchers in banking and finance management, because they confront archives recently scrutinised – thus renewing somewhat narrative history – with the business models and the evolution of the finance system. Throughout the process of maturing our programme, we could observe once again the extreme variety of investment banking and the adaptive character of strategies carried out by financial actors in relation to widely different contexts, circumstances and institutional frameworks. Our debate has shown that it is hard to rely upon a too strict definition of investment banking and that the sector is susceptible to changes stemming out both from autonomous strategies and external regulation or interventions. Moreover, economic historians are aware that, as a matter of fact, investment banking ever modified its characters, profiles, and rules over time as well as it differs, say, between the US and Europe, advanced economies and "followers", core countries and peripheries or emerging markets. The emphasis on the variety of business models and practices – *in lieu* of the idea of the "one best way" or model – is probably the main point of our specific contribution to the comprehension of the evolution of this peculiar industry, from which all major financial innovations have often spun off. And we know that such variety has even fostered arguments about the very vocabulary used to nominate and define investment banks[5]…

Our attention to regulation, national contexts and peripheral or emerging markets thus tries to add to the analysis of investment banking and its main tendencies in history.

To put it in a nutshell, we think that the very core of this book is the extreme variety of investment banking and the adaptive character of strategies carried out by financial actors in relation to widely different contexts

2 Samuel L. Hayes & Philip M. Hubbard, *Investment Banking: A Tale of Three Cities*, Boston, Harvard Business School Press, 1990. Also see: Samuel Hayes, "Investment banking: Power structure in flux", *Harvard Business Review*, No. 49, 2, 1971, pp. 136-152. Samuel Hayes, "The transformation of investment banking", *Harvard Business Review*, No. 57, 1, 1979, pp. 153-170. Samuel Hayes, A. Michaël Spence & David van Praag Marks, *Competition in the Investment Banking Industry*, Boston, Harvard University Press, 1983.

3 Alan Morrison & William Wilhelm, *Investment Banking. Institutions, Politics and Law*, Oxford, Oxford University Press, 2007.

4 Richard Roberts, *Inside International Finance*, London, Orion Business Books, 1998 [Chapter 3: "International commercial banking (pp. 46-56); chapter 4: "Global investment banking" (pp. 57-79)]. Also see: Richard Roberts (ed.), *International Financial Centres: Concepts, Development and Dynamics*, Aldershot, Edward Elgar, 1994.

5 Richard Roberts, "What's in a name? Merchants, merchant bankers, accepting houses, issuing houses, industrial bankers and investment bankers", *Business History*, 35/3, 1993, pp. 22-38.

and circumstances. The underlying evolutionary approach will help us putting together all various chapters and cases in a coherent frame. As we all know, investment banking took the stage during the last years of financial turmoil, raising worries and being blamed for the part it took in the crisis. Many voices have been calling for a tougher regulation of this segment of the financial industry, though, more recently, others have been arguing for lower controls and supervision, especially major investment banks, which claimed for their peculiar functions and specific status.

Investment banks are today in the eye of a storm, of an extensive and devastating crisis. They had huge responsibilities in igniting it, and a part of the public opinion blames them for the derailment of the world economy from "Main Street toward Wall Street", and for all the consequences such a turn has had. Some of them, such as Bear Stearns and Lehman Brothers,[6] paid a steep price for it, though nothing compared to the huge costs the crisis imposed to so many countries. This notwithstanding, nothing of what happened in the last few years was implicit in their very original nature, in intrinsically distorted mechanisms of management of a risky business. The choice of many investment banks to venture in highly risky operations is due to the historical evolution of the banking industry as a whole and to relevant institutional changes, that can be understood in the light of the historical evolution of the industry during the last thirty or forty years. The current crisis has been ascribed to the greedy sharks swallowing the fundamentals of capitalism and even of the market economy. Nonetheless, we think a better explanation lies in structural and operational changes in the financial industry that increasingly weakened global capitalism because they did not provide for protection nets and disincentives to adopt hazardous behaviours and to build major conflicts of interests, finally resulting in huge information asymmetries.

Here we would emphasise two main aspects that we consider particularly relevant in the understanding of the past and, in its light, of the present, too. They indeed emerge more or less explicitly in all the contributions to the book, and seem to have had an important role in shaping the peculiar evolutions of investment banking in the various contexts. The first one is regulation, also meant as the interaction between banks and non-bank institutions and the financial markets. The second one is the deeper and deeper chasm that might divide the "real" from the "financial" economy. The processes of steep "financialisation" of the economy can lead to the accumulation of distortions in the propensity to invest, shorten the investors' time horizon, and subvert the "natural" and sound

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6 Alan Greenberg (with Mark Singer), *The Rise and Fall of Bear Stearns*, New York, Simon & Schuster, 2010. Peter Chapman, *Lehman Brothers, 1844-2008. The Last of the Imperious Rich*, New York, Portfolio Penguin, 2010.

hierarchy of the industrial and financial capital yields, and the prospects of the programmes of investments into manufacturing or services infrastructures. Investment banks place themselves on the faulty lines, they can contribute to stitch up as well as they can widen the divide between the two worlds. The history of finance of modern industrial capitalism shows alternate phases of conjunction and disjunction.

Investment banks do have some common features: they have usually enjoyed wide degrees of freedom in their activities, wider than those granted to banks; the long-lived ones were founded by merchant-bankers at the end of the 19th century, or even before, and they kept many of their original characters over time, in particular their specialisation in activities such as corporate finance,[7] corporate control, originating, issuing, underwriting and trading financial assets, etc.; they have seldom entered the business of deposit taking; they have often been protagonists in promoting financial innovations connected with market activities, a role that became progressively more relevant since banks had been excluded from regularly and massively operating on the stock exchanges, or in those countries where the universal bank had been banned.

These being the scope and framework "defining" investment banks, their evolutionary paths show an increasing variety of patterns over time and places, that further deepened differences among national cases. Why was that? Some hypothesis can be suggested, in the light of the chapters contributing to this book. Investment banks playing a growing role in granting highly specialised services and funds to industrial companies were confined to some countries, where a few but relevant institutional conditions were present: financial markets were able to grow bigger and deeper, not being constrained by strict regulation on monetary fluxes; state bonds did not have relevant effects of crowding out; markets for corporate control were relatively open and contestable, transparency and publicity of information relatively high.

In the last decades of the 20th century many things have changed. The demise of the Bretton Woods' system put an end to the long run stability of the monetary variables resulting in the diffusion and increase of risks, both on credit activities and on financial trading operations. The necessity to handle higher risks fostered financial innovation aimed at securing against them, and triggered an increase in the volume of hedging operations that eventually had the effect of boosting risk. The development of the markets for future contracts and other derivatives resulted in an opportunity of growth for investment banks and other similar financial intermediaries. Deregulation then was a further

7 See Jonathan Barron Baskin, *A History of Corporate Finance*, Cambridge, Cambridge University Press, 1997, 1999 & 2003.

incentive to the growth of this kind of activities and services. More recently in some countries, especially in the US, investment banks transformed into big corporations, characterised by large dimension in terms of capital, asset volumes, number of employees, scope: many among them became multi-business firms and global players. The variety of 'flavours' of investment bankers, the differences in the craft are grown further.

