

THE IRISH CURRENCY REPORT OF 1804¹

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Introduction

May 2004 marks the 200-year anniversary of the publication of the House of Commons report of "*The Committee on the Circulating Paper, the Specie, and the Current Coin of Ireland*"². The report of this committee – the 1804 Report – has rightly been hailed by economic historians as "... a milestone in the history of monetary theory"³. The significance of this report has, however, been overshadowed by the Bullion Report of 1810. It addressed essentially similar issues, and indeed cites with approval significant tracts of the Irish Report and was produced by a committee which contained some of the most influential members of the Irish Currency Committee of 1804⁴. The Bullion report probably assumed iconic status for the modern equivalent of bullionists, namely, monetarists, by the pivotal involvement of the great economist David Ricardo in its deliberations.

The decade preceding the publication of the Irish Report was an eventful one, both for Ireland and Britain. Witness Britain's declaration of war on France in 1793, the resulting alarms about a French invasion, the growing pressure for political and social rights, the insurrection of 1798 in Ireland and finally the move to the union of Ireland and Britain. It was also an eventful decade for the Irish economy. The integration of the Irish and British economies had proceeded through the eighteenth century; by 1800, over 80% of Ireland's trade was with Britain and Ireland accounted for over 10% of Britain's trade⁵. A period in which Irish government revenue and expenditure were in balance and the national debt under control was followed by one in which, from 1793 onwards, the deficit and the debt expanded at an unprecedented rate. Ireland had its own currency,

² Fetter, F.W., 1955, *The Irish Pound, 1797-1826*, Allen and Unwin, London.

³O' Grada, C., 1991, "Reassessing the Irish Pound Report of 1804", *Oxford Bulletin of Economic Research*, 43,(1): 5-19, p. 17.

⁴Fetter, *ibid.*, p. 5.

⁵ The information on trade is taken from L.M. Cullen *Anglo-Irish Trade 1660-1800*, Manchester, 1968, Chapters 3 and 4.

whose exchange rate with respect to the English currency was fixed at a discount of 8.33% for much of the eighteenth century. However, the final years of the 1790s were the start of a period of over twenty five years in which the Irish pound effectively floated against Sterling. From 1797, the Irish currency entered a period of unusual volatility and by the end of 1803 it had depreciated by 10%, to be at a discount of over 18% against Sterling.

This episode is referred to by historians as the Restriction Period because it coincides with the Bank Restriction Orders of February and March 1797 which restricted both the Bank of England and Ireland from paying “specie” (that is, gold and silver) on demand for their paper currency⁶.

The proximate reasons for the enactment of these orders can briefly be told. In August 1795, France returned to the gold standard, causing a major outflow from London. As it managed to do in earlier turbulent episodes in the 1790's, the Bank of England survived. Although gold flowed back to London in 1796, increasing political tension and fear of a French invasion eventually, early in 1797, triggered a financial panic in Britain. To intensify it, the French actually landed a small number of troops in Wales on February 25, 1797; they didn't attempt to fight and were taken prisoner immediately, but the damage was done. Gold payments were suspended on February 26, 1797. The period of “Bank Restriction” thus commenced.

The issues which arose from this episode were to have profound implications for the understanding of a number of economic phenomena which still have a resonance to the present day. The focus for the debate that ensued was the factors which were behind the depreciation of the Irish currency in the years immediately after the Restriction and this issue was the chief concern of the parliamentary committee which was established in March 1804. The lessons of the Restriction Period and the enduring legacy of the 1804 Report are to be found not so much in the events themselves as in the insights which deliberation on these events gave, and continues to give, to two interrelated

⁶The British Restriction became law on May 3 1797 and the Irish Restriction was enacted by the Irish Parliament on July 3 1797 (Fetter, *ibid.*, p. 5).

monetary questions:

- the process of paper money creation and constraints on this process; and
- the relationship between relative money growth between two countries and the course of the exchange rate between the same countries.

The paper is organised as follows. We first examine the fiscal policy context and especially the Irish Government's demand for funds in the years preceding and overlapping the Restriction. The relationship between the Government and its Banker, the Bank of Ireland is next discussed. We then proceed to consider note issues in Ireland prior to 1797. We then examine note issues during the Restriction period and the role of the Bank of Ireland in the overall expansion of notes that occurred. The relationship between the relative expansion of notes and the depreciation of the Irish Pound relative to Sterling is next considered. We conclude the paper by looking at the performance of the currency in the years following the publication of the Report.

The Public Finances and the National Debt⁷

Throughout the eighteenth century, both British and Irish governments raised loans by means of conventional government fixed interest debentures and annuities, but also through "lottery loans". These loans involved a combination of conventional loan and a lottery, in which subscribers received lottery tickets. Lottery prizes were often paid in debentures.

In the early 1780's, during the years of the war with the United States, the Irish government ran deficits: the deficit in 1782/3 was almost 16% of total expenditure and in the following two years it averaged 12% of expenditure. Retrenchment followed; in fact, in 1787, with a view to reducing the interest cost of the national debt, the government set out to raise £500,000 by the following means: £200,000 in 3.25% Debentures (2,000 at £100 each); £100,000 in Treasury Bills at 2.5d per day (1,000 at £100); £200,000 by the sale of 40,000 lottery tickets at £5 each, in respect of which a

⁷ The permanent debt of Ireland began in 1716, with a £50,000 loan at 8%. It was added to in subsequent years, but a period of debt repayments reduced it to £5,300 (£4,892-6-1 sterling) by 1760. It then resumed its growth.

special series of £200,000 debentures would be issued as prizes⁸. The tickets could only be sold at licensed lottery offices. A licence cost £100; to obtain one, the licensee also had to take up at least 100 lottery tickets at a cost £500 and subscribe for a corresponding proportion of the debentures and treasury bills. The cost was thus £1250 plus the cost of the licence, £1350 in all. These lottery tickets could be sold in Britain, except within the Universities of Oxford and Cambridge. The scheme was, to quote Hall⁹, "an outstanding success ... In fact, this lottery appealed so strongly to the sporting instincts of the people that the tickets were sold at £6-10-0 each".¹⁰ The finances were much more under control up to 1793; the financial year 1792-3 witnessed a small surplus. At the end of that year the national debt stood at £2,252,577, slightly less than it had been six years earlier. Debt charges were less than 10% of total expenditure.

In general, in the second half of the eighteenth century both Irish and British governments experienced little difficulty raising funds. After 1793, however, more than the sporting instincts of the people were required to raise the large sums the Irish government needed. Britain's declaration of war on France was to change the state of the public finances and the level of the debt beyond recognition. In the next seven years, expenditure rose by a factor of more than five, mainly due to military and naval expenditure, but revenue rose by a factor of only 2.25. Figure 1¹¹ shows how the public finances deteriorated, exactly in tandem with the rise of military and naval expenditure. The result was a rapidly growing national debt, as shown in Figure 2¹².

[Figures 1 and 2 about here]

⁸. See Hall, The Bank of Ireland 1783-1946, Hodges Figgis, Dublin and Blackwell, Oxford, 1949, p.60.

⁹. Hall, op.cit.

