

THE FAILURE OF THE BANK OF BOMBAY, 1840-1868

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ABSTRACT

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When the American Civil War broke out and cut off the chief source of cotton to the European trade, the price of cotton rose and merchants and cotton dealers in Bombay were given the opportunity of realizing profits previously unheard of. These profits as they returned to Bombay, produced a plethora of wealth far beyond the requirements of a bona fide trade. Therefore an extraordinary means of investment became a necessity. People came to possess money for which they saw no legitimate vent and so hunted out new schemes in which to invest their money. Diverse, bubble concerns sprang up and Bombay went mad with the spirit of speculation. Shares rose to a price which invariably led to the formation of more, and credit was extended and speculation encouraged.

The Bank of Bombay, chartered in 1840, one of the three Presidency Banks of India, played a prominent role in fostering this speculation. Under a new charter, Act X of 1863, which relaxed its previous strict banking code and with weak, unknowledgeable officials as managers who had come under the corruption of Premchund Roychund, the greatest entrepreneur of the island, the bank broke every sound principle of business finance. The Government of India seemingly the protector of the bank, in truth had no effective

control over the bank's practices.

The panic which followed the cessation of hostilities in America brought about a reaction in prices in Bombay. Buyers could no longer be found for shares in the market place and soon the new companies were forced to liquidate. The Bank of Bombay unfortunately continued to practice unsound banking practices, and kept on advancing money on poor security. Finally in January 1868 the Bank of Bombay went into liquidation. It returned only about one-fiftieth on a fully paid share.

A Royal Commission chosen by Governor General Lawrence performed an investigation into the causes of the failure of the bank. The report issued by this Commission condemned the management of the bank and the unorthodox banking procedures granted by the Government Act of 1863, citing the exceptional nature of the times which should have caused more vigilance on the part of everyone concerned with the bank.

The new Bank of Bombay, Limited, which was chartered shortly thereafter, flourished, profiting by its predecessor's example and reverting to a strict charter and wise, experienced management.

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CHAPTER I

FIRST YEARS OF THE BANK OF BOMBAY:

BACKGROUND AND CHARTERS OF

1840 AND 1863

A well-known Liverpool merchant visiting Bombay in January, 1863 wrote of the striking changes which had taken place since his last visit. He noted the presence of

tall chimneys with dense volumes of black smoke issuing from them, reminding one of our own manufacturing towns in England. . . . there are already nine mills at work or in process of erection on this island, and there is little doubt but that the manufacturing interest has got a permanent impulse and will continue rapidly to advance. Bombay is just now beginning to make great strides in commercial progress and you may rely upon it, it is destined to become the emporium of the East.¹

During the whole of the British period Bombay was, with Calcutta, one of the two largest and most important cities in India. Bounded within the confines of a long, narrow island, Bombay is extremely picturesque, facing the sea with the magnificent Western Ghats Mountains towering in the background. Bombay had the finest natural harbor in India and was the nearest port of call for the traffic of the Indian Ocean

¹London Times, February 16, 1863, p. 5, col. 6.

as well as for trade with Europe and Asia. The expansion of trade during the first half of the nineteenth century resulted in the multiplication of the island's commercial facilities. A group of English and Indian merchants established a Chamber of Commerce in 1836 and joint-stock banks gradually replaced the old system of agency houses for banking, the first being established in 1840.

Lord Elphinstone, the Governor of Bombay from 1854 to 1860, upon leaving his post, commented on the rapid growth of Bombay trade:

This rapid extension of commercial enterprise is, I am happy to think, not owing to wild speculation or to any other temporary and fortuitous cause. It is chiefly owing, I believe, to the steadily increasing demand for European manufactures in this country and to the growth of a corresponding demand for our exports in Europe. The extension of railways and the gradual improvement of our internal communications, must have an important influence on the development of our trade.²

Until 1860 the progress of the trade of Bombay had been a sober, steady evolution advancing with the growth of railways and communications. But the great growth and change of Bombay which the Liverpool merchant noted in 1863 was due to a novel factor--the American Civil War. The blockading of the southern ports and the cessation of American cotton

²D. E. Wacha, Premchund Roychund (Bombay, 1913), pp. 25-26.

exports, forced the European textile industries to depend on Indian cotton. This led to an expansion of trade which brought large sums of money into Bombay, money which could not all be employed and so triggered a mighty speculation which engulfed public officials as well as peasants. As one journalist put it, India, which had long been an out-of-the-way uncommercial country, had now become an in-the-way commercial country.³

As the importance of Bombay grew in the area of commerce and trade, so did the need for an adequate banking system. When English traders first came to India in the seventeenth century they could not make much use of indigenous banking establishments owing to their ignorance of the latter's language and owing to the Indian inexperience in matters of trade. Therefore the Agency Houses which British companies had established to conduct commercial affairs began also to conduct banking business. The Agency Houses in Calcutta and Bombay served as bankers for the East India Company, the members of the services, and the European merchants in India. Some banks were chartered by the East India Company, but none lasted more than a few years. They were followed by banks established under Acts of the Indian legislature. These consisted of two types, the first consisting of three

³Economist, May 13, 1865, p. 558.

Presidency Banks, and the second of the Indian Joint-Stock Banks.

The Banks of Bengal, Bombay, and Madras, known as the Presidency Banks were established in 1800, 1840, and 1843 respectively. The Bank of Bombay was established after much difficulty--for it took three years of negotiations to pass the charter of 1840. The Bank of Bombay was incorporated with a capital of 52 1/4 lakhs (£525,000). This capital was increased to some 209 lakhs by 1864, then in January 1867 it was reduced to 104 1/2 lakhs. The Bank went into liquidation in January, 1868. A discussion of the rise and fall of the Bank of Bombay is the subject of this paper.

On December 26, 1836, encouraged by the extension of Bombay commerce, a public meeting was held in the office of John Skinner and Company which adopted a prospectus for a bank for the Presidency of Bombay. It appointed a committee to secure a Charter for the bank. It was agreed that the charter should be modelled after the charter of the Bank of Bengal. Within a month of this meeting applications for shares were received for nearly double the agreed capital of 30 lakhs. The capital was then raised to 50 lakhs with the sanction of the Bombay Government which had also approved the request for a charter. Two forms of a charter were prepared, one providing for the holding of shares by the East India

Company and the other omitting this provision. Both charters were dispatched to England in January 1837 with the opening of the bank being deferred until one of the charters should be returned with the confirmation of the Court of Directors of the East India Company. A great delay ensued. The project was stoutly opposed by certain Bombay capitalists who had hitherto enjoyed a practical monopoly of banking, and in addition since the Government of India was at the same time considering a scheme for a Bank of India, the Court of Directors declined to deal with the Bombay proposals until an answer had been received from India on the larger question. These questions were resolved in December 1838 and an Act of Incorporation was sanctioned by the Court of Directors. The Government of India however refused to recognize this Act of Incorporation. The Bank of Bombay appealed this decision to the Indian government and eventually won.

On February 17, 1840, Act III of 1840 constituting the Bank of Bombay was passed by the Government of India. The Bank opened its doors on April 15, 1840 with a capital of 52 1/4 lakhs, including 3 lakhs subscribed by the Bombay Government. Three of its nine directors were nominees of this Government. The Bank enjoyed the privileges of note issue, the maximum limit of which was fixed at 2 crores, and the smallest denomination of notes issued being Rs 10. For

some twenty years the Bank of Bombay prospered under prudent management; it paid good dividends to its shareholders and never incurred great losses. It adhered strictly to the rules of its charter. In November 1848 it faced a short panic caused by a few forged notes being put into circulation. Payment of these notes was refused by the Bank.

In 1860 a Government Paper Currency Office was established and by Act XIX of 1861 (took effect March 1, 1862) the Bank of Bombay was no longer to enjoy the privilege of issuing bank notes. In 1861 the Bank's board of directors determined in consequence of the new arrangements for note issue, to prepare an Act similar to that of the Bank of Bengal in 1857. In 1857 the directors of the Bank of Bengal had given the government notice of their impending infringement of the terms of their charter. No longer would they be under the mechanical checks of the government and the minimum cash reserves clause would be disregarded. The government, which had taken little interest in the bank up to this point, did not choose to intervene. And so now the Bank of Bombay also prepared to ask for a relaxation of the strict rules of business and an increase of the Bank's capital to 210 lakhs. This Act, passed by the Indian Government as Act X of 1863 differed greatly from Act III of 1840. The situation in Bombay in 1863 differed greatly from that of 1840, and this

new charter along with the brisk economic activity in Bombay in 1863 in consequence of the American Civil War were the prelude to disaster for the Bank of Bombay.

The history of cotton cultivation in India is a long one, but until the nineteenth century the export of raw cotton was a rare occurrence. Before the nineteenth century India was chiefly famous for exporting elegant fabrics to Europe, but inventions of machinery for spinning and weaving and the consequent competition of cheap goods had considerably diminished the markets for such elegant fabrics. But at the same time the possibility was revealed for India as a supplier of raw cotton. By 1830 America was the principal supplier of raw cotton to the growing English industry. The main reasons for this were that American cotton was cleaner and had longer staple than Indian cotton, also that difficulties of communications and lack of a stable export market in India posed problems. Workers as well as employers preferred the American cotton--there was 20-25 per cent wastage with Indian compared to 10 per cent for American and the short stapled Indian cotton had to be twisted harder (12 turns per inch, while American needed only 8). Thus a machine would produce 10-20 per cent more yarn from American cotton.⁴ However at times

⁴A. Silver, Manchester Men and Indian Cotton (Manchester, 1966), pp. 294-295.

the European textile markets were forced to buy Indian cotton when American suppliers were unable to keep up with their growing demands, or when American prices were deemed too high.

The commencement of a cotton spinning and weaving industry in Bombay also dates from the mid-nineteenth century.

In 1850 even the model of a cotton mill could not have been found in Bombay; but shortly afterwards the enormous imports of piece-goods and yarns from Lancashire set the merchant community wondering whether it might not be feasible to fight Manchester with her own weapons and themselves supply the demands of the island and the Presidency.⁵

In 1854 the first mill, the Bombay Spinning and Weaving Company began operations. By 1861 there were a total of six mills operating in Bombay with a total of 90,500 spindles and 240 looms. Manchester's alarm at the possibility of Indian competition was quite unjustified as this compared to some 33,000,000 spindles operating in England at this time.⁶ But though in comparison to England, Bombay's cotton industry was small, yet the economic impetus it provided attracted a considerable industrial population to the island.

Among those responsible for the growth and development of the mill industry in Bombay, were the Parsees. An

⁵S. M. Edwardes, Gazetteer of Bombay City and Island (Bombay, 1909), II, pp. 153-154.

⁶Silver, op. cit., p. 308.

enterprising commercial people, the Parsees had migrated to India from Persia in the eighth century. They settled on the western coast of India north of Bombay, in the territory of Gujerat. They were culturally distinct as fire-worshipping followers of Zoroaster. They never identified themselves with any Indian group; they maintained a close-knit, yet progressive group and thus avoided submersion into the Indian population. Their light complexions, tall stature, and aquiline features, the Europeans found very agreeable. When European traders first began to appear in India, the Parsees were quick to learn the business and act as brokers for the importers. Then too they began to engage in business on their own account, especially in the area of raw cotton, yarn, and cloth. The cotton mills in Bombay were the chief area of Parsee activity. In trade however the Parsees ranked second to the Europeans and the influence of Jews and Hindus is not to be discounted.

On April 12, 1861 the Southern states of America opened the Civil War by firing upon Fort Sumter in Charleston Harbor, South Carolina. This war brought to Bombay city in particular, and to the Bombay Presidency in general a period of buoyant prosperity and accelerated the growth of the mill industry. The effects of the creation of a sudden demand for Indian cotton were truly enormous. The government of Bombay, led.

by the very able Sir Henry Bartle Frere exerted itself vigorously by appointing cotton commissioners to aid cultivation and check quality, and by pushing forward construction of roads and railroads to facilitate the movement of cotton to Bombay Harbor for shipment to England. The cotton cultivators and dealers quickly realized large profits for their crops.⁷ As Lancashire cried for cotton, Indian warehouses rid themselves

⁷D. R. Gadgil, The Industrial Evolution of India in Recent Times (London, 1944), p. 16.

Price of Indian cotton in annas per pound

1859	1860	1861	1862	1863	1864	1865	1866
2-7	3-7	4-2	6-4	10-5	11-5	7-1	6-2

Gadgil, op. cit., p. 16.

Imports of raw cotton in UK from India (in bales)

1859	1860	1861	1862	1863	1864	1865
509,695	562,738	986,280	1,071,768	1,229,984	1,399,514	1,266,513

Robert Hogarth Patterson, "Our Trade," Blackwood's Magazine, October 1864, p. 498.

	1860	1861	1862	1863
Quantity imported, cwts.,	12,419,096	11,223,078	4,678,333	5,973,422
Price	£ 35,756,889	£ 38,453,398	£ 31,093,045	£ 56,277,953
From U.S.	£ 30,069,306	£ 26,570,399	£ 1,221,277	£ 644,138
From other countries	£ 5,687,583	£ 12,082,999	£ 29,871,768	£ 55,633,815

of old and probably damaged stock, and "all the rubbish that could be got together and screwed into bales, including even, it is said, the wadding of furniture, quilts and cloaks [were] shipped to England."⁸

The period of the American Civil War was known as the cotton famine of Lancashire. But in fact in a way it was a good thing for the manufacturing district and probably saved the trade from ruin. In anticipation of the outbreak of the American War there had been overproduction in 1859-1860 and the cotton famine now allowed this surplus to be drained off. There was great suffering among the mill employees in Lancashire especially during 1862;⁹ a group of Bombay merchants sent

⁸Mangles, "The Progress of India," Edinburgh Review, CXIX, 1864, p. 111.

⁹The London Times of September 26, 1863, p. 6, col. 4, gave the following chart of the number of paupers by cotton manufacturing union (per 1,000).

