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THE BOOM THAT NEVER WAS? LATIN AMERICAN LOANS IN LONDON 1822-1825

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**THE BOOM THAT NEVER WAS?
LATIN AMERICAN LOANS IN
LONDON 1822-1825.**

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“Nor do the mines of Mexico and Peru now render the public funds of those countries more safe, than the wilds of America add to the security of those of the United States.”
Bernard Cohen *Compendium of Finance*,
London 1822, p.x.

1) The first cycle of indebtedness of the Latin American countries, which started in 1822 and ended in 1825, has attracted much attention and has given rise to an extensive polemical literature in the countries concerned, to some detailed official assessments as well as to some scholarly studies on a few specific loans. But it is only in more recent years that we have academic works where these various loans have been studied in a wider context instead of being seen only in their national setting. Three recent works deserve special mention. The first is a history of all Latin American debts from 1820 to 1930 in which the 1822-1825 episode is seen as the first chapter of a much longer story¹. The second is a detailed history of this first cycle of indebtedness clearly explained in its historical context, with a systematic exploration of the London press of the period and of the original prospectus of the loans². More recently a study by Neal³, using sophisticated statistical analysis and modern economic theory, discusses the evolution of the London financial markets and institutions; although in his work the Latin American loans of 1822-25 occupy a marginal role and are briefly discussed in order to evaluate their role in the terrible financial crisis that

¹ Carlos Marichal *A Century of Debt Crises in Latin America. From Independence to the Great Depression, 1820-1930*, Princeton, 1989.

² Frank Griffith Dawson *The First Latin American Debt Crisis. The City of London and the 1822-25 Loan Bubble*, New Haven and London, 1990.

struck London at the end of 1825, he places them in their financial context, the London money market where rates of interest had fallen. Some of the broader questions he discusses will be briefly discussed at the end of this paper.

The aim of this paper is to give some indication of the difficulties involved in ascertain some basic facts concerning these loans; it also tries to highlight the dangers of interpreting this data without great caution. In order to do this I will briefly discuss some peculiar characteristics of these loans. In recent discussions of financial crisis a growing attention has been given to the role of information; the problem will be discussed in the context of these loans. I will also give some evidence on how the London episode of 1822-25 was seen from Latin America based on periodical publications published at the time in Buenos Aires. The rest of the article will discuss how the whole episode could arise; in doing this I touch some of the questions of broader interest relating to financial crisis.

2) First it is necessary to give a few details on how the loans were issued. Great Britain had become the centre of finance only during the Napoleonic wars taking Amsterdam's place. After the Peace of 1815, the first big international financial transaction is the 1817 loan to France, conducted by Baring and Hope. It was a loan to allow France to pay war indemnities and obtain in this way the evacuation of foreign troops. An important financial innovation of this transaction is that Baring promises to pay a certain sum to France, but if the price of the bonds fetches a higher

³ Larry Neal «The Financial Crisis of 1825 and the Restructuring of the British Financial System», *Review*, Federal Reserve Bank of St.Louis, May/June 1998.

price in the market, the bankers are entitled to keep the difference.⁴ The bonds however are French *rentes*, that is, denominated in francs and payable in France. The innovation that will allow international loans to grow enormously is introduced by Rothschild in the loan to Prussia of 1818: the debt is denominated in sterling and interest payable in London and in the other important European capitals; furthermore, the loan will be repaid in a certain period with an amortisation fund. “Previous to the advent of Mr.Rothschild, foreign loans were somewhat unpopular in England, as the interest was receivable abroad, subject to the rate of exchange, liable to foreign caprice, and payable in foreign coin. He introduced the payment of the dividends in England, and fixed it in sterling money, one great cause of the success of these loans in 1825.”⁵ The exchange risk seems to vanish ; the fact that it is now easy to cash the interest on these foreign bonds makes foreign investment possible for new social groups.

In order to understand how speculation developed, it is necessary to understand how bonds and shares were sold. The first day of issue the public buys only a subscription (the word *scrip* denotes the slip of paper that documents the subscription) for a small sum, a fraction of the price of issue. Successive instalments will have to be paid at predetermined intervals. When all instalments have been paid, bonds are handed over to investors. This technique had been used for the British loans of the Napoleonic wars.

⁴ This sort of contract is xcalled “taking a loan ‘firm’”. E,Victor Morgan and W.A.Thomas *The Stock Exchange. Its History and Functions*. London 1962, p.80.

⁵ John Francis *Chronicles and Characters of the Stock Exchange*, London 1859 ,pp.298-9; Niall Ferguson, *The World’s Banker. The History of the House of Rothschild*, London, 1998, pp.132-3.

Those who buy are mostly petty professional speculators, with very little capital, called *stags*, who are really buying an option. “With huge pocket-book containing worthless scrip; with crafty countenance and cunning eye; with showy jewellery and thread-bare coat; with knavery in every curl of the lip, and villany in every thought of the heart; the stag, as he was afterwards termed was a prominent figure in the foreground.”⁶ Stags are not interested in buying the bond or share and they usually do not have the necessary capital to pay further instalments. They want to make a quick capital gain after paying an instalment. If a bond issued at 80 rises quickly to 84, those who have bought *scrip* paying the first of ten instalments, will be able to sell for 12 what they paid 8, a capital gain of 50% in a few days. If the price doesn’t rise, scrip is sold and the bond or share are at a discount, creating serious difficulties for the success of the loan. Because of this it is important to have a strong underwriter, able to support quotations while the successive instalments fall due. This was not easy, as most Latin American countries had difficulty in gaining access to first class merchant bankers. Their governments had not yet been recognised by Great Britain and often their representatives were not able to move in the fashionable London circles, not least because often they did not speak English

In order to encourage buyers after the first instalments have been paid, often full interest is paid on bonds that have not yet been fully paid. The loan contracts themselves reflected the fact that investors did not pay the whole market price immediately because they usually stipulated that the governments concerned would get their money in instalments in a certain lapse of time. Some examples: the first Mexican loan specified that the

⁶ Francis, op, cit, p262 refering to the 1824-5 episode.

money had be at the disposal of the Mexican government within one year (clause.7). The second Mexican loan, of a nominal value of £3.2 million, specified monthly payments of £200000 (clause 4); the first Peruvian loan refers to six instalments payable by the contractors to the Government.

