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Photographs by Jim Harrison

“The Damn'd South Sea”

*Britain's greatest financial speculation
and its unhappy ending, documented in a rich
Harvard collection*

by CHRISTOPHER REED



After the shattering and scandalous crash of 1720, financial pamphleteering boomed, one writer proposing that all bargains made during the Bubble should be construed as made by lunatics and should therefore be annulled. This grouping includes *The Snake in the Grass*, *The South-Sea Scheme Detected* ("By a Lover of his Country"), *Exchange-Alley: or, the Stock-Jobber turn'd Gentleman* (a "tragi-comical farce"), *News from Hell*, and *A Panegyric Epistle of 1721*, said to be the work of John Gay. To his friends Gay pronounced himself "fixed for life" when his South Sea stock zoomed to £20,000, but he held on too long and lost it all. Seven years later he would write *The Beggar's Opera*.

under the newish joint-stock principle, as a corporation with transferable shares. Holders of the national debt were obliged to exchange their government securities for shares at par in the company. The company could raise working capital--a huge amount of it--by borrowing on the security of the debt due

Irrational exuberance pervades the stock market. Speculators pay ever-higher prices for shares despite scant evidence of underlying value. Skeptics warn that the bubble will burst. This must be England in 1720.

The South Sea Company was founded in 1711 by Robert Harley, who wished to create political allies. The leader of the Tory party and soon to be lord treasurer, Harley wanted an end to the unpopular War of the Spanish Succession. The South Sea Company, as set up by act of Parliament, had a monopoly to conduct England's trade with Spain's colonies in the West Indies and South America. Harley advanced the notion that permission to conduct such trade would be ceded by the Spanish king as part of the price of peace.

The company had the further splendid purpose of relieving the government of its burdensome unsecured public debt--obligations for which Parliament had assigned no funds--which then amounted to £9,000,000. South Sea was organized

from the government. In addition to its trade monopoly, the company would get an annual payment from the Exchequer of £568,279 10s., or 6 percent of the debt taken over. Stockholders had no promise that they would see any of this as dividends, but who could blame them for thinking that capital gains based on trading profits were a certainty?

It was an optimistic age. People had a passion for business and followed developments avidly through a newly burgeoning medium, the newspaper. In 1702 London had one daily newspaper; by 1709 there were 18. Harley had able propagandists, Jonathan Swift and Daniel Defoe among them. (Critics included Joseph Addison and Richard Steele.) The managers of the South Sea Company understood the value of publicity (as well as fine print) in the advancement of their affairs and once issued a press release, surely an early example of that genre.

Historians wishing to study the company and the era can be awash in source material if they go to the right place--the Kress Library, Harvard Business School's rare-book collection, housed in Baker Library. Its books, broadsides, pamphlets, acts of Parliament, manuscripts, and sundry ephemera concerning the South Sea Company and the speculative fevers that racked England and the Continent in the early eighteenth century form one of the four great collections of such material in the world, and the most numerous. The items illustrating this article are a miniscule sampling of the archive. Almost all of it was assembled by Hugh Bancroft, A.B. 1897, A.M. '98, LL.B. '01, president of Dow, Jones and Company. After his death in 1933, his wife presented the Bancroft collection to Harvard. It offers true value to scholars wishing to explore a seminal lunacy.

The South Sea Company was a confection of politics, commerce, and finance. None of its governors or directors had any experience of trade with the New World, but John Blunt, who wrote the charter and was the company's dominant director, had been a scrivener and then director of the Sword Blade Bank. He and cohorts had a fine understanding of financial manipulation.

The late historian and civil servant John Carswell, former secretary of the British Academy, wrote an esteemed study, *The South Sea Bubble* (Sutton, revised edition, 1993), chronicling the heady, fraudulent proceedings launched in 1711. He characterizes Blunt as of "powerful jowl and heavily-lidded eyes, an industrious, domineering man whom it was equally difficult to like and to resist." His lieutenant was young Robert Knight, company cashier. "Blunt provided cunning, bluster and technical draftsmanship, but Knight's was the power of innovation, charm and the ingenuity that made the thing possible...." Scottish



Het Grootte Tafereel der Dwaasheid (The Great Mirror of Folly), Amsterdam, 1720. "The wind-buyers or wind-catchers, who, for wind, lose money and goods, and ruin their wives and children," one of 74 prints in a stout folio volume "showing the rise, progress, and downfall of the bubble in stocks and

economist Adam Smith, born three years after the Bubble burst, would write of "the knavery and extravagance" of the South Sea Company and of "the negligence, profusion and malversation" of its staff.

The Peace of Utrecht, reached in 1713, yielded few trading concessions from Spain. Why should it have? asked Defoe (whose support of Harley waxed and waned), "Unless the Spaniards are to be divested of common sense, infatuate, and given up, abandoning their own commerce, throwing away the only valuable stake they have left in the world, and in short, bent on their own ruin...."