[Partial Listing]

Union	Michaelmas Quarter 1861	Maximum Week Dec. 1862	Last Week Aug. 1863
Haslingden	853	11,504	3,865
Ashton-under Lyne	1,758	35,080	19,187
Burnley	1,356	8,812	3,001
Rochdale	1,995	14,027	6,214
Blackburn	2,720	24,067	6,825
Manchester- township	5,974	41,692	17,391

money to aid that distressed community but the Manchester Chamber of Commerce remarked, "It was not charity they wanted but ~~cotton~~." ¹⁰ By 1863 the raw cotton reaching the Liverpool market began to supply adequately the industry's needs. From 1863 to the cessation of the Civil War in 1865 there were periodic slowdowns in the cotton market as cotton dealers in Liverpool hearing of the continued successes of the Federal armies felt the war would soon end. An article in the Economist of April 15, 1865 warned that by anticipating the war's end, England may fall very short of cotton and even after the end of the war there would be at the very least a period of fourteen months until shipments from the south would be forthcoming. He commented further:

Sooner or later, no doubt, as we have always said, the United States will beat all other cotton growing countries out of the market, with the exception of moderate special qualities from Bombay, Egypt, and Brazil--but it will be later and not sooner, and we need not augment the catastrophe by anticipating it. ¹¹

While England was cautiously awaiting the end of the war, Bombay ignored all warning. While Lancashire suffered for lack of money, Bombay suffered for lack of sound investment

¹⁰ Arthur Redford, Manchester Merchants and Foreign Trade, Vol. II (Manchester, 1956), p. 15.

¹¹ Economist, April 15, 1865, p. 430.

for money. So tremendous was the demand for cotton, so high the range of price and so vast the profit from it, that an economic disturbance literally overtook Bombay. Money seemed to lose its purchasing power as prices of goods as well as wages of laborers rose.

The economic history of most commercial countries had shewn that when money in vast quantities seeks for and fails to find sound investments, it will be wasted. The wastage takes the form of unwise or insane speculation. It was to such speculation that Bombay fell a victim during these years.¹²

The Bank of Bombay played an important role in the general demoralization which overtook the Presidency. The alterations to its charter by Act X of 1863 had but opened the door to unorthodox banking practices. Worse deeds were to follow.

The Annual Report of the Bombay Government of 1862-1863 included the following statement regarding the reconstitution of the Bank of Bombay passed as Act X of 1863:

The object of the present bill is to grant to the Bank a new charter of incorporation, similar in most respects to the old one, but adapted to the change in the business and to the altered circumstances of the Bank, consequent upon the withdrawal in pursuance of Act XIX of 1861, of the privilege to issue Bank Notes payable to bearer on demand, and upon the transfer of the Bombay General Treasury to the Bank and the acceptance by the Bank of an agency of issue, payment, and exchange of the Government Notes, payable under the Currency Act, in accordance with the provisions of Act

¹²Edwardes, Gazetteer, op. cit., II, p. 164.

XXIV of 1861.¹³

The report missed the real significance and impact of the new bank charter. This was its alteration from a charter insisting on caution and security, to one which allowed more latitude to the directors and officers, latitude which could be misused. Among the main points of difference between Act III of 1840 and Act X of 1863 were that while the former Act prohibited the discount of negotiable securities unless two persons or firms unconnected by partnership were bound by such security; the later Act allowed the discount of any negotiable security. Act III had prohibited any advance on bank shares or any certificate of shares; Act X allowed advances on the security of shares in public companies in India and did not require that all the calls on such shares should be paid up or prohibit advances on the premia of shares. The new Act allowed an advance to any one firm for a larger amount than 3 lakhs and for a longer period than three months; this had been prohibited under the old Act. In addition, Act X of 1863 allowed advances on all goods and merchandise whether perishable or not, it contained no definite provision against overdrafts of accounts nor a

¹³ Annual Report of the Administration of the Bombay Presidency for the Year 1862-1863 (Bombay, 1863?), p. 112.

provision prohibiting any discount or loan unless the cash in the bank equalled one-fourth of all the claims outstanding against it at the time. Act III had included provisions against such practices. Also Act X empowered the proprietors to increase the capital at a special general meeting to not over two crores and 10 lakhs.

This act was passed by the Bombay legislative council on March 24, 1863 and was assented to by the Governor-General on July 4, 1863. Act X went into effect on August 1, 1863. The passing of the Act was immediately followed by the increase of the bank's capital. At a special general meeting held on September 21, 1863 it was resolved to double the capital by the issue of 5,225 new shares of 1,000 rupees each. This was the start of the first of the four main periods leading to the bank's ruin as delineated by the Royal Commission which later investigated the causes of the bank's failure.

This first period of the bank's history from August 1, 1863 to June 1, 1864 was significant in that the bank's directors failed to move at this point to provide for the safe working of the new Act. In the forming of the new Act a certain Schedule B which contained the proposed byelaws for the bank had been omitted. Instead, a clause, section 45, had been inserted which enabled the bank's directors to pass

byelaws with the sanction of the Governor in Council. But the directors neglected to prepare any byelaws and the bank operated without any code to regulate its practice or to define the duties or powers of either the directors or the secretary.¹⁴ The directors during this period were Mr. Birch, a Government director, President, Messrs Gavin Steel, R. Mac Ilwraith, J. A. Baumbach, George Foggo, F. F. Lidderdale, M. H. Scott, Limjee Manockjee, Rustomjee Jamsetjee Jejeebhoy and Cowasjee Jehangeer, Commercial Directors, and Messrs. A. D. Robertson, G. Inverarity and H. A. Mangles, Government Directors. These directors are open to great blame, for the bank's secretary, Mr. James Blair and the deputy secretary Mr. Ryland, determined to avail themselves of the powers which the new act conferred. Mr. Blair found much opportunity to launch a radical change in the practice of the bank as to cash credits. Instead of insisting on the former practice which required Government paper (guaranteed railway shares or bullion) to be deposited as security for cash credits, Mr. Blair began to grant advances on personal security alone..

¹⁴According to a resolution of August 6, 1863 (in effect until May 4, 1865) passed by the directors. "Resolved that for the present and until further orders, any applications for advances on any bank shares, on any public company other than Government banks, be submitted to the board, and not made by the secretary." Commission Report, op. cit., p. 6.

A promissory note signed by one borrower or by joint borrowers was deemed sufficient.

During the Royal Commission's questioning of Premchund Roychund, a financial speculator and wheeler-dealer par excellence, some of Blair's dealings were revealed. Roychund stated that many of his associates were hesitant to have their names brought up before the directors of the bank in order to procure loans, and consequently he had suggested to Blair that if the bank would grant loans upon personal security he would get plenty of applicants to come forward to take loans.¹⁵ Blair liked this idea and though apparently telling Roychund that he would consult with the directors on this matter, he bypassed this step and began the practice of advancing credit on personal security. Coincidentally Premchund Roychund and his father Roychund Deepchund were the first to receive cash credit under this new system. Roychund told his friends about this method and even received from Blair a book of blank forms of promissory notes for obtaining such loans!

Not only did Blair not ask the directors about such cash credits, he also failed to enter them in the application book which was laid before the directors at the weekly board meetings. Joseph Maria De Ga, the ledger-keeper at the Bank

¹⁵Commission Report, op. cit., India minutes, p. 4.

of Bombay, under testimony to the Commission stated that, "all applications for cash credits on personal security were omitted from this book by order of Mr. Blair."¹⁶ Instead, De Ga kept a small memorandum book which only the secretary had access to, and in which De Ga entered such cash credits. Blair, whose testimony the Commission declared to be "far from satisfactory," at first denied any knowledge of this credit, then admitted that he must have acted upon the authority of one of the directors.¹⁷ The Commission failed to find that this was the case. The directors themselves had no reason to suspect that the secretary was keeping a separate ledger.

Another change in banking practices which Blair began was to discount promissory notes signed by a single borrower, without taking additional security. Under testimony all of the directors, with one exception, denied knowledge of this practice. Mr. Mangles, a Government director said that he had found out about this practice in 1864. He described his investigation as follows:

I wrote a letter to the secretary and asked him whether he was in the habit of discounting promissory notes only, as it seemed to me to be a violation of the charter. He wrote back, saying that it was a hard

¹⁶Commission Report, op. cit., Summary, p. 7.

¹⁷Ibid., p. 8.

term to use, but that the board of directors considered that they could do it under the charter. I then wrote a private note to Mr. A. D. Robertson, who was then one of the directors, and he said that he thought that it could be done under the charter. I then went to Mr. Birch and asked him whether he was aware of it, and he said that he was; and I asked under what clause of the charter it could be done. He said as a cash credit. I said that I did not agree with him. I then wrote to Mr. Lidderdale and asked him whether, as a mercantile man, he could conscientiously sanction that kind of cash credit. He wrote back, and said no, certainly not, but that it was the custom of the bank to discount bills of that sort.¹⁸

Upon questioning the men whom Mangles mentioned in his statement, the Commission discovered that Birch could not recollect the transaction and Robertson appeared to have misunderstood it.

Blair instituted yet another change in bank practice. Under the former charter the bank had kept a frequently revised discount list, showing the amount of credit which could safely be advanced to different commercial men in Bombay. After 1863 the bank no longer kept this list. Blair also discontinued the procedure of referring all questions as to how much credit should be allowed to applicants to the directors at their weekly meeting. Blair excused this by saying that the questionnaires had been continually returned to him with the request that he refer to a native director and so he from this point conferred with only one native director, who, at first, was Cowasjee Jehangeer.

¹⁸Ibid , 8.

In the subsequent testimony before the Royal Commission the directors were asked about their omission to set up byelaws. Typically Mr. Foggo stated that he was unaware that the Schedule B had been struck out but added that no doubt there should have been byelaws. He said that he knew of no applications for a cash credit on personal security only.¹⁹ Furthermore, there was no statement defining what the powers of the secretary were and though some directors did, from time to time consider that there should be a letter of definition written, along with byelaws, other business seemed to be more pressing and so they neglected to take action. The Commission found the directors at fault in thinking that the bank's business could be carried out legally, without byelaws. But the secretary was even more at fault. Section 27 of Act X had authorized the secretary to endorse and execute transfers, and to draw, accept, and endorse bills, promissory notes, and letters of credit, and to sign other documents on behalf of the bank, and so dispensed with the seal of the bank, or the signature of the directors to such documents, and made the signature of the secretary valid for the purpose of binding the bank. But no section of Act X empowered the

¹⁹ Report of the Commissioners Appointed to Inquire into the Failure of the Bank of Bombay, minutes taken in India, p. 7.

secretary to lend money on his own authority. The Commission suggested that it should have been up to the secretary to see that his own duties were more clearly defined and also as secretary he should have reminded the directors that they had neglected to pass any byelaws.

Along with this change in the rules of the bank there also was a change in the economic atmosphere of the city of Bombay. Daily, more and more capital was flowing into the Presidency. An examination of the reaction of the Government to this new situation is quite revealing in that like the bank's directors, it failed to interfere when it should have.

CHAPTER II

THE SPECULATION MANIA IN BOMBAY: THE BANK OF BOMBAY INSTITUTES DANGEROUS PRACTICES (1863-1865)

The commercial crisis was one of the dominating factors of the governorship (1862-1867) of Sir Henry Bartle Frere. Formerly an assistant to Lord Canning at Calcutta, Frere was appointed Governor of Bombay in March 1862 by the Indian Secretary, Sir Charles Wood, succeeding Sir George Clerk who had resigned because of ill health. A tall, slender man, Frere had a soft voice and spoke clearly, yet deliberately-- "the great charm of his presence lay in the expression of his open countenance and sweet and ready smile. . . in his absolute self-forgetfulness and ready sympathy."¹ Frere was a man of much initiative and he determined to do great things for Bombay, but in the end the commercial crisis and the subordination of his power to the central government at Calcutta hampered his every move.

The Bombay Governor and his three man council were appointed directly by the Crown. The Council was comprised of a commander-in-chief of the Presidency whose duties were confined chiefly to military matters, and two civil members,

¹John Martineau, The Life and Correspondence of Sir Bartle Frere (London, 1895), I, p. 130.

one who dealt with revenue and finance, and the other who handled judicial affairs. Generally each member transacted the business of his department separately with the Governor. Frere, being interested especially in public works, took this department under his personal direction. Before the days of railroad and telegraph communications it was practically impossible for Calcutta to oversee Bombay's every action. Thus in most matters Bombay officials would act first and ask for approval later. During Lord Dalhousie's administration (1848-1855) however, a policy began to develop which tended to curtail any independent action by the Presidencies. As the problems of administration grew in India, so did this trend towards more centralization. Frere did not like this centralization. His conflict with Calcutta accelerated, when in December, 1863, Sir John Lawrence was appointed Viceroy.

A centralizer by conviction, Lawrence held firmly that only a centralized system would maintain the Empire intact, and so he set himself to follow the lines of consolidation begun by Lord Dalhousie. Too, Lawrence had had a distinguished career as an Indian civil servant but the interests of the Punjab and the Northwestern Provinces which he knew, far outweighed his interests in the rest of India. Frere soon discovered that not only did this system check his actions, but that Lawrence really had little appreciation for the problems

of Bombay. Then too Frere and Lawrence differed as to fiscal policy. Lawrence wrote about this:

Our financial prospects are very gloomy indeed. The furore for expenditure is excessive. A considerable sum must be laid out in building new barracks and improving the old ones. But the tendency is to overdo the matter. I would limit this, if I could hope for any support, but this I do not see. Sir Hugh Rose and Napier have no regard for financial considerations and Frere is worse than anybody.²

A biographer of Lawrence comments that ". . . Lawrence thought he was bound to be just before he was generous and to look before he leaped. Sir Bartle Frere too often leaped before he looked; and sometimes it may have been to the advantage of India that he did so."³ Frere had been quick to recognize that the unprecedented demand for Indian cotton created by the American Civil War and the stimulus it gave to the production of cotton in India, if regulated and controlled would be wholly advantageous to the Presidency. Frere saw that prompt and effective measures must be taken to enable the ryots and merchants to meet to the fullest extent possible this sudden demand for cotton. Not only must production be increased, but the type of cotton produced must be changed to

²Baman Das Basu, India Under the British Crown (Calcutta, 1933), p. 83.

³Reginald Bosworth Smith, Life of Lord Lawrence (New York, 1883), II, p. 378.

meet the requirements of the English spinners, and transportation from the inland districts to the wharves must be improved upon.