¹⁰ There is ample evidence of the popularity of lotteries in this period among people of all income levels. Lottery tickets were expensive; to meet demand for participation by the less wealthy, lotteries were run on the results of the State Lottery - an early example of a financial derivative. In fact, there were wholesale breaches of the Lottery Acts whose main purpose was to effect a state monopoly of lotteries. Interest in lotteries went even further, if contemporary accounts are to be believed; a few examples from a London writer in 1772 illustrates the point:

"... lottery tailors,...,lottery tea merchants, lottery barbers (where a man for being shaved and paying 3d stood a chance of receiving £10),...lottery eating houses (where for sixpence a plate of meat and a chance of sixty guineas was given),...and, to complete a catalogue which speaks volumes, at a sausage stall in a narrow alley was the important intimation written up that for one farthing's worth of sausages the fortunate purchaser might realise a fortune of five shillings".

¹¹ Royal Commission on Financial Relations Between Great Britain and Ireland, Minutes of Evidence to 28th March 1895, London, 1895, C-7220-I, Appendix I, B, Tables II, IV, pp.369-372.

¹² Royal Commission, op. cit., Appendix I, C, Table II, p.380.

Between March 1793 and March 1796, the debt had risen to £5.577 million; by March 1798 it exceeded £10.135 million; two years later it had more than doubled to £23.101 million, more than ten times its level seven years previously. By the beginning of 1804, it was £38.65 million and continuing to increase rapidly.

The obvious question raised by this debt explosion is that of funding: how and where did the government raise the money?

The Government and the Bank of Ireland

It was after 1793 that relations between the government and the Bank of Ireland moved to centre stage. The Bank of Ireland was established in 1783 as the first incorporated bank in the country. The Bank's charter was similar in many respects of the Bank of England's, which had been founded in 1694, but there were crucial differences, especially in relation to the power to issue of notes, which are discussed below.

At this point it's useful to present a brief account of the monetary background to the events of the late 1790's. As already mentioned, the exchange rate between the Irish and British pounds was that the IR£ was at 8.33% discount to Sterling. Thus an exchange quote of 8.33 represented par; a rate of, say, 6 implied appreciation of IR£, 12 represented depreciation of IR£. Bank notes were convertible into gold at the Bank of Ireland and the Bank of England. The transactions costs of gold transfers between Dublin and London were £1 1s.8d. per £100, approximately 1.08%. In the 1780's there was a strong demand for gold in Ireland though its precise cause is not clear. Further, there was a seasonal factor in gold demand; it peaked between March 25 and June 25 i.e. in the second quarter. The Bank of Ireland held 20% of its current liabilities in gold in second quarter and 16.67% for rest of year. These compare to 10% in purely commercial banks and 40% (later reduced to 33.33%) in the Bank of England. The gold ratios were adjusted through the year by selling Treasury Bills when demand for specie was high and buying them when demand for specie was lower, that is, by open market operations. The consequence of the big increase in gold in circulation was a big increase in quantity of "light coins" - due to the clipping and sweating of coins. "By 1787 the quantity of light coins in circulation had become so extensive as to constitute a

national problem”¹³. (p74). The Bank of Ireland refused to accept light coins at full value from Revenue Collectors despite strong Government requests, an early example of government pressuring the Bank to do its bidding. Hall cites a case in which 996 guineas were sent to the Bank by the Revenue Collectors of Newry and Drogheda; 832 were found to be of standard weight and accepted but 164 (16%) were light and returned. Copper coinage was seriously debased; there was extensive counterfeiting. The reason was an inadequate supply of coins.

There was a lull in the importation of gold from London to Dublin from November 1786 to 1788. Importation resumed in May 1789 and its volume was influenced by how the Irish pound stood on the exchange. When the exchange was at 7, that is, the IR£ at a premium, bullion was imported to Dublin. In September 1789 the exchange was at 7.25, which was effective par given transactions costs of 1.083%; bullion transactions were no longer profitable at this rate and dried up. This episode shows the ability and willingness of the financial institutions of the time to engage in arbitrage where the opportunity arose.

From 1793, as government borrowing began to mount, the public's willingness to lend to the government declined. In 1794, the government was able to sell 5% Debentures at par but gradually it was forced to offer 5% debt at a discount and to add annuities to the interest already payable. In 1795, annuities were added to the interest; by 1798, 5% debentures were being issued at 63 and in 1799 they were issued at 61. It had become very expensive to borrow.

Not surprisingly, as its reputation with the public deteriorated, the government first turned to the Bank of Ireland. The question of the government borrowing from the Bank of Ireland began to be addressed in 1793, when a regulation apparently prohibiting the Bank from lending to government without parliamentary approval was encountered. Legal advice was sought which cleared the obstacle and in July 1793 the Bank made a loan of £350,000 in exchange for a mixture of debentures and treasury bills. In August a further £170,000 was advanced under similar terms. The Government was back in June 1794 and got £700,000 repayable in two months; in December 1795, however, the government asked for a loan of £1 million, which apparently shocked the Bank and it refused to comply. Instead it agreed to the rescheduling of debt repayments that were

¹³. See Hall, *op. cit.*, p. 74.

due early in 1796. Government pressure on the Bank remained through the year; the Bank's resolve to resist the pressure showed real signs of strengthening when on 26 February 1797, the Bank of England was relieved from the obligation of redeeming its notes in specie through the enactment of the Bank Restriction Orders of February and March, 1797.

The Irish Government reaction was interesting; to quote Hall¹⁴, "The Irish Government did not realise the dangers of the new situation and appeared to regard the incident as an opportunity for relieving the public finances by inflationary borrowing". Alternatively, it understood the situation only too well! Immediately the Bank of Ireland was invited to issue £1 million in notes to the government in return for government paper; the Bank refused.

The other source of funds embraced by the Irish government was the London market. In 1798, the Irish Government began to raise loans in London. Almost immediately London became its dominant source of borrowed funds. By the end of 1800, half of Ireland's outstanding National Debt had been funded in Britain, when three years earlier none of it had been (Figure 2). The idea of foreign borrowing took root quickly. The combination of pressure on the Bank of Ireland to issue notes to the government and the amount of foreign borrowing being undertaken in London made almost inevitable a significant expansion of the Bank's note issue. This is examined in detail below.

Banking and Paper Notes in Ireland before 1797

Ireland evolved from a predominantly barter economy to a "specie"-based system of exchange in the wake of the English invasions. But for some unclear reason the Irish pound was traditionally less valuable than the British pound and it required, as we've noted earlier, 13 Irish pounds to exchange for 12 British pounds. This premium of about 8.33% for the British pound was apparently established by a proclamation of 1737^{15 16}.

¹⁴. See Hall, op. cit., pp. 64-5.

¹⁵Fetter, *ibid.*, p. 10.

¹⁶O'Brien, G. 1927, "The last years of the Irish currency", *The Economic Journal*, 1(2): 249-258, p. 250.