The company did secure a contract to transport and sell annually in Spanish America 4,800 "*piezas de Indias*" (a *pieza* was a black slave, with no defects, at least 58 inches tall) and could send to Cartagena or Vera Cruz one ship of no more than 500 tons loaded with British woollens and the like. The company lost money with the slaves, managed the other trade ineptly, and had to contend with venal Spanish officials. War with Spain in 1718 ended any pretense of a commercial basis for the South Sea Company.

There it then sat, an enterprise with vast, if nominal, capital and nothing to do that it had been chartered to do. "The directors were not long idle because they now turned to stock-jobbing," writes John G. Sperling, formerly professor at San Jose State College and now chairman and chief executive officer of the Apollo Group, in *The South Sea Company: An Historical Essay and Bibliographical Finding List* (Baker Library, 1962). "Within a year and a half the Company was to become the central institution in the greatest financial speculation in English history."

In 1719 the government again found itself awkwardly in debt. Blunt and his fellows again proposed that the debt--£30,981,712 of it--be converted to company stock, this time voluntarily, at terms to be named later, saving the government much in annual interest and bringing it, as well, a fee from South Sea of £7,500,000, potentially, for the privilege of making the conversion. (To put these sums in perspective, Carswell points out that a middle-class family could live very comfortably at the time on £200 a year.)

Lest influential folk doubt the attractiveness of the scheme, Knight distributed £1,259,325 of fictitious company stock-- bribes, later to be paid in cash with the public's money--to 40 or 50 members of Parliament, including Charles Spencer, earl of Sunderland (first lord of the treasury) and Charles Stanhope (secretary to the treasury), and to the Duchess of Kendal, the king's mistress. This was corruption on an audacious scale.

In early 1720 "Parliament accepted the South Sea Company offer and thereby committed the nation to

windy speculation, especially in France, England, and the Netherlands in the year 1720." These excesses, wrote the late Harvard professor of business economics Arthur H. Cole, in *The Great Mirror of Folly*, "seem to have caused a long continued delay in the evolution of the corporation in England, France, and Holland.



Top left: *The Bubblers Mirrour: or Englands Folley*, 1720. An engraving depicts a "Canting Miser," who sold his estate to buy stock and now despairs. Flanking him is a list of 26 major and numerous minor bubbles of the time, with subscription prices and what each stock sold at when highest. Thus, investors in rock salt got in for £1 5s. and might have sold at £15. **Top right:** "The Stock-Jobbing Ladies," sheet music, ca. 1720. Satirical songs, poems, plays, and the like appeared in profusion as the Bubble expanded and then burst. **Bottom:** A receipt for a dividend of £21 from the South Sea Company, 1717, signed by dramatist William Congreve, author of *The Way of the World*.

by a draught of cash to suck it up again, leaving the level higher than before." Success *required* that the level keep rising.

It did. Speculative zeal had risen steadily in the English breast during the preceding 30 years, the childhood of the London Stock Exchange. A gargantuan Mississippi Bubble had expanded in France. Cupidity was not unknown in Holland. From September 1719 through August 1720, 190 English speculative ventures had their initial public offerings. Some were honest, many not.

"In order to pay out profits, the South Sea Company needed both to raise more capital and to have the price of its stock moving continuously upward," writes the economist and MIT professor emeritus Charles P. Kindleberger in his classic work *Manias, Panics, and Crashes: A History of Financial Crises* (Wiley, third edition, 1996). "And it needed both increases at an accelerating rate, as in a chain letter or a Ponzi scheme." The company repeatedly raised cash through new issues of stock as its price spiraled upward in the summer of 1720.

a thrilling financial adventure," writes Sperling. "It was clear that the Company could only pay the £7,500,000 to the government if they exchanged South Sea stock for government obligations at prices far above par 100. And, the higher the price of stock at the time of conversion, the greater the profits which would accrue to the Company. In addition to the profits the directors could make by holding South Sea stock were those available through stock manipulation which, in this case, included transactions in non-existent stock. The directors could create and purchase stock at a low price and sell it for an inflated price. It was a foolproof way of making a large fortune and it proved to be an irresistible temptation."

Carswell employs a hydraulic metaphor to describe the action. The company first created £2 million in new South Sea stock, at £300 a share, and let investors pay for it in installments. Subscribers eagerly bought it up, and the company covertly issued £250,000 more for good measure. Then it announced that its cash position was so strong that it could lend shareholders money on the security of their South Sea stock. The price of the old stock at once rose to £325. The company issued yet more stock and made more loans, again and again. "So Blunt...had constructed a financial pump," writes Carswell, "each spurt of stock being accompanied

"The maxim that credit was not wealth unless it rested on a wealth-producing asset had been ignored....," writes Carswell. Greed blinded many, but not all. One unidentified observer saw clearly: "The additional rise of this stock above the true capital will be only imaginary; one added to one, by any rules of vulgar arithmetic, will never make three and a half; consequently, all the fictitious value must be a loss to some persons or other, first or last. The only way to prevent it to oneself must be to sell out betimes, and so let the Devil take the hindmost."

