



The Crisis of 1825 in Parliament: Economic Ideas at the Dawn of the Modern British Financial System

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The financial crisis of 1825 revealed the fragility of the British financial system, sparking an extended debate in Parliament over its causes, those responsible, and the measures needed to prevent another meltdown. This paper examines the views of the members of Parliament in this debate, many of whom had a background in political economy and/or economic expertise. A broad consensus emerged that the crisis had been driven by excessive speculation fuelled by over-issuance of banknotes by country banks and the Bank of England. Parliamentary economists played a particularly active role in the discussions, providing thorough analyses of the crisis, grounded in the principles of political economy, and drawing on the ideas of renowned authors, especially Tooke, but also Ricardo. The outcome of this process was the Banking Acts of 1826, the first step in the reorganization of the British banking system in the 19th century.



1. Introduction

The panic of 1825 in Britain has been deemed the first crisis of the capitalistic system. Marx remarked in the postface to the second edition of *Das Kapital* in 1872: “With the crisis of 1825 [modern industry] for the first time opens the periodic cycle of its modern life” (1887, xxiii). Sismondi (1827, 367–82) pointed to a crisis of overproduction. Bordo (1998) highlighted its particularities as the first example of an emerging-market-induced crisis. Dick (2012) also emphasized its foundational character, “the moment at which capitalism grew from an ideological enterprise into a global condition.” Béraud (2013, 238) underlined its novelties: an industrial, speculative, and international crisis; a monetary and banking crisis in which credit played a central role. Calomiris and Haber (2014, 114) considered it the first global banking crisis of the modern era. Some have compared 1825 to the meltdown of 2008. Turner (2014, 7), assessing banking stability, concluded that these two episodes constituted the only major banking-system crises in Britain in the last two centuries. Olmstead-Rumsey (2019, 3) noted that in both cases the crisis occurred after the quality of new securities was called into question. Neal (1998) placed the crisis in a wider context: Since the return to convertibility in 1821, the British financial system was affected by increased informational uncertainties within English institutions. “All this left the London private banks and their corresponding country banks, as well as their customers ... floundering in the resulting confusion” (1998, 2).¹

Contemporaries were overwhelmed by the collapse. The conventional idea held that overtrading was the result of speculation driven by greedy profit-seeking behaviour, enhanced by easy credit policies. Béraud (2013) analysed the explanations offered by Tooke, McCulloch and John Stuart Mill. While all three blamed speculation, they disagreed on the role of banks. Tooke believed the problems stemmed from an excess of paper circulating and credit. McCulloch argued that the crisis had its origins in country banks.² The young Mill maintained that credit was not the root cause, but it became essential once it expanded to meet the demand in speculative markets. The crisis began when credit disappeared.

¹ The Treasury had to cope with debt servicing without the revenues of the income tax, the Bank of England was searching for new returns after the profits of the war, and the London stock exchange was marketing new Latin American assets of unknown quality (Neal 1998, 2). Like Bordo, Neal believed that the main responsibility for the crisis fell on the Bank.

² In McCulloch's opinion, country banks had conducted discount operations quite carelessly, and note issuance had been excessive, triggering an over-demand for gold from the Bank of England, which responded by reducing its issues. All this led to a series of bankruptcies (Béraud 2013, 238).

This article analyses the ideas displayed in Parliament about the crisis. We examine the views of Members of Parliament (MPs) regarding the causes of the crisis, those deemed most responsible for it, and the measures to prevent a recurrence. MPs expressed serious concern for the stability of the financial and monetary system as a key for the progress of Britain. The debates were far from shallow, and the main participants were certainly not dilettantes: A significant number of MPs involved in the discussions were themselves economists (Fetter 1980). They trusted the principles of political economy and backed their contributions with renowned sources of authority, mainly Tooke and – indirectly – Ricardo. Fetter (1980, 227) noted the difficulty of assessing the influence of economists in Parliament. Here we attempt to provide evidence that political economy – and in particular the ideas of Tooke and Ricardo – played a significant role in the debate and its outcome, the amendment to the charter of the Bank of England, and the act to restrict the issue of small-denomination banknotes.

The role of economists in parliaments has been addressed in the literature across several countries. Augello and Guidi compiled national case studies in their comparative analysis of the 19th century (2005), as part of broader research on the institutionalisation of political economy. The British case has been among the most extensively analysed, although the specific case examined here has not received focused attention. Fetter (1975, 1980) explored the influence of economists in the British Parliament in the first half of the 19th century, identifying common traits in their political activity, but did not specifically address the 1825 crisis. Backhouse (2005) concentrated on the period 1848–1914. Gambles (1999) focused on the economic discourse of conservatives on protectionism in the first half of the century. Schonhardt-Bailey (2006) analysed the debates on the Corn Laws. Three studies come close to our research target: Gordon (1976) made an in-depth analysis of political economy in Parliament between 1819 and 1823; Grampp (1982, 1987) examined the Parliamentary declaration on free trade of 1820; and Harris (1997) focused on the debate on the repeal of the Bubble Act in 1825.

This paper is structured in four parts. The first outlines the context of the crisis. The second examines the debate in the House regarding the causes of the meltdown. The third addresses the discussion on the reforms proposed by the cabinet to strengthen the financial system. The fourth focuses on a sub-debate concerning the capability of political economy to address financial matters.

2. Setting the Scene

When Britain resumed convertibility in 1821, circulating currency consisted of gold or paper backed by gold. The charter of the Bank of England granted it the privilege of being the only joint-stock bank in the country. The Bank did not operate branches,

so local credit was provided by country banks. These banks did not hold gold reserves and, when needed, rediscounted their paper through banking houses in London, which acted as their agents with the Bank. Thus, the British financial system was composed of three layers: The Bank of England, the London banks, and the country banks outside London.³

The decade of 1820 was one of liberalisation for the British financial market. Restrictive rules of the usury laws were repealed and the Bubble Act was abolished in 1825. This regulation made it hard for the private sector to compete for funds. Once repealed, investment rates and capital-labour ratio rose, along with output, productivity, and real wages (Temin and Voth 2014, 186). The period 1823–1825 was one of frantic activity. Fetter (1965, 111) recalls a report by T.C. Salt, manufacturer in Birmingham: “During the whole 1824 and 1825 the stock went off so rapidly into consumption that we could hardly keep the shopkeepers supplied fast enough.” Production and prices rose. There was an investment boom, fuelled by easy credit policies. “Overtrading” was the term to describe the mania.⁴ Tooke (1838, 120) spoke of “memorable speculation.” Economic expansion was coupled with financial expansion. The Bank of England’s easy monetary policy enhanced the stock market boom (Bordo 1998, 77). Stock prices soared. Much capital was placed in bonds of the new Latin American republics, expecting fabulous returns.