2. Investment banking as leverage to financing firms

One of the most important differences among financial systems is probably the way by which firms' extraordinary financial operations are organised and realised. In this respect, as recent literature points out, financial systems are relevant in order to shaping, at least to some extent, various corporate governance national models.[8] Above all, firms need financial intermediaries during the most difficult phases of discontinuity in their life cycle, such as crisis, merger and acquisitions, changes affecting their major shareholders or management, active or passive takeovers, critical readjustment processes to contrast dramatic environmental changes (for example, typically, technological/product or market changes).[9] Under these circumstances, financial intermediaries enable firms to overcome such a difficult phases assuring them long term resources and stability, both in their capital structure and management. These functions are generally exerted by financial institutions whose main characteristics can vary according to the specific functional and regulatory structures of the national systems.[10] From this point of view, it does not matter whether the financial system is a market oriented or a bank oriented one: Market and bank oriented financial systems[11] have broadly the same functions, even if they act very differently and, indeed, they reach non homogenous degrees of success in providing resources to the economy, both to micro- and to macro-levels. Even though along

8 See Asli Demurgiuç-Kunt and Ross Levine (eds.), *Financial Structure and Economic Growth. A Cross Country Comparison of Banks, Markets, and Development*, Cambridge (Mass.), Mit Press, 2000. Franklin Allen and Douglas Gale, *Comparing Financial Systems*, Cambridge (Mass.), Mit Press, 2000.

9 See Mary O'Sullivan, "Finance and Innovation", in Jan Fagerberg, David Mowery and Richard Nelson (eds.), *The Oxford Handbook of Innovation*, Oxford, Oxford University Press, 2005.

10 See Bernard Amable, *The Diversity of Modern Capitalism*, Oxford, Oxford University Press, 2003.

11 See Daniel Verdier, *Moving Money. Banking and Finance in the Industrialized World*, Cambridge, Cambridge University Press, 2002. Douglas Forsyth & Daniel Verdier (eds.), *The Origins of National Financial Systems. Alexander Gerschenkron reconsidered*, London, Routledge, 2003.

different ways and methods, both these systems need special intermediaries for attaining a more efficient functioning of markets and firms.[12]

Probably, it is possible to attribute a part of responsibility to the financial system which has not been able to provide resources to new firms and emerging technologies. The relationship bias implicit in the merchant banking activities in Continental Europe has had some role in rationing credit to emerging entrepreneurs and sectors: indeed, a sharp contrast with the Schumpeterian attitude supposed to be the cornerstone of the banking activities.[13] During the 1950s and the early 1960s large industrial firms could finance medium and long-term investments essentially by self financing or, especially in Italy, through the domestic bonds market. From the late 1960s, instead, large firms needed more external financial support and French and Italian banking systems became to diverge: the first one modified its regulatory architecture in 1965, with a new banking law which allowed universal banks to operate, even if *banques d'affaires* – such as the most prestigious Lazard, Paribas or Indosuez – continued to exert their role. The second one did not modify its fundamental banking law and long term finance was exclusively committed to the so-called "*istituti di credito speciale*", such as *Istituto Mobiliare Italiano* (IMI) and Mediobanca, a well international linked institution and probably the only real merchant bank in Italy. Due to the lack of an effective market for corporate control, supporting firms' long-term growth and dynamic efficiency was assured by these merchant banking institutions, through issuing bonds or equity capital, providing advisory assistance in merger and acquisition, consulting for long term strategic alliances (both for financial or production and technological goals), assuring ownership or management turn over *vis-à-vis* firms' difficulties or crisis.

3. Specialisation vs. despecialisation

Traditional banking activity, that performed by merchant-bankers between the 18th century and the beginning of the 19th century, is basically un unspecialised activity in the sense that every banker would enter any financial business he is able to, unless he finds a comparative advantage in specialisation (e.g. in financing international trade, or in issuing activities), or he is constrained by institutional or consuetudinary restrictions,

12 As stated in Franklin Allen and Douglas Gale, *Comparing Financial Systems*, *op. cit.* This does not mean, of course, that every firm or sector need in the same measure external finance for growing, as underlined by Raghuram Rajan and Luigi Zingales, "Financial Dependence and Growth", *American Economic Review*, Vol. 88, 1998, No. 3, pp. 559-586.

13 Carlota Perez, *Technological Revolutions and Financial Capital*, Cheltenham, Elgar, 2002.

or finally by regulation. The institutionalisation of banking that took place around the mid-19th century, known as 'financial revolution' made some of those bankers gradually leave the old business to become promoters of new banks in the form of joint-stock companies, gathering deposits, mobilising them and lending on large scale. From then on, others further specialised their competences and skills to become 'pure' financiers.

These banking intermediaries had their particular traditions and features. They evolved over time according to practices, scope, and techniques in the United States, in Great Britain and in Continental Europe. The range of functions has been historically exerted by New York "investment banks" in United States, London "merchant banks" in Great Britain[14] and "*banques d'affaires*" in France, while in the rest of Continental Europe had been generally attributed to universal banks – even if some *Privat Banken* did assume activities in investment banking (Oppenheim, Bleichröder, Warburg, etc.).

It is worthy to observe that, nevertheless, the role played by these institutions in the international markets – in order to finance international trade, underwriting foreign and domestic public debts, organising syndicates for equity issuing or structured financing, etc. – induced the formation, so to speak, of a common stock of knowledge and the sharing of similar practices and techniques.

Moreover, this process of sharing worldwide instruments and techniques had naturally been enhanced by the cosmopolite character of the investment and merchant bankers.[15] It may be enough to remember, for example, that a German merchant banker, Paul Warburg, was the real promoter of the Federal Reserve after the 1907 crisis and of the Glass-Steagall Act during the Great Depression,[16] or similarly, after the second world war, that a French banker, André Meyer, was a prominent figure of the New York scene[17] until the 1970s and almost in the same period a German banker, Sigmund Warburg, was a leading

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14 Joseph Wechsberg, *The Merchant Bankers*, New York, Pocket Books, 1986. Bo Bramsen & Kathleen Wain, *The Hambros, 1779-1979*, London, 1979. Stanley Chapman, *The Rise of Merchant Banking*, London, 1984. Kathleen Burk, *Morgan Grenfell, 1838-1988. The Biography of a Merchant Bank*, Oxford University Press, 1989-1990. Richard Roberts, *Schroders. Merchant and Bankers*, London, MacMillan, 1992. Jehanne Wake, *Kleinwort Benson. The History of Two Families in Banking*, Oxford University Press, 1997. Niall Ferguson, *The World's Banker. The History of the House of Rothschild*, London, Weidenfeld & Nicolson, 1998. Niall Ferguson, *The House of Rothschild. Money's Prophets, 1798-1848*, London & New York, Penguin Books, 1998.

15 Youssef Cassis, *La City de Londres, 1870-1914*, Paris, Belin, 1987. Youssef Cassis, *Les banquiers de la City à l'époque édouardienne, 1890-1914*, Geneva, Droz, 1984.

16 See Ron Chernow, *The Warburgs*, New York, Random House, 1993.

17 See Cary Reich, *Financier. The Biography of André Meyer*, New York, Wiley and Sons, 1983.

and innovative London banker.[18] A number of investment and merchant banks have had a typical transnational origin, structure and history: the Rothschilds had a five-countries structure from the early 19th century, being present in Frankfurt, Vienna, Paris, London and Naples; the Morgans operated on the two sides of the Atlantic with JP Morgan in New York and Morgan Grenfell in London; similarly, the Lazards were established in New York, Paris and London; the Warburgs were based in Hamburg but had strong personal links with the Kuhn Loeb of New York and, after the Second World War, SG Warburg became a brilliant operator in London; from the beginnings Paribas used three bases in Paris, Amsterdam and Brussels.[19]

Investment and merchant banks were generally independent intermediaries in financial systems in which a credit specialisation principle is affirmed. Otherwise, universal or mixed banks played more or less the same role *vis-à-vis* financed firms by relating to them along side the position of a "*Hausbank*", according to a scheme of long term inside relations: according to some scholars, this kind of scheme was more effective in promoting the long run growth of industrial firms through a better screening and monitoring of the borrowers.[20] Our study therefore determines why and how these networks of relationship were more developed and active by the investment banks than by the commercial banks, why they were more able to confront the asymetry of information about projects requiring huge amount of middle and long term money, although the commercial banks did practice "industrial finance", e.g. intensified their relations with a core of key entreprise clients and accompanied them on the long run for their banking and financial needs. Why did the process of "specialisation"[21] take shape in several countries on several periods and led to a somewhat binary[22] division of tasks within the banking system?

