The Development of Financial Institutions and Markets

Course description: Study of the historical development of financial institutions and markets, in a comparative international context with emphasis on the USA. Covers monetary, banking, central banking, and securities market history, as well as pertinent aspects of the history of government finance and the emergence of corporations as a dominant business form. Topics include the emergence of modern financial systems in history, including the roles of public finance and stable moneys, as well as banking, central banking, and securities and insurance markets; the composition, growth, fluctuations, and determinants of the money stock; the development of banking systems and their regulation; the emergence of central banking; monetary policies; major trends and fluctuations in stock, bond, and money markets; and the history of financial crises.

Readings: For a course such as this there are no ideal texts, despite the richness of the literature in book and article form. As a compromise between ideal and real, I have chosen several books that are comprehensive in treatments of their subjects (and perhaps one or two are worth keeping on your shelf after the course is over).

The books we will use are:

(1) Jonathan B. Baskin and Paul J. Miranti, *A History of Corporate Finance* (Cambridge pbk, 1999). This book covers its subject from the Middle Ages and Renaissance to LBOs and 1990s corporate governance issues (with an appendix on ancient Greece and Rome for those with broad interests). It "confronts" some tenets modern finance theory (e.g., Modigliani-Miller on capital structure and dividend policy—‘dividends don’t matter’) with evidence from history (‘dividends matter’).


(Wiley pbk, 2000). Lays out a model of how financial crises arise, and uses several centuries of history to elucidate and confirm typical patterns. Raises issues of how, if crises cannot be avoided, the damage can be contained.

(4) Richard H. Timberlake, Monetary Policy in the United States--An Intellectual and Institutional History (Chicago pbk, 1993). This is a comprehensive if eclectic discussion of U.S. monetary, banking and central banking institutions and policies from the 1780s to the 1990s. Shows how US history impacted the financial system, and vice versa. Strong on legislative developments as shapers of the system. The author would like to get rid of the central bank. The issue is worth considering because the US did not have a central bank in the middle period of its history, although we’ll see that there were substitutes of sorts for it.


Also recommended:
(6) S. Homer and R. Sylla, A History of Interest Rates, 4th ed (Wiley, 2005). This contains most of what a layperson, although perhaps not an MBA, might want to know about the subject.

(7) Larry Neal, The Rise of Financial Capitalism--International Capital Markets in the Age of Reason (Cambridge pbk, 1993). Neal describes and documents activity in the world's first regular securities markets, Amsterdam and London, in the 18th C., including a century or so of end-of-month price data for leading issues and a study of the famous and influential South Sea Bubble. He tests history with modern finance analysis, and finds that it passes. Baskin and Miranti summarize parts of it.


(10) Roger Lowenstein, Origins of the Crash: The Great Bubble and Its Undoing (Penguin pbk, 2005). A top financial journalist’s account of the 1990s and the antecedents and aftermath; journalists often do the first drafts of history.

Expectations: Plan on doing assigned readings and participating in class discussions; to help
that along, there will be frequent one-page max. (typed) writing assignments that address questions about the readings. Your one-pagers will be read and returned to you, creating an accumulating record of the course as it develops. They won’t be graded, but each one not completed reduces your grade by a mark (e.g., a B becomes a B-). One-pagers can be handed in at class, or emailed. To get the most out of the course, you should do these assignments in the week they are assigned.

As for graded stuff, there will be (1) a take-home midterm assigned the week of March 6-8 and due no later than March 28. (2) A ‘final’ that has two parts: 1) a two-person team presentation (PowerPoint) to the class on an assigned financial crisis, and 2) an individual paper either on the chain of events leading up to the crisis (one member of the team), or on the crisis itself, how it unfolded, and how it was ‘resolved’ or went away. The team presentations will be scheduled in April, and the final papers will be due at the last class on 5/2.

Course grades will be a weighted average of midterm (40%) and final (60%, 20% on the team presentation and 40% on the individual paper) grades, adjusted if necessary for weekly assignment deficiencies. Active participation in class discussions will break borderline grade averages in your favor.