In 1825 the tide began to shift. Optimism faltered and stock values stalled. Credit became more difficult to obtain. In June 1825 a debate in the House on whether an individual could refuse Bank of England notes as a payment, demanding gold instead, sounded alarms. On December 12th, the London banking house Pole, Thornton, and Company – the agent for 47 country banks – collapsed, triggering a wave of failures across banks and business. The demand for gold to supply country banks and bank runs forced the Bank of England to act as lender of last resort, draining almost all its gold to the verge of insolvency.⁵ The government advised the Bank “to pay out notes and gold up to the bitter end” (Jones 1967, 114–17). Tension mounted, as the cabinet refused to allow the Bank to suspend cash payments.⁶ On December 15th, it gave its acquiescence

³ Country banks used these intermediaries to mobilize funds from saving areas and to provide capital for investing areas in the country (Parnell 1956, 1).

⁴ Smith (1776, 304) had already mentioned overtrading as the cause for the excessive circulation of paper money in the *Wealth of Nations*.

⁵ In *Lombard Street*, Bagehot cited a Bank official explaining how the Bank lent money “by every possible means, and in modes we had never adopted before” (quoted in Bignon, Flandreau and Ugolini 2012, 596). Timbs (1864, 220) recalled that at the height of the panic, on Saturday 17 December, the Bank closed its doors with slightly over one million pounds in its vaults.

⁶ London bankers and their customers lobbied the government to suspend convertibility to allow them to maintain their credit, but the government refused. William Huskisson, the President of the Board of Trade, threatened the Bank with suspension of its charter if it stopped payments. Kynaston (1995, 21).

to the Bank to issue one-pound notes for the first time since the resumption of cash payments. Eventually, some gold was brought in from France, thanks to Nathan Rothschild. The Bank of England – and the gold standard – stood.

Alexander Baring captured the uniqueness of the episode. A mania like that in London in 1825 had never been seen before. A “frantic spirit” overran the country: “The greatest exertions were made by everybody to get rid of their capital. The bankers in London, their agents in the country, and the customers of both, were actuated by the same universal desire to put out their money in whatever way they could.” Then, suddenly, the mood reversed. Panic seized the public: “Men would not part with their money on any terms, nor for any security, and the consequence was general distress.” The assistance of the Bank of England could provide relief, but not a cure (HC 2 Feb 1826, 76–82).

The time for reforms had come. After a month and a half of debate, the Parliament passed two acts which restricted the issue of banknotes and amended the charter of the Bank of England, allowing the creation of joint-stock banks outside London.⁷ The push for these reforms was led by the government. The Chancellor of the Exchequer Frederick John Robinson presented them in the House of Commons, and the Prime Minister Robert Jenkinson, the Earl of Liverpool, did the same in the Lords.

3. The Causes of the Crisis: Speculation Enhanced by Easy Credit Policies

Parliament opened on 2 February 1826, with the crisis as its main focus. The King’s Speech at the opening session in the House of Lords began: “His Majesty has seen with regret the embarrassment which has occurred in the pecuniary transactions of the country, since the close of the last session of Parliament.” It noted that the cause of the crisis was not an external shock as was usual hitherto. Problems were now different (HL 2 Feb 1826, 1). A lively debate ensued over its causes, the institutions that could be held responsible, and the measures to be taken. The most active MPs in the discussions were “economists” or had an expertise in economic matters, according to the classification provided by Fetter (1980, 7–13) in his study of members of the British Parliament.⁸ These economists aligned mainly with the Whigs. The main participants in the debates were the Earl of Lauderdale, the Marquis of Lansdowne, and Peter King

⁷ The government also tried to extend the gold standard to Scotland, facing strong opposition from the Scots. Protests were led by Sir Walter Scott (Helleiner 2003, 127).

⁸ Fetter distinguished three types of economists: Academicians, “experts” working in relevant economic fields such as finance or industry, and politicians who had acquired economic knowledge through dealing with economic matters. According to his list (1980, 267–268), in 1826, there were 16 economists sitting in the Commons and 5 in the Lords. Not all of them intervened regularly. Some MPs not on Fetter’s list also demonstrated knowledge in political economy during the debates.

in the Lords, and Joseph Hume, Alexander Baring, Edward Ellice, and Henry Brougham in the Commons. On the Tory side, Robinson and Liverpool supported the cabinet's actions and plans, aided by Robert Peel, William Huskisson, and George Canning.⁹

There was broad consensus that the crisis resulted from excessive speculation. The government primarily blamed the over-issuance of paper by country banks, although it acknowledged that the Bank of England's charter should be reformed to allow the establishments of larger banks. Those siding with the Whig opposition argued that it was the actions of the Bank of England that had encouraged overtrading, censuring the Bank's privileges and its concerted actions with the cabinet. They grounded their criticism largely in the works of Tooke, frequently cited, as we will see.¹⁰ Ricardo's influence would have also played a significant role in the amendment of the Bank's charter. Ricardo had been a severe critique of the Bank. In his *Proposals for an economical and secure currency*, Ricardo (1816, 30, 42, 98) condemned the Bank's power to arbitrarily increase or decrease the paper circulation, the excessive payments it received for services rendered to the state, and demanded transparency in its affairs. He denounced the directors of the Bank in the Commons – where he was widely respected – for their conduct during the resumption of cash payments, accusing them of ignoring the principles of currency (Ricardo 1822, 4–5). In his *Plan for a National Bank* – published posthumously – he proposed removing the Bank's power to issue money, transferring it to the government, thus redirecting the profits from interest on issued money to the public (Ricardo 1824, 10). Ricardo's ideas would have contributed to foster an atmosphere hostile to the Bank's privileges. The crisis would have created the momentum necessary to pursue reforms in the Bank.¹¹ On the matter of restricting circulation of banknotes, consensus was not so widespread, even though most economist MPs voted in favour. Tooke (1826b, 138) welcomed it, albeit with some reservations, while Joseph Hume, a close follower of Ricardo, suggested that it run counter to Ricardo's ideas (HC 27 Feb 1826, 356).