3) It is important to start from the basic facts concerning the Latin American loans during 1822-25, although we shall see that this is not easy. First of all it is necessary to know when the loans were issued; it is also important to have an idea of the sums involved.

The first loan was issued in 1822 and the last in 1825. The first country to issue a loan was Great Colombia (that will later split into Venezuela, Colombia and Ecuador) in March 1822 for £2 million (all values are nominal), followed by Chile in May for £1 million, Peru in October (£1.2 million) and Poyais (£200.000) in the same month. There are no loans in 1823 while there are four in 1824: Brazil (£1.2 million), Buenos Ayres (£1 million), Colombia (£4.75 million), Mexico (£3.2 million). (In 1824 Peru issued £750.000, but it was part of the £1.2 million launched in 1822, which I have already included in the list for that year). In 1825, the last year of the cycle, there are four new loans: Brazil (£2 million), Mexico (£3.2 million), Central American Confederation (£163.000) and Peru (£616.000). The loans enumerated above total £20.529 million, of these nearly two thirds (64%) are accounted by just two countries, Colombia and Mexico. The total given by Neal, £43 million, is far too high; this fact however strengthens his main

conclusion that “the amount was small relative to the remaining sum of British government’s funded debt”.⁷

4) Not all these loans were issued against cash, some were issued to pay for previous debts incurred during the revolutionary wars and their nominal value had no relation with the real value of stores received. This was in particular the case of the first loan, the one issued by Colombia. It was given in exchange for claims of merchants that had given goods and weapons in the early phases of the war of Independence. As the outcome of the struggle was quite uncertain, they felt quite free to inflate their claims. To pay these debts, in November 1819 Bolivar’s representatives offered at 50 bonds that fell due in three months with a nominal value of 100. Debts were rolled over and in May 1821 the Colombian representative recognises debts for £547783, claiming that dignity doesn’t allow him to examine in detail the claims of merchants. With every renewal, debts increase dramatically: in May 1821 debts for £91712 are exchanged for new bonds of the value of £140000. When the loan of £2 million is finally issued, there are £890.000 of old debts that are once more exchanged for £1.1 million of new bonds.⁸ General Miller, who fought in Chile and Peru, and knew the situation well , was very sceptical of the real value of this type of loans: “A very small proportion of the loans raised, for the American governments, was received in specie. No inconsiderable part was remitted in arms, which were

⁷ Neal, Review,op.cit. p.63.

⁸ Dawson op.cit.pp26-8

sometimes serviceable, and sometimes damaged, but always charged at an exorbitant price.”⁹

5) The sum of £21.279 million is not the total amount of issued outstanding at the end of 1825 because in the cases where two loans were issued by the same country, due to the contract of the first loan, part of the proceedings of the second loan had to be used to redeem a part of loan already issued. The second Mexican (Barclay) loan is instructive. It was issued at 86 $\frac{3}{4}$ with for a total nominal value of £3.2 million, of the £2.776.000 apparently raised, £694000 had to be used to redeem a part of the loan of the preceding year (Goldschmidt loan) The Goldschmidt contract had a provision “that one-fourth of the proceeds of any loan floated before the completion of the operation should be devoted to the redemption of the bonds issued in 1824.”¹⁰. After commissions, expenses, retained sums for future interest payments and amortisation, of the nominal £3.2 million, according to the official Mexican report, only £1.218.918 were received.¹¹ The difference between what investors paid and what countries received was substantial. There were commissions and expenses which were high, apparently Goldschmidt’s commissions on the first Mexican loan were about 8%, that is, over £200.000. But commissions and expenses were not always the main explanation for this difference; in some cases the loans were issued at a certain price while the contractors were only bound to

⁹ John Miller *Memoirs of General Miller in the Service of the Republic of Peru* London, 1829, vol.2.p.261.

¹⁰ Edgar Turlington *Mexico and her Foreign Creditors*, New York, 1930, p.44.

¹¹ Manuel Payno, *Mexico y sus cuestiones financieras con la Inglaterra, la España y la Francia. Mexico* 1862 p.7; Dawson (p.95) gives a slightly higher figure.

transfer a lower amount. The Buenos Ayres loan is a good example: the contractors issued the loan at 85 but had a contract that allowed them to sell at 70. They could keep the difference. In this case, the loan being of £1 million the difference was £150.000, an enormous amount. In order to have an idea of this, it may be mentioned that in 1823 the capital of the House of Barings, the most prestigious merchant bank in London, was £226.146.¹² In one single transaction the contractors of the Buenos Aires loan hoped to make a profit of about two-thirds of the capital of Barings.

6) Complicating factors abound: usually the loan contracts had a clause that forced borrowers to leave with the bankers who had floated the loan enough money to pay for interest and amortisation for one or more frequently two years. This may seem exorbitant because interest was paid on money which had not been received. Bankers could however later point out that this had proved to be wise because for quite a few loans the only interest paid in time was that for which the bankers had retained the amounts due. Many countries paid their debts only for the period for which their bankers had kept the initial money, that is, they paid interest with the money of lenders and when these sums had been used, defaulted. This practice, however, further reduced the sums received by debtors.

Things get even more complicated because some bankers went bankrupt while having retained very huge sums of Latin American countries, including sums that had been earmarked for future payment of interest. Colombia lost £350.000 when B.A.Goldschmidt failed in February 1826.