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Financial Development of the US
Outline and Readings

I. Introduction to course; historical background. (2/7)

A. What is a modern financial system? What are its key institutional components? Its key functions? Why do they matter?


Baskin, Intro. and Chs. 1,2
Chancellor, Preface and Ch. 1
II. The first modern financial systems and their famous bubbles. (2/14)

A. Early capital markets and their famous bubbles through 1720.

B. Maturing and integration of 18th-century capital markets. British financial developments, and financial relationships with the America.

Baskin, Ch. 3
Chancellor, Chs.3-4


(A to N below, roughly 2 per week, 2/21 to 4/11, 7 weeks)

A. Creating the American financial system; the role of ‘the bastard brat of a Scotch pedlar.’ The US as an "emerging market."
Sylla, “Hamilton and the Federalist Financial Revolution, 1789-1795.” BB
Sylla, “Political Economy of Early US Financial Development.” BB

B. Development and functions of banks and securities markets.

Sylla, "US Securities Markets and the Banking System, 1790-1840" BB
Timberlake, Ch. 1.
Sylla, Wilson, and Wright, “Integration of Trans-Atlantic Capital Markets, 1790-1845.” BB


Timberlake, Chaps. 2-5
D. The maturing US financial system: Developments, reversals and transitions, 1830s-1870s.

Timberlake, Chaps. 6-8.

E. Financial Modernization: International comparisons

Sylla, "Emerging Markets in History: the US, Japan, and Argentina” BB

F. The Gilded Age: Railroad finance and capital formation.

Baskin, Ch. 4
Chancellor, Ch. 6


Timberlake, Chaps. 11-14.


Timberlake, Chaps. 15-16.

I. The Fed’s shaky start (1914-1920), high tide (1920s), and low tide (1930s Great Depression)

Timberlake, Chaps. 17-19.
Sylla, “The Great Crash of 1929 at Seventy-Five.”

J. The rise of securities-market regulation

Baskin, Ch. 5
Chancellor, Ch. 7
Midterms due 3/28

K. Bretton Woods system and the revival of monetary policy, 1940s-60s

Timberlake, Chaps. 21-22

L. Stagflation; ‘center-firm’ finance; international banking

Baskin, Ch. 6

Sylla, “United States Banks and Europe: Strategies and Attitudes”


Baskin, Ch. 7

Chancellor, Ch. 8

Lowenstein, Ch. 1

N. Monetary policy innovation and stabilization, 1979-present

Timberlake, Chs. 25-27


IV. Analyzing bubbles and financial crises.

(A, B, 4/18)

A. Money, credit, and the build-up to financial crises. The 1990s bubble

B. Manias, scandals and swindles

Kindleberger, Chs. 1-6

Shiller, Chs. 1-7

C. Financial crises: propagation, resolution, solution

D. Applications of the crisis model.
V. Asset price and yield history, Presentations on Crises (4/25 and 5/2)

A. Two centuries of US interest rates, bond yields and returns

B. Two centuries of US stock prices and returns

Sylla, “The New Media Boom in Historical Perspective,” *Prometheus* 19, 1 (2001), 17-26

[Final papers due May 2]
Biographical Summary

RICHARD SYLLA

Richard Sylla is Henry Kaufman Professor of the History of Financial Institutions and Markets, and Professor of Economics and Entrepreneurship at the Stern School of Business, New York University. He is also a Research Associate of the National Bureau of Economic Research.

Sylla received the B.A. (1962), the M.A. (1965), and the Ph.D. (1969), all from Harvard University.


Sylla is a former editor of *The Journal of Economic History* and has served as a consultant on institutional history to such firms as Citibank and the old Chase Manhattan Bank. His current research focus is on the financial history of the United States in comparative contexts. He served as chairman of the board of trustees of the Cliometric Society, 1998-2000.

In 2000-2001, Sylla was president of the Economic History Association, the professional organization of economic historians in the United States. In 2002, he was elected trustee of the Museum of American Financial History, now the Museum of American Finance, a Smithsonian-affiliated museum in New York City that will open in new space at 48 Wall Street in 2007. Sylla recently was president (2005-06) of the Business History Conference.