It was hoped that the needed improvements in the type of cotton exported was secured by handing out instructions to the cultivators on how to raise a more efficient crop and by imposing harsh penalties (Cotton Frauds Act, 1863) on those convicted of adulterating cotton bales. Frere upheld his action explaining that it made it possible for the merchant "to deal safely in the article without fear of taking in their European customers."⁴

A letter published in the London Times on July 28, 1863 from a member of the House of Commons underlined Frere's points on a broader scale:

. . . one point I will venture to urge upon the attention of the Indian government. If the American troubles should happily cease during the year, and we get some cotton from the United States, and increased supplies from other countries also, then our Indian imports of cotton would realize to the holders £10,000,000 sterling less in value in 1863-4, and very probably some Indian secretary would have to assign as a reason for a falling revenue that Lancashire, as in former times, would not take, because she could supply herself elsewhere with good cotton, rubbish from India. At all events, I do not think a revenue based largely on opium, salt, and practically monopoly prices for cotton ought to be relied upon as a stable one. Without laying myself to the charge of renewed unsound propositions on behalf of

⁴William Basil Worsfold, Sir Bartle Frere (London, 1923), p. 34.

Lancashire, I venture simply to suggest that it might be prudent and sound policy for a Government like that of India descended from a trading company and as yet a trading one, dealing in opium and farming other sorts of produce, to aid or persuade, if you like, its own tenant cotton-growers to produce a better quality of the commodity upon which so large a share of its revenue is evidently dependent. I don't know that we, the cotton interest, have really done more than this heretofore, I venture again to repeat the suggestion, still thinking it sound and economic advice.⁵

Along with the abnormal demand for cotton, Bombay experienced an abnormal need for roads, railroads and canals. Frere himself said that "the question of a vastly increased supply of cotton from Western India was almost everywhere a question of roads."⁶ But it was difficult to obtain the necessary funds from Calcutta to build the roads, and there was much red tape from Whitehall as well. A Whig aristocrat and experienced minister, Sir Charles Wood led an able administration as Indian secretary for seven years (June 1859-February 1866). But Wood, as Lawrence, was a cautious man in financial matters and "a somewhat unconstructive reformer he reflected in exaggerated form the limitations of the Imperial viewpoint in the mid-nineteenth century."⁷

⁵ Times, July 28, 1863, p. 12, col. 5.

⁶ Worsfold, op. cit., p. 34.

⁷ Robin James Moore, Sir Charles Wood's Indian Policy 1853-66 (Manchester, 1966), p. 254.

The East India Company which ruled India until 1858 had been remiss in its attention to public works. Following an unfortunate policy of neglect knowing that most Britons considered India only as somewhere east of Suez, the company did as little as decency permitted in this direction.⁸ In 1853 Lord Dalhousie had written:

Great tracts are teeming with produce they cannot dispose of. . . [and] England is calling aloud for the cotton which India does already produce in some degree and would produce sufficient in quality and plentiful in quantity if only there were provided the fitting means of conveyance for it.⁹

Dalhousie recommended a comprehensive system of railways and got approval in 1853 for building extensions on to the few existing lines. Unfortunately this was only a small start.

At a meeting of the Manchester Chamber of Commerce in January 1861 its president expressed alarm over the inevitability of the American Civil War. He echoed others' belief that while the manufacturers' future depended on Indian cotton, the main obstacle to its increased import "lay in the defective and expensive mode of transport."¹⁰ They urged Wood

⁸Leland Hamilton Jenks, The Migration of British Capital to 1875 (London, 1927), p. 209.

⁹Ibid., p. 211.

¹⁰Moore, op. cit., p. 138.

to borrow money to build railroads and in June he announced:

Those [railways] which we have determined on pushing forward with utmost dispatch. . . are lines which in the present crisis in America must be looked to with the greatest interest. One pierces the cotton district [the Great Indian Peninsular Line] and the other skirts its every edge [the Bombay and Baroda]. The only delay which will arise will be occasioned by the natural obstacles that present themselves.¹¹

Indeed these natural obstacles were great, for at a distance of only forty miles from Bombay rise the Western Ghats Mountains and their surrounding hills which stretch hundreds of miles from north to south. But nevertheless work began, due mainly to this influence of Manchester on Wood and the vigor which Frere aimed towards improving Bombay's commerce. Unfortunately this work started at precisely the wrong moment, for it got caught up in the same speculative mania which later wrecked the Bank of Bombay.

The Back Bay Reclamation Company which later gained much notoriety, equal to that awarded the Bank of Bombay, had its origin in the need by the Bombay and Baroda Railroad of land on which to build its terminal. An Indian terminal railway station required a great amount of land. Because of the rainy season a large proportion of traffic had to be

¹¹Hansard, Parliamentary Debates, Vol. CLXIII, June 3, 1861, p. 493.

handled in a short period of time, and due to the tropical climate, more space had to be allotted for air circulation. In face of the increase in the cotton trade, the Bombay and Baroda Railway Company was too busily engaged in connecting missing gaps to construct this terminus. The railway company pressed the Bombay Government into constructing the terminus. By this time however, with the influx of silver from the cotton trade the cost of labor as well as land had risen to enormous heights in Bombay. The Government which had guaranteed to provide the railroad with the needed land, was now quite indisposed to pay the fabulous price the times now required. Facing such a dilemma it was decided to route the railroad over land to be reclaimed from the shallow waters of the Back Bay area of Bombay and to build its terminal there. Concession was given to a group of Bombay merchants, the Back Bay Reclamation Company, who after reclaiming the land and giving the Government the acreage required for the railroad, would make its profit from sale of the remainder of the reclaimed land. This project was on the western part of the island from Colaba to the foot of Malabar Hill. As originally presented, the Government was to be allotted four hundred shares of ₹500 each in this Company, and be part manager of it. But though John Lawrence approved this outlay, Charles Wood became apprehensive and refused to concur. When, considering the

interests of all of India as he had to do, he probably concluded correctly that it would be unwise for the Government to be involved in such a scheme. Then too he was only following his belief that public works did not seem to be remunerative and that "railways and roads improve the country but do very little for revenue."¹² And so the Back Bay Reclamation Company was left without Government participation or more importantly, Government control. The shares which had been set aside for Governmental purchase now sold for ₹ 2,650 each, a 500 per cent increase. A great stimulus was thus given to the growing mania for speculation in Bombay at the time when it needed to be checked; the second period (June 1864-April 1865) in the narrative of the failure of the Bank of Bombay had begun.

Railroads were not the only area in which Frere pressed for improvement. Bombay under his governorship entered upon an Augustan age, in fact it is said he had the ambition to leave Bombay a city of marble.¹³ Well he might have succeeded but for the commercial and financial crisis. Frere did level many of the older areas of the city, embark upon the construction

¹² Moore, op. cit., p. 149.

¹³ Dinshah Edulge Wacha, A Financial Chapter in the History of Bombay City (Bombay, 1910), p. 5.

of public buildings and urban improvements such as wider streets and sanitation facilities. But indeed just as Wood was perhaps too inclined towards economy, Frere was perhaps too liberal in his spending habits. To embark upon a period of feverish government spending just as wages and material costs were rising was not a sound idea. The launching of such a large public works improvement program only aggravated the situation and when the crash came the government suffered discredit along with the bubble companies. But Frere did transform Bombay from a mercantile town into a splendid and populous city and modern Bombay is said to date from his administration.¹⁴

Just how tremendous the economic activity was in Bombay is reflected in the results of a census initiated in 1864 by Frere. This census recorded a total population for Bombay of 816,562. Though perhaps a slightly inflated figure, nevertheless the influx into Bombay during the cotton crisis was

¹⁴Reclamation projects such as the Back Bay Reclamation Company on the west, and other companies on the east of the island, begun under Frere's administration hoped to remedy such conditions as had been described by a traveller to Bombay in 1845; "all round the Island of Bombay was one foul cesspool, sewers discharging on the sands, rocks used only for purposes of nature. To ride home to Malabar Hill along the Sands of Back Bay was to encounter sights and odors too horrible to describe. . . ." Stephen Meredyth Edwardes, The Gazetteer of Bombay City and Island (Bombay, 1909), I, p. 66 and II, p. 160.

amazing. In 1842 the island was inhabited by "about 200,000 persons increased by a floating population of 70,000 seamen, merchants, pilgrims and peasants. Nearly two thirds of the population are Hindus, about 20,000 are Parsees and the remainder Musalmans, Jews, and Portuguese Christians."¹⁵

In 1849 another study proclaimed the residents of Bombay to number nearly 500,000.¹⁶ An accurate measure of how many of the 816,562 number recorded in 1864 were there because of the cotton crisis may be seen when in 1872 another census showed that the population had decreased to 644,405.¹⁷

This abnormal influx of people into Bombay at a time when more money was pouring into the island than could be used in legitimate means of investment created a text book result--excessive speculation. The Bank of Bombay now entered its second phase towards its downfall and incurred losses from which it would never recover.

As was previously stated, the Back Bay Reclamation Company had given much stimulus to speculation by the public sale of 400 shares of stock originally intended for Government purchase. The public auction on July 6, 1864 lasted less than two hours. By the close of the following day the entire amount

¹⁵Ibid., I, p. 163.

¹⁶Idem.

¹⁷Ibid., I, p. 164.

of purchase money, over a million pounds, was at the bankers--striking proof of the wealth of Bombay.¹⁸ In a letter dated July 23, 1864 Frere wrote to his predecessor, Sir George Clerk:

All Bombay have gone mad, about Back Bay. I was anxious that Government should have had a share in the work, such as it has in the Bombay Bank, not so much to secure a share in the profits as to have the only possible effectual hold over the management in such matters as allotment of shares. I do not think any one realized, as clearly as you did, the danger to the morale of the public service from these undertakings. One might as well try to stop a cyclone as to check such speculations. . . . But if Government are large shareholders in every such work and have a potential interest in its management, the evil may be kept within some kind of bounds.¹⁹

These were high hopes, but in the end it mattered little that the Government had a "share" in the Bank of Bombay while it had no connection with the Back Bay Reclamation Company, for it was now too late to stop the speculative mania which had overtaken Bombay.

During the remainder of 1864 and the early part of 1865 companies were started for every imaginable purpose--banks and financial associations, land reclamation, trading, cotton cleaning, pressing, and spinning companies, livery stables and veterinary companies, and companies for making bricks and

¹⁸Times, August 5, 1864, p. 10, col. 2.

¹⁹Martineau, op. cit., II, p. 7.

tiles.²⁰ The Times noted:

Every day a new company enters the market, and there is a rush for shares, with endless heart burnings and counter accusations. Hardly one of these companies has paid a dividend, yet the shares sell at premiums which the maddest speculator never dreamt of, and which can never make a return to the victim who will be caught in the reaction that is bepending. . . at present men in Bombay do not think of such contemptible things as dividends. They buy shares cheap to sell them dear. . .²¹

And a contemporary, Wacha, wrote:

In the Bombay of 1864-1865 every tenth man was either a promoter, embryo promoter or director. And as to the number of bankers and managers it was legion, each and all absorbed in pocketing the largest premium on share allotments made by hundreds every day.²²

This was just the time when the Bank of Bombay should have been extremely cautious as to its advances. But unfortunately the mismanagement which was begun in 1863, continued, and the Presidency bank became a principal factor in fostering financial speculation in the city.

The Bank secretary, Mr. Blair now determined to obtain the directors' sanction for the practice which he had been

²⁰Wacha lists 25 banks, 39 financial associations, 7 land and reclamation companies and approximately 30 miscellaneous companies as being established, or in the case of banks, significantly enlarging their capital, during 1863-1865. Wacha, A Financial Chapter, pp. 24-32.

²¹Times, January 24, 1865, p. 9, cols. 4-5.

²²Wacha, Rise and Growth of Bombay Municipal Government (Madras, 1913), p. 21.

carrying on for months, that of granting cash credits solely on the security of the borrower's signature. On June 2, 1864 the board of directors voted in favor of such a resolution. Robert Hannay (later on the board of the Bank, December 1864-April 1866), testifying before the Royal Commission, explained the circumstances behind this sanction. Hannay recalled that Blair had approached him sometime before June 1864 asking him to jot down what he considered to be the Scotch system of cash credit; Hannay obliged and told the Commission that he had heard no more from Blair about the matter. The Commission examiners showed Hannay a copy of the resolution of June 2, 1864. Hannay saw immediately that Blair had altered his statement. Hannay had correctly outlined the Scotch system of cash credits as requiring a bond signed by the primary party together with two good names as security. But the resolution which Blair presented to the board members read as follows:

It is respectfully suggested that the number of credit accounts might be greatly increased if the system practised in Scotland was introduced, viz., on a bond for a certain amount being signed by the party requiring the accomodation with or without good names as security according to the credit of the party. At present no person, in however good credit, can have a credit account with the bank unless he can lodge Government paper as security, besides signing a bond which has to be renewed every three months. Whereas, if the above system was adopted, the account might run on from year to year.²³

²³Royal Commission Report, Appendix, Exhibit A48, p. 32.

The underlined portion of the statement had been added in what the Commission determined to be Blair's handwriting. Hannay said that he was unaware of this alteration, even when he became a member of the board. Blair, on the other hand, knew that this statement was incorrect in two areas. First he knew that he had altered Hannay's definition of the Scotch system of credit. Secondly, in saying that no person, in however good credit, could get a cash credit from the bank unless he could lodge Government paper, Blair was conveniently forgetting that he had already been following this practice for some months.

The resolution of June 2, 1864 is important in that now the directors gave their open approval to a reckless system of banking. The commercial directors during this period were Hannay, Steel, Mc Ilwraith, Scott, Lidderdale, A. Brown, Tracey, Cassels, Cowasjee Jehangees, Premchund Roychund, and Cowasjee Manockjee. The Government directors included Birch, Mangles, Ravenscroft, Jacomb, F. S. Chapman, and Livingston. These men share varying amounts of guilt, as some only served the bank for a short length of time. Whether they had known of Blair's previous intrigues or not, they now sanctioned the carrying out of such a policy. As businessmen themselves, the directors should have used caution in such action and not relied so heavily upon the secretary. The directors along

with everyone else in Bombay who had money or could borrow some, engaged in much speculation in the new companies springing up at this time and so had little time to give to their bank duties. Mr. Hannay admitted under questioning that he depended entirely upon Blair for knowledge of what was going on and said, "the bank had got on well under his management, but sometimes I wondered how it was that it had paid such good dividends."²⁴ As a director and later president of the bank, Hannay should have found out for himself.