18 Jacques Attali, *Sir Siegmund Warburg, 1902-1982. Un homme d'influence*, Paris, Fayard, 1985. Niall Ferguson, *High Financier: The Lives and Time of Siegmund Warburg*, London, 2010.

19 Éric Bussière, *Paribas, l'Europe et le monde, 1872-1992*, Anvers, Fonds Mercator, 1992.

20 Charles W. Calomiris, "The Costs of Rejecting Universal Banking: American Finance in the German Mirror, 1870-1914", in Naomi Lamoreaux & Daniel Raff (eds.), *Coordination and Information: Historical perspectives on the Organization of Enterprise*, Chicago, University of Chicago Press, 1995, pp. 257-315.

21 See Maurice Lévy-Leboyer, "La spécialisation des établissements bancaires", in Fernand Braudel & Ernest Labrousse (eds.), *Histoire économique et sociale de la France*, Paris, Puf, III, first volume, 1976.

22 If we don't consider local banks (saving banks, cooperative banks, petty family banking), which constituted everywhere a third (and influent) sector of the banking system.

For instance in Britain, commercial banks[23] enlivened their own deposit banking activities instead of competing directly with merchant banks. Even in West-Germany, the decline of the *Privat Banken* in the first third of the 20th century[24] was followed in the 1950s-1970s by the emergence of mixed banking[25] with a large part dedicated to "*banque d'affaires à la française*", that is a mixture of commercial banking and investment banking – even with actual proprietary investments in the equity of large customers.[26]

Our chapters achieved thus some kind of a process of "disaggregation" of investment banks' portfolio of skills in order to gauge their key specialties. Using present models of analysis of banking activities, we determine how much difference appeared in the past between investment banks and commercial banks, what was the degree of specialisation for each key sector of activity. Several questions have been raised: Did investment banks assume a key role in the structuration of the economy of their country and thus assume a "historical function" within its banking system? What was their "historical usefulness" or even "necessity" as a leverage to growth and as parts of the financial machinery? As tools or lubricants to help money to "circulate" (from piled up assets to investing facilities or to financial markets) and to be "transformed" (from short term cash to middle and long term investments)? Such key questions find answers throughout the various chapters there.

Sure, regulation, monetary policies and overall economic policies of the State were equally or more important in the building of each

23 See Margaret Ackrill & Leslie Hannah, *Barclays. The Business of Banking, 1690-1996*, Cambridge, Cambridge University Press, 2001. Weyer Vander, *Falling Eagle: The Decline of Barclays Bank*, London, Weidenfeld & Nicolson, 2000. J.R. Winton, *Lloyds Bank, 1918-1969*, London, Oxford University Press, 1982. A.R. Holmes & Edwin Green, *Midland. 150 Years of Banking Business*, London, Batsford, 1986. Michael Collins & Forrest Capie, "Industrial lending by English commercial banks, 1860s-1914: Why did banks refuse loans?", *Business History*, Vol. 38, No. 1, 1996, pp. 26-44. David Kynaston, *City of London: Illusions of Gold, 1914-1945*, London, Chatto & Windus, 1999. Bernardo Batiz-Lazo & Douglas Wood, "A case study on the strategy and stock market performance of Lloyds Bank Group, 1980-1993", *Journal of European Financial Services*, 4(1), 2000, pp. 31-63.

24 Youssef Cassis, "Banque et industrie en Grande-Bretagne et en Allemagne, 1870-1939", *Entreprises et histoire*, No. 2, 1992, pp. 7-18.

25 See Harold Wixforth & Dieter Ziegler, "Bankenmacht: Universal banking and German industry in Historical perspective", in Youssef Cassis, Gerald Feldman & Ulf Olsson (eds.), *The Evolution of Financial Institutions Markets in 20th century Europe*, Aldershot, Ashgate, 1995. Caroline Fohlin, "Universal banking in pre-World War I Germany: Model and myth", *Explorations in Economic History*, 36, 1999, pp. 305-343.

26 Lothar Gall, Gerald Feldman, Harold James, Carl-Ludwig Holtfrerich & Hans Büschgen, *The Deutsche Bank, 1870-1995*, London, Weidenfeld & Nicolson, 1995.

banking system, whilst the process of internationalisation and integration of the markets (foreign exchange, international credit, stock exchanges, then futures markets or else) fixed the background for banking and finance activities. But, within such patterns, specialised investment banks became among the main developers of the banking system, owing to the transformation of "ancient banks" into "modern banks" (French *maisons de Haute Banque* joining into Paribas or *Banque de l'union parisienne*;[27] British merchants banks into investment banking business, US investment bank houses contributing to the building of big corporate banks, etc.) or institutions created from scratch thanks to financiers and institutional investors – like Italian *Mediobanca*.

4. From specialisation to differentiation: Business models challenged

In 2008, arguments among economists challenged the re-establishment of the "business model" of "universal banking" which had been suspended by national laws (US Glass-Steagall act in 1933, Swiss and Belgian laws in 1934-1935, French 1941-1946 laws, etc.) or limited by cultural and historical habits separating banks alongside patterns of liquidity, in the UK or in Germany. New impetus has been thus be given to reflections about the "business model" of investment banking ("*banque de financement et d'investissement*" or "*banque d'affaires*", in French; "merchant banking" in the UK, etc.). Historians have therefore to take part to the present debates and bring their contribution through analysis of the very nature, the portfolio of skills, the corporate culture, the advantage edge, of investment banks.

A first flow of books had been published in the 1960s-1970s, which provided a first mainframe for a comprehensive understanding of the factual history of investment banks. Since then a fresh flow of researches gathered momentum, thanks to new generations of historians (and economists), to the access to large amounts of archives, and even to the collection of testimonies. A reconsideration of the history of investment banking seemed relevant, through the confrontation of historians and economists, and of national histories, through the assessment of the degree of internationalisation of investment banks and thus of the reality of a money and banking market within a transatlantic business community, then at the scale of a worldwide and now globalised business community. Key issues could be: Was there a business model of internationalised investment bank? How much

[27] Hubert Bonin, *La Banque de l'union parisienne (1874/1904-1974). De l'Europe aux outre-mers*, Paris, Publications de la Sfhom, 2011.

investment bankers were able to be "ground-setters", "path-breakers", "trendsetters", or "rainmakers" of national and international economy and growth? What core competences were those of investment bankers?

Banking history has considerably benefited from numerous individual and collective studies: deposit banking, merchant banking, family banking, local and regional banking, and thematic approaches (industrial banking, etc.) complemented such breakthroughs. But investment banking might seem to have escaped to such deepening of knowledge and analysis – beyond the fate of merchants or investment banks about which monographs have already been published (Kleinwort-Benson, Schroders, Morgan Grenfell, Goldman Sachs, Lazard, Baring,[28] etc., and in France: *Banque de l'union parisienne*, Paribas and a few merchant houses of the *Haute Banque*[29] community). In the meanwhile anyway, micro-economists did gauge the business model of investment banking, their portfolio of "functions", their leverage force on the range of commercial, market and merchant banking, their part on the big banking and financial places, which can lead banking historians to a better understanding of these issues between the past and the present times.

Such issues may join one key issue, about "differentiation". We mean there the distinction between commercial banks and investment banks. The present krach revealed how far commercial banks did practice what is commonly called "investment banking", that is commitment to

[28] Peter Austin, *Baring Brothers and the Birth of Global Finance*, London, Pickering & Chatto, 2007.