Easy Credit and Speculation

Lord King opened the debate in the Lords by ranking the culprits for the crisis: "The causes were, in some degree, to be attributed to the government; in a greater degree,

⁹ They all are in Fetter's list as economists, except for Ellice and Robinson.

¹⁰ Tooke was well-known in Parliament. He had written the famous *London's merchants petition for free trade*, introduced by Alexander Baring (Grampp 1987, 88).

¹¹ Some MPs in the debate were Ricardo's friends or followers, such as Brougham, Hume, and Parnell. Others sympathised with his trade liberalisation ideas, like Huskisson and Robinson.

to the country banks; and in a still greater degree to the Bank of England monopoly.”¹² The government had pursued expansionary policies, allowing country banks to issue one- and two-pound notes, and lowering the rate on Exchequer bills, which led to a reduction in interest rates. Country banks, for their part, had overissued paper. However, the biggest problem was the Bank of England, “a most faulty machine ... an establishment to do mischief” (HL 2 Feb 1826, 7–8). King censured the Bank for having increased its paper issuance. He provided evidence with Tooke’s *Considerations on the State of the Currency*, just published in January 1826, quoting it to describe the effect of the Bank’s issues: “Speculative operations ... necessarily created a large mass of paper and of transactions on mere credit, thus adding to the circulation already swelled by the increase of country bank notes.” This circulating paper “gave a fresh and powerful stimulant to that spirit, and assisted in converting incipient delusion into absolute insanity” (HL 2 Feb 1826, 7–8; Tooke 1826a, 47). Tooke’s work, which apparently circulated widely among MPs, concluded that the Bank had the power to influence the entire circulating medium through various mechanisms: the discount rate, the volume of commercial paper discounted, the sale or purchase of securities (especially Exchequer bills) and advances to the government (Smith 2011, 138–39). When summoned to the Commons committee in 1832 to examine the Bank’s charter, Tooke censured the Bank. Its issues should be regulated according to its reserves and the exchange rate. “In 1824, the drain on the Bank’s treasure should have caused the contraction, and not enlargement of their issue ... the conduct of the Bank, from the close of 1824 till the panic, was perfectly unjustifiable” (Tooke 1833, 78).¹³

Alexander Baring, drawing on his expertise as financier – which gave him the confidence to intervene frequently – also attributed the crisis “to the extent to which the circulation of paper money had been pushed about eighteen months ago,” holding both country banks and the Bank of England responsible.¹⁴ But he criticised the Bank, first, for having triggered speculation by allowing an excess of paper circulating (the Bank could decide the quantity of paper money it issued, but the very business of country banks was to issue all the paper they could), and second, for failing to consider the sterling exchange rate, since overissuing could depreciate the currency. The

¹² Lord King was an “acute analyst of money and the foreign exchanges” (Fetter 1975, 1052). He wrote in 1805 *Thoughts on the Restriction of Payments in Specie at the Banks of Ireland and England*, criticising the suspension of specie payments and warning of excess banknote circulation.

¹³ In his *History of Prices*, Tooke (1838, 181) recalled the “great error committed by the Bank in having extended its circulation in the interval, from the summer and autumn of 1824, to the end of April 1825, instead of contracting it.”

¹⁴ Alexander Baring was the son of Francis Baring from the Baring Brothers banking house. He claimed his outstanding expertise throughout the debates. He later wrote a pamphlet, *The Financial and Commercial Crises Considered* (1847), on the financial disruption of that year.

Bank, “by the facilities which they afforded, had been the authors of that dangerous redundancy of money, that gave rise to the wild speculations which some time ago abounded in every part of the country.” Consequently, the country became saturated with paper money, without regard for the effect it should have had on the exchange rate, which, Baring stated, should be the regulation for the issues of paper money, “as businesspeople know” (HC, 2 Feb 1826, 76–82).

The link between the paper circulation and exchange rate fluctuations was a major concern during the debate, as a significant outflow of gold had occurred in the months preceding the meltdown. Joseph Hume also blamed the Bank for allowing the exchange rate to fall:¹⁵ “If the Bank of England had known the true principles of banking, or if it had taken example by the events of 1793 [the war with France and drain of gold reserves], it would never have allowed the course of exchange to remain for seven whole months against this country” (HC 2 Feb 1826, 57). Even Prime Minister Liverpool, while mild in his considerations of the Bank’s performance, acknowledged that “the state of the exchanges was an infallible medium for regulating the circulation” of paper in the country. He admitted that, when the exchange rate was favourable to Britain (up to September 1824), the Bank should have decreased its issues, but instead, increased them. Nevertheless, he maintained that the Bank soon recognized its error and reduced issues throughout 1825 (HL 17 Feb 1826, 453–54).

The Marquis of Lansdowne did not directly blame the Bank, but also noted that the excess of paper in circulation led to a depreciation of sterling and an outflow of gold:¹⁶ Like King, Lansdowne relied on Tooke’s *Considerations*: “That gentleman had justly stated, that the effect of such an excessive issue of small notes was not only to form an addition to the general capital of the country, but to operate immediately as an addition to that part of the capital which was employed in speculation; and, in proportion as it operated to swell the amount of capital devoted to speculation, it had a direct tendency to raise prices in an artificial degree” (HL 9 Feb 1826, 132–34).¹⁷ Lansdowne observed an accumulation of unsold stock that would be corrected by increased demand triggered by a fall in prices. Drawing on Tooke, he outlined the sequence of events following excessive

¹⁵ Former official of the East India Company, Hume was a reputed author of anonymous pamphlets. Fetter (1980, 235) noted that he “believed in political economy” and understood its broad concepts. He was a firm supporter of Ricardo.

¹⁶ Lansdowne had attended Stewart’s lectures on political economy. He was Chancellor of the Exchequer in 1805–07 and authored *Statement of a Plan of Finance, proposed to Parliament in the Year 1807*, containing projections of expenses, loans, debt, etc. until 1826. He was a member of the Political Economy Club and a leader of the Whigs.