¹² John Orbell *Baring Brothers & Co., Limited. A History to 1939*, London 1985, p.23. For the Buenos Aires loan, see Samuel Amaral, «El empréstito de Londres de 1824», in

Mexico suffered tremendous losses, about £400.000, on money it never received. It had been forced to leave the sums necessary for payment of future interest with her bankers but they went bankrupt, leaving Mexico legally liable for the coupons that had not been paid. Clearly it is very difficult to determine how to calculate the effective rate of interest demanded in these cases.

These loans carried a nominal rate of interest of 5% or 6%, while the creditworthiness of Latin America was quite low and investors demanded much higher rates of interest. The solution was to issue the loans at a price which was lower than their nominal value, sometimes very much so.

Also the rate of interest paid for the first period is very different from what it seems. The first payment is often made very soon after the issue of the loan, when only scrip has been issued and only a few instalments paid. Interest is charged in full against the debtor country's account, but only a small proportion of the loan has been cashed. The effective return on the first instalment can be very high. In the case of the Rothschild Brazilian loan of 1825, the contract stipulated that it would be paid in twelve monthly instalments of £166.666-13-14 each. The rate of interest was 5% and the nominal amount of the loan £2.352.900, that is interest per semester was £58822. Interest on the full loan was recognised however from October 1824 although the loan contract was signed on January 12th 1825¹³. In this case, Rothschild paid interest to investors only from April 1825, keeping the

Desarrollo Economico, January March 1984, pp.559-587.

¹³ Liberato de Castro Carreira *Historia financeira e orçamentaria do Brazil desde a sua fundação*, Rio de Janeiro 1980, (first edition 1889), reproduces the contract. See in particular the 3rd clause, Vol.1, p.129.

first payment for themselves.¹⁴ Instalments being paid on the 15th of each month; by April 1st, when about £59,000 of interest was paid, Rothschild had paid £500,000, a part of which had been paid by investors. The rate of interest for three months was about 11.8%, that is, an annual rate of almost 50% excluding any compounding of interest; for Rothschild it was higher because they had not given all the money although they received the whole interest..

We also have to be careful about the dates of default, as often our sources need careful reading. For instance, it is possible to read that Buenos Aires paid interest until 1829. “No interest was paid on this loan after 1829, and arrears thus accumulated to the extent of £1,500,000.”¹⁵; “no regular payments have been paid since 1829”¹⁶ But Buenos Aires interrupted payments earlier. The explanation is that some coupons up to 1829 were paid years later. “The last payment by Messrs. Baring and co. was advertized on the 13th December, 1855, on the coupons due 12th July, 1829,…”¹⁷ The fact is that Buenos Aires serviced its debt until the first semester of 1827 included, that is, it actually remitted payment for two coupons out of its own proceeds after the sums that had been retained in London for interest payments had been fully used.¹⁸

¹⁴ Dawson, op.cit. p.93-94.

¹⁵ *Fenn's Compendium of the English and Foreign Funds*, Ninth Edition, London 1867, p.251;

¹⁶ *Ayres's Financial Register of British and Foreign Funds, Banks, Etc., Etc., for 1857*, London, n.d.p.316.

¹⁷ *Fortune's Epitome of the Stocks & Public Funds, English, Foreign & American...*¹⁷ edition, London 1856, p.244.

¹⁸ Ernesto J. Fitte *Historia de un empréstito. La emisión de Baring Brothers en 1824*, Buenos Aires 1962, pp.146-153.

7) The fact that the bonds are paid in instalments is crucial, because the public information we have on most loans refers to the price of issue on the first day. But usually time was needed to sell even the first instalment and we know very little of what actually happened later. For example, according to the investment handbooks¹⁹ and the literature, the third Peruvian bond was apparently issued at 78; but there is evidence that a part was sold much later at less than 30.²⁰

We do not know how often scrip was abandoned as worthless, with investors refusing to pay successive instalments for bonds when the nominal price of bonds had collapsed. This must have happened with many bonds that had not been fully paid yet when monetary conditions started to worsen in London in the second half of 1825.

The Peruvian loan of 1822 is an early example. Launched on the 12th October 1822, it was for £1.2 million, the contractor's price was 75 and he was bound to transfer the money to Peru in six instalments, interest on the bond being 6%. Among wild scenes, the contractors managed to sell a good part at a price oscillating between 88 and 90; the launching ended at 87 ½ or 88. A week later £120000 from the first instalment were paid at the account of the Government of Peru at their bankers²¹. About a week later

¹⁹ *Fortune's Epitome of the Stocks & Public Funds*, Seventeenth Edition, 1856, edited by D. Morier Evans, London, p.302; *Fenn's Compendium of the English and Foreign Funds*, Fifth Edition, edited by Henry Ayres, London, 1855, p.196; *Ayres's Financial Register of British and Foreign Funds, Banks, etc., etc., for 1857* by Henry Ayres, London 1857, p.348., William H.Wynne *State Insolvency and Foreign Bondholders. Volume II Selected CASE HISTORIES of Governmental Foreign Bond Defaults and Debt Readjustments*, New Haven, 1951, p.109, n.1. quoting the 1877 report of the Corporation of Foreign Bondholders, Marichal, op.cit. Table 1, p.28.

²⁰ Carlos Palacios Moreyra *La deuda anglo-peruana 1822-1890*, Lima 1983, p28.

²¹ R.A.Humphreys *Liberation in South America 1806-1827. The Career of James Paroissien*, London 1952,p.123.

the news arrived that Colombia had not authorised its agent to issue a loan, there were also rumours that the Peruvian capital had been recaptured by the Spanish troops, and the price of Peruvian scrip went into heavy discount. Investors had to pay the second instalment of the loan on November 25th, but as it was unlikely that they would throw good money after bad, it was decided to postpone this payment until May 1823. In January 1823, when the third instalment had to be paid, the situation was no better; also this instalment was postponed although the envoys from Peru demanded that the banker advance £50000.²² Given to these and other complications, by November 1823 only the first instalment had been paid by investors, that is £144000.²³ In the literature one usually finds references to this loan as a loan for £450000 issued at 88²⁴; sometimes as “Part of the 1822 loan was issued in that year at 88, and the balance 2 years later, at 82.”²⁵

There seems to be no clear account of how much money was paid by investors, nor how much was actually remitted; we do know however that interest payments for the whole value of the loan, 6% of £1.2 million had been retained by the contractor for 1823, as interest was supposed to be paid

²² Humphreys, op.cit.p.123-5.