[29] David Landes, "Vieille banque et banque nouvelle: la révolution financière du dix-neuvième siècle", *Revue d'histoire moderne*, III, July-September 1956, pp. 204-222. Herbert Lüthy and Alain Plessis, *Mallet frères et Cie: deux cent cinquante ans de banque*, Paris, Mallet, 1963. Bertrand Gille, *Histoire de la maison Rothschild* (*1817-1870*), Geneva, Droz, 1965 & 1967. Jean-François Belhoste & Henri Rouquette, *La maison Seillière-Demachy, banque de l'industrie et du commerce depuis le XVIIIe siècle*, Paris, Floch, 1977. Jean Bouvier, *Les Rothschild*, Paris, Fayard, 1967; second edition, Brussels, Complexe, 1985. Christian Grand, *Trois siècles de banque. De Neuflize, Schlumberger, Mallet, de 1667 à nos jours*, Paris, E/P/A Éditions, 1991. Frédéric Barbier, *Finance et politique. La dynastie des Fould, XVIIIe-XXe siècles*, Paris, Armand Colin, 1991. Jacques Wolff, *Les Perier. La fortune et les pouvoirs*, Paris, Economica, 1993. Geneviève Daridan, *MM. Le Couteulx et Cie, banquiers à Paris. Un clan familial dans la crise du XVIIIe siècle*, Paris, Loysel, 1994. Robert Hentsch, *Hentsch. Banquiers à Genève et à Paris au XIXe siècle*, Paris, self-edition, 1996. Alain Plessis, "Une maison de la Haute Banque parisienne: les Mirabaud et le financement des entreprises de la fin du XIXe siècle à la Seconde Guerre mondiale", in Philippe Marguerat, Laurent Tissot & Yves Froidevaux (eds.), *Banques et entreprises industrielles en Europe de l'Ouest, XIXe-XXe siècles*, Geneva, Droz, 2000, pp. 239-250. Isabelle Chancelier, *Messieurs Mirabaud et Cie. D'Aigues-Vives à Paris, via Genève et Milan*, Paris, Éditions familiales, 2001. Alain Plessis, "The Parisian '*Haute Banque'* and the international economy in the nineteenth and early twentieth centuries", in Youssef Cassis & Philip Cottrell (eds.), *The World of Private Banking*, London, Ashgate, 2010, pp. 127-140.

financial markets (proprietary trading, M&A, secondary markets) beyond their classical portfolio of commercial banking dedicated to companies, that is "corporate banking". On several periods of banking history (and also business history), bank managers often followed "fads",[30] along with sheepish trends or herding behiavours. Some chapters ponder how far deposit and commercial banks did practice investment banking whilst extending their range of services in corporate banking, to propose them the engineering of schemes about project financing, issuing of securities, international credits, middle and long term banking or financial products adapted to the development of equipments and investments – which had been the "prehistoric" purpose of new types of investment banking in the mid-19th century, to supply means of growth to emerging big firms of the first industrial revolution (1780s-1880s).

5. The "originality" of investment banking?

Such arguments about differentiation cannot but foster reflections about the historical "necessity" of investment banking will also be a key issue. Despite the recent trend towards "universal banking" on one side, and towards "financialisation", on the other side, which somewhat short-circuited banking intermediation from the 1980s in favour of investment funds and direct access to stock exchanges, our book assess how investment bankers – within universal banks or elsewhere – preserved their ability of being influential and active on the markets of mergers & acquisitions, of project financing, in issuing. Despite the building of huge corporate and investment banking bodies (mainly in the US, with a very few "national champions" in each European countries and in Japan), the resurgence of "*boutiques*" – little investment banks – in the 21st century draws attention to such an issue of the "necessity" of investment bankers. This led our book to a long term argument about the "usefulness" of investment banking, to determine in conclusion why such competences kept momentum through three industrial revolutions, and also through the various stages of banking history and even through what we can call "banking revolutions".[31] At each period of growth or at each cyclical "boom", new instruments to act on the fields of financial markets and medium-long term credit were set up, and new actors were created by speculators, feeling the windows of opportunities for profit, and more frequently by innovators or

30 See Hubert Bonin, "Fashion trends in banking business models since the 1850s", *Business & Economic History On-Line*, Vol. 7, 2009 <http://www.thebhc.org/publications/BEHonline/2009/beh2009.html>.

31 Hubert Bonin, "Peut-on parler de révolution bancaire (XIX^{e}-XX^{e} siècles)?", in Éric Bonhomme (ed.), *Les révolutions industrielles et scientifiques à l'époque contemporaine*, Bordeaux, SCEREN-CRDP Aquitaine, 2007, pp. 13-29.

followers of the move: that was the case during the ultimate boom of the first industrial and banking revolutions in France in the 1870s-1880s with a burst of *maisons de Haute Banque*, during the *Gründerzeit* in Germany, during both booms in the US in the 1890s-1900s or in the 1920s, for instance. "Fever" provoked such initiatives on every banking and finance place, all the more that emulation guided ground-setters among "capitals of capital".[32]

Our table there under could appear as an attempt to summarise what paths of differentiation could be followed to identify pure investment banking, investment and corporate banking, and mere commercial banking, along with the various functions and fields of activity – the very issue being that of their "identity" indeed.[33]

Table 1. Towards a process of "disaggregation" of investment banks' portfolio of skills: A first assessment of specialisation

Managing the primary market	issuing and underwriting (as co-lead-managers of syndicates) brokering equity and bonds assessing the market's ability of absorbing fresh financial paper committing insider trading buying the financial press negotiating with the state entertaining networks of family merchant banks, etc. managing special relationship with a few states for bonds issuing
Managing the secondary markets	Trading on equity and bonds Managing of speculative trends, etc. Managing discreetly emerging bids or counter-bids operations Lead-managers of syndicates helping to maintain the value of the equity of enterprises as customers
Money markets management	Managing debt assets and liabilities for customers (with rates risks); swaps of debts Forex (with exchange risks), swaps of currencies

32 Youssef Cassis, *Capitals of Capital. A History of International Financial Centers, 1780-2005*, Cambridge, Cambridge University Press, 2006. Youssef Cassis, *Les capitales du capital. Histoire des places financières internationales, 1780-2005*, Geneva, Slatkine & Pictet, 2005; Paris, Honoré Champion, 2008.

33 See Éric Bussière, "Les banques d'affaires françaises au xx^{e} siècle: des établissements en quête d'identité?", in Maurice Lévy-Leboyer (ed.), *Les banques en Europe de l'Ouest de 1920 à nos jours*, Paris, Comité pour l'histoire économique & financière de la France, 1995, pp. 223-235.

Assets management	[Linked with the above sectors] Proprietary management of assets Assets management for institutional investors (insurance companies, retirement funds, etc.) Development and management of real estate assets "Research" (financial analysis) and economic studies
Wealth management ("private banking")	In favour of family business, of well established fortunes, of rich managers, etc. Managing inheritance processes within privately-owned companies Managing (blinded or not) investment trusts
Tailor-made advice activities	Mergers and acquisitions advice Managing bids Conceiving structured financement: project financing (huge equipments, plants, ship then planes, etc.) Conceiving syndicated credits Advice in "haut de bilan" operations, banking engineering
Financing innovation	Raising funds to finance: start-up companies innovative specialised credits units companies involved in industrial revolutions
Investing in companies' capital	Practicing industrial finance for proprietary investments [see above] Stabilising the equity of partner companies and being part of their stakeholding Managing financial groups, with industrial and services "partners" or almost "subsidiaries" Helping investors to become stakeholders in companies (today: "private equity investments")
Sustaining internationalisation	Managing Foreign Exchange activities Networking the City (then also in New York or in Asia) Financing and managing the spreading of banking managerial skills on emerging banking markets (Central Europe, colonial areas, Latin America, Asia, etc.) Project Financing [see above]
Taking part to classical corporate commercial banking, but with trends towards:	Financing commodities trading Structuring credits for export or import Conceiving middle and long terms credits

6. Delving into investment banking in the making

Several issues were raised through our book. We applied the methods of business history to banking history, that is we questioned the history of investment banking through the spectrum of issues raised about stakeholders, strategies, internationalisation, innovation, corporate culture, portfolio of management skills, knowledge capital, differentiation, performance, and competitiveness, which required questioning the data and facts accurately. Despite our focus on the relevant balance of the "organisation of firm" and its overall portfolios of strategic activities and of skills, we provided sometimes biographical approaches, to assess how much investment bankers as personalities did orient the fate investment banks, as innovators, go-betweens, managers, financiers, "market markers", etc.