On January 1, 1720, the price of a share of South Sea stock stood at £128. On June 24 it hit £1,050. In September came the crash. By December the stock had returned to £128. Thousands declared themselves ruined. Banks could not collect loans on inflated stock and failed. Specie was in short supply. Work stopped on half-built homes. Investigations and revenge ensued, and a long struggle to restore stability.

Some of the guilty were thrown in the Tower, brought to trial, and separated from part or almost all of their estates to replenish the company's coffers and help restore its credit. The House of Commons left Blunt only £5,000 of his £183,000; a back-bencher had suggested one shilling. Postmaster-general James Craggs the elder, who denied complicity in the affair (although his son, secretary of state, had been active in it), killed himself on the eve of his trial. Others of the miscreants were protected for political expediency.

Alexander Pope declared:

How goes the Stock, becomes the gen'ral Cry.
Rather than fail we'll at Nine Hundred Buy.
Instead of Scandal, how goes Stock's the Tone,
Ev'n Wit and Beauty are quite useless grown:
No Ships unload, no Looms at Work we see,
But all are swallow'd by the damn'd *South Sea*.

Fury was widespread. Speculators who had thought themselves wealthy now found themselves not. Yet, for many of the players, those who had held on until the crash, something roughly akin to the status quo ante was restored. Robert Walpole, who became first lord of the treasury and chancellor of the Exchequer in April 1721, persuaded Parliament and the public to accept a scheme of reconstruction by which, writes Carswell, "thousands of private bargains--and this was the most remarkable thing of all--were statutorily cancelled or adjusted, so that imaginary



Top: Playing cards, ca. 1721, sketch ruination in variety. **Lower right:** "A Ruin'd South-Sea Jobber of Renown, Leaps from a Lofty Window, Head long down, When taken up, he crys Adzounds I'm broke, Who gives Eight Hundred Pounds for South Sea Stock." **Left:** "A certain Lady when the Stocks run high, Put on Rich Robes, to Charm her Lover's Eye, But South-Sea falling, Pawn'd her fine Brocades, And now appears like other homely Jades."

wealth could be sucked out of the system."

"The next age," writes Carswell, "was one of cautious conservatism, hardening social distinctions, ever more clearly formalized patronage, and hostility to change." The so-called Bubble Act of 1720, passed at the urging of the South Sea Company to squelch competing speculations, had banned all joint-stock corporations without parliamentary or royal authority. That helpful way of raising capital was thus not available. The Bubble may have stifled economic development for years. Carswell notes "a strange sense of arrest" in the 50-year interval of conservatism between the decades of innovation at the start of the century and the start-up of the Industrial Revolution. What if the lull had been shorter? Carswell imagines "Doctor Johnson holding forth in his compartment as the Edinburgh train puffs northwards."

For those who had realized big losses or gains, the mania redistributed wealth. The largest honest fortune was made by Thomas Guy, a stationer turned philanthropist, who owned £54,000 of South Sea stock in April 1720 and sold it over the following six weeks for £234,000. Sir Isaac Newton, scientist, master of the mint, and a certifiably rational man, fared less well. He sold his £7,000 of stock in April for a profit of 100 percent. But something induced him to reenter the market at the top, and he lost £20,000. "I can calculate the motions of the heavenly bodies," he said, "but not the madness of people."



One of numerous manuscript documents in the Kress Library concerning the South Sea Company. On a company form, the Most Noble Henry Duke of Kent gives Henry Allen power of attorney to sell, assign, and transfer £6,600 of stock.



Lucifer's new Row-Barge, 1721. Devils convey Robert Knight, the South Sea Company's former cashier, into the jaws of Beelzebub. A master

dispenser of bribes, Knight was a central figure in the swindle and made more money out of it than anyone else. When the frothy scheme collapsed, he absconded to the Continent but was imprisoned in Antwerp. King George publicly demanded his extradition for trial, but the king's mistress secretly assured foreign officials that His Majesty would be grateful if Knight and his secrets remained abroad. Through the connivance of the British and Austrian governments, he was allowed to escape from jail and lived in exile for more than 20 years until receiving a royal pardon. Knight was "a man of exceptional abilities, unlimited ambition and complete lack of scruple," wrote historian John Carswell. The legend on his hat in this engraving reads, "How Glorious was my Beginning."

Christopher Reed, a stranger to high finance, is managing editor of this magazine.

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