¹⁷ In his 1824 work *Thoughts and Details on the High and Low Prices of the Thirty Years from 1793 to 1822*, Tooke (1824, 63) explained that a great proportion of country banknotes was issued upon land property, farming stock, etc. A tendency towards rising agricultural prices led to increased borrowing and lending, and hence, to the increase in notes.

issuance, culminating in gold outflows: “The first effect of an issue of country bank paper was, to create an artificial abundance of capital; the accumulation of capital caused a reduction of the rate of interest; by the reduction in the rate of interest facilities were afforded for speculation; speculation produced an effect upon prices; the alteration in prices checked the progress of mercantile exports, and that caused the precious metals to be sent out of the country.” The accumulation of stocks at high prices eventually gave way to distress, forcing people to sell at reduced prices. Lansdowne questioned whether a pure metallic system might have prevented such an increase in prices. He argued that issuing paper drives metal out of the country, creating a vacuum, that causes prices to fall far below what they would be under a metallic system. Therefore, he concluded that the alarm some people felt at the withdrawal of paper currency was unfounded (HL 9 Feb 1826, 135–37).¹⁸

Some MPs, in contrast, praised the Bank for acting as lender of last resort at the crisis’s height, breaking standard rules. John Maberly, while blaming the government for having flooded the country with their promissory notes, applauded the Bank’s injection of liquidity during the panic in December 1825:¹⁹ “The weight of thirty millions of Exchequer bills was calculated to produce a great languor in the money transactions of the country ... if the Bank of England had not gone into the Exchequer market, and taken up those bills, the panic would have been ten times more dreadful.” Concerned about the link between paper and the exchange rate, Maberly noted that, if another glut of Exchequer bills triggered a new crisis, it was uncertain whether the Bank could provide relief if exchanges turn against Britain, as the Bank would then be obliged to contract rather than expand its circulation (HC 2 Feb 1826, 66–67). This countercyclical action had other supporters. Vincent Stuckey, a banker, explained in the 1832 Commons committee that if the Bank had followed the state of foreign exchange as a guide and refrained from issuing paper, banks in London and the country would have stopped functioning. He added insightfully: “In ordinary times, if rules are acted on, panics would not occur; when they do occur, new principles come into action.” Nevertheless, he remarked: “It would be a great improvement if bankers were taught to regard the course of exchanges” (Stuckey 1833, 125).

¹⁸ Lansdowne did not mention that in the work he cited, Tooke (1826a, 64) blamed the Bank for having increased “both directly and indirectly the mass of the circulation” when there ought to have been a contraction, promoting extravagant speculation.

¹⁹ John Maberly opened a bank in Scotland circa 1818, with five branches, to exploit the differential on the rates of exchange on bills between Edinburgh and London (Symes 1998).

Adding Fuel to the Fire: Lowering Interest Rates

A key factor in explaining the meltdown was the fall in interest rates, driven by the actions of the government and the Bank, sometimes acting in connivance. Whig MP John Calcraft believed that the Bank's lending money on mortgages and on the security of stock was the origins of the crisis. "Owing to the state of the money market, people could get money at so moderate a rate of interest, that the Bank could not make that profit by their notes to which they thought they were entitled, then it was that they placed themselves in competition with the other bankers who were lending money at a smaller discount." This was the main cause of distress (HC 2 Feb 1826, 75–76).²⁰ McCulloch (1826b, 87) shared this view: The Bank had reduced the rate of discount (preceding or following other banks, this was unclear), leading to a general fall in interest rates. This in turn stimulated borrowing, diverting capitals to supposedly high-yield projects.

Joseph Hume offered a comprehensive explanation of the crisis grounded in the fall in interest rates. In his view, however, the main culprit was the government: It encouraged speculation by reducing interest rates in conjunction with the Bank. The government's policies had been "bolstered up, conformably with the views of the Bank and other public bodies with which the government ought to have had nothing to do." Hume claimed that the conversion of public securities and the reduction of the public debt had been carried out in an underhanded manner. As a result of the reduction of interest on public securities, investors sought better returns by speculating on a range of joint-stock companies and extravagant projects.²¹ But this, he argued, was not the consequence of paper circulation: the same problems would have occurred if circulation was made up entirely of metal. The consequence had been an outflow of gold aimed at foreign investment projects: This shift in mercantile business and the diversion of capital from Britain (which Hume calculated in 25 to 30 million pounds) accounted much better for the distress than the over-issue of a few millions of one- and two-pound notes (HC 20 Feb 1826, 580–95). William Maberly also blamed low interest rates for the speculative mania, holding the government responsible for previous expansionary policies (HC 10 Feb 1826, 222).²²

²⁰ Jones (1967, 114) recalled that the Bank's policy of lending on mortgages (he calculated 1.5 million pounds into circulation before 1826), seemed to have been carried out independently, "without suggestion or supervision by [Chancellor] Robinson." Since 1821, as its charter was not soon to be renewed, the Bank had been acting on its own, feeling free to ignore government advice on policy.

²¹ Horsley Palmer (1833, 17–18), governor of the Bank between 1830 and 1833, endorsed this idea: The reduction of government securities in 1823 and 1824 "excited a feverish feeling and the most absurd projects for investment were readily entertained."

²² William Maberly, son of John, was a member of the Political Economy Club. He evoked Tooke on the causes of the crisis and later opposed the cabinet plan to restrict the circulation of small notes.