²³ This fact is stressed in the letter, discussed below, from London dated 24th November 1823 reproduced by Juan Carlos Vedoya in *La verdad sobre el empréstito Baring*, Buenos Aires 1971, p.223.

²⁴ Hyde Clarke, On the Debts of Sovereign and Quasi-Sovereign States, Owing by Foreign Countries, *Journal of the Statistical Society*, June 1878, Table in p.313, *Fortune's Epitome of the Stocks & Public Funds*, Seventeenth Edition, 1856, edited by D. Morier Evans, London, p.301; *Fenn's Compendium of the English and Foreign Funds*, Fifth Edition, edited by Henry Ayres, London, 1855, p.196; *Ayres's Financial Register of British and Foreign Funds, Banks, etc., etc., for 1857* by Henry Ayres, London 1857, p.348., Marichal, op.cit. Table 1, p.28.

²⁵ William H.Wynne *State Insolvency and Foreign Bondholders. Volume II Selected CASE HISTORIES of Governmental Foreign Bond Defaults and Debt Readjustments*, New Haven, 1951, p.109, n.1.

on April 15th and October 15th, starting on April 15th 1823. That is £72000 of interest for the £144000 that had been paid by investors. Given the troubles of the Peruvian loan, it is most unlikely that this interest was disbursed by the bankers or by the contractors, but the Peruvian Government does not seem to have heard anything more of these £72000. In the fall of 1823 those who had paid their first instalment wanted their £144000 back while the contractors wanted to keep the money. It seemed possible to reach an agreement that envisaged the cancellation of the £1200000 loan with no more instalments due and the conversion of the first instalment of the old loan into a new loan. In this way the contractors could keep the money that was always in danger of falling into further legal problems and the investors could unload their new bonds on the market.²⁶The deal collapsed, but we should be sceptical about the success of the so-called second Peruvian loan, the proceeds of which were further reduced by the decision of the new Peruvian agent, John Parish Robertson who also negotiated the Buenos Aires loan, to deduct £216000 for the payment of interest for *three* years on the preceding £1.2 million loan. What probably happened is that not having been able to raise the money, he was forced to be creative in finding reasons for not remitting it.

8) What do the quotations of these bonds tell us? There is reason to believe that the quotations we have, as the ones given in *The Course of the Exchange*, in many cases reflect support buying by the issuing house, that wanted to induce investors to continue paying for the remaining instalments. The fact that the price of the Buenos Aires loan had increased to 91 $\frac{3}{4}$ in

²⁶ Letter dated 24 November 1823, in Vedoya, c. it. pp222-223.

April 1825 would normally be interpreted as a sign of strong demand, but it would be a mistake to use this indicator for the Latin American bonds of the period. The official history of Barings tells us the inside story.

“In 1824 Buenos Aires contractors had agreed with the provincial government to take \$5 million (£1 million) six per cent loan at 70. In London the house agreed to sell the stock at 85 for a 3 per cent commission but the mood of the market had been badly misjudged and not even a house of Barings’ standing could induce the investing public to take a large scale interest. Speculative buying had forced up prices but interest could not be sustained and so prices collapsed as speculators without funds to take allotments unloaded their stock. Buying in by Barings failed to stem the fall and the stock was soon at a discount, leaving the house with much of it unsold and on its hands, apart from that held as an investment for its own account. Matters turned from bad to worse when, in 1828, war left the Buenos Aires treasury so depleted that interest payments ceased, not to be resumed in full until 1860.”²⁷

It must be stressed that all sources give this loan as issued at 85 and don’t even suspect that a part was not sold. One of the most complete studies on this loan adds: “As can be seen, the operation was a complete success, achieved without any major effort, and the interested parties virtually fought over the privilege of buying for £85 shares that would later be redeemed at 100.”²⁸

That a loan issued by the most prestigious London merchant bank, for a borrower that apparently had put its financial matters in order and had been free from Spain for thirteen years, could face such difficulties in the most favourable period (second half of 1824-first half of 1825) of the whole

²⁷ John Orbell *Baring Brothers & Co., Limited. A History to 1939*, London 1985, p.25-6.

²⁸ Ernesto J.Fitte *Historia de un empréstito. La emisión de Baring Brothers en 1824*, Buenos Aires 1962, p.72.

episode should make us very cautious in accepting similar stories for other, much murkier, loans.

9) It is easy to conclude that Latin American governments simply jumped at the opportunities offered by the London market but the evidence is not always so clear cut. In the cases of the first two loans issued, those of Colombia and Chile, both countries did not instruct their agents to raise a loan. This is usually ignored. “But neither the free constitution nor the popular government could do without money. The Chilian republic, therefore, borrowed one million of the English people, at 6 per cent.; and, having received the cash, thought it unnecessary to pay interest after 1826.”²⁹The truth is more complex and is very well documented. Chile had needed money to finance the expedition to Peru by sea, but managed to raise internally, with much hardship, the necessary resources which were less than 400.000 pesos, about £80.000. This gives us an idea of the real costs involved, which were usually in the Latin American cases, in the order of tens of thousands of pounds and not of the order of hundreds of thousands; certainly not millions. Suspecting that its envoy wanted to issue a loan, the Chilean government formally instructed him not to do so. Irisarri, their envoy in London, insisted; because of this there was a study on the possible usefulness of a loan, done by the director of the Chilean mint that concluded that it was unnecessary and dangerous “the loan not being absolutely necessary, can any advantages accrue from it? I do not in truth perceive