We focused on the portfolio of skills of investment banks along with some kind of "an inside outlook", that is *grosso modo*: How did it function? How did they do it? What was their capital of knowledge and competence? What did characterise actually investment banks in front of deposit banks? This led the authors to determine what achieved an investment banker in his day to day activities, and how he was working (teams, access to information, networks of relationship, links with the State, international minds) and how he used his networks of communication.

But, meanwhile, our collective and comparative investigation considered one key issue: What type of organisation did characterise and today characterise investment banking firms? How managers of such companies succeeded in balancing creativity, reactivity, resiliency, openness to information, trust building, closeness to innovative entrepreneurs, action through moving connections on one side, and the drastic (and classical) management of firm organisation, the building of an array of processes to assess risks, and the development of auditing balance sheets, especially in proprietary trading and proprietary investment portfolios. And such paths were followed to gauge the process of building business models, portfolio of skills and corporate cultures through an evolutive analysis, about each "*Belle Époque*" of booming investment banking.

Classically but methodically, our chapters pondered how investment banking did constitute to the conception and to the development of new financial and banking products. We linked banking history and the history of innovation, because we dedicated studies on the part played by investment banks and a few investment bankers or teams in the emergence and structuration of some activities, like: leasing, specialised credits, industrial banking, collateralisation, mutual funds, financing of real estate development, financing of developing or emerging countries, structured project financing, public-private project financing, the creation and functions of investment funds, etc. We focused on the entertainment of networks of capital, to reconstitute how investment bankers succeeded in mobilising "sleeping" capital, assuming a function of intermediation between wealthy industrialists or estate owners, institutional investors, family entrepreneurs with available cash, then the assets of mutual funds, on one side, and the course of financial markets. How did they exert such a capacity of leverage, within the circuits of capital?

We have indeed to question the role played by investment banks in setting up tools to invest funds into the equity of (quoted or unquoted) firms. Did investment banks became key stakeholders of their national capitalism through direct investment in national companies? How much did they become "financial holdings" or "financial groups" (like in France in the 1960s-1970s)? Did they exert any influence on the industrial or services strategy of their national capitalism and firms? Were they bankers of influence? Or only of intermediation? How did they create, develop and manage investment funds? Did they play a key role in the strategies of customers' firms? Did they control their boards? How did function this interlocking of individuals, finance, influence? Proprietary investment and trading will be a crucial issue. Did investment banks used their own capital (either owned or borrowed) to become global players on the secondary stock trading markets and foster "speculative moves" in order to broaden their revenues? Can we estimate the weight of proprietary trading within the activities of investment banks? How much did they live and earn through such market finance activities? Several chapters enhanced the function of investment banks as cornerstones of financial innovation; the became market makers for many functions: those shown in the previous table, but also, at key stages of the financial history, they especially vitalise and foster the new markets, as they did very recently (OTC, futures; diffusion of derivatives and so forth).

Internationalisation has been one core issue too. We determined how investment banks entertain some specific corporate culture within their country because they were steadfastly oriented toward foreign perspectives, relationships, and markets. We precised whether they were some kind of an "off-shore" pole of services in their country, dedicated to European, transatlantic or worldwide markets; or how much they contributed to the opening of their national economies to internationalised scopes.

Competitiveness drew consideration because, on the long term, the ability of national market places was at stake; the future of the financial power was challenged. We argue about the ability of some market places to keep pace with the changes of the banking industry, to adapt to financial, technological and commercial revolutions. We question thus the frailness of investment banks to keep momentum in front of new competitors; and we determine whether the size and prosperity of national economies had effects on the existence and the strength of national investment banks: could such banks still be active in countries of which the economy was declining? In contrary, were all powerful countries destined to be equipped with powerful investment banks? The apex then the decline of British merchant banks, the fate of German and Swiss investment banking between *Privat Banken* and universal banks, the uncertainty about Dutch and Belgian investment banks to keep momentum in face of considerable competition, the rapid upsurge of American investment bankers, the limits to Asian types of investment banking, fuel analysis.

Banking "business models" mobilised the book, because the competitiveness and performance of investment banks relied on the relevance of their strategy, on the efficiency of their organisation, and on the effectiveness of their management. Monographs and comparative studies can help determine "the best ways" to get relevant business models at investment banks, perhaps also in comparison with deposit banks.

The durability of the model of family investment banking has been gauged, in order to determine how the capital of skills and relationships could be renewed within family banks, or had to be transmit to larger institutions – as in France when merchant banks (*Haute Banque* houses) created large investment banks. What business model could preserve the existence and competitiveness of family investment banks?

The importance of investment banking within deposit banking drew attention to precise how much competence in issuing, brokerage and M&A had been acquired by specialised divisions of deposit banks. Such a trend towards "universal banking", within managerial or law limits, will be somewhat analysed, explained and assessed.

The key roles assumed by investment banks in the development of national economies and in their involvement into international markets led to crucial positions within the circles of national power. Our book reconstituted the relations between investment banks and national authorities, to precise how much they exerted influence on the State or political circles, how much the State could orient they choices, for instance in favour of the reinforcement of the national economy and companies.

Banking economic models are presently at stake: "universal banking" and "specialised banking" are once more been challenged during the crisis of the recent years 2007-2008, even with the Glass-Steagall Act reconsidered. Historians will thus contribute to the debate through arguments about investment banking portfolio of skills, range of risks, and business models – therefore fuelling analysis about the firm organisation, governance and strategy, and about patterns of business management in banking – mixing banking history and business history, and the institutionalised economy of the firm too.

Such issues allow a comprehensive approach to the history of investment banking. Comparative approaches were tackled, long term considerations also. But monographs and moreover biographies play a significative role in a few chapters. Fresh access to archives and/or testimonies foster several developments, in order to renew our understanding of the innovations of path-breaking bankers and the key role on several market-places of trendsetters. One key originality of our book might be the confrontation of historians and of economists, to ponder about the business models, the strategies, the issue of universal banking, etc.

Chapter 2

Summaries

Janette Rutterford

Sir Everard Hambro, born in 1842, was a fourth generation banker who held a dominant position in the London banking world during the late nineteenth and early twentieth centuries. He died in 1925, with net wealth of £2,132,340 [*Financial Times*, 20 April 1925]. Hambro was a personal friend of John-Pierpoint Morgan, the American investment banker, helping him to recruit Clinton Dawkins as a partner in the British Morgan firm, J.P. Morgan. However, Hambro's attitude to helping British industry was very different from that of his American counterpart. For a limited number of British companies seeking to raise finance on the stock market, Hambro provided legal, financial and Stock Exchange regulatory expertise but did not build up long-term relationships with the directors of the companies involved, nor did he invest personally in these concerns. This chapter explores in detail Everard Hambro's input into two new issues of London-based firms: Thames Ironworks in 1899 and Trollope, Colls & Co. in 1903. This is done by using archives which include correspondence between Hambro and the chairmen of the two companies, as well as draft prospectuses and press cuttings. The chapter first looks at the input of Hambro into the following aspects of the Thames Ironworks & Trollope, Colls & Co. new issues: capital structure, disclosure of financial and other information in the prospectus; the role of the broker, and underwriting and new issue costs. It then compares Hambro's role with that of J.P. Morgan in the US, and concludes with a brief analysis of Hambro's personal investments in the context of investments in British industry.