Suspensions that the Bank had deliberately acted to lower interest rates revealed an institutional problem that some MPs identified as the true weak point of the British financial system. The Bank owed its loyalty to its shareholders rather than to the public interest. Therefore, it could not be trusted to maintain the proper level of circulation or to link it to the exchange rate. Some claimed that the government was in connivance with it, disregarding national interests.²³ Lord King made it clear: The Bank was a monopoly closely tied to the government. Its directors had “no interest in the profits or loss of the concern ... neither hopes nor fears for the result of their conduct ... no interest in managing it well” (in fact, “they had a strong interest in mismanaging it”).²⁴ The Bank had become too large to be properly managed. Its monopoly should end (HL 2 Feb 1826, 7–8). Henry Brougham asserted that “twenty-four men could not have in their hands the interests of the country,” as they were guided by their own self-interest in managing issues, rate of interest, etc.²⁵ He called for the revocation of the Bank’s monopoly for the sake of the stability of the money market and commercial transactions (HC 2 Feb 1826, 35–40). Joseph Hume also opposed the Bank’s privileges, noting that its directors had the power to raise and sink the market at their pleasure. Quoting Ricardo, he stated that it was actually the duty of the directors to make the best bargain with the government, for the benefit of the proprietors (HC 2 Feb 1826, 58 and 419). Henry Parnell, another economist siding with the Whigs, argued that the Bank would continue issuing paper as it remained profitable for its proprietors. He cited Tooke’s *Considerations* to show how stocks and property had been sold at losses of 20–30 percent during the crisis. He supported abolishing the Bank’s joint-stock monopoly in London (HC 14 Feb 1826, 390–92).²⁶

²³ William Maberly noted two prevailing opinions on the causes of the crisis: first, that it was occasioned by the connection between the Bank and the government; second, that it was due to overtrading and mania for speculation (HC 10 Feb 1826, 221).

²⁴ Calomiris and Haber (2014, 115) argue that the public learned three lessons about the Bank during the crisis: It could not be relied on to manage the supply of money and credit in the economy; it was insufficiently committed to the public good; and its privileges made the system too centralized in London.

²⁵ According to Fetter (1980, 24), Brougham attended Stewart’s lectures on political economy in Edinburgh. He made some economic contributions in the *Edinburgh Review*.

²⁶ Parnell was one of the main bullionists in the bullion controversy, advocating a return to convertibility to avoid excess note issuance and hence inflation. He proposed implementing Ricardo’s plan of paying notes on demand in bars of gold to economise gold coins while keeping the gold standard. Ricardo’s Ingot Plan was considered unworkable by Tooke, based on his empirical research, as the Bank of England did not have enough control over the quantity of country banknotes in circulation (Skaggs 2003, 180).

A Matter of Trust? The Scottish Banking System

The differing behaviour of the Scottish and English banking systems during the crisis emerged in the debate as another key explanatory factor of the crisis. Scotland had a system of joint-stock banks and there had been no over-issuance of banknotes. Lord Lauderdale attributed this to trust: The Scottish banking system had the confidence of the people – something that could not be said of the English. In Scotland, bankers knew each other, met regularly, exchanged notes, and settled balances in gold, or in Bank bills at sight. For this reason, he opposed the withdrawal of small banknotes in Scotland (HL 17 Feb 1826, 477–78). McCulloch expressed a similar view in *On Fluctuations in the Supply and Value of Money and the Banking System of England*, published in 1825. In Scotland, with scarce population and economic activity, financial institutions had detailed knowledge of the circumstances of merchants and dealers. The small number of issuing banks enabled them to assist each other in time of distress. In contrast, England had hundreds of country banks issuing paper, making it impossible to detect when over-issuance had occurred (1825, 19–21). This did not imply that the Scottish banking system was invulnerable: McCulloch (1825, 20) admitted that, during the crisis, Scottish banks “were then, we shall not say on the brink of destruction, but certainly in a state of very great danger.”²⁷ Edward Ellice attributed the stability of Scottish banks both to good fortune and sound management (HC 2 Feb 1826, 55–56).²⁸ The idea that the Scottish financial system was more robust than the English was endorsed by Thomas Joplin in his popular pamphlet *On the General Principles and Present Practice of Banking, in England and Scotland*, first published in 1822, with some re-editions. He called for the end of the Bank’s monopoly so that joint-stock banks could spread (Joplin 1826, i–iii). Liverpool and Robinson had likewise acknowledged the solidness of the Scottish banking system in their exchanges with the directors of the Bank of England.

Dissenters: The Crisis was Not monetary but Real

The main dissenter on the causes of the crisis was Lauderdale.²⁹ He denied that it was the result of excessive paper circulation: The rise in prices stemmed from an alteration in the proportion of the quantity of various commodities relative to one another. The

²⁷ Lauderdale read McCulloch’s pamphlet and expressed absolute rejection: “The writer did certainly advance a most extraordinary proposition—extraordinary from its total inaccuracy in point of fact, and no less extraordinary from its total absurdity in point of argument” (HL 17 Feb 1826, 477–78).

²⁸ Ellice was a businessman with interests in Canada. In 1819 he supported the resumption of cash payments.

²⁹ Lauderdale was a strong supporter of the idea that paper currency convertible to gold on demand was best suited for business transactions. He advocated Britain’s return to the gold standard as a measure to stabilize the currency in his *The Depreciation of the Paper-currency of Great Britain Proved* (Lauderdale 1812). Lauderdale appears as a Whig in Fetter (1980), but in the 1820s sided increasingly with the Tories.

cause of this imbalance was the sinking fund: It had within a few years been established on an effective footing of 5 million pounds annually, instead of the former 1 million. This capital was being “thrown in annually to seek employment among the other interests,” thereby generating increased demand and, consequently rising prices (HL 17 Feb 1826, 468–71).³⁰ Lauderdale would oppose the bill restricting the circulation of one- and two-pound notes, arguing that there was no solid evidence that an excess of paper, payable in cash on demand, produced a rise in commodity prices. The true cause of the distress lay in the transition from a situation in which the country benefitted from an extra supply of capital to one in which there was an extra demand for it. The “forced conversion of revenue into capital by the sinking fund” had pushed prices upward. The fall in interest rates in 1824 and 1825 led investors to engage in speculations. The demand for capital drove interest rates up, which limited credit and led to a contraction in transactions, ultimately causing suspension of payments and bankruptcies (Thorolds 1875, 1–4).

Another dissenting voice – albeit a later one – was that of Parnell. In his *Observations on Paper Money* of 1828, he challenged the prevailing view that the crisis had been caused by the excessive issuance of paper. His new thoughts were that the origins of overtrading lay in “higher prices arising from causes wholly belonging to trade” (Parnell 1828, 39). The decline in trade and prices in 1821–22 had led to reduced production and imports, which was followed by prosperity and inflation in 1824–25. This was the outcome of the previous drop in production, an improvement in agricultural output, the opening of South American markets, and the loans raised for these new republics. In 1824 demand started to fall, but producers continued increasing their output. This caused over-supply, a general glut, and falling prices, resulting in stagnation. So, the deep cause of the crisis was a miscalculation by merchants and manufacturers regarding the persistence of high prices (1828, 44–45).