Money creation is synonymous with the emergence of paper money. The south of Ireland enthusiastically took to the banking business and the printing of paper money. Louis Cullen has suggested that Ireland and Scotland were the two leading centres in the development of banking in the early eighteenth century¹⁷. Cullen also points out that Ireland provided a leading innovative thinker on banking and monetary matters in the person of Richard Cantillon - the colourful banker from Ballyheigue in Co. Kerry - who was to make such a mark in the banking world of Louis XIV's France¹⁸. By the 1720s notes were in widespread use not just in Dublin but throughout the south of Ireland. A writer of the period remarked that "... were it not for bankers' notes which we have been passing in good plenty, it would be impossible to manage our domestic affairs half as well as we do"¹⁹.

By 1752 Irish note circulation was double or probably treble the level of the 1720s²⁰. Around this period Cullen reckons that the value of note circulation was about equal to that of precious metals. This was the heyday of the involvement of merchants in banking and a period of rapid expansion in trade and commerce. Up to this period banking was the preserve of the landed classes whose rents provided a burgeoning capital base for the propagation of paper money. Following an act of 1756 merchants were effectively shut out from banking activity and were not to appear prominently again until the *Restriction Period*. With the gentry-backed banks now in the ascendancy again their more conservative disposition put a brake on the creation of paper money so much so that by 1797, the year of the *Restriction*, notes were only about one fourth of the circulation of precious metals.

Curiously enough the northern part of Ireland exhibited a distinct distaste for paper money and it was not until 1808 that a bank was set up in Belfast and notes emerged. Cullen suggests that the preference of northern landlords to be paid their rents in gold

¹⁷Cullen, L., 1984, "Landlords, bankers and merchants: the early Irish banking world, 1700-1820" in A.E. Murphy (ed.) Economists and the Irish Economy, Irish Academic Press, Dublin.

¹⁸Murphy, A.E., 1984, "Richard Cantillon - an Irish Banker in Paris" in A.E. Murphy (ed.), Economists and the Irish Economy, Irish Academic Press, Dublin.

¹⁹Cited by Cullen, *ibid.*, p. 28.

²⁰Cullen, *ibid.*, p. 29.

was a factor and it also seems likely that the more pervasive influence of manufacturing industry at that time in the south had a bearing²¹. This activity could only advance with the aid of credit creation which ironically was provided by the landed-interest banks of Dublin and the other cities.

The powers and range of competence of the Bank of Ireland differed from those of the Bank of England in crucial respects which were to have important ramifications for the events which took place in the early years of the *Restriction*. The most important factor was that it did not enjoy a monopoly of note issue in its charter and had not established one even in Dublin in its brief 15 year existence up to the abandonment of the gold standard.

Money Creation in Ireland During the Restriction

The creation of the Bank of England in 1694 marked the beginnings of the modern central banking system. With the establishment of the Bank and its successful efforts to monopolise the issue of paper notes in the London area throughout the eighteenth century Britain and Ireland were effectively on a gold standard during this period. The Bank did not possess the full panoply of powers to eliminate bank failures but its operation certainly minimised their occurrence.

The Restriction Act was foisted upon Grattan's parliament without on the surface, at least, there being the same "specie" problem in Ireland as in Britain. However, the outward impression of calm concealed a very deep concern among the Irish Treasury and the Bank of Ireland of impending crisis. The ink was not dry on the legislation when the Bank were informing the public " ... that the situation of the Bank is strong and its affairs in the most prosperous situation ... " ²². But as recently as December the Bank of Ireland were telling the Treasury that they expected a "run" early in the New Year²³. In an effort to subvert the crisis the Bank had resorted to a credit squeeze which severely impaired commerce and would no doubt have irked government. Then as now

²¹Cullen, *ibid.*, pp. 39-40.

²²Cited by Mc Cavery, T., 1981, Finance and Politics in Ireland, unpublished Ph. D. dissertation, Queen's University Belfast, p. 312.

²³Mc Cavery, *ibid.*, p. 312.

public protestations by the authorities on the absence of monetary crises frequently turn out to be no more than wishful thinking.

The reality probably was that given the Bank of Ireland's dependence on its sister bank for "specie" in times of crisis, the Irish banking system could not have maintained convertibility for very long even if the Restriction had not been mandatory in Ireland²⁴.

It was Francis Bacon who wrote that "... money is like muck, not good except it be spread" and spread it certainly was in the early years of the Restriction. Reliable data on note issues during this period are only available for the Bank of Ireland. The data are depicted in Figure 3²⁵ for quarterly circulation for the full period 1797-1826. The data comprise ordinary banknotes but exclude what were known as "post bills". These were effectively post-dated cheques²⁶ and were introduced to counteract the robbery of cash in transit. These bills were only valid in exchange seven days after being sent from Dublin²⁷. If the consignment were robbed the bills would simply be cancelled. They were quite significant in Ireland, and in the first six years of the Restriction they amounted on occasion to a third of the total note issue. Their importance is perhaps a testimony to the hazards of the transport and communication system of the time.

[Figure 3 about here]

The scale of expansion of paper money by the Bank of Ireland was staggering, especially in comparison with the Bank of England, notwithstanding the fact that an unknown proportion of these additional notes would have simply replaced "specie"²⁸. Between 1797 and 1804-05 the circulation of Irish notes increased by about 400% in contrast to 50% for the Bank of England. From these years to the end of the Restriction the growth in paper money was evidently much more modest.

²⁴Fetter, *ibid.*, p. 13.

²⁵ Hall, R.G., 1948, The Bank of Ireland, 1783-1946, Hodges Figgis, Dublin and Blackwell, Oxford, Appendix E and House of Commons, 1832, Report of the Committee of Secrecy on the Bank of England Charter, Appendix No. 82.

²⁶O'Grada, C., 1993, "The Irish paper pound of 1797-1820: some cliometrics of the Bullionist debate", Oxford Economic Papers, 45: 148-156, p. 154.

²⁷ Hall, R.G., *ibid.*, p. 55.

²⁸O'Grada., C., 1993, p. 155.

In the wake of the Restriction it would indeed have been perverse if the Bank of Ireland had not increased its money supply since the objective of the government in abandoning the gold standard was of course to loosen up the credit creation process. While the Bank of Ireland were undoubtedly not adverse to making a profit out of the situation, Mc Cavery's conclusion seems reasonable that the Bank "... were by no means reckless in the issue of their notes" and were put under intense pressure to accede to the government's intense demand for funds²⁹.

The real problem of note issue in the wake of the Restriction was the activity of the private banks and the medley of houses which acted as *de facto* banks. Unlike the Bank of Ireland we do not have accurate information on the extent to which this motley body of institutions added to the *total* supply of paper money in the country. What evidence there is points to a substantial increase in money creation from this source. Fetter suggests that paper money produced by private banks (excluding I.O.U.s) could have increased from about £2 million on the eve of the Restriction to £6 million by 1803. This three-fold increase may well be an underestimate as the 1804 Report suggested that the number of private banks had grown from under a dozen in 1797 to between 40 and 50 by 1803-04³⁰. While there are certain doubts about the accuracy of the latter numbers the conditions were ripe for rapid expansion of the banking business and especially the lucrative activity of note issue. Basically "... anyone who enjoyed a modest degree of trust in the community, however meagre his assets, could become a banker"³¹.

The anecdotal evidence on the monetary expansion of the period is more evocative. For several years before the Restriction there had been an acute shortage of small coins in Ireland and this problem was exacerbated by the Restriction. As noted above, such coins which did circulate were so debased and clipped as to be worth only a fraction of their intrinsic value. It was reported in 1798 that shillings and sixpences were

²⁹Mc Cavery, *ibid.*, pp. 314-316.