²⁹ Francis, op.cit.p.268.

them..”³⁰When reports arrived in Santiago that the loan had been contracted anyway, the Minister for Foreign Affairs gave very clear instructions to Irisarri: “the clear opposition to this scheme that exists in this country moves us to reiterate our instructions to you not to contract such a loan and, if because of the absence of news to this effect you have already signed contractual agreements, you must find ways of revoking them.”³¹ When part of the money (£40.000) arrived there was no idea of what to do with it. It was proposed to buy back the loan in the London market, but in the end part of it was lent to Peru. The arrival of the money seem to have encouraged political intrigue of those who wanted power to get nearer to gold and contributed to cause a revolution. “But the expectation of the arrival of the first instalment in gold, from London, caused rival candidates to spring up, and O’Higgins was induced to give way to men, under whose successive administrations the power and respectability of the republic have been almost uniformly retrograding.”³²

The opposite case is that of Iturbide in Mexico, who desperately needed money to pay his troops and issued a loan for £4 million, and was willing to accept any conditions insofar he could get the money. “These conditions offer a tempting bait and the loan is completely safe if Iturbide remains in power. It is true that if he is dethroned lenders would face a total loss, but demanding a high rate of interest, proportional to the risk, they may get their capital back before this happens”, was how a Buenos Aires periodical

³⁰ Report of José Santiago Portales, 15 April 1822, as quoted by Veliz in his excellent “The Irisarri Loan”, *Boletín de Estudios Latinoamericanos y del Caribe*, December 1977, p.11.

³¹ Veliz, op.cit.p11.

³² Miller, op.cit.Vol.2, p.260.

³³reported on the affair using as a source an article from the London *Times*. Iturbide was executed shortly afterwards, but Mexico was left with the burden of his debts.

10) How much money was actually received by the Latin American governments will probably never be known, we can only be sure that it was a fraction of the nominal amount of £21.279 million. The interpretation of these figures raises important questions that have to be kept always in mind. For example, the Poyais loan was a swindle by a certain Gregor MacGregor who proclaimed himself Gregor I, Cacique of Poyais.³⁴ Is it reasonable to include it in this list? Poyais was apparently in Latin America, or so investors believed, but MacGregor hoped to keep the money in Britain. This is an extreme case, but many of these loans had some aspects in common with Poyais. The Chilean loan, for example, was issued against specific instructions of the Chilean government that prohibited its envoy to put the country in debt. But the envoy, Irrisarri, wanted the money, and spent a good part of it with a beautiful woman in Paris. Seeing how the proceeds of the other loans were spent, it could be tempting to conclude that this was the money spent best, although this does not help us in classifying the loan. Most of the money wasn't remitted to South America nor received by Chile; British investors, however, ended with Chilean bonds in their portfolio.

³³ *El Argos*, January 11th 1823.

³⁴ Frank Dawson has published numerous articles on MacGregor and Poyais. His paper on the Poyais loan, presented in the Conference Latin America as an International Debtor and Creditor: a Long Run View, Trento 26-27 May 2000, when published, will be the definitive account of this fantastic episode.

The preceding discussion should make it clear that the relevant total involved varies according to the problem one has in mind. The sums paid by investors are very much higher than those received by Latin American governments; the nominal value of Latin American bonds circulating in London was higher still. But if we are interested in the mechanism of international transfers and are concerned with movements in the exchange or bullion shipments the amounts are very small, as most of the sums received were not remitted outside Britain.

11) It must be stressed that the mania did not concern the Latin American loans; it was about mining companies. The only loan that created wild scenes was the Peruvian loan of 1822 and although at the time there was talk of wild speculation, the bonds almost never made it to their nominal price. And even during the feverish atmosphere of the launch of the first Peruvian bond, speculators were not blind. “At length 88 was named, and was followed by a burst of indignation from the crowd, and the words ‘Shame, shame!’ ‘Gross extortion!’ resounded on all sides.”³⁵ With mining it was altogether another matter. A letter from Princess Lieven, the wife of the Russian Ambassador in London to Prince Metternich, one of her lovers, describes how the boom was seen at the top of British Society.

“You cannot imagine how mad everyone here has gone over the companies in South America. Everybody is buying shares. Everybody, from the lady to the footman, is risking pin-money or wages in these enterprises. Huge fortunes have been made in a week. Shares

in the goldmines of Rial (sic) del Monte , bought at £70, were sold, a week later, for £1350. These sudden fortunes, and the passion for speculation, remind one of the Mississippi Bank in the time of the Regency. It was the cause of many of France's misfortunes, both then and later. Will Mr.Canning become the English Law?"³⁶

It is the mines that explain great part of the optimism about the new South American States which allowed them to float the loans in London. Even during the chaotic period between 1819 and 1825 over £5 million in precious metals were sent out of Peru on British warships.³⁷

For centuries the silver of Mexico and Peru had inflamed European imagination; now these riches seemed open to British enterprise and capital. Because the old colonial system could extract from Latin America a very substantial revenue, it was taken for granted that under British management much more silver and gold could be extracted. This was well understood both in London and South America. *El Argos*, in March 1824 reproduce an article from the *Courier* on the guarantees that South America could give to British lenders, that concluded that there could be no doubt that debts could be honoured because a country that could remit to the mother country seven or eight million pesos per year while chained to the restrictive Spanish system and burdened by the enormous expenses of the great and complicated vice-royal establishments would obviously have bigger sums at their disposal with free trade and less expenses. The article also suggested that only the duties paid by British merchants could be one of the best

³⁵ *New Times* 14 October 1822 as quoted in David Kynaston *The City of London*, Vol.1, London 1994, p.50.