4. Discussing the Reforms: The Bank Charter and Issuance of Banknotes

In January 1826, after the peak of the crisis had passed, the government prepared its response. The cabinet had two points for action: First, the cause of the crisis was “the rash spirit of speculation” enhanced by over-issuing of notes by country banks. It was deemed necessary to check it. Second, the banking system had proved defective. To strengthen it, joint-stock banks should be allowed, which required that the Bank of England relinquished its monopoly. On January 13, Liverpool and Robinson sent a memorandum to the Court of Directors of the Bank, outlining the two measures they

³⁰ Lauderdale said that Tooke attributed to high prices the propagation of joint-stock companies and speculation (HL 17 Feb 1826, 470).

envisaged.³¹ To redress country paper circulation, they proposed a return to gold by repealing the act which enabled country banks to issue one- and two-pound notes. This would control speculation, ease pressures on the Bank and on London arising from potential currency depreciation, and counteract the exports of metal. However, the main problem of the British financial system was the Bank of England, “no longer sufficient ... to meet the demands of the present times.” While the cabinet lacked the competence to regulate country banks, it could attempt to establish a “sound system of banking” by allowing joint-stock banks and branches of the Bank. They thus urged the Bank to surrender its privilege (Bank of England 1826, 200–15). The Bank was not caught off guard. An internal committee had already concluded that branches would be beneficial to the Bank: deposits and circulation of its notes would increase, and they would compete with joint-stock banks. The committee noted that resisting government pressure would likely prove difficult. Eventually, after some resistance, the Directors accepted joint-stock banks outside London (Bank of England 1826, 222–31).³² The cabinet obtained its objective: the Bank’s concession to be presented to the Parliament.

Liverpool outlined these plans in the Lords, insisting that the cause of the crisis was speculation – “rash spirit of speculation,” “general spirit of mad speculation,” “over-trading and rash speculation” – primarily encouraged by country banks. He refused to enact measures against speculation and warned that those involved should not expect public assistance: The remedy would rather lie in individuals’ awareness of risk.³³ He denied that the government had pursued policies to lower interest rates: The rise in the price of public securities and the fall in interest rates were outcomes of economic prosperity, from which the government profited to reduce both taxes and the interest on the national debt (HL 2 Feb 1826, 16–19).³⁴ In the Commons, Robinson presented the government’s plan to limit the issue of small notes and withdraw one- and two-pound

³¹ Robinson was considered among the most liberal members of the cabinet. According to Jones (1967, 35), he had probably read Adam Smith and should have known Ricardo’s work on currency and bullion.

³² The model was the amendment of the charter of the Bank of Ireland in 1821. The Bank would remain a chartered corporation and the only institution managing public debt.

³³ Tooke (1833, 80) said that the system relied on bankers’ interests in maintaining a stable system. He stated: “The crisis of 1825 was necessary to purify the system of banking in town and country.” Despite Robinson and Liverpool’s vows not to aid speculators, merchants – backed by the Bank of England – demanded that the government issue Exchequer bills, which they could cash at the Bank. Robinson feared government loans would foster more speculation. Eventually he found a compromise: the government would fund part of its debt to the Bank, which in turn would lend to merchants using their merchandises as collateral (Tooke 1838, 169–70).

³⁴ The government’s position was endorsed by McCulloch (1826b, 84): The crisis was the consequence of both over-trading and excessive issuing by country banks, but especially the latter. McCulloch (1826a, 271–74) explained that country bankers increased issues when prices rose (he recalled opinions that country bankers proportion their issues to the price of corn). In 1823, prices rallied, confidence grew, and the issues of country banks exploded. When prices fell, paper contracted “occasioning a most destructive revulsion.”

notes from circulation, replacing them with metallic currency.³⁵ His argument was that small notes primarily circulated mostly among the labouring classes, who were most vulnerable to country banks' failures. The damage caused by panic and depreciation when paper became worthless far outweighed any benefits of their circulation (HC 2 Feb 1826, 47–54).³⁶ Tooke had also made this argument: Small banknotes exposed the lower classes – constrained to accept them as wages and for other payments – to losses in the event of issuing banks' failures (Smith 2011, 154). Ricardo had also referred to this problem (1816, 55–56).³⁷

The amendment of the Bank's charter to allow joint-stock banks was not contested: There was consensus to restrict the Bank's monopoly. The bill on small notes sparked debate, as some MPs disagreed. Robinson and Baring engaged in a tense exchange. Drawing on his financial expertise, Baring emphasized the importance of uncertainty and expectations in finance, urging the government to clarify its measures to reduce uncertainty: if a curtailment of country bankers' powers was announced, investors might rush to withdraw their capitals.³⁸ The key to building solid banks in towns, he argued, was public confidence. This could be achieved either through branches of the Bank – although these would face opposition for interfering with provincial interests – or through large joint-stock banking companies. Baring thus supported the reform of the Bank's charter, but remained doubtful about its supposed beneficial consequences, as investors would be reluctant to participate in such schemes, risking their capitals without having decision-making capacity. To encourage them, Baring proposed limiting the liability of associates in such banks. He also strongly supported the idea that circulation in Britain should consist of silver and gold (HC 2 Feb 1826, 76–82).³⁹

³⁵ Robinson's bill allowed circulation of promissory notes dated before February 5, 1826, only until April 5, 1829, and restricted new issuing. He acknowledged that his plan would not prevent speculation, but that issues would be more secure (HC 10 Feb 1826, 168–93).

³⁶ There were few mentions in the debate of the crisis's effects on the working class. Lansdowne pointed out that workers should be protected from speculation: "Excessive paper despoils people of their property," as if they were robbed. In country towns, local paper was usually the only currency in which labourers were paid. Lansdowne supported the withdrawal of small notes (HL 9 Feb 1826, 132).

³⁷ Adam Smith (1776, 274) had already warned in this direction.

³⁸ The role of expectations was highlighted by some MPs. Beliefs, even unfounded, played an important role in the panic. MP Thomas Green stressed that the fall of the weakest country banks pulled down others that were solvent but could not meet a sudden demand for cash (HC 2 Feb 1826, 29–31). J.S. Mill pointed this out in his analysis of the crisis (Béraud 2013).