³⁰This estimate is repeated by Mc Cavery, *ibid.*, p. 317 but is considered suspect by Hall, *ibid.*, p. 119 and O'Grada, 1991, *ibid.*, p. 12.

³¹Fitzpatrick, A.J., 1975, Economic Effects of the Revolutionary Wars in Ireland, unpublished Ph. D. dissertation, Manchester University; cited by Mc Cavery, *ibid.*, p. 317.

25% and 38% respectively of their legal weight³². With the Restriction the shortage of coin became more acute as gold and silver were shipped to Belfast and London to fetch higher prices. Speculation about the war and perhaps the potential for a much devalued paper money stock encouraged hoarding of precious metals and served to support the adage that “bad money drives out good”. An Irish official summed up the phenomenon by stating that “ ... the terror of invasion set the misers and old women ... to make up their purses...”³³.

The shortage of small coins encouraged the issue of small denomination notes and early in the Restriction so-called “silver notes” began to appear. These were supposedly redeemable in silver but they “ ... all too frequently appear to have been inconvertible even in terms of the debased silver coin”³⁴. As well as these notes of dubious value, unlicensed traders began issuing I.O.U.s which were supposedly redeemable in goods. Naturally it was also a field day for forgeries of counterfeit notes and silver coin.

An anonymous pamphleteer of the period, writing under the beguiling *nom de plume* of the “Candid Cobler” probably gave an accurate picture of the nature of the money supply in circulation in the early 1800s when he wrote:

“This medium in three provinces (with the exception of the metropolis) at this moment consists of a very moderate quantity of National Bank paper; a much larger amount of Dublin private bank paper; an incalculable influx of country coinage in paper, for gold and silver; and an accumulated mass of counterfeit silver and copper, base beyond sufferance, description or example”³⁵.

The “Candid Cobler” was also prophetic in his speculation on where this orgy of money creation would lead when he wrote:

“ ... breweries, distilleries, flour mills, even chandlery - have their paper issues, (not tokens to pay their workmen) but banking notes unstamped, to extend their credit and create capital:- how this may end, Heaven knows! but it of more immediate consequence to us individually, than the price of Bullion, or the

³²Lord Liverpool, 1805, A Treatise on the Coins of the Realm, London; as cited by Fetter, *ibid.*, p. 16.

³³Camden (the Lord Lieutenant) and Cooke (the Civil Under-Secretary), as cited by Mc Cavery, *ibid.*, p. 310.

³⁴Fetter, *ibid.*, pp. 17-18.

³⁵Cited by Fetter, *ibid.*, pp. 35-36.

exchange to Hamburg. We are at this moment arrived at the period of abuse in coinage that articles in detail (if they do not form an aggregate nearly to a pound note) cannot be purchased; for the trader will not accept the coin tendered, nor the consumer the change offered; ... ”³⁶.

Matters came to a head at the end of March 1804 when the Post Office refused to accept counterfeit currency and retail trade came to a virtual standstill. There were real fears of severe deprivation for the mass of the population if some redress were not attempted. Bowing to fierce pressure the government relented by mid-April and a number of steps were taken to remedy the situation. Official agencies were encouraged to be less rigid in their acceptance of currency. The Bank of Ireland, among other expedients, to ease the crisis also issued Spanish dollars and half dollars which were over-stamped with the head of King George III. These were procured from a store of plundered gold in the vaults of the Bank of England. A contemporary poet, of some wit, remarked of the Bank of England's action that:

“The Bank, to make their Spanish dollars pass,
Stamped the head of a fool on the neck of an ass”³⁷.

The measures adopted seemed to resolve the small coin problem and the government's attention now switched to the value of the exchange rate.

The Bank of Ireland and the Total Note Issue

That the abandonment of convertibility of paper money into “specie” should lead to a substantial advance in the total money supply cannot be in doubt. Much the same events occurred in the American colonies in the wake of the many attempts to set up a durable central banking institution³⁸. The really difficult problem which the 1804 Currency Committee attempted to clarify was the role of the Bank of Ireland's note issue in relation to the *total* money supply. In other words, what, if any, was the relationship between the Bank's note expansion and the note expansion of the private banks and other credit-creation institutions? Here the Committee was wading through uncharted theoretical waters.

³⁶Cited by Fetter, *ibid.*, p. 48.

³⁷Cited by Galbraith, J.K., 1975, Money: Whence it Came, Where it Went, Penguin, New York, p. 45.

³⁸Galbraith, *op. cit.* , Chapters 7 and 8.

As noted already the Bank of Ireland did not operate in the same way as a modern Central Bank. It was first and foremost a private institution responsible to its shareholders, notwithstanding the obligations it had to the state given its charter. But the crucial distinction between the Bank of Ireland of the time and a modern Central Bank was that it did not have the sole monopoly in the issue of currency in Dublin, let alone the rest of the country. In this respect the Bank of Ireland was in a much weaker position than the Bank of England as Henry Thornton, a member of the 1804 Committee, remarked:

“There was a material difference ... between the banks of England and Ireland: In Ireland there was no bank that took upon itself to manage and regulate the circulation of the country; whereas in England it was perfectly well known, that the Bank commanded the whole paper circulation of the metropolis, and regulated that of the kingdom”³⁹.

In the pre-Restriction period all banks had to back their note issues with gold. If the Bank of Ireland enjoyed the influence of the Bank of England one would expect private banks to be equally content to hold Bank of Ireland paper as reserves. After the Restriction the constraint on note issue was now considerably more lax but that did not of course mean that banks would create money with abandon. Prudent banks would wish to main sufficient reserves to prevent a “run” on their institutions. However, given the relatively short life of the Bank of Ireland at the time of the Restriction it does not appear to have lead to a situation where its notes were universally acceptable as a reserve stock throughout the country. As Fetter writes “ ... Bank of Ireland notes might serve as a means of payment, or as bank reserves, depending on the customs of the community”⁴⁰. The Restriction can only have served to make the situation even more unclear.

The Bank of Ireland denied that it had a reserve role and by implication its note issues, in its view, could thus bear no relationship to the issues of the private note-issuing establishments. The Bank's witness before the Committee, Jeremiah D'Olier, who was a former governor, went so far as to suggest that private bank issues would actually

³⁹Cited by Fetter, *ibid.*, p.12.

⁴⁰Fetter, *ibid.*, p. 37.

offset any change in the note issue of the Bank of Ireland⁴¹!

Unfortunately there is no hard evidence available on the *total* money supply to enable clear conclusions to be drawn. If the Bank did perform a reserve function for the private banks then the change in the note issue of the latter would be proportional to the Bank's. In the absence of a reserve role, and given the circumstances of the Restriction, our hunch is that the increase in the note issue of the private banks was proportionately much greater than the growth in the paper creations of the Bank of Ireland.