Peter Hertner

Railways, invented during the earlier part of the 19th century, were an essential tool of transport and communication during the following decades. By the 1880s practically each angle of Europe had been opened up through their construction. In South-Eastern Europe this process had started during the 1870s, and by 1888 Constantinople/Istanbul could be reached by rail from Paris or Vienna. There were, however, still large gaps in the transport system of this part of the continent. The chapter tries to show how a railway line was eventually built between 1893 and 1896 which was to link Salonica/Thessaloniki to Dedeagatch/Alexandroupolis. Thus a Southern connection through Eastern Macedonia and Western Thrace with the Ottoman capital city was created. The two most important founders of this railway company were the Imperial Ottoman bank, essentially an Anglo-French institution, and *Banque de Paris et des Pays-Bas*. A third important partner was the Frankfurt private banking house of Bethmann Brothers. With the British partners refusing at the end to participate in this venture the bank became rather a Franco-German affair with the French side dominating the matter. The *Compagnie du chemin de fer ottoman Jonction Salonique-Constantinople*, as it was finally called, was founded as an Ottoman company in March 1893 with the issue of a huge amount of bonds and a rather small part of shares, only 7.2 per cent of the entire capital. Construction and running of the railway were handed over to the Paris-based *Régie générale pour la construction et l'exploitation de chemins de fer*, a prominent French group which had built railways all over Europe. The entire business could not have been started without a sizeable kilometrical guarantee offered by the Ottoman state, a guarantee which was also granted at different levels to the other Ottoman railway companies, almost all of them financed by Western European – French, German, British – capital. The aim of the Ottoman authorities, connected with the concessions given to the *Jonction Salonique-Constantinople* railway company, was above all strategic: thus, in the case of an armed conflict, troops from Anatolia could be rushed to all possible war theatres in the Balkans. As a matter of fact, this was done successfully during the war with Greece in 1896. Until 1911 the *Jonction Salonique-Constantinople* developed slowly and its profit situation remained more modest than the results of the other two railway companies built by foreign capital in the European South-East (not counting Rumania). One of the reasons for this must have been the fact that navigation on the Mediterranean remained a strong competitor for this railway company. Everything changed during and as a result of the two Balkan wars in 1912-13: The Ottoman Empire lost most of its European possessions and the line ended up to be situated on territories handed over to Greece and Bulgaria. As was to be expected, the share and bond holders had to negotiate with these two powers, and it took them more than a year to get at least part of the money claimed. WWI, the 1929-33 economic crisis and then WWII complicated everything and it took another fifty years to find a compromise which seems to have given at least a partial compensation for the *Jonction Salonique-Constantinople* bondholders. Through this case study, the chapter determines how investment banking worked concretely in a sector, the railways, which proved to be fundamental for economic growth during most of the 19th century, along cross-borders projects joining Berlin and Vienna places and Eastern and Balkanic Europe. First, the overall issues of financing railway infrastructures are recalled, which opened doors to "project financing" design at investment banks, relying on their teams of experts, engineers and financiers. Second, the various types and origins of banking stakeholders have been precised, through the balance of power between European places and big banks of the second half of the century and the turn of the 20th century. But, thirdly, the chapter insists on the permanent *modus operandi* within the communities of banking and business competing to gain contracts, concessions, building and equipment orders, and, finally, finance issues and banking credits. On one side, competition prevailed, but connections were established among the competitors to share information and alleviate the load borne by each bank, thanks to syndicates. The organisation and way of life of these latter are scrutinised, and the chapter insists on the close cooperation between "old bank", that is the merchant banks at the apex of their role on a European level, and "new banks", the joint-stock firms which scrambled for issuing and distribution missions throughout the successive project financing operations to be conceived. The portfolio of skills of investment bankers are therefore detailed and assessed, to contribute to insights into the very nature and function of investment banking.

Juan Flores

The historiography on the Baring crisis, both in Britain and Argentina, is vast and rich. The interactions between banks in Europe on the one hand, and the national, provincial and municipal governments in Argentina, on the other, have been described and analysed in a number of works since the very moment of the crisis. The cycle of capital flows to the so-called "new countries" experienced an inflexion point in 1885. During this year, a currency crisis erupted in Argentina, ending the gold standard regime that had been set up only two years before. Far from deterring new capital to be invested in Argentina, the effect was precisely the opposite. The true boom of foreign investment to the country really took off during that year, and peaked in 1888 before its sudden collapse in 1889 and mainly in 1890. This chapter aims to explain this apparent paradox through an analysis of London's underwriting strategies, their business structure and their risk management. Their implication in the issuing of bonds also affected investors' risk perception. In particular, the involvement of Baring, the historical underwriter of Argentina's bonds in London, was regarded as a seal of approval by financial markets. However, overindebtedness in Argentina, along with political instability and a number of external shocks contributed to freeze the demand for new bonds, triggering thereby Baring's own fall in 1890. We argue that despite the general environment of competition between underwriting banks, in 1885 they colluded to impose on Argentina a set of conditions to continue borrowing. Among them, two conditions were particularly relevant, one related to Argentina's fiscal policy and another on the suspension of new external borrowing. Financial markets' reacted positively to the announcement of the agreement, although in the medium term none of these conditions were met. Moreover, they served to open up Europe's capital markets to Argentina's provinces and municipalities. We speculate on the possible perception of the market on Baring's acting as a lender of last resort to Argentina.

Piet Geljon & Ton de Graaf

In this chapter, investment banking is defined as including the following activities: new issue business, both national and international; securities trading and holding of securities portfolio's; investment advice and fund/asset management; advice and intermediation regarding company formations, mergers, acquisitions and restructuring (corporate finance); special forms of credit and financial innovation. The origin of the Dutch securities sector lies with the establishment of the VOC (United East India Company) in 1602, the shares of which were traded on the exchange. The wealth accumulated by the Dutch merchants was later on used for the granting of loans to foreign sovereigns or countries. Among a number of merchants/bankers active in this field, Hope & Co. gained prominence, in particular with its Russian loans. The decline in commerce and industry, followed by the French occupation in 1795, was a severe blow to the financial activities. After 1815 international issues became rare. As far as domestic issues occurred banking or securities houses were not used; subscriptions took place via a notary public or the Nederlandsche Bank (in particular state loans). The stock exchange continued its activities, including trading in the new shares and bonds. Since 1774 also investment funds were known. From about 1860 economic growth in the Netherlands started to accelerate and gradually an industrialisation process took place. The Dutch remained active investors, in particular abroad, but given the relative size of the economy they could only occupy a minor place internationally. Domestic issue activity increased slowly, but began to grow after the turn of the century. The stock exchange flourished with a.o. American and Russian railway companies. New banks were also established (Rotterdamsche Bank, Amsterdamsche Bank), which under foreign influence Crédit mobilier) combined from the beginning commercial banking (deposits and credits) with new issues and securities trading. Institutions that were initially active in another field, ventured in the securities business to increase their profitability (the pure commercial bank Twentsche Bank, the trading company Nederlandsche Handel-Maatschappij). Apart from Amsterdamsche Bank, which became prominent in the new issue business, smaller private banking houses developed investment banking activities of various kinds. Already before 1914 a banking concentration movement had started, in which the bigger commercial banks not only spread over the whole country by taking over local banks/cashiers, but also strengthened their position in the securities business by mergers with older firms. The revival of economic activity after WWI caused an increase in the demand for capital, both in the form of bank credits and new issues. The ensuing crisis of 1921/1922 led to heavy problems for the most expansionary banks. In this period there were many newcomers in the securities business, mostly smaller firms, but also the Dutch overseas banks expanded in this field. In the 1920s, the Netherlands as a political stable and liberal country acted as a save haven for foreign capital. For a short period the international accepting business flourished. Foreign issues on the Dutch capital market also grew substantially. The turmoil of the 1930s brought largely an end to these international activities, while also domestic issues decreased strongly. After WWII, investment banking activities were restricted by regulation of the capital market and of international capital flows. As the economy gathered steam after a number of years and personal wealth rose rapidly, the emphasis fell on the expansion of banking services for the general public. As a result, even those banks that were rather strongly involved in investment banking tried to expand in commercial banking. So, what specialisation still existed disappeared and the general banking concept gained more and more ground. From the 1960s, however, the securities business was rather depressed and banks even thought of ending this activity. All this changed in the 1980s. The economic boom, together with the liberalisation of financial markets, led to a renewed and very strong expansion of investment banking activities, further stimulated by strong rises in share prices. New players appeared, both from abroad and domestically, where new financial conglomerates were formed. As a result, investment banking activities were more and more performed by big units within financial groups, which competed heavily with each other and with foreign institutions. As a result of the financial crises, over the past few years a completely new situation has arisen in investment banking. Conglomerates had to be split up, new groups were formed and new regulations were introduced. As yet, the situation is still not completely cleared up and the prospects of investment banking remain uncertain.