³⁹ Fetter (1965, 124) pointed out that the crisis increased interest in bimetallism among a reduced group of Tories. Huskisson prepared a memorandum to the government supporting Baring's bimetallic proposals. Huskisson thought that silver monetization would enhance commercial relations with Latin America, provide a wider metallic basis to the monetary system and give the Bank more freedom to meet external drains. Lauderdale also supported a bimetallic standard, recommending the adoption of silver as a standard (HL 17 Feb 1826, 476). He held this position in the debate on the gold standard in 1816.

On the specific issue of country banks' paper, Baring bitterly observed that the proposed remedy – “unworthy of men who ought to know what was the situation of the country” – would likely aggravate rather than alleviate the distress. While he acknowledged that one-pound country banknotes were problematic, he considered that their reduction and replacement with gold should only begin after the emergency had passed. Gold was necessary to replace paper, but it was a mistake to claim that, by contracting its issues, the Bank could attract gold into the country. This would only occur if Britain exported commodities in exchange for it. Britain had obtained gold easily after the war because there was strong demand for British manufactures – something that was no longer the case. For Baring, it was then the time to restore the currency, but the government did not do it because it feared strong opposition from country banks. The Bank had accumulated a large store of gold and silver in 1823 and 1824, increased dividends, and made large issues of paper. Country banks followed suit. This excess circulating led to a fall in interest rates: “The Bank saw and felt what was going on” (HC 10 Feb 1826, 194–99). Baring did not stand alone in his rejection of this measure. Hume also declared himself against it. In his opinion, the crisis was unrelated to the circulation of small-denomination paper, so the proposed remedy was misguided (HC 13 Feb 1826, 356). Moreover, following Ricardo, he stated that the plan implied that “[paper] must be replaced by a much more expensive currency, which would have to be purchased by substantial capital, and must, consequently, withdraw so much of it from being applied in advancing the trade and manufactures of the country” (HC 27 Feb 1826, 879).⁴⁰

Another major critic of the government's measures was Lauderdale. In his view, the crisis was not monetary, and therefore the remedies were misguided. The cabinet attributed the depreciation of the exchange rate to the over-issuance of paper, but Lauderdale argued that other causes – such as an unfavourable balance of trade or payments – could be responsible. He maintained that the exchange rate could never run against a country beyond the expense of transporting gold between countries. He asserted that the exchange had never shown a depreciation of the currency when paper was convertible into gold (HL 14 Mar 1826, 1357–58). Lauderdale believed the crisis had been artificially triggered by Liverpool's speeches, which led the country to believe that “it was rotten to the foundation,” and that the primary cause of the problems lay

⁴⁰ Other economist MPs who opposed this measure included Matthias Attwood, John Calcraft and both Maberlys. William Heygate was also against it. Charles Grant acknowledged that Ricardo was opposed to the principle, but he believed that, had he witnessed what had occurred, he would have changed his opinion. He voted for the bill (HC 13 Feb 1826, 273).

in the one- and two-pound notes. To restore confidence, he supported providing relief to merchants through the use of Exchequer bills (HL 27 Feb 1826, 874).

Eventually, resolutions were passed prohibiting the issuance of new promissory notes under 5 pounds in England, allowing those already issued to circulate until April 1829. The Bank was granted temporary permission to issue small banknotes until October 1826. The Bank's monopoly on joint-stock banking beyond 65 miles from London was repealed and the establishment of provincial branches was authorised.⁴¹ The extension of the Bank's right to issue notes provoked considerable protest, revealing the Bank's lack of credibility among some MPs. Brougham claimed that the Bank would fill the vacuum in paper circulation with more of its own notes, returning the country "to the same state of little else but paper" (HC 20 Feb 1826, 635). Maberly demanded that the Bank publish a monthly account of its issuance of notes (HC 20 Feb 1826, 578). He cited Tooke in criticising "the secrecy and mystery in which all the proceedings of the Bank of England are enveloped" (HC 27 Feb 1826, 894). Hume extended this demand to include all banks (HC 27 Feb 1826, 881), while Pascoe Grenfell suggested such accounts be published weekly (HC 20 Feb 1826, 573). Robinson accepted reports on the Bank's small notes circulation, but not on every issue it made (HC 27 Feb 1826, 893).⁴²

The Parliamentary debates prompted Tooke to publish a second edition of his *Considerations* with some new notes and a postface addressing the discussions.⁴³ Interestingly, Tooke's views aligned with those of MPs who, while welcoming the measures, also expressed doubts, which suggests that he could have had influence in the debate, on both the cabinet and the opposition.⁴⁴ Tooke (1826b, 138–43) welcomed the prohibition of country banks' notes under five pounds, but criticised the extension granted to the Bank's own notes. The justification – to fill the vacuum in the country circulation – was insufficient, since it might result in an oversupply of the Bank's notes, rendering the eventual substitution of coin for those notes a matter of great difficulty. Tooke also endorsed the amendment of the Bank's charter but feared its benefits would be insignificant due to the weak incentives for capitalists to engage in such ventures. Like Baring, he proposed limiting the liability of the proprietors to the amount of their shares. Finally, to restore confidence in the banking system, Tooke

⁴¹ They crystallized in the Bank Notes Act of March 22nd and the Country Bankers Act of May 26th, 1826.

⁴² One of the main conclusions of the 1832 Commons committee was that the Bank should be placed under Parliamentary scrutiny ("Observations" 1833, 83–84).

⁴³ The "Advertisement to the second edition" is dated February 22nd, when the debate was already well advanced.

⁴⁴ At one point, John Maberly observed that Tooke's opinions seemed to have formed the basis for many of Robinson's measures (HC 27 Feb 1826, 894).

recommended that joint-stock banks provide biannual reports of their transactions, funds and engagements.