The Money Supply and the Exchange Rate

The foundations of much of our modern understanding of exchange rate fluctuations can arguably be traced to the Irish Currency Report of 1804. Since the early part of the eighteenth century the Irish pound exchanged at a fairly constant discount of 8.33% against the British pound. Then when writers referred to the exchange rate being at "par" they did not imply a one-for-one relationship as was the case from 1826 to 1979. We should also note that since Ireland and Great Britain operated under a common jurisdiction it was natural to refer to the exchange rate quoted in Dublin as the units of Irish currency per unit of British currency. Thus a rise in the exchange rate above its "par" value implied a depreciation and a fall an appreciation. In passing, we might note that nowadays we usually quote the exchange rate in Dublin as units of British pounds per unit Irish and thus a depreciation is, perhaps more naturally, represented as a fall in the exchange rate and an appreciation as a rise in its value.

Fortunately there are extensive data on the exchange rate during the Restriction Period. Data for quarterly readings are plotted in Figure 4⁴². Recalling that a rise in the value implies a depreciation and a fall an appreciation, we can divide the experience of the Restriction into three periods. The period 1797 to 1803 witnessed a substantial depreciation of the Irish pound of almost 10% and it was this event which led to the establishment of the parliamentary committee. The period 1804 to 1815 was a period of relatively stability when the exchange rate hovered around its pre-Restriction "par" level. The final period, up to the assimilation of the two pounds, was again marked by a depreciation of the Irish pound but on a somewhat lower scale than the earlier

⁴¹Fetter, *ibid.*, p. 39.

⁴² Course of the Exchange, Goldsmith Library, University of London Library.

depreciation. For the period as a whole the trading range was from 91.4 pence British to 104 pence British when we calculate the “par” of the exchange at unity.

[Figure 4 about here]

An interesting footnote to the course of the exchange rate quoted in Dublin was that the rate quoted in Belfast and Newry did not depreciate *vis-a-vis* the British pound⁴³. In fact in Newry, only 60 miles from Dublin, two exchange rates were quoted; one for paper - basically Dublin paper - and one for “specie” and naturally paper was at a substantial discount to “specie”⁴⁴. As noted earlier, paper effectively did not circulate in the North of the country and its depreciation relative to “specie” was proof to many that a monetary explanation lay at the root of the depreciation.

The main purpose in setting up the Irish Currency Committee was to inquire into the causes of the fluctuations in the exchange rate up to 1804. Little interest was shown in the behaviour of the rate up until this year. This may simply have been due to the fact that such an event would only be of interest to a tiny minority of the population at the time. We have noted that the small coin situation caused more widespread concern. Moreover there were gainers and losers from the depreciation and this, as now, modulated the political response. Those effected were firstly absentee landlords who had to convert their Irish pound denominated rents into British pounds upon remission to London. Also merchant importers from Great Britain would suffer competitiveness' losses. We might add that resident landlords, especially those who were high consumers of wine, were hardly much worse off as a consequence of the depreciation than the absentees! However, exporters and thereby farmers naturally benefited from the rise in the exchange. An interesting footnote to the saga of gainers and losers was

⁴³O'Brien, *ibid.*, p. 254.

⁴⁴For 1803 and the first quarter of 1804 the quotes were as follows:

Exchange rates in Newry (% above parity)

	Highest	Lowest
1803	Specie 9	5
	Paper 17.5	12.75
1804(Q.1)	Specie 8	5.25
	Paper 17.5	14.75

Source: Irish Currency Report as cited by Hall, *ibid.*, p. 85.

that Irish treasury officials, whose salaries were denominated in Irish pounds, received payment in British pounds at the pre-Restriction exchange rate. The revelation of this fact in the House of Commons caused some embarrassment for the government and may have provided the final political push for the establishment of the Committee⁴⁵.

The question which exercised the Committee was of course why the depreciation of the currency? The modern view on the factors which determine the medium-term evolution of the exchange rate is a useful lens with which to examine the deliberations of the 1804 Committee. A change in the exchange rate is no more than a change in a price ratio between national monies. To understand exchange rate movements we thus need to understand what causes relative movements in national prices.

Changes in relative money supplies clearly affect relative price movements since, no more than for other commodities, the greater the supply, other things equal, the less valuable the commodity. Thus a country whose money supply is growing faster than another's will tend to find its overall price level also rising faster which of course suggests that its exchange rate will be depreciating in a floating system. This might be termed the monetary approach to exchange rate determination which was championed as the main cause of the depreciation of the Irish pound by the 1804 Report.

But the modern theory would also emphasise other factors as having a role in determining the course of the exchange rate. A country whose money supply is growing relatively faster than another's need not experience relatively higher inflation if the growth rate in the goods and services it produces relative to the partner country is sufficiently high. By the same token also, a depreciation could be in part caused by a relatively higher money supply and a relatively lower output growth. Economists tend to emphasise relative money growth as being the chief culprit in high inflations and depreciations in the medium term. But in the short term factors like poor harvests, for instance, would cause price hikes and a depreciating exchange rate. Moreover, a poor harvest will raise imports above what they otherwise would be, implying a worsening balance of payments deficit which in turn will further weaken the exchange rate. Factors like these can be termed real explanations of exchange rate fluctuations. Modern theorists would also emphasise the role of uncertainty and speculation in determining short-run movements in the exchange rate.

⁴⁵Fetter, *ibid.*, pp. 27-28.

Against the background of this very brief sketch of the modern view of exchange rate determination it is interesting to consider the deliberations of the 1804 Committee. What is striking about the Report is the polarisation between the views of the Committee itself and the position adopted by the vast majority of witnesses who appeared before it. The Committee espoused the view “[t]hat this depreciation in Ireland arises almost entirely, if not solely, from an excess of Paper, appears highly probable ... ”⁴⁶. The certainty and conviction with which this view was articulated, not just in the body of the report itself but in the questioning of the Committee's witnesses, suggests a zealotry characteristic of recent converts. The Committee members were very much the “Young Turks” of the Parliament⁴⁷. They were very much a new generation of parliamentarians receptive to the theories of the relatively new discipline of economics and conversant with the writings of Adam Smith, Richard Cantillon, and especially David Hume’s “specie-flow mechanism”. As Francis Horner, who was to be the future chairman of the 1810 Bullion Committee, remarked of some of the members of the 1804 Committee:

“It is a curious proof of the degree in which Adam Smith's speculations and others of the kind are studied by the Young men in Parliament, beyond the attention that was paid to such topics by the politicians who were educated at an earlier period of the last century ... ”⁴⁸

If the members of the Committee could be accused of being too ready to embrace the monetary explanation for the depreciation, then most of the witnesses, with the exception of Robert Marshall, the *Inspector General of Imports and Exports of Ireland*, displayed either a total rejection or ignorance of any possible role for a monetary explanation. This was perhaps most apparent in the evidence of the Bank of Ireland representatives, Jeremiah D'Olier and William Colville. In this they were in agreement with the views of the Irish Treasury. The position of the latter, prior to the setting up of the Committee, was that the depreciation could be explained by real phenomena. Principally they suggested a temporary balance of payments difficulty caused in part by a rise in imports after the disruption of the rebellion of 1798 and by bad harvests which checked exports at the turn of the century. When, prior to the Committee's

⁴⁶Fetter, *ibid.*, p. 45.

⁴⁷O'Grada, 1991, p. 6.