From the date of the resolution a most unchecked system of advances began. The directors who now were aware of the bank policy and surely must have known of the large sums being borrowed, made no effort to inquire as to the credit of those borrowing money. Loan applications were no longer brought up before the board for their sanction. Hannay by means of excuse stated before the Commission, "I heard it said by the directors then that it was impossible to state what a man was worth, and that a reliable discount list could not be made out."²⁵

The President of the Bank at this time was Sylvester D. Birch, a Government director who had served in that capacity

²⁴ Ibid., evidence given in England, p. 247.

²⁵ Ibid., p. 240.

previously in Bombay and Madras. Birch believed in lending money on personal security and so took no measures to stop Blair's actions. Under testimony Birch admitted that Blair disobeyed bank policy by advancing money on shares, "yet he neither brought his conduct before the Board, nor took steps to put a stop to the practice, but contented himself with telling Mr. Blair that he had no right to make such advances."²⁶

Birch did not attend any bank meetings during July, August, and September 1864, explaining that he had been ill. Apparently this was not the case, for the Commission discovered that he was not too ill to attend to his other personal business during this period. The other Government directors at this time, Mangles, Ravenscroft, and Jacomb took little interest in the bank's affairs. They attended weekly meetings and that was all. Testimony revealed that Ravenscroft thought that the secretary had powers secured to him by byelaws and beyond that acted in conjunction with the President and commercial directors, whereas Mangles and Jacomb thought the bank was managed by the President and secretary.²⁷

In July 1864 Blair came under the influence of the powerful Hindu financier, Premchund Roychund who that month,

²⁶Ibid., Summary, p. 13.

²⁷Idem.

became a native director. Premchund Roychund was a very enterprising young man. The son of a merchant, Premchund became a sharebroker in Bombay at sixteen years of age. Possessed with exceptional ability as a financier he quickly went to the top--by 1863 his reputation as the leading share-broker as well as one of the most venturous of the cotton merchants and speculators was established, though he was only thirty-three. There is no parallel to his career between 1863 and 1865 as the Caesar of Bombay finance. During this time of prosperity Premchund's advice and cooperation were most eagerly sought by both company promoters and speculative investors. He seems to have been himself a moderate man, a contemporary writes that "he endeared himself by his simplicity, amiability, and many private virtues, to all of the people, irrespective of color, caste and creed."²⁸

He donated vast sums of money to charity and to various causes in Bombay, the most notable being a gift of 2 lakhs of rupees for the erection of a University Library in the city. But Premchund did not use his wealth and powerful influence for solely benevolent ends. The Royal Commission blamed much of the bank's reckless policy on Premchund:

²⁸Wacha, Premchund Roychund (Bombay, 1913), p. 77.

. . . intelligent and subtle, Premchund Roychund was not slow to fathom the imbecility and weak moral character of Mr. Blair, and soon acquired great influence over him and his subordinates, with complete command of the funds of the bank. . . . Premchund Roychund also bought and sold shares for Mr. Blair, and entered into joint speculation with him, and never charged him a rupee for brokerage."²⁹

Premchund was aided in his bid for influence at the Bank of Bombay by the retirement of the former native director Sir Cowasji Jehanghir. Sir Cowasji had leant a certain amount of restraint to the Board of directors though he frequently had stood alone in his opposition to proposals including that of increasing the bank's capital and of advancing money on bank shares. It has been stated that the "vigorous and increasing vigilance of Sir Cowasji, while on the Board, was so great, and his moral influence so over-powering, that the management dare do no wrong or advance so incautiously as to incur a loss."³⁰ Sir Cowasji's retirement was the signal for Premchund to do as he pleased--there now was no check or control of the kind Sir Cowasji had exercised.

As the European directors were constantly changing, and were immersed in their own firms or in speculation, they had little inclination or time to become very familiar with

²⁹Royal Commission Report, Summary, p. 14.

³⁰Wacha, Premchund Roychund, pp. 123-124.

their responsibilities to the Bank. In consequence they left the job of investigating applicants for loans to the secretary and the native director. Soon Premchund's position with the Bank became so potent that he had only to recommend to Blair that a loan or advance be given, and it was done. "The result was that the Bank became Premchund's,"³¹ stated the Royal Commission report. A contemporary of the period adds, "to say that the directors entrusted the destinies of the Bank to the Secretary, that the Secretary left them at the mercy of Mr. Premchund and that Premchund left them to Providence is no exaggeration of the real state of the Bank."³²

Premchund ran an extremely complex operation. As the myriad of new companies grew, he found himself in a position of such prominence that his name and influence were considered essential to the safe launching of any of the ephemeral schemes of the day. If not himself the promotor of a company, he would receive a large allotment of shares in it and the promoters would then allow him to help distribute the much sought after shares.

Premchund was a master of this type of operation for he knew the people who would make the best shareholders. He

³¹Royal Commission Report, Summary, p. 14.

³²Wacha, A Financial Chapter, p. 91.

was always careful to see that the managers and directors of banks, including naturally Blair and Robertson, the new deputy secretary of the Bank of Bombay, got an allotment of shares. He also distributed shares to the friends of the promoters and to persons who might prove useful in the new company's undertakings. If any of his friends needed money with which to buy wanted shares, Premchund had only to write a letter of recommendation to Blair and a loan was easily procured. If Premchund himself had shares to sell he might offer them to a friend and at the same time aid the buyer obtain the needed purchase funds through a loan from the Bank of Bombay. Premchund at times helped his friends procure loans in their names though he was the ultimate user of the money for speculative purposes. Blair was Premchund's accomplice in such "transactions," the bank directors knew nothing of them. To remain on friendly terms with Blair, Premchund entered into joint transactions with him, with Premchung supplying all of the money to purchase the shares!

The total amount of his dealings was tremendous. His personal debt to the bank was 42 lakhs (₹420,000); the loans obtained by him for others who then used the money to purchase shares from him amounted to 66,900,000 rupees (₹669,000), of which 43, 45, 478 rupees (₹434,547) was lost with the failure of the bank; the loans procured not in his name though

ultimately used by him amounted to 29,58,938 rupees (₹295,893) of which 13,02,408 rupees (₹130,240) were lost.³³

Testimony before the Royal Commission revealed how the loan transactions took place. Most cases were similar to that of Sorabjee Jamsetjee Jejeebhoy, who states:

Premchund came to me one day in July 1864 at my bungalow on Malabar Hill, and asked me if I had any Bombay Reclamation Company's shares. I said, "No." He told me to apply for them to Mr. Cowasjee Jehangeer. I wrote a note to Cowasjee Jehangeer. He said in reply that all the shares he had were distributed amongst his friends, and that there were no more remaining with him to give me.

Next day Premchund called on me and asked whether I had received a favorable reply from Cowasjee. I said, "No," and produced Cowasjee's note. He read it and said it was all bosh. . . He said, "Never mind, I will manage all that for you," and told me to give him a commission to purchase for me as many shares as I wished. I told him that I was short of money, and I could do no more than purchase a few shares. Premchund thereupon said, "Take my word, Sorabjee, and do not trouble yourself about money. I will get you as much as you require. But do not go in for less than one hundred shares." I expressed surprise at his proposal, seeing that I was unable to pay for all these shares. He told me that he could procure ten lakhs of rupees in a twinkling. I agreed to it, and asked how he could manage it. He said he would get the money from the Asiatic and the Bombay Banks. The next day or the day after that, he sent me two notes, one addressed to Mr. Morrison, the Manager of the Asiatic Bank, and one to Mr. Blair. In the latter he wrote--"My dear Mr. Blair could you accomodate Sorabjee with five lakhs?" The letter to Mr. Morrison was of the same purport. On the other side of the two chits he had got replies from Mr. Blair and

³³Royal Commission Report, Summary, p. 15.

Mr. Morrison, saying they would give the money with pleasure.

Next day he called on me at my office, and asked me if I was able now to go in for shares. I said "No, not the hundred," and gave him a commission for forty-three shares only. Ten lakhs were not sufficient for the purchase money of forty-three shares, so Premchund asked me to send in some money to the Banks to my credit. I accordingly did so. It was about Rs 60,000; Rs 26,500 to the Bank of Bombay, and Rs 40,000 to the Asiatic. On the 14th of July he came to me personally for the cheques, and asked me to hand them over to him. I accordingly did so. I cannot remember whether I ever signed a promissory note. Cash credits had been opened in my name. I think that was all. I gave Premchund cheques for the whole amount out of both Banks.

. . . A few days after he sent me allotment certificates of forty-three shares, standing in the names of Premchund himself, his father Roychund, Navalchund his brother-in-law, Herrjee Jehangeer, brother of Cowasjee Jehangeer and Mr. Cassels. . . I was rather at a loss to account for shares belonging to Premchund, his father, and brother-in-law, and other Directors of the Bombay Reclamation Company being for sale . . . parties whose shares I should not have expected to be in the Bazaar.³⁴

A merchant, Kursondass Madhowdass gave the following account:

Premchund came to me and said that he was asked by the Bank of Bombay to get money invested, and asked me whether I would take a loan of three or four lakhs. He said, "They do not know what to do with their money." I took four lakhs (£40,000) for three months. I gave a promissory note without security.³⁵

Fleming, a partner in the firm of Nicol and Company, obtained a cash credit for 10 lakhs (£100,000) in January 1865,

³⁴Ibid., evidence given in India, p. 44.

³⁵Ibid., p. 42.

on the security of a promissory note. He recounted his negotiations with Blair:

The Elphinstone Company, of which my firm were the secretaries and treasurers at that time, owed my firm 12 lakhs of rupees, and they were not likely to be in a position to repay the advance for rather more than a month. I required a part of the money, and I went over to the Bank of Bombay to see Mr. Blair, and to ascertain whether I could obtain an advance from the Bank of Bombay. I was prepared to make explanations as to why I needed the money, and, if need be, to offer security. Mr. Blair granted me the loan at once, immediately on my asking for it. He refused to hear any explanations at all, but turned to Mr. Robertson, who, if my memory serves me right, was in the same room, and said, "Let Mr. Fleming have 10 or 20 lakhs, or whatever he requires." I urged very much making some explanation, for it was an anomalous thing my borrowing such a sum of money at the time, but he would not listen to anything which I had to say.³⁶

If the secretary, Blair and his ally Premchund were unwise managers of the Bank of Bombay they were even less so when it came to managing the bank's six branch offices.³⁷ These branches were under the superintendence of the secretary alone. The weekly accounts of the business done at the branches were never shown to the board of Directors. Clearly, from testimony before the Royal Commission these branches were directly subordinate to Blair and to an inspector of

³⁶Ibid., Summary, p. 16.

³⁷These branches were located at Poona, Ahmedabad, Surat, Dharwar, Kurrachee, and Kalbadevi.

branches. These inspectors had no set instructions to follow and in fact seldom if ever visited the branches. Visits were made only if there were cause, for as Blair observed, "it was so expensive to send inspectors through India, that I fancy it was not necessary unless something was really wrong--because everything was going on well."³⁸

The managers of these branches had few defined duties. William Bullock, the manager of the Kalbadevi Branch, admitted that he only had verbal instructions, that he kept in constant touch with Blair and when he did try to extract instructions from him he "never could get anything more from him than a direction to follow Premchund's advice."³⁹ As there were no discount lists the agents were told that they should be the judge as to the credit of the applicant, or else refer to Premchund for his judgment.

This policy of handing out loans to whomever wanted one for whatever purpose, was obviously a dangerous affair. Not only did it foster the already rampant speculative fever, but the bank began to suffer losses of capital in consequence of the inadequate check made on the borrowers.

³⁸Royal Commission Report, Summary, p. 17.

³⁹Ibid., evidence given in India, p. 48.

In its Annual Report for 1863-1864 published in October 1864, the Bombay Chamber of Commerce issued only a mild warning concerning the speculation which was taking place:

One of the principal features of the year in Bombay has been the great increase in banking and financial companies which we have lately witnessed. Another feature has been the excessive speculation in all sorts of Joint-Stock shares which has been pushed to an extent which the Committee cannot but regard as full of danger to the well-being of the community.⁴⁰

The report spoke mainly about the continued prosperity and increasing wealth of Bombay. Unfortunately, the Chamber of Commerce delayed until the following year the circulation of a more definitive condemnation of the economic situation in Bombay, by then it was too late.

The Government of India and Frere did not ignore the situation, but their efforts at checking the speculative fever proved abortive. As the Chamber of Commerce Annual Report stated, there was both a good and bad side to the commercial revolution underway in the Presidency. Miserable hovels and bungalows, filthy streets and disgraceful sanitation facilities began to give way to new buildings, streets and even a university. But a darker side progressed just as rapidly. The rich became richer, utterly demoralized by the speculation, and the poor became poorer. Among those who

⁴⁰ Wacha, A Financial Chapter, p. 22.

suffered the most were those men with a fixed income, notably British Government officials. Prices in Bombay for services, food and housing had quadrupled in less than four years, yet their salaries had not been increased proportionately. A reporter for the Times wrote:

It should be known in England that it is impossible for a married man to live in Bombay on a thousand a year; that Englishmen are separating themselves from their wives and families for years, because they cannot afford to keep them in Bombay; that there are many subalterns and even captains of Her Majesty's army, who live like poor curates, in a country where so to live is death, who, in sober truth, cannot afford to have butcher's meat on their tables more frequently than once a week.⁴¹

Those who could left Government service or took extra jobs, while those who remained were tempted to dabble into the share-market.

Sir Bartle Frere realized the gravity of the situation.

In a letter to Sir George Clerk he states:

But in the case of stipendiary people, especially Government servants . . . they are really starving, and I never in my thirty-one years of service, saw and heard of so much real distress among that class. All are more or less affected.⁴²

But Frere's entreaties failed to convince Wood to raise the civil servants' salaries, perhaps because to increase them

⁴¹Times, January 24, 1865, p. 9, col. 4.