³⁶ Letter of January 27 1825.Peter Quennell editor *The Private Letters of Princess Lieven to Prince Metternich 1820-1826*, London 1948, p.282.

guarantees for the payment of interest and principal of any loan to Latin America.³⁸

Those who issue loans are often involved in promoting mining companies. James Paroissien negotiates the first Peruvian loan and then dedicates his energies to the *Potosi. La Paz and Peruvian Mining Association*, which had been formed by Irisarri after his particularly pleasant trip to Paris. Robertson, who had negotiated both the second Peruvian loan and the loan to Buenos Aires, is involved in the Famatina Mining Company together with Kinder, who had issued the Peruvian loan. This is not the place to discuss the mining boom; it should be enough to say that also here apparently there were many companies that issued shares for millions of pounds, but that also here also the reality was very different from appearances.

12) Thanks to Dawson's excellent work we have very detailed information on how the different newspapers informed their English audience on the various Latin American loans. It is simply impossible not to conclude that for the vast majority of loans investors were warned repeatedly on the dangers involved. The success of the first Peruvian loan, which had created a craze, induced *The New Times* to comment that 'if the very respectable Mr Lemuel Gulliver were to appear on stage again, and to issue proposals for a loan to the Republic of Laputa, he would run the hazard of being suffocated by the pressure of subscribers to set down their

³⁷ R.A.Humphreys, *Tradition and Revolt in Latin America and Other Essays*, London, 1969, p.128.

³⁸ *El Argos* 24 March 1824, Consideraciones sobre las garantias que puede ofrecer Sud America a los prestamistas ingleses.

names.³⁹ The same article also pointed out that ‘here is a country on the other side of the globe, of which we know absolutely nothing, but that it is or has lately been the scene of a desperate conflict between two contending parties.’

We know that journalists were paid to publish favourable articles on the various loans. For instance a journalist who worked for the Morning Chronicle was paid to write positively on the Peruvian loan (he was also in the pay of other Latin American countries). But venality may cut both ways: other journalists were paid to write negatively on the same loan by the contractors of the Colombian loan who had wanted the Peruvian business themselves.⁴⁰ Every loan had favourable press articles, often written by journalists who were paid by bankers or promoters but on the whole there was adequate information on the risks involved.

In 1826 the press was attacked for its behaviour during the boom and performed its *mea culpa*.

‘For the share which “the gentlemen of the press” had in these sheep-shearing schemes we have the ingenuous testimony of the Morning Chronicle. “The press”, says the editor,”for the most part, by taking shares in these schemes when at a premium, (and we blush to say few editors of newspapers in this metropolis are not to be found in the list of those who benefited by them,)had, at all events, no particular interest in opening the eyes of the public.”-Morning Chronicle, February 3.”’(1826)⁴¹

The corruption of the British press during our period, however, cannot be compared with the corruption of the French press in the early 20th

³⁹ Quoted by Dawson op.cit. p.38

⁴⁰ R.A.Humphreys *Liberation* op.cit. p.120 and 123

⁴¹ *Digest of Facts and Principles on Banking and Commerce with a Plan for Preventing Future Re-Actions*, London, 1826, p.82,fn.

Century, when most of it was paid by the Czarist Government to prevent the collapse of its loans.

As the boom went on, warnings were issued by worried statesmen and bankers, especially concerning mining companies. But warning the public can be a dangerous affair as it attracts the hostility of the powerful groups that are behind the issues.

The young Disraeli was paid by Powles, a promoter of loans and companies in South America, to write propaganda for his schemes. His brilliant pen attacked those who issued warnings about the dangers of the boom:

“all the political parrots have been dashing about their gilt cages, pluming their feathers for action, looking very fierce and very indignant, and, as if to show their disapprobation of the times, and their determination not to be taken in, have, with untired lungs and most praiseworthy perseverance, been bawling "Bubble!Bubble!" for the last six weeks.”⁴²

Disraeli attacks openly those who talk about the dangers of speculation; Lauderdale in the House of Lords had warned on the “rash and inconsiderate speculations now afloat” while in the same House of Lords another speaker had “pledged himself to prove that the Pasco Peruvian Mining Company had no foundation whatever, and no object in view, except to work mines on the Stock Exchange.”⁴³ When Baring attacks speculation on South American mining companies on March 16th 1825, Disraeli replied that what was now said of these mines was the same thing that was said at the time of the French loan on which Baring had made so

⁴² *An Inquiry into the Plans, Progress, and Policy of the American Mining Companies. Third Edition with considerable additions*, London, 1825, p.125.

much money.⁴⁴It is clear that to denounce fraudulent situations involves risks; however, in Britain at the time, there were many willing to take that risk and the public was informed of the dangers that were present. We should however be aware that Disraeli himself believed in his schemes and borrowed money to invest in them; it took him twenty years to repay his losses.⁴⁵

13) One aspect that to my knowledge has not been seriously explored concerns the information available to Latin American Governments and public opinion on the London market for Latin American loans. If we take the press of Buenos Aires for 1822-25 as a possible example, some interesting facts emerge. First of all, there was much information of what was happening in Europe. This is not surprising because during those years there was still the possibility that the Holy Alliance would help Spain and Portugal to regain control of their American colonies. The press therefore reported extensively on European political matters and diplomatic exchanges of the main European Foreign Ministries, reproducing whole documents and reporting Parliamentary sessions. For this it relied on European publications and newspapers, as well as on private letters from Latin-Americans in Europe who wrote to friends at home and on letters received by merchants. Articles from *The Times*, *The New Times* and *The Courier* , if we restrict ourselves to London, were regularly reproduced.

⁴³ *Lawyers and Legislators: or Notes on the American Mining Companies*, London 1825 p.41; for Lauderdale p.38.

⁴⁴ *Lawyers and Legislators cit.*, p.60.

⁴⁵ Robert Blake, *Disraeli*, London 1969, p.24-5.

On financial matters, interest was concentrated on prices of the bonds issued by the various nations and on the general mood of the market. News from the other Latin American countries were also available from periodicals and letters, as well as from officers of the Army that had fought in Chile and Peru. Peru was still a fighting ground between the Spanish Army and forces from other Latin American countries, and therefore the unfolding of events was followed with the closest interest. This meant that in the same number of a publication there could appear some catastrophic military news concerning Peru of a few weeks earlier and the high price of Peruvian bonds in London of two months before. News from Mexico were often reproduced from the Baltimore press.