Hubert Bonin

The chapter is focused on the function of French investment banks as "pathbreakers" to accompany and stimulate the rebirth of French economy after WWII. First it finds out why investment banks escaped to the move of nationalisation which was achieved in 1944-1946 and which involve Banque de France, banks and insurance companies. The balance of powers, the networks of influence, the commitment of investment bankers to the rebuilding of France within an internationalised economy, and the issue of the connections to be re-established with the City and the US bankers and financiers are at stake through the scrutiny. Second, it assesses the strengths and weaknesses of investment banks (Paribas, Banque de l'union parisienne, Rothschild, Lazard), precises the emergence of new competitors (Banque de l'Indochine, the Jack Francès group, etc.), and as a consequence determines the strategy followed by these players. For example it precises the effects of the nationalisation of numerous big companies and the dwindling of the financial market on their issuing and brokering activities. Third it considers the evolution of the portfolios of strategic activities and skills within the "classical" investment banking services. It gauges their ability to regain momentum in favour of corporate customers (merchant banking, corporate banking), either nationally or internationally. It reconsiders the "path-breaking" activities of investment bankers on the international market of structured finance, as a leverage force of French industrial investments abroad. Fifth, it reconstitutes the competitive edge of investment banks on the imperial/colonial market, and argue about the priorities fixed, either "obsolete strategies" or the involvement of colonial sectors into internationalised and modern business models. Sixth, it tackles the issue of investment bankers as "pioneers" about the new credit and financial products and techniques which were being either transferred mainly from the US or engineered in Paris, as a way to find out new sectors of activity to balance those being assumed by the public institutions, or as a way to establish bridges on promising activities in connection with real estate development, the restart of outlets for bourgeois building, and the construction of the society of affluence.

Carlo Brambilla

The banking crisis of the early 1930s put an end to investment banking in Italy and led to a radical reform that almost "nationalised" the banking system and entrusted state-owned special credit institutions with industrial financing and investments. This chapter traces the development of investment banking in Italy from its appearance in the 1860s to its collapse in the early 1930s. Following shortly other European experiences, big joint stock investment banks played a relevant role both in supporting investments in infrastructures and public utilities, and in fostering the first wave of industrialisation. This chapter argues that the affirmation and consolidation of Italian investment banking was an evolutionary process of innovation aimed at allowing big banks to root in a newly emerging financial system, tweaking to the developments of markets and institutions, as they gradually came forth, mainly in response to crises. Financial innovation, however, was not always attended and steered by "regulative" and "institutional" innovation, thus compelling banks to adapt their strategies to the specific kinds of guarantees and risks they can rely upon and have to cope with. Big universal joint stock banks had to face up to an institutional framework that did not provide incentives for information disclosure by companies, did not limit the speculative attitudes and prices' volatility of the stock exchanges, thus allowing for high degrees of opacity as for the quality of investments and for overly high risks connected with capital investments. Moreover, persistent segmentation of the banking system and the presence of large shares of non-contestable financial intermediaries limited universal banks' external growth and curtailed their ability to collect resources. Big banks' responses to those issues tended to improve capital markets weaknesses and instability, and to expose the banks themselves to liquidity risks and financial crises. Indeed hazardous credit policies and highly risky asset-liability management strategies they adopted in the 1920s transformed universal banks into quasi-holding companies, an "innovation" in the pattern of investment banking that eventually led to its failure in the early 1930s.

Luis J. Coronas-Vida

The 'Six big banks' group, consisting of a genuine investment bank, four mixed-type banks and a commercial bank, dominated the financial sector in Spain until the 1970s. The nature and evolution of this group is analysed and characterised during the interwar period and the Franco regime. Spanish banking grew up in a very protectionist environment in which relations between banks and companies were established in several ways. The big banks of Madrid and Bilbao acquired shares and participated in the launch of some of the most important firms in Spain. Their directors also sat on the boards of numerous companies and exercised voting rights on behalf of individuals with shareholdings in their banks. Banks also helped to finance firms through short-term credit; although renewable, there was always a risk that these loans might be refused at any time. The Bank Regulation Act of 1962 introduced greater specialisation, in an attempt to achieve better long-term credit facilities. Nevertheless, the performance of industrial and investment banks, as company shareholders at least, during the 1960s and 1970s, failed to meet the objectives that had been expected of them. The economic crisis of 1973, the Spanish banking crisis (1977-1985) and the entry of Spain into the EEC (1986) all changed the banking panorama in Spain. Nowadays there are two big banks which hold securities portfolios, but their nature is far from the former mixed-type of banking.

Sofya Salomatina

The chapter analyses investment banking in pre-revolutionary Russia. In the focus of its attention there are banking services on initial public offering for private companies' securities. This activity became a mass phenomenon in the 1890s for the first time. This research is an attempt to investigate making and evolution of Russian investment banking in the aspect of banking models' development. It proves that investment banking for private companies appeared throughout traditional activity of several commercial banks in St. Petersburg, dealing with services to public and mortgage bond market and intensive currency speculation caused by fiduciary standard. However, private companies' demand for investment banking appeared persistently in the peak of pre-revolutionary economic growth by 1895, and the Petersburg banks switched over to private stock as a new subject for exchange transactions. In the beginning of the 20th century the crisis revealed weak points of the 1890s investment banking, and they were overcame by universal banking development by the 1910s.

Gergana Taneva

This chapter presents a model of development of Franco-Bulgarian financial and economical relations in the late of 19th and early 20th century. The chapter explores the role and impact of French banking groups in the Bulgarian foreign loans, consolidation of the banking structure and their influence on the Bulgarian economy and industry. The French banking groups occupied an important place in Bulgarian history due to their structure and their influence on social organisation. They entered the market to promote its development through a portfolio of skills. Such a study, dealing with investment banks (*Paribas*, Bup) and the financial activities of commercial banks (*Crédit lyonnais*, *Société générale*) intends therefore to examine the role and the impact of financial groups, first in the formation of a Bulgarian State, and then in its institutional reorganisations. To study the impact of French financial institutions in Bulgaria means analysing their strategies and their operations on stock exchange and financial markets, whose competition and collaboration represent the form of bank investments.

Chris Kobrak

Deutsche Bank's acquisition of Bankers Trust was an important milestone in the creation of multi-service, transnational mega banking institutions. This chapter traces the major steps in and justifications for the acquisition. The narrative is put into both its German and American social and political context, including short histories of both banks. It highlights the mixture of technological, regulatory and general economic changes that led to the purchase and suggests some insights about contemporary financial architecture that can be gleaned from this cross-cultural event.