⁴²Martineau, II, p. 10.

throughout India. Costs in Bombay had risen at a significantly higher rate than in the rest of India, and though increases were needed elsewhere, the need was more critical in Bombay.⁴³ In a letter of November 20, 1864 to Wood, he writes:

The distress among all except the higher paid classes of Government servants in Bombay and Poona, is really beyond belief, and I am assured that officers on the pay of captains, and the lowest paid grade of the Civil service can barely live as single men, and that married men have to submit to privations of food, house-room, and conveyance for themselves and their families. . . . To our last appeal on this subject, the Government of India has finally answered in a few lines that it makes no change in their previous opinions.⁴⁴

While thousands of government officials left the service, Frere attempted to counsel those who remained as to the evils of speculation. He resurrected a minute formerly published by Clerk, as well as by Dalhousie and Elgin regarding the interference by civil servants with the management of Joint-Stock Companies. It states:

⁴³An article in the Economist of February 4, 1865 suggested that the state of things in the Bombay Presidency required watchfulness and perhaps reorganization. It noted that "a formal proposal by the Governor of a Presidency, himself a civilian, for an increase of salaries to the extent of one-half a million a year at one blow, is, to say the least of it, an unusual phenomenon. Even to make such a proposal is to spread discontent at its rejection over a whole Presidency, and to grant it would have involved fresh taxation. The true solution, if the need is not temporary,--which we doubt--is to employ fewer men on better salaries; but Sir Bartle Frere and Bombay generally require looking after." Economist, Vol. XXIII, Feb. 4, 1865, p. 128.

⁴⁴Martineau, II, pp. 11-12.

The Governor in Council now desires to point out to all public servants of Government, at this particular period, when there is so strong a tendency to speculation in Bombay, the extreme importance of obedience to the spirit of all the previous orders, rather than to the mere letter of the law. He believes it to be sufficient to remind all public servants of the great importance of avoiding any connection, however remote, with any undertaking which might tend under any contingency to fetter their actions, or divert them from the numerous and important responsibilities imposed by the public service upon them.⁴⁵

But though Frere as Governor could suggest what the proper conduct of a civil servant should be, he had no power to prohibit a government employee from engaging in speculation. In a letter of February 14, 1865 to Sir George Clerk he shows his frustration:

A few words from Sir Charles Wood as to the absolute necessity of keeping clear of share-jobbing would have a great effect. But it is cruel; while enforcing this, to withhold any improvement in the pay of our servants. It is rather hard to a High Court Judge, an Advocate-General, or Secretary to Government to have more work than his fellow in Calcutta and less pay, but still they can live and save a little. I can without compunction tell them to resist dipping into the golden stream which flows on every side but it is hard work for the smaller fry to keep straight with a wife and children skimmed at home. You would be shocked at the stories I sometimes hear of men, and women too, dancing attendance on "promoters," native and European, and justifying it to themselves as "duty to their families."⁴⁶

The speculation in Bombay may never have assumed such massive proportions but for the introduction of the use of

⁴⁵ Ibid., p. 13.

⁴⁶ Ibid., pp. 13-14.

"time-bargains" into the share and cotton markets. As the price of cotton varied from month to month, as much as from ninepence to two shillings, this price fluctuation began to be the subject for "bets" as to its worth on a particular, future date. Shares of stock were "bet" on in a like manner. A "time-bargain" is essentially a contract in which one party agrees to sell to another party a certain number of shares in a certain company with delivery at a future agreed date at the price specified at the time of the contract. These "time-bargains" were legally invalid in England, but India had no prohibitive laws. Frere offered his support for a bill to prohibit these "time-bargains." Such a bill passed the Bombay Legislative Council and was sent to Calcutta for Governmental sanction in November, 1864.

Time was running out. Though in theory these "time-bargains" were to run for three to six months, in reality it seems that the settlement day for the vast majority had been set for July 1, 1865. A governmental decision was imperative before the Indian courts became jammed with cases arising from problems that certainly would arise when the buyers found they could not pay for the shares. As the government delayed its decision fresh "time-bargain" sales developed. Party B who had bought from Party A, now sold to Party C to procure funds to pay for a "time-bargain" secured from Party D. Each paper

transaction brought fantastic profits to the seller, and as word spread in the Share Bazaar, more and more people rushed to enrich themselves. It greatly annoyed Frere that the Government of India ignored his repeated requests for action. He writes to Sir John Lawrence on June 22, 1865:

The Bill did not propose to interfere with time-bargains in any way beyond applying the existing English law to them, and leaving them out of court to be dealt with as mere gambling debts, or debts of honour. . . I therefore approved the Act, which was passed by a majority of the Council, and sent it to you in November, and have since heard nothing more about it. . . .

Cotton has risen in price fifty per cent in two months, but the cotton-market is stagnant, not for want of cotton, or of buyers, or sellers, or of money, but because every man is holding every rupee he can command to be ready for a great settlement of time-bargains in July, when, I am assured on good authority, some thirty or forty millions sterling will change hands, according to the then price of cotton, opium, Government-paper, but above all, of shares of joint-stock companies, many of which exist only on paper.

Of course there must be a tremendous crash, and the best and most cautious will find great difficulty in getting paid what is owing to them in legitimate trade. The Court will be overwhelmed with business, and be sorely puzzled to apply the law, for it is in a very doubtful state, and all that is certain is that the later English Acts do not apply here.⁴⁷

Again, he writes, on July 7, 1865:

I hope you will now assent to our Act for throwing these time-bargains out of Court. There can be no doubt they have been one great cause of all the misery and ruin we see around us here now. There would, of course, have

⁴⁷Ibid., pp. 15-16.

been over-trading and mad speculation of all kinds under any circumstances when so much money was thrown into a community peculiarly prone to speculation and gambling. But the evil has been intensified by these time-bargains. They have this peculiarity as compared with all other kinds of betting, that they are carried on under the guise of trade, and the settling day is so far off that any unusual change in the price of the article bet on may cause such prolonged uncertainty as to the solvency of the betters, as seriously to embarrass all non-betting people who are connected with them.

It is easy to say "do not bank with a banker who thinks more of the Derby or rouge-et-noir table than his counting-house." But if the betting be carried on in the counting-house and under the forms of ordinary trade, the most cautious man in Lombard Street may be taken in. . . .

You must not suppose that because the first of July is past there is an end of the evil consequences of time-bargains which then fell due. The only step gained was each man's knowledge of his own losses; a few slipped out of their liabilities by informalities in the tender, or similar modes of getting off their bets; some of the smaller fry compromised on the spot, promising to pay twenty-five or thirty per cent of their losses, but to the great majority in number as well in character and wealth, the effect was merely to fix the liability and amount, and to allow the lawyers to commence a settlement by pettifogging duello instead of the summary settlements of Tattersall's and the Jockey Club Committee.⁴⁸

Finally in July 1865 it turned out that the time-bargains bill sent some eight months earlier to Calcutta had been lost by a government official while in transit between Simla and Calcutta. John Lawrence had never even read it, so could scarcely have acted to right the situation.

⁴⁸ Ibid., p. 16.

The role played by the Bank of Bombay in lending money for these "time-bargains" was not generally known, at least not by the right people. Frere under testimony to the Royal Commission states he had no evidence of any wrong doing until March 1865. On March 3, 1865 Sir Charles Wood wrote to him:

I cannot help being in some alarm at the possibility of a crash in your Bombay speculations. We hear disagreeable rumors, and after the way in which they have been going on I am afraid that it is probable. Pray look after your bank and currency matters. We must stand clear; but I would send for your Government directors in the bank, and desire them to look very carefully into what the bank is doing, and to keep you informed.⁴⁹

Exactly how Wood had found out about the bank's indiscretions is not clear; Frere states that Wood acted after receiving information from the Agra and Masterman's Bank that the Bank of Bombay was making advances upon shares.⁵⁰

Frere acted immediately to look closely into the Bank's management. He charged a newly appointed (March 8, 1865) Government director, Francis Chapman, to pay particular attention to the bank's proceedings. Frere recounts his first hint of wrongdoing came when Chapman reported that;

On his asking to look at some of the books, when he first went to the bank, the secretary for the time (I am not certain which of them it was) said, in rather a sarcastic manner, "We are glad to see a Government director taking an interest in the business of the bank."

⁴⁹ Royal Commission Report, evidence given in England, p. 227.

⁵⁰ Ibid., p. 208.

Mr. Chapman mentioned this casually. That was the first intimation which I ever had that anything less than a most complete devotion to their duty characterized the proceedings of the Government directors.⁵¹

Chapman's own testimony is most revealing. He particularly remembers his first board meeting--"I made my bow to my brother directors, and we were told that there was no business to be done, and we walked out."⁵² At subsequent board meetings, no business of any sort was brought up, nor were any of the bank's books presented for the directors' scrutiny.

And so the Government of India and that of the Bombay Presidency began to look into the affairs of the Bank of Bombay. But this was no easy task. Frere kept in constant touch with the Government directors but the full truth was not discerned for some months.

On March 2, 1865, Robert Hannay a member of the firm of Grey and Company, who had been a commercial director since the previous December, and who was a member of the consulting Committee of the Asiatic Bank, was elected President of the Bank of Bombay. He succeeded the inept Birch who had resigned in February and whose leaving the directors duly recorded by unanimously resolving "that the most cordial thanks of the directors be conveyed to Mr. Birch, for his long continued and most valuable services to the Bank of Bombay." And

⁵¹Ibid., p. 227.

⁵²Ibid., p. 145.

as if this were not enough they further resolved:

That Mr. Birch be requested on his return to England to have a full length portrait of himself painted by a good artist, at the expense of the bank, and that the same be placed in the board room of the new building, as a record of Mr. Birch's valuable services to the bank, during the five years of his chairmanship.⁵³

On becoming President, Hannay made no immediate alteration into the practices of the Bank, but began to make some inquiries and soon he discovered that money was being lent on promissory notes, with as well as without, shares being deposited for safe custody. Hannay, though seemingly disapproving of such a practice felt that such a policy was needed in view of the tight money situation in Bombay because of rumors of the approaching end of the American Civil War and with it a depression in the cotton market. On April 12, 1865 Hannay introduced a resolution to sanction the transactions which had already taken place and to relieve the money market by permitting additional ones. The resolution read as follows:

With reference to the following Board Resolutions of 6 August and 17 September 1863, as regards advances on the security of shares:⁵⁴

⁵³ Ibid., Summary, p. 18.

⁵⁴ These resolutions prohibited advances on shares without their being brought before the full board. Blank

Resolved, that the Secretary be authorized at his discretion, to advance on the shares of the under-noted companies to the extent of the amounts marked opposite each.

Shares so deposited are not to be transferred to the Bank, but the certificates to be accompanied by blank transfers signed by the transferor.

Bank of Bengal,
 paid up 8,000 rupees (~~₹~~800)
 present market rate 16,000 rupees (~~₹~~1,600)
 premium old and new shares
 advance 6,500 rupees (~~₹~~650) on each share

Bank of Madras,
 paid up 1,000 rupees (~~₹~~100)
 premium 123%
 advance 75%

Agra Bank,
 paid up 500 rupees (~~₹~~50)
 premium 160%
 advance 100%

Asiatic Bank,
 paid up 200 rupees (~~₹~~20)
 premium 105%
 advance 75%

Oriental Banking Corporation,
 paid up 250 rupees (~~₹~~25)
 premium 170%
 advance 125%

Commercial Banking Corporation
 paid up 250 rupees (~~₹~~25)
 premium 75%
 advance 50%

space was left for their subsequent insertion. This never took place. Few, if any, of the directors were familiar with them and thus did not realize what they were rescinding.

Bombay Reclamation Company,
 paid up 5,000 rupees (₹500)
 premium 30,000 rupees (₹3,000)
 advance 20,000 rupees (₹3,000)

Elphinstone Land and Press Company,⁵⁵
 paid up 1,000 rupees (₹100)
 premium 1,450 rupees (₹145)
 advance 1,000 rupees premium (₹100)

In granting such advances the Secretary will in all cases intimate and insert in the bond, that should the shares deposited be depreciated in value during the currency of the loans, the security must be increased or a partial payment made to reduce the debt; one percent above regular rate to be charged on such advances; and it is to be distinctly understood that such advances are only to be granted to first-class applicants.⁵⁶

Under testimony before the Commission Hannay stated that it was the secretary who decided who was a first-class applicant. And when asked why the particular companies were selected, Hannay said he believed implicitly in land companies. No doubt another consideration involved was that Hannay was then a director of the Bombay Reclamation Company, and other bank directors, Premchund Roychund and

⁵⁵ Founded in 1859 for the purpose of reclaiming land on the eastern foreshore from the sea, constructing wharves and piers, erecting warehouses, buildings for pressing cotton, and other facilities for the Port of Bombay. The company had established a strong foundation before the speculative mania began, but nevertheless its shares being in the market, men began to gamble with them and the price of the shares was highly inflated.

⁵⁶ Royal Commission Report, Appendix, Exhibit A183, p. 62.

Tracey, had interests in this company as well as the Asiatic Bank. Another director, Brown, was the secretary of the Elphinstone Land and Press Company.

The directors apparently voted on the rates at which the shares of the companies were to be taken. When Lushington objected to the rate for the Bombay Reclamation Company, as being too high, Hannay had countered; "I believe that there is no gentleman in this room who would not be glad to buy any number of those shares at 25,000 rupees (~~£~~250) instead of 20,000 (~~£~~200)." ⁵⁷ The Commission Report commented that such an observation was one which "Messrs, Tracey and Premchund, with their recent experience of buying shares at premia of 33,500 rupees (~~£~~3,350) and 34,000 rupees (~~£~~3,400) would no doubt confirm." ⁵⁸ And so Lushington thinking his colleagues knew best, withdrew his objection and the resolution was passed.

The powers of the secretary were now confirmed and Blair was allowed to lend any amount on shares upon deciding that the applicant was a first-class one. In the period from its enactment, to June 10, 1865, twenty-two advances on shares were made. Of this number, fourteen later resulted

⁵⁷ Ibid., evidence given in England, p. 184.