What is certain is that, although communications were slow, the information was good and acted upon. In its message to the Provincial Legislature at the opening of its third term, the government of Buenos Aires explained why it still had not issued a loan in Europe: the reason was that in London the credit of Latin American countries in 1823 was low. “The Government has abstained until now from using the permission to negotiate a loan it received by the law of August 19 1822, notwithstanding the fact that it could have used it with great utility. It has believed it was better not to expose the credit of our province to be involved in the disgrace that the loans from American countries have suffered in the great markets (plazas) of Europe. It is undoubtedly better to wait until the state of our affairs and the principles of our administration are well known: at that time we will obtain advantages that will compensate the sacrifice that we are now making

to circumstances.”⁴⁶ In order to have an idea of the delays involved, the quotations of loans in London of mid May were reported in *El Centinela* on August 10, 1822, about three months later.

There was a clear perception that European investors did not distinguish clearly between the different Latin American countries and that therefore what menaced the credit of one nation could have devastating consequences for far away countries. In February 1823 it was reported in Buenos Aires that Bogotá’s *Gaceta de Santa Fe* of July 7th 1822 had arrived to London in October with a *Manifiesto* of General Santander, who governed Colombia in Bolívar’s absence, in which he explained that there was nobody in Europe entitled to negotiate loans for Colombia. Although those involved in the loan tried to sustain the price of Colombian bonds, their price fell from 97-99 to 80.5-85. The whole episode was defined by the Buenos Aires periodical *El Centinela* “an event that without doubt will have a baleful influence (funesto influjo) on all the loans of Latin America.”⁴⁷ *El Centinela* was right, in 1823 no Latin American country issued a loan in London.

The frenzy in London must have attracted much attention and must have been the subject of amusement. I have found two interesting examples in the same periodical publication that prove this. The first is an ironical reference to Gregor MacGregor, who had issued a loan for a non-existing country after proclaiming himself Gregor I.

A Buenos Aires periodical refers to “the famous Mac Gregor who condecorated himself with the title of King of Poyais, a country on the

⁴⁶ *La abeja argentina* N.13, 15 May 1823 reporting on the session of May 5.

⁴⁷ *El Centinela* 16 February 1823.

Mosquito coast south of Mexico, near the Straits of Panama and where he founded an excellent city”⁴⁸. His enterprise probably gave food for thought to local capitalists. Not only MacGregor was famous in Buenos Aires but jokes concerning the boom in London must have been frequent. One of them was even mentioned in the press. An article that reports the totals issued in London by Mexico, Colombia, Peru, Chile and Buenos Aires ends: “The imagination of the wits of Buenos Aires has been original: two days ago they spread the news that also H.M.of New Zeland, Tippae Cupa, was going to England to negotiate a loan.”⁴⁹ It seems reasonable to deduce that the London bubble must have produced many other ironical comments that were not reported in the press.

There was also excellent private information circulating in Buenos Aires. A very detailed letter in English, dated London 24 November 1823, about the private meetings between the main parties involved in the dispute on the Peruvian loan was bought at an auction in Buenos Aires together with other manuscript material concerning the Buenos Aires loan, and published in 1971.⁵⁰ It is one of the more perceptive analysis we have today of the issues involved and of the problems that faced by those who had lent to Perù and by those who had collected the money. It strongly suggests that there were a few people in Buenos Aires that were extremely well informed of what was going on in London behind the scenes; they had much better inside information than that available to the average London investor.

⁴⁸ *El Argos* of August 7, 1824

⁴⁹ *El Argos* 20 October 1824

⁵⁰ Juan Carlos Vedoya La verdad sobre el empréstito Baring, Buenos Aires 1971; the letter is reproduced in pp.222-5.

Reading the local press one has the impression that there was a very clear perception that Latin American loans were extremely risky both because of political risk and because of the fragile budgetary position. The Peruvian loans had been issued even before the troops still loyal to Spain had been defeated; they even retook Lima in a later period. Chile was in turmoil, with Spanish troops still fighting in the south and a power struggle at the top. In Mexico Iturbide, who had proclaimed himself Emperor, was deposed and in Argentina the situation was far from calm, with the provinces in civil war and insurrections in Buenos Aires. On top of this there was no certainty, at least in the first two years after the first loans were issued, that the Holy Alliance would not help Spain to retake control over her Spanish

The dangerous impact of the foreign loans was perceived, at least insofar other countries were concerned. Describing the fiscal position of Chile, where income was about 1.300.000 pesos and expenses 1.567.000 pesos, *El Argos* mentions that with the added burden of the London loan (400.000 pesos per year) the deficit would be over 666.000 pesos. To those who argued that a similar deficit had been financed in the past, it replied that in the past forced loans had been tolerated. These violent and uneconomical methods were not possible any longer.⁵¹

There was also a clear perception that the budgetary position was usually precarious because of their reliance on customs duties: any possible blockade was likely to have a disastrous effect on revenue and the capacity to service loans. “Lately our economists have demonstrated that four-fifths of the revenue of the State derives from custom duties, whose arbitrary is precarious (sic), as we lack a strong Navy to protect our trade from the

attacks of a foreign nation.”⁵² The preoccupation was justified: Buenos Aires defaulted on her loan four years later when Brazil imposed a blockade on the harbour.

We can conclude that parts of the Latin American opinion, which included British merchants and their partners, was well aware of what was going on in London and that their evaluation was that the London market was excessively accommodating in granting loans making the feverish optimism of Britain’s financial circles the object of general amusement.