Giandomenico Piluso

As it is well known, banks have liquid liabilities against potentially illiquid assets. Normally, such a "maturity mismatch" does not affect financial stability, as it is unlikely that all depositors would request their money back exactly at the same moment. Yet, when a wider lack of trust occurs a run could follow by menacing the very financial stability, possibly with a serious impact on capital formation and, in the end, on economic growth. Such a problem was particularly apparent up to the first decades of the last century, when financial systems were loosely regulated and central banks were rather reluctant to intervene during liquidity crises as they were tied up by gold standard constraints. In the 1930s, as the financial crisis hit hardly all major economies, maturity mismatch and related instability issues were dealt with by central authorities and lawmakers. The emerging idea was that financial intermediaries needed to be set in a more regulated environment, where commercial banking was to be separated by investment banking, in order to preserve stability. In Italy the Banking Act of 1936 was accordingly conceived. The new Banking Law mirrored the vision of a group of technocrats, connected to the Bank of Italy, who experienced directly to which extent universal banking could degenerate and produce systemic instability that could affect capital formation in the long term. It adopted specialisation as its cornerstone and, therefore, investment banking was rigidly separated from commercial banking and universal banking was at least formally banned up to the reforms of the early 1990s. The chapter aims to sketch a general picture of dynamics of forms, institutions and mechanisms of long-term financing in Italy from the mid-1930s to the mid-1970s. It offers a short illustration of the genealogy of the regulatory model and its main principles depicting the main evolutionary dynamics of the model during the Golden Age when it was regarded as substantially fitting to investments and firms' demand. The chapter illustrates what factors were mostly responsible for the decreasing allocative efficiency of the model since the mid-1960s and, especially, during the 1970s when it entered a major crisis. It concludes discussing whether the model implied a trade-off between stability and efficiency or, instead, other factors, such as monetary policy, affected the efficiency of investment institutions and, in the very end, the overall allocative performance of financial intermediaries up to the late 1970s.

Part II

Portfolio of Skills and Networks: Investment Bankers, and Institutional and Private Investors

Chapter 3

Everard Hambro, between Investment Banker and Investor

Janette Rutterford

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"I confess that personally I have a horror of all industrial companies and that I should not think of placing my hard-earned gains into such a venture":[1] Sir Everard Hambro, born in 1842, was a fourth generation banker who held a dominant position in the London banking world during the late nineteenth and early twentieth centuries. He died in 1925, with net wealth[2] of £2,132,340. Hambro's bank was truly international, involved in numerous overseas government bond issues and also in mining and American railroads. Hambro was also a personal friend of John-Pierpoint Morgan, the American investment banker, and helped him to recruit Clinton Dawkins as a partner in the British Morgan firm, J.S. Morgan.[3] However, his attitude to helping British industry was very different from that of his American counterpart. For a limited number of British companies seeking to raise finance on the stock market, Hambro provided legal, financial and Stock Exchange regulatory expertise; help on drafting the prospectus; access to brokers; and underwriting if required, but did not build up long-term relationships with the directors of the companies involved, did not help on corporate strategy nor with access to government officials, and did not invest personally in these concerns.

This chapter will explore Everard Hambro's input into two new issues, those of two domestic companies, Thames Ironworks ('Thames Iron')

1 Quote in 1911 by Lord Revelstoke of Barings, cited in Peter Ziegler, *The Sixth Great Power, Barings, 1762-1929*, London, Collins, 1988, p. 186.

2 See *Financial Times*, 20 April 1925.

3 Mira Wilkins, *The History of Foreign Investment in the United States to 1914*, Harvard, Harvard University Press, 2004, p. 863 and p. 58. One third of Hambro's Bank's investments in 1898 were in American railroads.

and Trollope, Colls & Co. ('Trollope, Colls'), both London-based firms, in 1899 and 1903 respectively. This is done through the prism of correspondence archives which include correspondence between Hambro and the chairmen of the two companies, as well as various drafts of the prospectuses, newspaper clippings, etc.[4] The role of Hambro as an investment banker will be compared with that of JP Morgan. Finally, the portfolio of Hambro at death will be analysed with respect to the types of investment held, showing that Hambro held only a handful of investments in companies operating in Britain and concentrated his portfolio on foreign bonds and companies with foreign operations.

The chapter looks at the Hambro's input into the following aspects of the Thames Iron and Trollope, Colls new issues: capital structure, disclosure of financial and other information in the prospectus; the role of the broker, and underwriting and new issue costs. It then compares Hambro's role with that of J.P. Morgan in the US, and concludes with a brief analysis of Hambro's personal investments in the context of investments in British industry.

1. Hambro structuring new issues for companies

We intend to gauge the reality of the portfolio of skills of Hambro merchant bank in tackling one main activity of an investment bank, that is, the issuance and underwriting of equities and bonds. The case studies will help our understanding of how the emergence and development of the London Stock Exchange required the extension and intensification of investment bankers' skills, in particular the balancing of the interests of their clients, the companies whose securities were being issued and possibly underwritten, and the interests of the subscribers and investors who might also be wealth management clients of the bank.

A. Hambro as senior adviser to Thames Iron

Established by Charles J. Mare in 1846, Thames Iron was one of the leading shipbuilding firms on the Thames from the 1850s, building the first ironclad warship, the Warrior, in 1859, thereby becoming a household name.[5] It suffered a number of downturns,[6] being re-formed in 1864 and 1870.

4 Janette Rutterford, "The merchant banker, the broker and the company chairman: A new issue case study", *Accounting, Business & Financial History*, 2006, 16, 1, pp. 45-68.

5 Sidney Pollard, "The decline of shipbuilding on the Thames", *The Economic History Review*, New Series, 1950, 3, pp. 72-89.

6 *Ibidem*, 1950. A.J. Arnold, *Iron Shipbuilding on the Thames 1832-1915*, Aldershot, Ashgate, 2000, pp. 72-89.

a. Background

Its banking relationships were problematic, with Prescotts bank pressed to lend £50,000 when a Turkish debtor had defaulted following the banking crisis initiated by the collapse of Overend Gurney in 1866. Prescotts did so reluctantly, noting that it only did so as "many of our customers are shareholders". In 1870, after the restructuring, Prescotts refused to become the new company's banker, being replaced by London & Westminster.[7] Originally run by Mare and his father-in-law, Peter Rolt, MP, influence had shifted by the 1870s to F.C. Hills, a successful Deptford chemist. His son, Arnold Hills, joined the board in 1880 and later became managing director; one of three sons, he attended Harrow and Oxford, was a champion footballer and held the record for the mile in 1878, although his official biographer was grudging in praise, commenting that he won the three-miles race at the inter-university championship in 1879 in "creditable time". Concerned with worker welfare, A. Hills spent the first five of his years at Thames Iron living in the East End of London, "devoting his days to the shipyard and his evenings to the recruitment and recreation of his workpeople".[8] He organised many educational and recreational clubs, of which the most famous later became West Ham United Football Club. He was president of the London Vegetarian Society and of the Vegetarian Cycling and Athletic Club. He funded the first vegetarian restaurant in Britain and was a firm teetotaller, arguing that he had been "led to the conclusion that it is the American habit of abstinence from alcohol that is one fundamental cause for their commercial prosperity".[9]

In the 1880s and early 1890s the firm suffered industrial unrest. Although the Thames shipbuilding workers were better paid than their counterparts on the Clyde and the Tyne,[10] they were still prepared to down tools. Hills believed in having the freedom of choice of labour, and Thames Iron endured a number of strikes[11] with Hills having a proposed profit-sharing scheme voted down. He took this to heart, writing later in the *Thames Ironworks Quarterly Gazette* (*TIQG*) that he would "not easily forget the brutal rejection. I was assumed to possess some

7 D. Souden, *The Bank and the Sea. The Royal Bank of Scotland Group and the Finance of Shipping since 1753*, Edinburgh, The Royal Bank of Scotland Shipping Business Centre, 2003, p. 128.

8 *The Times*, 8 March 1927.

9 *Thames Ironworks Quarterly Gazette*, 1895, 3, p. 152.

10 Bids by Thames shipbuilding firms were on average 9.4 per cent higher than the successful bids in the period 1889 to 1996 (Hills, 1896, cited in A.J. Arnold, *Iron Shipbuilding*, *op. cit.*, p. 136.

11 Including, at different times, (a) boilermakers, (b) shipwrights, (c) engineers, (d) carpenters, (e), labourers, Directors' Report for 1898, CLC/B/110/MS19096, London Metropolitan Archive.