⁵⁸ Ibid., Summary, p. 21.

in losses to the bank amounting to 13,47,152 rupees (~~₹~~134,715)

Hannay testified that shortly after this resolution had been passed that he found loans on shares made at Blair's discretion which he felt to be poor risks; in fact loans had been advanced on shares of companies other than those authorized. And so Hannay instructed Blair to make no future advances without the sanction of the directors or the weekly committee. Blair seemingly saw the light, and left for England on April 29, 1865. Donald Robertson who had been "trained" by Blair and was a party to some of the worst dealings in Blair's period as secretary, succeeded him. With the termination of Blair's career at the Bank of Bombay, the bank entered the third period of its decline, May 1865 to April 1866.

CHAPTER III

THE COMMERCIAL CRISIS: THE BEGINNING OF THE END (1865-1866)

There were additional causes for alarm in Bombay besides the affairs of the Bank of Bombay. Early in 1865 an Indo-European telegraph service had been inaugurated. The first messages spent some eleven days in transit and not only were they quite garbled, but as they had been sent in French, there was a difficulty of translating them into English upon reaching India. By March much of the difficulty had been solved and the transmittal time had been reduced to about three days. Thus Bombay/Liverpool commercial and mercantile information could now be put on a more current basis. A correspondent for the Times expressed skepticism over this:

Marvelous fact! exclaims everyone; but the truth is, people in India are not so grateful as you would expect them to be. Interference in details, such as the telegraph tempts both statesmen and merchants to indulge in, may yet do much evil here. We don't want the Horse Guards to direct our campaigns, or the Bombay market to fluctuate, when the Atlantic cable is laid, with every change in that of New York and New Orleans. One of the first mercantile messages received announced a panic in Liverpool and Manchester as the result of intelligence that Mr. Lincoln had consented to open peace negotiations with the South. Peace when it does come to America will cause a crash in India that men held their breath, and the truth of the telegram is not yet known, because it has not been confirmed by subsequent information, though it has not been contradicted.¹

¹Times, April 6, 1865, p. 12, col. 5.

The American Civil War which had so completely changed the economic foundations of life in Bombay at its inception in 1861, had an even more profound effect on Bombay, at its close in the spring of 1865. Abraham Lincoln had been inaugurated for his second term on March 4, 1865. He then summed up his immediate tasks:

With malice toward none; with charity for all; with firmness in the right, as God gives us to see the right; let us strive to finish the work we are in; to bind up the nation's wounds; to care for him who shall have borne the battle, and for his widow, and his orphan--to do all which may achieve a just and lasting peace, among ourselves, and with all nations.²

He achieved his goal of peace early in April 1865 with the surrender of Robert E. Lee. It took approximately two months for the full impact of the cessation of the American War to be felt in Bombay.

Meanwhile Frere along with the newly appointed Government directors, F. S. Chapman and J. Lushington (later President of the Bank, from August, 1866 until its liquidation) began to take a close look into the management of the Bank of Bombay. Alexander Brown, a newly elected commercial director joined forces with Chapman and Lushington.

²Malone and Rauch, Empire for Liberty (New York, 1960), vol. I, p. 793.

Under testimony, Brown stated that soon after becoming a director he heard,

. . . that the Bank was involved in loans to men who had speculated largely, and who had large time-bargains in shares for settlement on the first of July following. . . . On taking my seat at the board on the 27 April 1865, I asked Mr. Tracey (a commercial director) whether in his opinion there was any ground for the rumours afloat. Business was just about to commence, and I had only time to get his answer that we had better not discuss the subject, as the Government directors were only too apt to take alarm.³

Brown continued by saying that Tracey's answer made him quite uneasy and he nearly determined to retire from his directorship, but instead he resolved to stay and endeavour to bring about a change for the better.

Chapman took a step towards solving one of the bank's most blatant errors when, before the board meeting of May 4, 1865 he questioned Brown as to whether he was satisfied with the way in which business was being conducted. Brown recounted the meeting:

He particularly referred to the utter ignorance in which the directors were kept as to the business and everything that was going on, and we agreed in opinion that the directors were ciphers, and the secretary apparently uncontrolled. Mr. F. S. Chapman then told me that both he and Mr. Lushington, the two Government directors, had come prepared to move in the matter, and I willingly agreed to support him.⁴

³ Royal Commission Report, evidence given in India, p. 49.

⁴ Idem.

At the board meeting that day Lushington proposed that restrictions should be imposed upon the secretary's powers to make advances. Lushington's proposal was strongly opposed by Hannay, then the President of the Bank, who said that "men of standing had too much self-respect to submit to have their applications scrutinized by the whole board, and that, if we insisted, the bank would lose much valuable business."⁵ Lushington testified to the Commission that he had felt that the sooner those who might be dissatisfied with such a check left the bank the better--"if they were ashamed of their loans, or were ashamed that their loans should appear."⁶ Lushington's proposal before the board resulted in a resolution which stated: "Resolved, that no new constituent of the bank be allowed credit beyond rupees three lakhs (£30,000) without the special sanction of three directors."⁷

Obviously this resolution did not do what Lushington had expected. The effect of the resolution was to allow the secretary, who was not even mentioned in it, to continue to make advances up to three lakhs, and only restricting him in lending over that amount when new constituents applied. At

⁵Ibid., p. 50.

⁶Ibid., evidence given in England, p. 185.

⁷Idem.

the time, as Lushington stated in his testimony, he had felt that this resolution would be a limit on the powers of the secretary. But though the written resolution as recorded in the minutes of the meeting does not state it, Lushington said that there had been a general discussion among the directors and an understanding was reached that all future applications for loans should be brought up before the board. The resolution certainly fell short of stating this. Such action is but another example of the inexperience of the directors in carrying out sound business procedures and keeping accurate records; an impression is not as good as a written statement.

Thus, although the new directors felt that they had inaugurated a better state of things, there was little improvement in the practice as to advances. In fact loans continued to be granted on promissory notes on a single name without any additional security. The directors would need the experience of several more months to see the danger of such banking.

Early in May, 1865, a native merchant, the largest exporter of cotton, Byramjee Hormusjee Cama, failed for an enormous amount of money (£3,300,000), owing the Bank of Bombay 17,71,682 rupees (£177,168). When he convened his creditors on May 17, they resolved to transfer his entire estate to some appointed trustees.

The news of this first and quite extensive failure spread quickly throughout Bombay and led to a panic which lasted the remainder of the month and the first part of June. There was a run on the Bank of Bombay, and the directors fearing a suspension of payment applied to Frere who in turn telegraphed Lawrence on June 15. Frere requested permission for the Government of Bombay to advance, if needed, 150 ^ll^{ks} (~~£~~1,500,000) from the currency reserve, stating the importance of quick action lest it "be too late to avert disaster financial, and political, more extensive than the failure of the banks."⁸ Lawrence agreed that this might be done, and as soon as it was generally known in Bombay that the bank would be supported, the run ceased, and no monetary assistance was needed.

The Economist of June 10, 1865 devoted extensive space to a commentary on this crisis at Bombay. It felt that the crisis had been an entirely predictable event:

The collapse of a mania is a certain result of the nature of a mania. It does not need an external force to destroy it, though an external force often helps, but it dies of itself and by the sudden substitution of the real difference of making money for the supposed facility of making it.

⁸Ibid., Summary, p. 28.

At Bombay no kind of "shares"--nothing of this new imaginary unrealized wealth, is not saleable. For the moment there is no longer a just distinction between good undertakings and bad, all are in much danger of suffering alike. "Woe to the last holder" is the motto of a panic. . .

It is impossible to predict the exact end of such a mania, to fortell what precise quantity of ruin it would cause, to specify nicely where safety will begin. . . Two considerations . . . may be suggested. . . . First, a great deal of money was made in Bombay. Much actual profit had accumulated there. . . . Bombay may lose much of its new cash, and yet still be richer than Bombay used to be. Secondly, it is probable that though the Indian cotton trade cannot be the unnaturally profitable trade it has been of late, it will still be a profitable trade. The Southern States of America must for a considerable period be disorganized; no one knows what their precise condition twelve months hence will be. . . . it is not possible that American production can for a long time reach its old quantity, and till it does so⁹ the India supplement must be needed and must be valuable.

Frere described the situation in Bombay in a letter of June 23, 1865 to Colonel Herbert Bruce:

We have just now fallen on a commercial crisis of which no one not on the spot can form an idea. I have seen such things in London, but all is here multiplied in the ratio of the greater credulity, timidity, and want of frankness which characterize the natives as compared with the Europeans, and the extent of failure is incredible. I see in the papers that there were three failures in a fortnight for over a million, and I hear of one impending for six million sterling.

It is of course a very anxious time for me, and the work, with only one colleague to help me, is very hard; but I have great confidence in him, and we have no minuting; and whatsoever may happen, I have no fears for

⁹Economist, June 10, 1865, Vol. XXIII, pp. 685-686.

the honour of Government. In this respect I feel grateful to Sir Charles Wood for his support in ridding me of sharejobbers, and do not regret the black looks I have received from some of the cliques in Bombay.¹⁰

Though the Bank of Bombay had somehow weathered the storm while other companies were forced to liquidate, both Lawrence and Wood communicated their interest in the situation to Frere. Lawrence telegraphed the Bombay Government on June 21, 1865 to ask if steps had been taken to ascertain the quality of the outstanding bills and securities which the bank held. Frere replied that this had been done and that "the advances on shares without collateral security were not large, nor the prices at which they were then valued high."¹¹ The Commission Report later chastised Frere for not checking more thoroughly into the "collateral security" which in many cases represented promissory notes on shares and nothing more.¹²

Lawrence's letter of June 22, 1865 to the Government of Bombay, requested a full report as soon as possible regarding the bank's affairs and outlined seven specific areas of interest. The chief points on which information was desired were; first, as to the assets and liabilities;

¹⁰Martineau, II, p. 23.

¹¹Royal Commission Report, Summary, p. 28.

¹²Idem.

secondly, what had been the losses of the bank since the commencement of the crisis; thirdly, what was the amount of overdue bills; fourthly, what proportion of that amount might be fairly expected to be realized; fifthly, what were the prospects of the bank with reference to the bills which had yet to run; sixthly, whether the provisions of the bank charter as defined in Act X of 1863 had been violated; and seventhly, what had been the rates of advances on shares.¹³

Frere received a private note from Wood at about this same time in which Wood asked:

Pray desire your Government directors to look after the bank's proceedings. Their advancing on shares, such as you have at Bombay, is contrary to all banking principles. It would be contrary to the charters of the banks of Calcutta and Madras. Unfortunately not so as to Bombay; but it is not the less wrong.¹⁴

In addition there had been a dispatch from the Secretary of State of India on June 2, 1865 in which referring to advances made by the Bank on shares of joint stock companies, directed the Bombay Government to restrict the Bank's business to the same business as had been authorized to be transacted by the Bengal and Madras banks. It specifically called upon the Government directors to take measures to

¹³Ibid., evidence given in England, p. 209.

¹⁴Ibid., Summary, p. 29.

check such advances.¹⁵ The Government of Bombay referred this dispatch to the Government directors, and shortly thereafter, on June 29, 1865 another letter was sent to these directors requesting a confidential report on the state of the bank at that time.

Certainly it cannot be denied that the Bank of Bombay as well as the Government of Bombay were now faced with a responsibility to answer these requests. Their reply was most regrettable--the seven point inquiry made by Lawrence was ignored, and the directors contented themselves by only replying to the June 2, 1865 letter from the Secretary of State.

The report of the Government directors dated June 30, 1865, concerned only advances made by the bank on shares. It referred to the resolution of April 12, 1865 failing to explain that the August 6 and September 17, 1863 resolutions prohibiting advances on shares without their being brought before the full board were now rescinded. The letter further stated what shares had been taken as collateral security subsequent to the Act of April 12, 1865, failing to mention that these shares were simply collateral securities to promissory notes of the borrowers. The letter misled the Government of

¹⁵Idem.

Bombay into believing that all was well. The Bombay Government accepted this report, and forwarded it to the Secretary of State on July 8, 1865.

Frere's letter of this date which accompanied the directors' reply stated that there could be little doubt that the value of the securities referred to in the directors' report would improve, that the rumors about advances on Back Bay shares had been exaggerated, and that the Bombay Government would reserve judging the elected bank directors until a promised report from the Government directors had been studied.¹⁶ This was the only reply offered to the Governor General's letter of June 22, 1865. Under testimony, Frere failed to produce a plausible explanation for this, stating only that the crisis had been more prolonged than expected, and it had been difficult to compute the value of any one security from day to day and hence make any judgment on it.

Bombay, indeed, was in turmoil. The depression reached its very depth on July 1, 1865--the day on which hundreds of the time-bargains had become due. It was the black day of Bombay. The Economist reported:

The whole commercial condition of Bombay is locally so peculiar and complicated, that we may expect to hear of very singular occurrences. We are told, for .

¹⁶Ibid., p. 30.

example, that lately large quantities of diamonds and pearls and precious gems bought a few months ago by the wealthy traders of Bombay chiefly for show, have been urgently offered for sale in the bazaar, in order to obtain silver for the payment of engagements.¹⁷

And the Calcutta correspondent to the Times noted:

The lowest sum at which we can fairly take the extra profits made by Bombay in cotton during the four years of the American War is 50 millions. . . . From the 50 millions which were available for other purposes than legitimate trading, we must deduct 10 as the amount of extra profit kept by the peasantry and middle men in the interior. This will leave 40 millions for speculation in the island of Bombay. What has become of it? At least 5 have been sunk for the moment unproductively, in various land reclamation companies . . . and I believe that 5 more have been taken to England by Scotch merchants. This leaves 30 millions, of which at least 10 have been lost in re-drafts for cotton. . . . We are thus reduced to 20 millions, the debris, as it were, of the ruin now taking place. The local estimates of the liabilities of Bombay speculators for shares alone vary from 16 millions to 30 millions. That is, one part of the community has paid, or promised to pay to the other for shares in barren companies at least 16 millions more than these shares are worth at par. These 20 millions are still in Bombay and will be available for legitimate trade and the completion of the best of the reclamation works when the crisis is over. At present, they have simply changed hands,--changed, too, from a large number of small capitalists to half a dozen large millionaires. Six men may come out of the crash now going on with very heavy purses; all the rest of the island is insolvent.¹⁸

In view of this tense financial situation in Bombay, the board of the bank meeting in July decided not to declare a dividend for the past half year ending June 30, 1865. This

¹⁷Economist, July 1, 1865, Vol. XXIII, p. 781.

