

The day the King defaulted

Prof Moshe Milevsky | York University | 15 March 2016

On 5 January 1672, almost a decade after King Charles II was restored to the throne, the British Exchequer, which was part of the government's Treasury department, suspended all payments to depositors, investors and bondholders. By the King's direct orders, no interest, no principal and no money was to be paid to anyone. And despite this being the middle of the 17th century, it was an unprecedented act that ruined many prosperous goldsmith-bankers of that era who had advanced the majority of the money.

This episode is known as the infamous "stop of the Exchequer" and it is the last time the British government or monarchy defaulted on debt payments. It seems that – not unlike many indebted consumers in the 21st century – King Charles II had incurred large personal debts to support his lavish lifestyle, opulent castles and many mistresses. And, when he experienced what today might be labeled a "liquidity shock" (in this case, an expensive war with the Dutch after some ill-timed plagues and fires), his house of cards came crumbling down. The King defaulted.

Alas, the goldsmith-bankers who had lent him millions of pounds in loans amounting to over a quarter of national tax revenues were themselves debtors to many smaller depositors, creating a chain reaction of financial misery. The goldsmith-bankers, London's leading financiers, ended-up languishing (and dying) in debtor's prison. Unlike today, in the 17th century, creditors couldn't declare bankruptcy, walk away from their obligations and start afresh. They faced a miserable existence in the Marshalsea or Newgate. Of course, the King himself couldn't be locked-up! The buck stopped at the goldsmith-bankers.

I should emphasise that although many readers might have never heard of the stop of the Exchequer and few modern financial economists and authors have given it much attention, it wasn't a minor or trivial episode of financial misery. It reverberated throughout England and was no less scandalous than (that better known shenanigan) The South Sea Bubble.

Now, don't take my word for it. Writing in his celebrated book History of England about the stop of the Exchequer, the famous 18th century philosopher David Hume stated: "The measure was so suddenly taken, that none had warning of the danger. A general confusion prevailed in the city, followed by the ruin of many. The bankers stopped payment and merchants could answer no bills."

The prominent diarist John Evelyn, and contemporary of Samuel Pepys, wrote in his entry for that particular date: "An action which not only lost the hearts of his subjects, but ruined

many widows and orphans and the reputation of the Exchequer for ever. Never did his majesties affairs prosper to any purpose after it."

Even three centuries later, the verdict on "the stop" is unambiguous. "The effect was largely destructive and it figures in English history as a catastrophe little less scandalous than the South Sea Bubble," according to one of the most prominent (mid 20th century) economic historians, Professor Henry Roseveare.

I believe this fascinating (but neglected) episode serves as a launching pad into the very modern day problems, stresses and risks of too much debt. I plan to tell the complete story of the financial default of the Merry Monarch, but through the lens of modern financial planning. I will cover the precarious history leading up to the infamous day in 1672, the intrigue surrounding "the stop" – including those who traded on inside information beforehand – as well as the attempt by distressed creditors to gain financial restitution. (One banker tried to seize Queen Catherine's Portuguese dowry!) Of course, most English commoners had little sympathy for the plight of these rich bankers, echoing sentiment after the financial crises of 2008.

The story here is more than a 360-year-old tale of government finance or political economy. It offers practical lessons to indebted consumers in the 21st century. How much debt is too much? What is the optimal amount of debt? At what age should your debts be paid off? These are critical (and deep) economic questions.

Stay tuned for more...



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