

Banking in the Rothschild Era

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Milestones in the Rothschild History

- Mayer Amschel (1744-1812) born in Frankfurt's Jewish ghetto active in various trades (textiles, discounting, rare coins and antiquities) that soon get him into contact with the Elector of Hesse-Kassel (rich from mercenaries) for whom he performs financial services. From commissions and interest earned, the family business builds strong capital basis.
- M.A.'s third son Nathan leaves Frankfurt for Manchester, after success as a textile merchant, he moves into merchant banking and represents the family's interests, goes to London in 1808 – managing the Electors English investments during Napoleon's occupation, Nathan can use this capital to get started as a banker
- Napoleonic Wars as a chance: M.A. and his five itinerant sons are uniquely positioned to provide the risky services of transactions to the Wellington and allies (combination of various gold-into-paper-and-back exchanges) and financing their war debts; Napoleon's 100 days return nearly brings losses (open positions as they expected longer war) but being first to receive news from Waterloo saves the Nathan Rothschild
- Five houses established by the sons of Mayer Amschel in London (Nathan), Paris (James), Frankfurt (Amschel), Vienna (Salomon) and Naples (Carl) who form a transnational partnership based on regularly revised agreements
- In 1818 Rothschilds make the first bond issue (for Prussia) in multiple markets, denominated in a foreign currency (sterling), payment of interest at any Rothschild office and a sinking fund, effectively creating an international capital market and initiating their key role in transfer of British and French capital abroad
- After financing restoration regimes, Concert of Powers means slow business; armed peace more profitable but outright war in Europe endangers R's positions (caught on all sides of a conflict e.g. in 1871 and more so in 1914)
- Since 1820s business in North and South America as a pillar of the London house, but failure of the group to establish a house in the United States leaves lucrative market to fast-growing competitors that then take on the old continent
- Financial crises after 1830 & 1848/49 revolutions let many banks fail, but houses in Vienna and Paris can be bailed out thanks to multinational character of a still “fraternal” partnership – after crisis joint-stock banks arise as competitors
- Paris and Vienna houses enter into industrial finance in 1840s (railways), London house builds up mining empire (DeBeers, gold mines, copper,...) in 1890s and generates business from floating debt and stock of mining companies
- In 1870 London house finances Disraeli government's purchase of Suez Canal shares; in 1871 Paris and London houses organize financing of French repatriation payments to Prussia
- Due to lack of male successors Naples in 1863 and Frankfurt in 1901 dissolved. Partnership ends in 1905 as houses drift apart, stagnation in interwar years, after disaster of WW2 only slowly rebuilt: opened for non-family partners

Key features of the “Rothschild-System”

- Core business: merchant banking (bills of exchange) and government finance (bond issuance), gold and silver brokerage – not only floating for commission (*primary market*) but also speculation on exchange rate and price fluctuations (*secondary market*) – no common credit and deposit business => partly eroded by public subscription issues of bonds, increasing competition from private and joint-stock banks and more liquid markets
- During the Gold and Bimetallic monetary standards of the 19th and early 20th century, Rothschild Paris and London serve as quasi-central banks and clearing houses for balance of payments transfers of gold and silver
- Organizational innovation: “fraternal unity” as a principle allows to build a multinational banking enterprise out of family ranks and maintain it in times of crisis (diversification); capital base and business kept together by male inheritance and endogamy => middle position between the loose early modern trade and finance networks and modern banking corporations: a “family” response to the crucial issue of “institutionalizing trust” for doing business
- Rapid capital accumulation by reinvestment of profits – massive capital base (biggest bank by 1825) that by cooperation of the several houses permitted unparalleled financing operations and reduce their risk-exposure
- Family partnership system as an organizational obstacle: does not permit to promote ambitious employees on base of their merits – even though talent and interest for finance wanes over generations; and is slow in innovating (1905 still no double-entry bookkeeping); and failure to be fully present in financial centers where only “agents” were dispatched to
- Premium on first-hand and first-obtained information: own courier system, rapid and frequent correspondence between the houses (financial, political, private information), and close contacts to those close to key politicians and royals => arbitrage opportunities and insider information => partly eroded by telegraph, telephone and integrated financial markets
- To generate and retain business in their core area of government finance, the Rothschilds seek and cultivate close contacts to decision-makers in finance ministries and politicians (Elector of Hesse-Kassel, Metternich, Duke Wellington, Louis Philippe, Leopold I, Prince Albert, Cavour, Disraeli,...) with gifts, services, favors and bribes => banking as people's business (relationships are key) => partly eroded by republican/democratic transparency and accountability
- Leveraging of political relations to offer non-official channels for diplomacy and attempt to avoid general European war, in addition to their controlling for some time the market for debt issues needed to finance war