¹⁸Times, August 7, 1865, p. 7, col. 3.

turned out to be a wise decision, for though the bank had been most profitable for the better part of the time period, the extent of its losses in the late panic was still not known.¹⁹

By late summer the situation had been alleviated somewhat; prospects for cotton were improved with a slight price increase. Hope revived of a return to the past and once again the share bazaar became active. The Times of India voiced an unheeded warning:

The maxim that a burnt child dreads the fire does not hold good in the case of those with whom speculation has become a vice in their blood. Rather are they like the foolish moth which nothing but total destruction will cause to cease from folly.²⁰

As the price of shares gradually rose at least one director, Cowasjee Manackjee (a Commercial Director), advised selling all shares which the bank had deposited as security for overdue bills. This would either pay off the debt or at least insure that the loss would not be total. But most

¹⁹The secretary Robertson wrote in the report to the shareholders on August 7, 1865: "Taking rather an unfavorable view of the liabilities current on the 30th of June last, the directors estimate that the losses will not exceed thirty lakhs; it is quite possible that the ultimate loss will be much less, so that there is every hope of the shareholders receiving a fair dividend at the end of the current half year." Royal Commission Report, evidence given in England, p. 116.

²⁰Times of India, July 14, 1865, as quoted by Radhe Shyam Rungta, The Rise of Business Corporations in India, 1851-1900 (Cambridge, 1970), p. 89.

directors, deluded by the promise of returning prosperity, wanted to wait for a better price. Some, especially those who had engaged in share speculation, felt that a deluge of shares such as the Bank held, onto the market, would cause another panic.

The bank secretary Robertson explained how he was able to dispose of some of his bank shares through Premchund. He remembered a conversation in June 1865 when he asked Premchund:

"I want you to sell all my shares. I want to get rid of all my shares;" which even then would have given me a very good return. I said, with reference to the Bank of Bombay shares, "They are very much down now, and I want to get out of them." They were at a par, I believe. He said, "The best thing for you to do is to take so many more to make an average." I consented, telling him that immediately the shares got up to a certain price I would tell him to hand them over. There was no writing, and no acknowledgement in any way. I never got a share in my possession; and in September or October 1865, when the shares were at about 70 rupees a share, I made a calculation, and found that with some money which he, or rather his nephew, who was conducting business for him, and for whom he was responsible, owed me for shares, I should be clear; and I said to him, "These shares must be handed over at such a price, which clears me the amount." He said, "Do not you want to make any money out of them?" I said "No, I want to get rid of them." He said "Very well, they shall be handed over;" and the account was made up in that way. I got some shares in the Bombay Reclamation Company. It was in September 1865, when the shares were at 7 or 8 per cent premium, and I considered them at an end."²¹

²¹Royal Commission Report, evidence given in England, p. 122.

If Robertson had acted in a like manner for the bank many losses would have been avoided. An opportunity had been lost which never would occur again.

In October the Bombay Chamber of Commerce issued its annual report for 1865. It opened with the statement:

The official year just closed will be notable in the history of Bombay as a year hitherto unparalleled in its commercial annals for the reckless spirit of gambling speculation which possessed a great portion of the community; speculation which resulted to large numbers--as might be expected from its character--in utter ruin and disgrace.²²

The report went on to state that the unexpected wealth which had poured into the lap of Western India by the incident of the American Civil War had not been used wisely. The mania for share speculation which had broken out two years before, had continued to grow in intensity until it seemed to absorb the time and attention of the community. The legitimate trade of Bombay came to be neglected, and the energies of the people had been devoted to the promulgation of schemes the utility of which to the public was probably the last thing thought worthy of consideration by the promoters. Bombay became flooded with "Financial Associations" and doubtful schemes of reclamation. When the mania was at

²²Raymond Sullivan, One Hundred Years of Bombay 1836-1936 (Bombay, 1937), pp. 74-75.

its height, intelligence was received of the unexpected termination of the American Civil War, and the gambling speculation suddenly collapsed, and insolvency and bankruptcy followed on a scale of magnitude unknown in any other crisis of modern share speculation. So numerous were the insolvencies and so enormous were the amounts involved, that the Chamber of Commerce report stated that it had requested the Legislature to give power to creditors to secure a more speedy liquidation of insolvent estates.

The report ended by declaring that the high position which Bombay previously had bore among the commercial cities of the world had been lowered by the gambling transactions. It resolutely stated however that the genuine trade of the place was at bottom thoroughly sound, and it depended on no adventitious circumstances of any kind for its prosperity, and now that the false line of wild speculation had been removed, the Chamber of Commerce had every reason to hope that the commerce of Bombay would be placed on a sounder and broader basis than it had ever known.

On September 8, 1865 Sir Charles Wood wrote to the Government of Bombay to acknowledge the receipt of their letter of July 8, 1865. This dispatch which Frere forwarded to the Bank of Bombay, and there termed by Hannay to be a "most tyrannical communication," directed the Bombay Government

to take measures for making an alteration to Act X of 1863 which would preclude the bank from advancing on the security of shares of public companies not guaranteed by the Government. It further stated:

But above all, it should be the care of the Government directors to watch very closely the proceedings of the bank, in order, so far as their influence extends, to prevent any repetition of imprudent management; and any disposition on the part of their colleagues to depart from sound principles should be forthwith communicated to you, in order that you may take such measures as may seem to you to be necessary in reference there to.²³

On November, 1865, the directors replied:

The Secretary of State has either been much misinformed relative to the transactions of the Bank of Bombay, or else has quite misunderstood the information supplied. The Bank of Bombay has never advanced money directly on shares, but during the crisis that occurred in the early part of this year the times were so exceptional that the directors considered it prudent, seeing so much money was lent on personal security only, to obtain as much collateral security as possible when granting loans. This was done, and it enabled the bank to assist many of their constituents who possessed shares in sound undertakings and of undoubted value, but required money.²⁴

The Directors continued by saying that upon calmly looking at the circumstances of the past they believed that, had any other course been adopted, the result would have been most disastrous; and had the Government directors not given their

²³Royal Commission Report, evidence given in England, pp. 211-212.

²⁴Ibid., p. 117.

consent to the course commented on, they would have been responsible for ruin, probably more general and widespread than had ever been seen before in any city or commercial community. Referring to the alteration of the Charter, the directors said that it was a matter over which they had no control, but since they knew that the clause referred to had never been taken advantage of, they did not see that any change was either necessary or desirable.

The statement by the directors that they had never advanced money on shares is untrue; the resolution of April 12, 1865 had enabled the Secretary of the bank to make such advances. When questioned by the Royal Commissioners on this point, Hannay explained that "we always considered that we had the security of the applicant as well as the shares."²⁵

In December, 1865 cotton prices dropped again and the hope which had been evident in the fall that the financial crisis would soon end, now vanished. Just before Christmas, Frere, then at Sholapoor, a few hundred miles from Bombay, received word from Lushington that the bank was in trouble and that suspension seemed imminent. Lushington reported that the bank had only 6.7 lakhs (£60,750) available in coin. Frere set out at once for Bombay, arriving the morning of '

²⁵Ibid., p. 248.

December 26. After meeting with the bank directors Frere discovered that the lack of coin was not so much the fault of the Bank of Bombay as of the Government Treasury and Currency Department at Calcutta who had sent the bank bills instead of the desired coins. The reason the bank had requested coins was related to the cotton situation. In times past the local cotton merchant bought from the cultivator on credit and sold the cotton again on credit to a Bombay merchant --the money not being realized until the English importer paid for the cotton, often many months hence. The risk of such long credit was now thought to be poor and so the rural merchants were selling only for cash. In some cotton districts bank notes were not used and so this necessitated a larger amount of coin to be available at the bank. Apparently the bank had warned Calcutta of this need for coin, but their requests had been ignored. Luckily this crisis being only accidental, was temporary.

On January 23, 1866 the bank directors met and resolved to pay an eight per cent dividend (totalling 8,36,000 rupees) to all shareholders for the six month period ending December 31, 1865. At this same meeting the directors appointed a committee to investigate the debts outstanding at the bank (the 30 lakhs declared lost in August, 1865) and decide the total amount which they deemed to be irrecoverable.

Why the directors did not wait to decide to declare a dividend until after this report had been received is but another example of their imprudent action. The Commission Report reckoned the bank's statement to be as follows:

Profits of 1865	Rs 30,69,967	
Reserve fund	Rs <u>10,56,983</u>	
		Rs 41,24,950
Losses computed in		
August 1865	Rs 30,00,000	
Add dividend for half		
year	Rs 8,36,000	
		Rs 38,36,000 ²⁶
	Balance of reserve fund	Rs 2,88,000 ²⁶

When questioned by the Commission as to the judiciousness of such a payment, Robertson said that the directors "were anxious to pay a dividend on account of the shareholders," and further reflected that, "perhaps in one sense it might have been an advantage to the shareholders, because if the money had not been paid to them it would probably have been thrown away like the rest; but that is the only way in which I can look at it as a prudent measure."²⁷

The Government of India had, on January 13, 1866, addressed a letter to the Bombay Government which noted that six months had now elapsed since the bank, in a critical

²⁶ Ibid., Summary, p. 33.

²⁷ Ibid., evidence given in England, p. 117.

state, had called for Government permission to advance money if needed from the currency reserve and had received that permission. Lawrence continued by pointing out that since that date no substantial improvement seemed to have taken place in either the condition or the management of the bank. He went on:

. . . the Governor General in council is of opinion that an examination into the affairs of the bank should no longer be delayed, with a view to such a revision of the terms upon which its business has been, and is conducted, as may seem expedient. The Governor General in council considers that the examination should comprise an investigation, not only into the assets and floating liabilities of the bank, but into its transactions especially during the past six months. In conclusion, his Excellency in council hopes that a full report on the several matters above referred to will be furnished by your Government without unnecessary delay.²⁸

The reply to Lawrence's letter was drafted by Government directors, Francis Chapman and G. Norman. It was dated March 31, 1866, but did not reach the Governor General until June. The following are extracts from this report:

The first of July (1865) found the bank with very many of its formerly best constituents either insolvent or embarrassed. It was plainly seen that unless a general policy of forbearance was exercised, loans which would, in all probability, prove ultimately good, would, if the parties were pressed, result in immediate and heavy loss. . . .

On the 30th June (1865) the amount lent from the head office was 321 lakhs, and on the 30th December, 313 lakhs.

²⁸ Ibid., p. 212.

Of the former amount 79 lakhs had been realized up to the 30th December, and 126 were overdue. The process of recovery has, it must be admitted, been slow, but then the very great delay attendant on all legal proceedings in Bombay, and the fact that the largest of the bank's debtors have not yet realized the proceeds of the current year's investments in cotton and other produce, must not be overlooked. . . We beg further to report that the total amount of loans and discounts outstanding on the 30th December at both the head office and branches was 381 lakhs of rupees; that out of this 163 lakhs of rupees are overdue, and that 30 lakhs have, after a careful and impartial scrutiny, been set down as the amount of the probable eventual losses. From the balance sheet, a copy of which is annexed, it will be observed the bank will, after allowing for all losses, and after having paid a half-year's dividend at the rate of 8 per cent, per annum, be possessed of about three lakhs in excess of its capital. . . .

The operations of the bank, not only during the past six but during the past ten months, will, we believe, bear the strictest scrutiny; and there is no prospect of the loss of a rupee on a single new transaction entered into during that period. . . .

With regard to the future, the only practical difference between the charter granted to this bank and that granted to the Bank of Bengal is that contained in section 32 of Bombay Act X of 1863, authorizing advances being made on shares; and we have reason to believe that the directors would have no objections to its being expunged, as for the last ten months this power has never been made use of.²⁹

It was unfortunate that Norman and Chapman had been chosen to draft the above report. Norman had just recently become a director and Chapman had never been employed in a bank before (he stated before the Commission that he wished

²⁹Ibid., Summary, p. 34.

he had never been in this one). The Commission report found that these directors did not search into matters deeply enough and took far too sanguine a view in estimating expected losses from overdue loans. It pointed out that:

"The statement that there was no prospect of the loss of a rupee on the transactions of the last ten months, unfortunately proved incorrect, and would never have been made, if the Government directors had understood the danger of advancing upon such personal security as the bank was still in the habit of taking," and further, ". . . the last statement, that the power given by section 32 of Act X of 1863 had never been made use of during the last ten months, was singularly inaccurate. During those ten months, from the 1st June 1865 to the 31st March 1866, there had been no less than 25 advances directly on shares, irrespective of numerous other transactions in which shares had been taken as security, subsequently to the advances being made."³⁰

The directors of the Bank of Bombay committed one last error during this period. In March 1866, Hannay about to depart for England, received a request from the directors to define the powers of the Secretary. In turn, Hannay wrote to the Secretary, Robertson, asking him to state what he felt his duties were. Robertson replied on March 7, 1866:

I consider that according to the practice in the Bank for some years past, I, as officiating secretary, am empowered to act as follows:

1. To have the entire control of the establishment, head office, and branches (of course under the directors)

³⁰Ibid., p. 35.

2. To discount bank bills and bills on good houses of a currency not exceeding 60 days. There is no limit, but I have hitherto seldom (sic) taken over three lacs of the paper of one house
3. To grant temporary advances to banks, houses, and other constituents of the bank
4. To discount bills, and to grant loans and credits on personal security to well known men
N.B. Since I have been acting, the times have been so exceptional, that I granted very few advances without consulting at least one director.
5. The renewal of bill, loans, and credits, I consider is left to my own discretion, of course bearing in mind the order of the board, not to renew for the full amount if possible, but to get 25 % in cash. Some bills, etc. for special reasons have been renewed in full.
6. To purchase hoondies for the purpose of providing branches with funds
7. To purchase and sell bills on Calcutta and Madras
8. To purchase and sell gold and silver bullion
9. Power given in July last to attend meetings of creditors of parties indebted to the Bank; to agree to propositions made at such meetings; to sign trust deeds, etc. at my discretion.

I think these headings include everything. I may say that I consider the order of the President in every case sufficient for me to act under, should he not request me to refer any matter to some of the other members of the board.³¹

Thus Robertson believed that he had great powers, and Hannay who then wrote to the directors, did not dispute this.

³¹Ibid., Appendix, Exhibit A35.