SOME CONCLUSIONS

What was the role of biased or insufficient information? We have seen that, although news took often three months to arrive, public opinion, both in London and South America, was quite well informed of what was going on insofar as the risks involved in lending to South American states. Most loans were received in the London press with both positive and negative reports. The loans encountered from the beginning very serious problems: both the Colombian and Chilean loans had not been authorised by their respective governments and this was soon known in London. Furthermore, British investors were quite aware of the risks of sovereign default as the King of Spain refused to recognise the bonds issued by the Cortes and the price of Spanish bonds collapsed. We have seen that no loans were issued by Latin American countries in 1823. After the troubles of the Colombian and Peruvian loans in 1822 the market was clearly not receptive and this was well understood in some Latin American capitals like Buenos Aires.

⁵¹ *El Argos* 5 November 1823

⁵² Reflexiones economicas, in *La abeja argentina* N.14, 15 June 1823.

The Scots, in particular, had learnt their MacGregor lesson of 1822 very well. “The swindle left a legacy, as Scottish investors were disillusioned with foreign investment at an early stage of the mania. As early as December 1823 the Aberdeen Journal reported that they had ‘...got heart-sick of Foreign Speculation..’”⁵³

Clearly there was plenty of information on the dangers of investing in Latin American loans. Therefore it is all the more surprising that in the two following years the loans seem to have been taken by the public.

Was information asymmetric? It is clear that there was a tightly knit group that met regularly and exchanged information, paying journalists to promote loans and companies. Communications were however slow and there was widespread uncertainty about what was happening across the ocean. It is relevant to point out that most “insiders” really believed in the opportunities offered by Latin America. They did not consider Latin America a “lemon”, they invested their gains in those countries and most were ruined as a consequence.

Could more information have prevented these loans, was this episode the fault of the press? It seems clear that the press, on the whole, informed quite accurately on the risks involved. True, there were many misleading and tendentious articles, but there were also very detailed warnings on the dangers involved. The problem, as usual, was not lack of information but how to choose between conflicting information. The press is usually blamed after a crash and every time it is said that its behaviour will be better in the

⁵³ R.C.Michie *Money, Mania and Markets. Investment, Company Formation and the Stock Exchange in Nineteenth-Century Scotland*. Edinburgh 1981. p.29.

future. When this happened after the boom and crash of 1875, Giffen made a comment that I think is permanently valid.

“Mr.Cohen seemed to think that the mischief done by “foreign loans” during the last few years would have been a great deal less if the press had done its duty better, and he looked forward to the press doing that duty much better in the future. But perhaps Mr.Cohen forgot a great deal of what the press really did during the issue of these foreign loans. He (Mr.Giffen) was connected with the press during a great part of that time, and he could say that it did service in warning the public against such investments; but the infatuation of the public at the time was so strong, that he did not think the strong attacks on such loans deterred many people from investing in them. The writing in some quarters was looked upon by many persons as being the proper thing to be said by respectable journals, but as very antiquated. When people were led to believe they could make 20 per cent., the warnings of the press were of no effect.”⁵⁴

The main danger for investors in Latin America was political instability, and on this count everybody was perfectly informed. Both “outsiders” and “insiders” underrated it dramatically and were ruined by it. Not only the small investor, but also bankers and the closely knit group of promoters of loans, mining and colonisation companies, all in the end lost money, many went bankrupt after investing the profits of one venture into another. The great exception was Brazil, where continuity prevailed. The real problem was not calculable risk, it was radical uncertainty. It is unlikely that theories of asymmetric information can explain the 1822-25 episode.

A interesting question concerns the problem of crisis. What is a crisis? In the last eighty years, the attention of economists has concentrated on the

⁵⁴ Giffen, in « Discussion on Mr.Hyde Clarke’s Paper», *Journal of the Statistical Society*, June 1878, p.344.

crash, but this was a break with an older tradition, which saw the beginning of the crisis when “irrational exuberance” takes over. “Panics do not destroy capital” according to John Stuart Mill, “They merely reveal the extent to which it has been previously destroyed by its betrayal into hopelessly unproductive works.”⁵⁵

The crisis for Poyais bondholders began in the moment they paid for a worthless bond, not when the fraud was discovered. The same is true for most Latin American loans, none of which was used for productive purposes. For Latin America the London crisis was beneficial because it prevented further disastrous schemes to go ahead. The government of Buenos Aires, for example, wanted to convert all its internal debt into a sterling debt negotiable in London. This would have been beneficial to the holders of rapidly depreciating peso debt, but would have saddled the country with a much bigger foreign debt and would have ruined some more British speculators. The money received from the loans, which was much, much less than the nominal amounts published, was stolen or wasted. In the end, for many years, most of those who dealt with these bonds were ruined.

Their melancholic state can be understood by the following verdict written in 1833.

“The dividends having ceased to be paid, for a long time back, on all these loans, they are looked upon in the market as turn-up chances, which, according to the politics or pretended news of the day, rise or fall in the opinion of the speculators, but remain at such prices as shew what they are. A prey to intestine wars, or civil commotions, the fate of those Nations hangs, as it were, on the hazard of a die. All Europe, almost, wishes them

⁵⁵ As quoted in Ellis T. Powell *The Evolution of the Money Market 1385-1915*, London 1916, p.325fn.1.

well; but what hope can there be where freedom is enforced at the point of the bayonet; where all love for the country seems but a name for aggrandizement, and a struggle for supreme power? Of financial arrangements, of course, there is a total absence and the holders of these loans must wait in patience the result of all the effervescence till it pleases to settle, and drop into a state of tranquillity and order; or, if tired of delays, they have no other resource but to take what they can.”⁵⁶

I hope to have shown that the data usually used for the Latin American loans cannot be accepted at face value and should be treated with many *caveats*. As far as the loans are concerned, perhaps there was no boom at all.

⁵⁶ «Appendix to the Columbia, Chile, Peruvian, Guatemala and Buenos Ayres Loans», in J.J.Secretan *Fortune's Epitome of the Stocks and Public Funds*, 13th Edition, London 1833, p.136

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