5. Political Economists vs. Practical Men

Many MPs in the debate grounded their interventions in the principles of political economy and the authority of economists. However, other – particularly those connected to the banking business – expressed reservations about the suitability of political economy to deal with the crisis. In their view, it was an overly abstract or theoretical field, whereas finance was a matter of experience and pragmatism, ill-suited to fit within theories. In the debate, they opposed to political economists the figure of the “practical man,” qualified through practise and experience. This friction became particularly evident in the discussions surrounding the withdrawal of small banknotes: “practical men” – that is, bankers and financiers – were generally opposed to the measure, while “political economists” were generally in favour (there were exceptions, such as Hume and Lauderdale). Interestingly, this divide did not align with political party lines: cabinet members backed the views of political economists, while some “practical men” sided with the Whigs.

In his exchange with Robinson, Baring notably described political economy as a vested interest in the House, competing with others: “There might be some gentlemen in the House who were disposed to legislate for our present difficulties on the pure principles of political economy; some whose remedies would have reference to the protection of the agricultural interests; some who would look chiefly to the commercial, and others to the banking, interests.” He accused Robinson (whom he regarded as a political economist) of dogmatism: “There were, in all cases, to be found men so wedded to theory, that when a particular emergency arose, they immediately recurred to their books and to the adoption of a certain set of rules there laid down, without ever considering, that it would be necessary to adapt the remedy to the actual situation of things” (HC 10 Feb 1826, 194–96). William Heygate,⁴⁵ a banker opposing the withdrawal of one-and two-pound notes of country banks, remarked acrimoniously: “Several theorists, who had written books on this subject, had stated, that it might be done, and that it would be a beneficial measure; but scarcely any of those theorists or book-writers agreed with one another, or even for two years with themselves. Mr. Tooke differed from Mr. Ricardo, and from Mr. M’Culloch, who had come down from Heaven to illuminate us on the subject of political economy; but, in truth, there was no reliance to be placed on these theorists.” Instead, he suggested “a practical man” to be asked the likely effects of that resolution (HC 13 Feb 1826, 277). Later, debating on free

⁴⁵ Heygate distinguished himself in 1819 as an opponent to the resumption of cash payments.

trade, he urged: "Let them abandon theory, and look to practical experience," adding that political economists did not care about the effects of free trade as long as it created profit: "If profit could be ultimately obtained, they overlooked the misery which was created in the interim" (HC 13 Feb 1826, 285–86).

Foreign Secretary George Canning, rejected the accusation of Heygate "of imputing to every man who thinks it possible to apply the principles of philosophy to questions of a practical nature, the character of theorist and enthusiast, a person disposed to resign the greatest benefits, and to sacrifice the dearest interests of the community, in order to give effect to his own abstract principles" (HC 13 Feb 1826, 321). Baring, in turn, drew a dividing line between "talented" political economists and "practical" bankers and merchants: "On the other side of the House there was great strength in the way of talent... great force of those who studied from books, and held practical men in contempt." He "complained of the great fondness that was entertained by some gentlemen for their particular views; who, when once they got the patient within their power, a theory having opened to them previously, proceeded with their operation; the agony and suffering of that patient causing no remorse or abatement in the rigour of their practice." He remarked that only one man of business had supported the withdrawal of small notes. Brougham likewise highlighted the clash between theory and reality when he argued that the coexistence of convertible paper with gold was impossible: This is "contrary to all theory upon the subject, and at variance with all the positions laid down by political economists; but it was a truth" out of experience (HC 13 Feb 1826, 343–45, 351).

The next day, Heygate reiterated his opposition to "cold-blooded" theories that ignored real-life circumstances and people's needs. He accused the government of having adopted a "liberal policy," contrary to the will of citizens, with the exception of political economists: "Everyone who spoke plainly, did not scruple to say that the people were to be sacrificed to a cold-blooded theory. Excepting the members of what might be called the Political Economy Club, there were no persons to be found who approved of ministers on this occasion." In contrast, Hume rejected that the "principles of political economy" were disconnected from practical affairs. He argued that these principles just sought to apply to the affairs of the State what would be reasonable for individuals to do in their own households, namely, to conduct domestic arrangements properly and ensure that expenditure did not exceed income (HC 14 Feb 1826, 393–94). In the subsequent discussion on whether assisting merchants conformed to political economy principles, Huskisson pointed out that "practical men" themselves were not consistent either: "Many of those practical men ... were not agreed amongst themselves, as to the measures that ought to be pursued; and not only so, but that, following their own particular theories, they came to conclusions diametrically opposite to each other" (HC 14 Feb 1826, 401).

6. Concluding Remarks

The crisis of 1825 had a profound impact in Britain. As Lansdowne witnessed, there was a “scene of complicated misery, and distress” in a town where a local bank had failed, with the evils being felt “in all their severity by the labouring classes” (HL 9 Feb, 133–34). Baring recalled: “The extent to which that distress had reached was melancholy to the last degree. Persons of undoubted wealth and real capital were seen walking about the streets of London, not knowing whether they should be able to meet their engagements for the next day” (HC 2 Feb 1826, 78).

The Parliamentary debate on the crisis was rich. The MPs most actively involved were economists or experts in finance. Most of them relied on the principles of political economy to support their arguments, citing and engaging with leading economic thinkers. Tooke was an immediate source of authority and Ricardo’s ideas were in the background. Some MPs, particularly those with banking experience, were sceptical of economic theoretical approaches. Economist MPs criticised the Bank and the cabinet for their easy credit policies, regardless of the public interest. They advocated for liberalising the British financial system by curtailing the Bank’s privileges and increasing its accountability. Most of them also supported the withdrawal of small-denomination banknotes and their replacement with gold – except, notably, those linked to banking, the “practical men,” but also some others. Calomiris and Haber (2014, 114) have argued that specific historical events can precipitate long-contemplated changes: “In English banking, the galvanizing event was the banking crisis of 1825.” The economic-political process examined here played a significant role in transforming this crisis into the galvanizing event that laid the foundation of a British banking system that became a pillar of its economic success.

As Grampp (1987, 87), noted regarding the 1820 free trade debate, economic ideas were influential because they were the ideas upon which politicians claimed to act. The same conclusion can be drawn here: Economic ideas influenced the Parliamentary debates and their outcome, namely the reduction in the Bank’s privileges and changes to monetary circulation in England. Neal (1998) acknowledged that, although the 1826 reforms were “minor in each particular and slow to take effect,” their cumulative effect laid “the basis for Britain’s dominance in the world financial system until the outbreak of World War I.” The economic ideas in both Houses during February and March 1826 had something to do in it.

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