⁴⁸Cited by Fetter, *ibid.*, p. 30.

establishment, the Bank of Ireland were accused in the House of Commons of causing the depreciation by an excessive issue of paper relative to that of the Bank of England, they privately responded to queries from the Irish Treasury that four factors could account for the depreciation:

1. the number of absentee landlords and hence their level of rent remittances had worsened since the 1798 Rebellion;
2. poor harvests in 1800 and 1801 had made Ireland a net importer of grain;
3. loans raised by the Irish Treasury in London caused a drain in interest payments; and
4. the price of coal had recently increased⁴⁹.

In other words the cause of the depreciation lay solely in adverse developments in the balance of payments.

These views were aired again in the hearings of the Committee. Colville for the Bank went as far as stating that a monetary expansion could actually cause the currency to appreciate!:

“ ... as far as the circulation of Paper went in Ireland, it had the object of keeping down the Exchange, and not raising it; the high exchange against Ireland being clearly and decidedly to be accounted for independent of the circulation of Paper at all”⁵⁰.

The strong rejection of the monetary explanation by the Bank was no doubt influenced by their belief that Ireland had experienced balance of payments difficulties since the introduction of the Restriction in 1797. However, this view was completely over-turned by the evidence presented by Robert Marshall, who it will be recalled was the Inspector General of Imports and Exports for Ireland, and his evidence suggested that, with the exception of the years 1799 and 1800, Ireland's balance of payments was in fact in surplus⁵¹. To be fair to the Bank's witnesses, however, the deficits recorded in the two exceptional years were substantial and it would have taken several years for the trade balance to turn in a surplus as great as its 1797 level⁵².

⁴⁹Mc Cavery, *ibid.*, p. 326.

⁵⁰Cited by Fetter, *ibid.*, p. 106.

⁵¹O'Grada, *ibid.*, p. 8.

⁵²O'Grada, 1991, *ibid.*, p. 9.

In attempting to draw together the strands on the debate on the currency's depreciation set out in the 1804 Report, a number of points are worth making. The Committee's view that the depreciation was due in some large measure to an excessive *total* issue of paper money relative to Great Britain seems highly plausible. However, the claim that the cause of this excessive expansion of the Irish money supply was the Bank of Ireland's own expansion of paper money “ ... rested upon general analysis rather than upon statistical evidence”⁵³.

The employment of modern statistical techniques in an attempt to discern the causes of the depreciation is not helped by the absence of separate price data for Ireland or information on British and Irish output performance. But Figure 5 appears to suggest a positive correlation between the ratio of the Bank of Ireland's note issue to the Bank of England's and the exchange rate as suggested by the Committee, at least for the first half of the Restriction Period⁵⁴. Even if this evidence is accepted, the Bank of Ireland can to a large extent be exculpated by the intense pressure they were under to provide funding to the government - a point that the Committee appeared to ignore.

[Figure 5 about here]

Finally, the Committee laid insufficient stress on real explanations for the depreciation in their zeal to champion the monetary explanation. It is unlikely, however, that balance of payments considerations would have overturned their central hypothesis.

The Exchange Rate After 1804

The fate of the 1804 Report was not too unlike its ilk today. Once completed it gathered dust with little public response by the authorities. Other matters were perhaps more pressing at the time! And with the depreciation of the British pound on the Hamburg exchange the focus switched from the Irish currency. The Bullion Committee of 1810 now took centre stage in monetary and exchange rate affairs. It will also be recalled from our chart of the exchange rate that the rate stabilised to a substantial extent between 1804 and 1812 and in fact hovered around the pre-restriction “par” of 8.33%.

⁵³Fetter, *ibid.*, p. 45.

⁵⁴More sophisticated analysis by O'Grada, 1993, *ibid.*, is less supportive of the Committee's position.

This situation would of itself have been sufficient to prevent any adverse public comment.

It would be a mistake, however, to suppose that this outcome was fortuitous. Factors which undoubtedly helped were the less liberal credit policy of the Bank of Ireland after 1803 and the outlawing of the issue of notes under £1 by the private banks in May of 1805. Also the spate of bank failures in the early years of the Restriction may have alerted the public to the adverse consequences of the Restriction. However, there is also evidence that the Irish Treasury pursued what we might term today a “managed float” strategy after 1804⁵⁵. Basically the Treasury were pursuing an exchange rate target which they believed was in the best interests of trade. When the market rate moved outside of the target area stabilisation measures were adopted by the authorities. Such a stabilisation strategy had in fact been advocated by the 1804 Committee. This strategy was based on the stabilisation scheme adopted by the Bank of Scotland to keep their pound tied to the London pound⁵⁶.

The currency depreciated significantly again between 1815 and 1819 but on this occasion there was no pressure for action unlike the earlier episode. The depreciating exchange must have seen like a godsend in the light of the collapse of agricultural prices at the time and this is probably the main reason for the absence of any public concern.

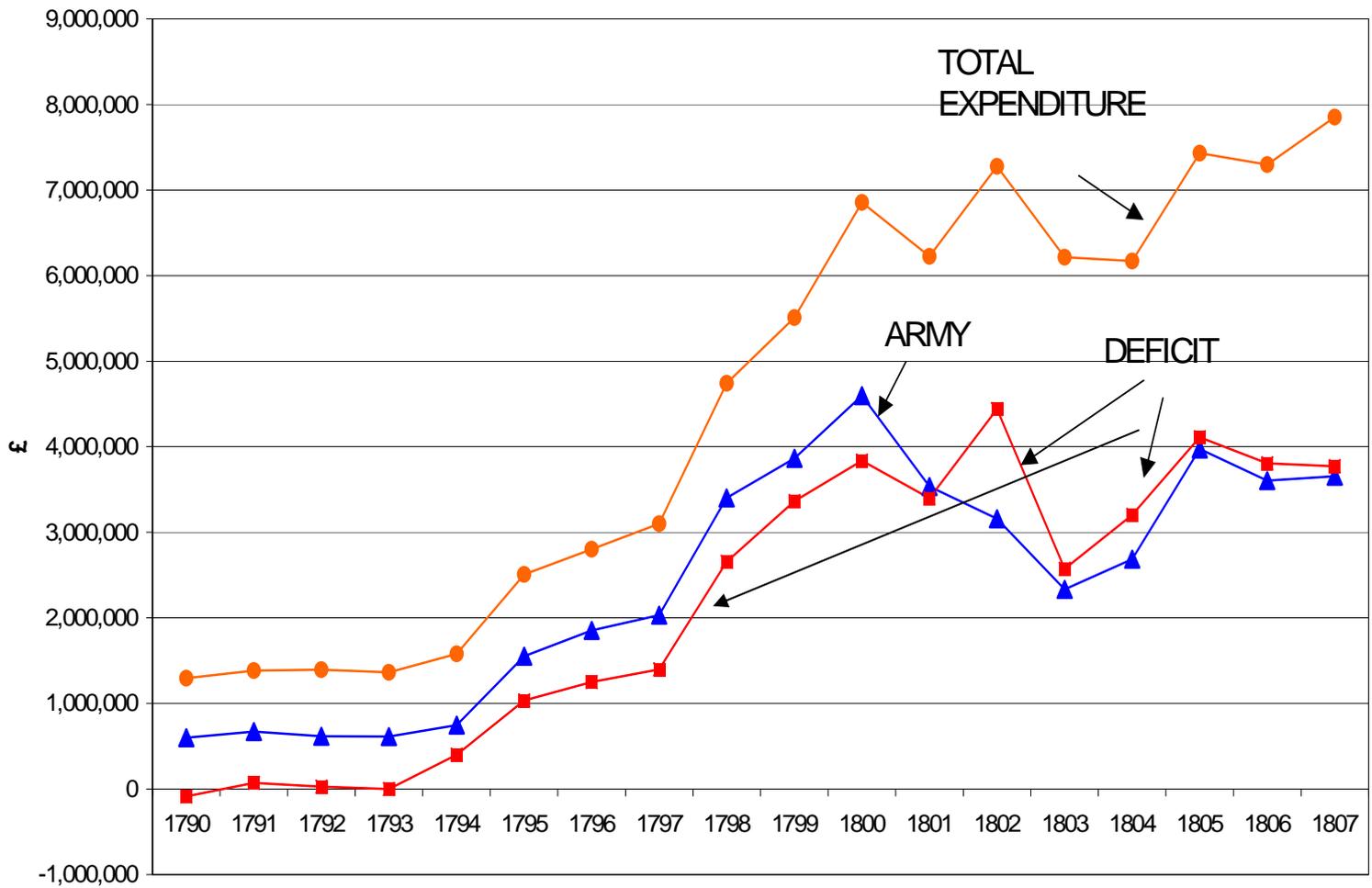
The saga of the Restriction finally ended in June of 1821, a month after the resumption of “specie” payments by the Bank of England. The last chapter of Ireland's first flirtation with a floating exchange rate was closed in January of 1826 with the assimilation of the Irish and British currencies. From then until March 1979 “ ... Ireland, as part of the United Kingdom, as a member of the British Commonwealth of nations, and as an independent Republic, ... maintained its currency at par with the British pound through the redemption in London exchange and sale of London exchange, in line with the recommendations of the Committee of 1804”⁵⁷.

