



**HISTORY OF FINANCIAL CRISES**  
Or “Money, Banking, and Financial Crises”  
PPHA 42521 Spring 2020  
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**COURSE SUMMARY**

Money, debt, and banking have all been central to the emergence of modern nation-states, and are critical to the functioning of any economy. Financial crises, however, have been a recurrent theme in both developed and developing economies. The 2008 crisis fits into a long history. We all know the Great Depression but the U.S. also experienced speculative booms and busts in 1907-08, 1892-93, 1873. France and England suffered speculative manias in the early 1700s (the Mississippi bubble in France, the South Sea bubble in London). The goal of this course is to investigate what we can learn about money, banking, debt, and macroeconomic or systemic risk through examination of financial crises throughout history. These lessons of history are important whether it is the South Sea bubble of 1700s or the mortgage debt crisis in the United States in the 2008, financial crises have shaped our world. Understanding history is the first step towards intelligent policy.

We will examine the financial and economic history, using episodes of crisis to learn about government debt, money, and banking. We will try to understand some of the mechanisms and processes that seem to generate financial crises. We will read some of the classics as well as some of the newer texts in this area:

- Fragile by Design* by Charles Calomiris & Stephen Haber (for a cogent and disciplined analysis of banking systems across time and across countries US, Canada, UK, Mexico, and Brazil)
- A Free Nation Deep in Debt* by James Macdonald (an interesting hypothesis that debt capacity and debt management has been central to the growth of democratic republics)
- A Monetary History of the United States* by Milton Friedman & Anna Jacobson Schwartz (for discussion and data on the financial crises of 1897, 1907, 1929)
- This Time is Different Eight Centuries of Financial Folly* by Carmen Reinhart & Kenneth Rogoff (for why this time is *not* different financial folly has a long history)
- Manias, Panics, and Crashes* by Charles P. Kindleberger (for a history of, but also a “theory” of financial panics)
- Extraordinary Popular Delusions and the Madness of Crowds* by Charles Mackay (for a history of the 18<sup>th</sup> century South Sea Bubble in Britain and the Mississippi Company in France)
- Lords of Finance* by Liaquat Ahamed (a popular and entertaining account of the 1920s and the Great Depression through the perspective of four central bankers: Strong, Norman, Moreau, Schacht)

**COURSE STRUCTURE & GRADING**

The class is primarily lecture, with student presentations every-other-Wednesday. I will choose two groups to do a short (20-minute) presentation in class:

- Noon Monday you post a discussion topic (by group) related to the readings
- Noon Tuesday I choose two to present on Wednesday – 20 minute presentation

I will assign a few problems related to past crises. There will be a final paper due at the end of the quarter, with a proposal due by the middle of the quarter. Both problems and presentations are to be done in groups. I may assign a mid-term. Grading will be roughly 10% problems, 30% class participation, 25% midterm, and 35% final project.

## TOPICS

This course will be as much about Money, Banking, and Debt as about Financial Crises – for the simple reason that financial crises fundamentally revolve around issues of money, banking, and debt.

We will cover three big topics:

### I. Government Debt and Financial Market Modernization

- Examine three episodes of financial crisis
  - South Sea (London 1720), Mississippi Co. (Paris, 1720), US 1792
- Often presented as irrational bubbles, manias, frauds.
  - Mackay, Kindleberger, The Economist
- They were, sometimes spectacular panics & manias. But there is more, much more, to the story.
  - In these three instances it involved building gov't debt markets and restructuring gov't debt. For US (1792), London (1720) the effort was successful. For Paris (1720) it was not terribly successful. France defaulted 1715, 1770, 1788
  - The US in 1792 was particularly extraordinary. In a few short years (roughly 1789-1793) the US built a modern financial system. Only the Dutch (roughly 200 years earlier) and Britain (roughly 70 years earlier) had managed this transformation. France failed in 1720.

### II. Money and Banking

- A. Through the lens of US Banking Crises 19th & 20th century
  - 1. Very regular: 1814, 1819, 1837-39, 1857, 1873, 1893, 1907, 1929-33, 1982-87, 2008
  - 2.
- B. We need to study “What is Money?”, “What is a liquidity crisis?”, and “What is a bank?”
- C. Money
  - 1. Liquidity crises through the lens of US banking crises, particularly 1893, 1907, 1930s
  - 2. Inflation & Hyperinflation – Germany. Surface: Ahamed chapters 7, 10. Underlying: Cagan
    - i) “Inflation Tax” vs default by inflation
    - ii) World inflation: section on inflation and default by inflation
- D. Banking
  - 1. Primarily through the lens of US banking crises, particularly 1893, 1907, 1930s
  - 2. Deposit Insurance: alternate views. Diamond & Dybvig, Calomiris & Haber, Calomiris & Jaremski

### III. Theory Behind Banking Crises – Calomiris & Haber *Fragile by Design*

- A. Theory of banking, financial system structure, and property rights
- B. The development and history of US banking
  - 1. 1830-1980s: Unit banking, populist agrarian / small banker coalition, and fragile US system
  - 2. 1990s-present: National banking and urban populist / large bank coalition
- C. Mortgage risk and the global 2008 financial crises