⁵⁵Mc Cavery, *ibid.*, pp. 333-380.

⁵⁶Fetter, *ibid.*, pp. 42-44.

⁵⁷Fetter, *ibid.*, p. 62.

Figure 1: Ireland, Total Expenditure, Defense Expenditure and the Deficit, 1790-1807



Note: year ended March 25; from 1801, year ended January 5.

Figure 2: Ireland, Total Debt and Debt Funded in Great Britain, 1792/93 - 1806/07

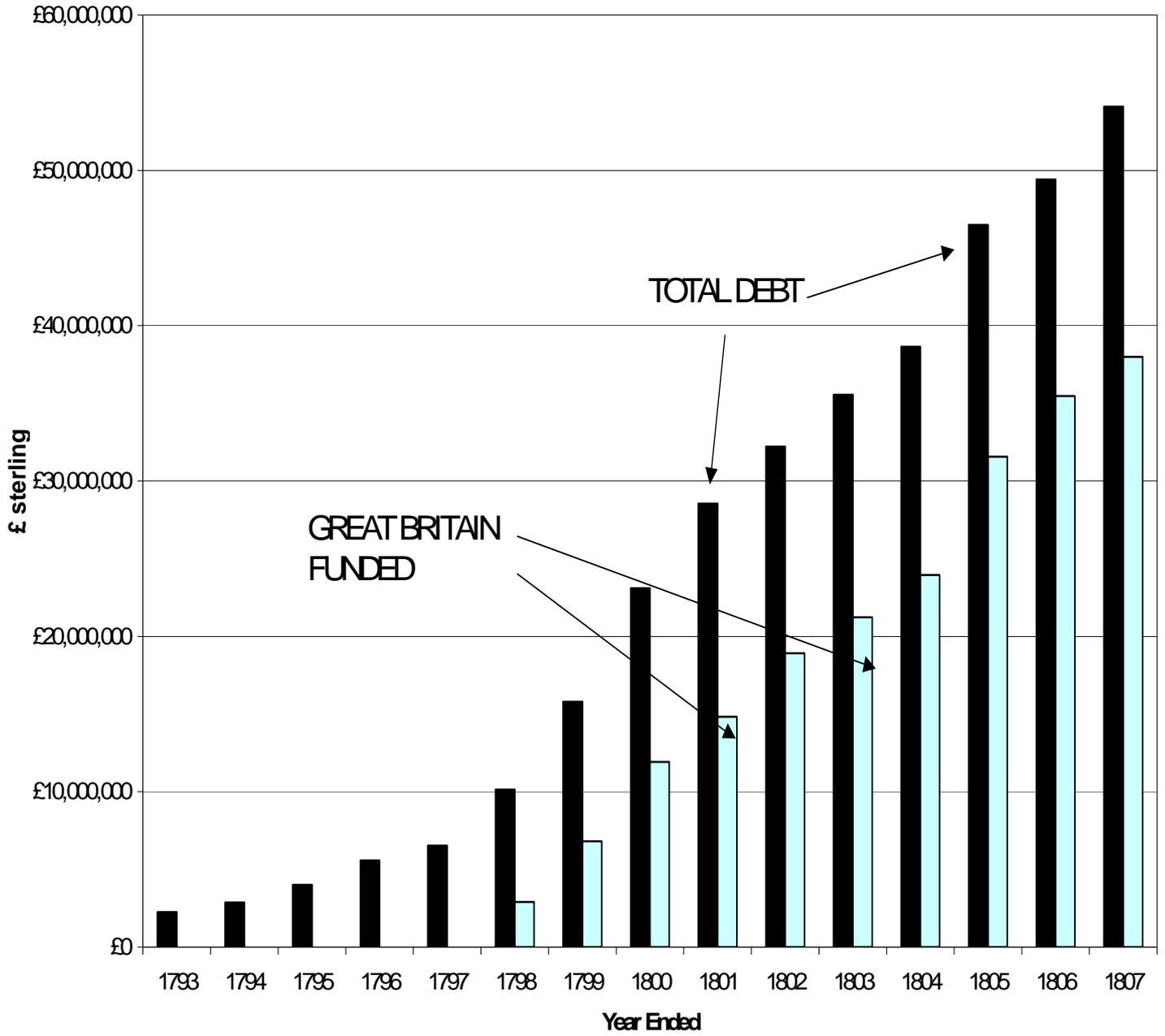


Figure 3: Irish and British Note Circulation 1793-1822, March 1793=100

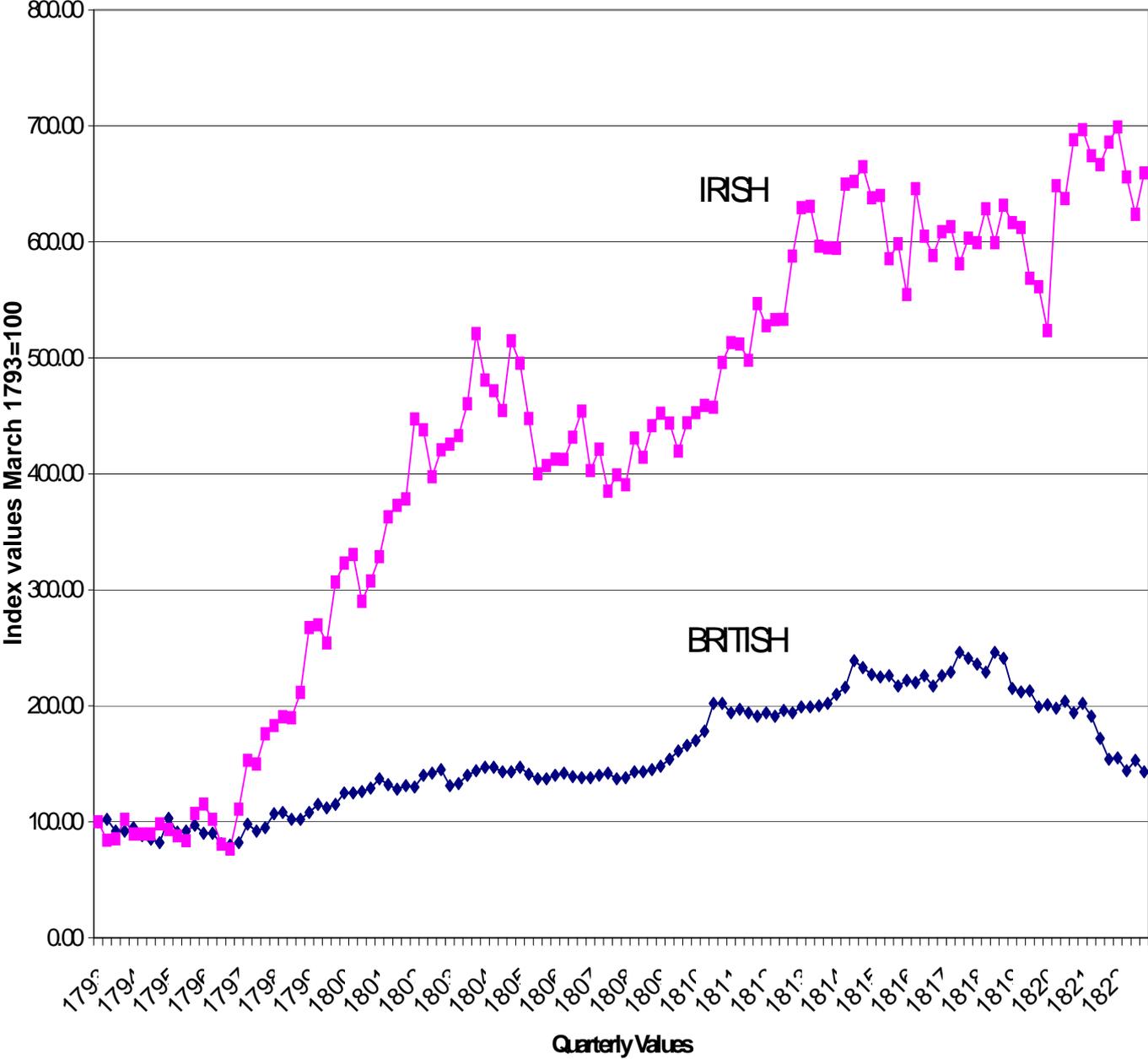


Figure 4: Irish Pound Exchange Rate 1793-1822, March 1793=100

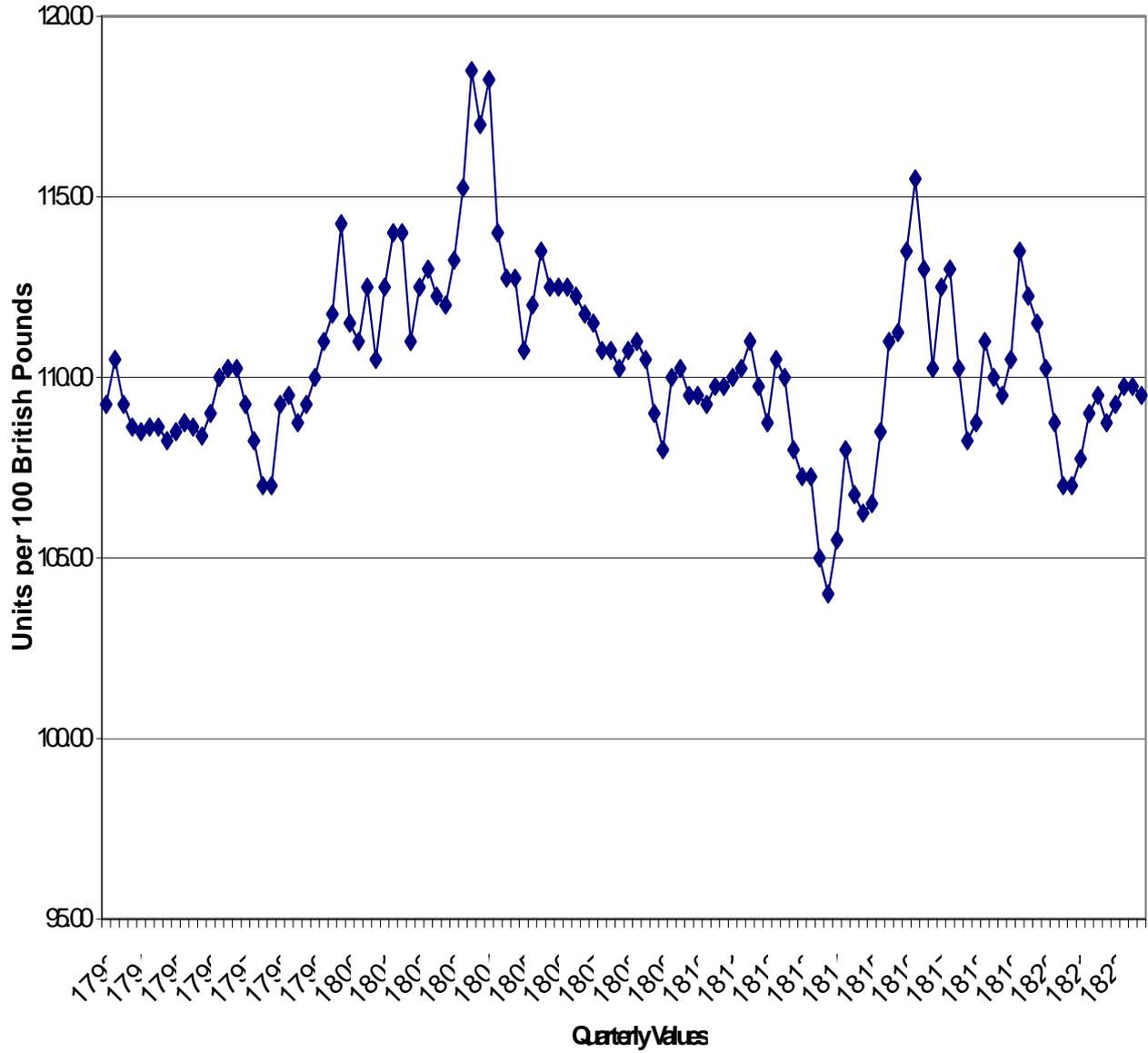


Figure 5: Exchange Rate and Note Circulation 1793-1822