He further stated that he believed that Robertson's capabilities as secretary were excellent and agreed almost fully with what Robertson had written. Thereupon the board of directors adopted Hannay's letter as the proper duties of the office and this letter was embodied on March 19, 1866 in the only byelaws ever passed by bank officials defining the secretary's powers. These byelaws unfortunately were never sent to the Government of India for sanction, and so never became valid.

Hannay retired from his post as president early in April 1866 and Lidderdale assumed the position. Hannay had been an industrious president, but as he was himself mixed up in the speculative game, he did little to help the bank recover losses or institute sound business procedures. Subsequently, in the next period of the bank's history, from April 24 to December 10, 1866, the ruin of the bank was completed.

CHAPTER IV

THE FAILURE OF THE BANK OF BOMBAY AND AFTERMATH (1866-1868)

The directors of the bank during this crucial period were Francis Lidderdale and J. Lushington, successively presidents, A. Brown, A. Stewart, R. Tracey, G.M. Stewart, Macdonald, Commercial Directors, and G. Norman and Charles E. Chapman, Government Directors. Each of these men neglected his duty to the bank and by doing so completed its ruin.

Premchund Roychund, the foremost speculator in Bombay whose reputation one writer has characterized as "the most renowned alchemist who can turn dust into the yellow metal and who by his magic wand, transmuted the sands of Back Bay into the solid nuggets of gold where with to pave the way to paradise,"¹ on April 26, 1866 needed the sum of 25 lakhs (₹250,000) to prevent his stopping payment. He was indebted to almost all the major banks and he applied to Robertson at the Bank of Bombay for these 25 lakhs. Robertson informed Lidderdale, the new president, who then summoned a special meeting of the directors to discuss this loan. As any

¹S.D. Mehta, The Cotton Mills of India 1854-1954 (Bombay, 1954), p. 29.

stoppage by Premchund would be a catastrophe to all banks in Bombay, Lidderdale also invited the managers of the Oriental, Chartered Mercantile, Asiatic and the Bank of Hindustan to attend this meeting.

Lidderdale presented Premchund's request before the gathered bankers. There apparently was little discussion, for everyone felt that Premchund would have to be assisted or else they all would fail with him. No statement of Premchund's affairs was brought forward, but the group agreeing that they should have one, adjourned until the following morning.

At seven a.m. on April 27, 1866 the bankers met again, this time at Lidderdale's home. Additional bankers from the Comptoir d'Escompte and the Commercial Bank were in attendance. On this occasion Premchund himself was present, though he remained on the porch and answered questions put to him by Robertson or Tracey who occasionally came out of the meeting. A rough statement outlining Premchund's affairs was drawn up at this meeting. It was not verified since those present felt there was no time for any investigation as Premchund seemed most pressed for the money. It was not even verified as to whether if the 25 lakhs were advanced that the amount would be sufficient to cover Premchund's needs.

As for securities, Premchund proposed to deposit his jewels, said to be worth from 15 to 20 lakhs, the title deeds to his landed property holdings, and to give a joint promissory note together with his father Roychund, Candass Narrondas, and Kursondass Madhowdass.

A memorandum which resulted from the meeting estimated the value of Premchund's jewels at 20 lakhs. No verification was made of this figure.

The value of the landed property was estimated in this memorandum to be some 26 lakhs. This was in spite of the fact that G. Norman, a Government director, who as collector of land revenue in Bombay was familiar with land prices on the island, estimated the property to be worth only 14 lakhs. Even Robertson, in a letter written at this time, estimated the land to be worth only 18 lakhs.² Those present discussed the value of the land and in the course of their discussion Tracey left the meeting several times to verify certain holdings with Premchund. After one such communication, Premchund who apparently did not like such an examination, cleverly told Tracey that "if they wanted to make a bother I would rather stop payment, and that if they made any difficulty about the securities I would give them the names of three

²Royal Commission Report, Appendix, Exhibit Q, p. 86.

other parties as guarantees."³ When Tracey returned with this statement the directors felt they had better complete the matter quickly to avoid Premchund stopping payment, and so took the "additional precaution in the interests of the shareholders"⁴ of having a joint promissory note signed by Premchund Roychund, Roychund Deepchund, Candass Marondass, and Kursondass Madhowdass drawn up.

And so it was agreed that a loan of 25 lakhs should be granted to Premchund for six months on the basis of the security offered. The Bank of Bombay agreed to subscribe 10 1/2 lakhs, the Oriental,Chartered Mercantile, Asiatic, and Commercial Banks and the Comptoir d'Escompte should each subscribe 2 1/2 lakhs, and the Bank of Hindustan, 2 lakhs. The Bank of Bombay agreed to advance the full sum, which was then to be recouped by the other banks in the amounts designated.

President Lidderdale directed the bank's solicitor, Kelly, to prepare a deed to carry out this agreement--but neither Kelly nor the secretary, Robertson, made any memorandum or minute of the arrangement that had been entered into. The signatures of the bank managers present at this meeting

³Ibid., evidence given in India, p. 89.

⁴Lidderdale so characterized this note. Ibid., p. 19.

had not been taken, nor had all the stipulated security been handed over by Premchund. Nevertheless that same afternoon (April 27), Premchund received a draw of the loan.

Not only had Robertson failed in his duty as bank secretary to see that some agreement had been signed by all the parties involved before the bank advanced any money, but Robertson also failed to inform the directors of the true state of Premchund's account with the bank. For already on April 26, Premchund had been indebted to the bank for the sum of 23 1/2 lakhs. Included in this amount was a 5 lakh overdraw on his account as well as an outstanding loan of 9 lakhs. Robertson knew of this, as did Tracey who in fact had been Premchund's business partner in many financial speculations. The other directors under testimony to the Royal Commission, stated that they did not know that Premchund had this liability in addition to the difficulties for which he needed 25 lakhs. Had they been aware of this they undoubtedly would have required Premchund to give further security for enlarging his debt. Unfortunately Tracey and Robertson had not been disposed to give out this information. Premchund testified to the Commission that he had only been questioned as to his pressing liabilities for which he presented the directors with a rough memorandum; as for his affairs generally,

he had given no statement as none had been asked for.⁵

The extent of Tracey's dealings with Premchund were revealed at the Commission hearings. Tracey and Premchund had jointly engaged in speculations, with Premchund supplying Tracey with money to such a degree that at one time Tracey owed Premchund 29 lakhs (₹290,000). This large debt was mostly paid off, though in November 1865 Tracey had been forced to write off a loan of 3.8 lakhs which he owed to Premchund. In early April 1866 Tracey had borrowed 4.5 lakhs from the Asiatic Bank in the name of his firm (Ritchie, Stewart and Co.) for Premchund. On April 19 Tracey gave the Bank of Bombay a guarantee for Premchund's overdrawn account to the extent of 3 lakhs. This guarantee, in the light of Tracey's financial situation, was utterly worthless, yet Robertson accepted it. After the 25 lakh loan had been granted to Premchund, Robertson asked Tracey if a portion of it should not be used to pay the overdraft, but Tracey said not. And still Robertson did not inform the directors of Premchund's true financial standing.

On April 27 some of the title deeds of the landed property of Premchund's security had been deposited with the bank. This same day the bank paid out 11 lakhs to Premchund.

⁵Ibid., p. 89.

The next day a further sum of 4.5 lakhs had been paid to the Asiatic Bank; this discharged the debt which Tracey had incurred for Premchund and partly explains the reason he helped Premchund obtain the 25 lakh loan.

Premchund deposited some of the jewels that formed a part of his security at the bank on April 29. Fraser, a bank official, accepted them and called in Courvoisier, a local jeweller to estimate their value. Courvoisier looked over these jewels and said they were worth between 2 and 3 lakhs. Fraser being very much disturbed at this low estimate went to inform the directors. He stopped in the secretary's room first, and there meeting Robertson and Tracey, told them of the low valuation. Fraser then did not go into the board room to tell the directors, believing that either Robertson or Tracey would do so. Notwithstanding the importance of this news, it was not communicated to the directors and Robertson continued to advance money to Premchund.

Premchund Roychund failed in August 1866 and the securities the bank had taken proved wholly insufficient. . The jewels were sold in England and India and realized only 2.5 lakhs. The landed property brought in 5.2 lakhs. The promissory note was not worth the paper it was written upon.⁶

⁶Roychund Deepchund evaded payment and absconded into the Guicowar's country. Candass Narrondass was Premchund's

Many of the bank managers who had been present at the meeting at Lidderdale's home repudiated the transaction which they had agreed to and refused to reimburse the Bank of Bombay for their part of the 25 lakh loan. The balance which Premchund owed the Bank of Bombay, the Commission computed to be 24.7 lakhs (~~₹~~247,369); the sum proved to be irrecoverable.

Shortly after making the large loan to Premchund, the Bank of Bombay had determined to aid the Asiatic Bank. The Asiatic Bank rivaled the Bank of Bombay both in fostering the speculation mania in Bombay and in its reckless business procedures. The Asiatic Bank had been formed in 1863 but the prosperous times and influential management soon caused this bank to be the most formidable competitor of the Bank of Bombay which had been chartered some twenty-three years before. Much like the Bank of Bombay, the Asiatic, because of the exceptional times, made large advances on a variety of questionable securities. It was the banker of the Bombay Reclamation Company and Premchund Roychund was involved in dealings and promotions with the Asiatic.

The Bank of Bombay had often loaned money to other banks in Bombay. In May 1866 the Asiatic, finding itself in

tool and passed through the Insolvent Court of Bombay. Kurlsondass Madhowdass failed on May 16, 1866 and his trustees repudiated any liability on the promissory note. Ibid., Summary, p. 38.

difficulty, applied for such a loan. Much the same fear that had prompted the directors to lend money to Premchund, that is that the failure of one bank would lead to the failure of many others, led the directors to grant a credit of 15 lakhs to the Asiatic Bank. On May 14, 1866 the Asiatic obtained this cash credit after depositing certain securities and promising that more would follow. As if this were not enough a week later the Asiatic still finding itself in difficulty applied for, and was given an additional 5 lakh loan.

On July 13 when the first cash credit expired, the Asiatic owed the Bank of Bombay 11.7 lakhs (£117,883). So far the Asiatic had sent in only one lakh of security to cover the loan. Thus the Bank of Bombay necessarily was forced to extend this loan with the hope that the Asiatic would somehow recover and be able to pay it off. September 1 was the new deadline and the Asiatic Bank agreed to deposit new securities. In late August the directors discovered that one such security for five lakhs had never been received. They called in Anthony Morrison, the manager of the Asiatic for an explanation and he apparently satisfied their questions, for in substitution for these five lakhs, further security was given.

When the second credit expired on September 1, the Asiatic owed the Bank of Bombay 16.8 lakhs (£168,282). The

few securities which the Bank of Bombay held proved to be either not negotiable or almost worthless. It seemed that Robertson, the bank secretary and a close friend of Morrison, knew that the majority of the promised security had not been sent to the Bank of Bombay. But he never told President Lushington of this. In spite of the expiration of the cash credit on September 1, Robertson allowed the Asiatic to continue drawing money from the Bank of Bombay up to September 20 on which day the Asiatic failed. The net consequence of the transactions was that when the Asiatic failed, it owed 19.6 lakhs (~~£~~196,656) to the Bank of Bombay.⁷

It was another case of bad banking and bad bookkeeping. The accountant J. De Ga had kept Robertson informed almost daily as to the status of the Asiatic's account and never passed a check unless authorized to do so. One such communication is presented in the Commission's findings:

Asiatic Bank's account is already overdrawn by Rupees 18,09,761; shall I pay this cheque for Rs 51,498?

(Signed) J.M. De Ga
Pro-Accountant

⁷The real loser when the Asiatic failed however, was the Bombay Reclamation Company for which the Asiatic had served as banker. Some 91 lakhs of the Company's deposits were lost, and the Company was put into liquidation in November 1866.

Bank of Bombay 8/8/1866

Pay

(Signed) D.R.⁸

Robertson seriously neglected his duty by not informing either the directors or the president of such overdrafts. The president and the directors never bothered to check the ledgers for themselves, and simply trusted that Robertson would tell them of such a situation. The result was as in the case of Premchund's failure, that the money could not be recovered.

Meanwhile after an unexplainable delay the last report of the Bank of Bombay's Government directors dated March 31, 1866 reached the Governor General on June 16, 1866. Lawrence replied to their communication in a letter dated July 13. In it he stated that the embarrassments of the bank were attributable to the abuse of powers which never should have been conferred on it by charter. He noted that the Government of Bombay had proposed to correct this error and to procure sounder management for the bank, but he added:

The Governor General in council, though fully sharing in the desire of the Bombay Government to uphold the credit of the Bank, cannot suffer the revenues of India to be indefinitely pledged to the support of an establishment of the affairs of which he is kept in ignorance. The information furnished by the report of the directors contains little more than is to be found in the general

⁸Royal Commission Report, Appendix, Exhibit A31, p. 30.

statements of assets and liabilities published in the newspapers.⁹

Lawrence requested a listing of the banks, firms, and individuals to which the bank was under advance, as well as the dates and amounts of such advances, and the securities upon which they had been granted, and the sums advanced on each security.

The Bombay Government postponed answering these questions from the Governor General. In testimony before the Royal Commission Frere said that he had considered that there was no practical way of responding to Lawrence's inquiry lest he send all of the bank's records up to Simla and such action he felt would surely have destroyed the bank. He felt that the bank was still solvent and such a request and its implications would have caused the directors to resign en masse and so destroy the bank. Frere asked the Commission to consider that "when you are in the height of a storm, it is not the time to inquire whether the captain was wise in putting to sea, or whether some better seamanship might have avoided the ship getting into danger."¹⁰

⁹Ibid., evidence given in England, p. 213.

¹⁰Ibid., p. 214.

On August 6, 1866 the annual general meeting of the shareholders of the Bank of Bombay was held. The report issued for the shareholders hedged on pertinent issues; it set forth that the capital had been encroached upon to the extent of 50 lakhs, without admitting that the sum to be the total loss incurred, or that it was a loss in addition to the 30 lakhs announced previously.

The Bombay Government appeared now to have understood the real status of the bank and were anxious to have some disinterested party give an accurate opinion as to the bank's position. As a prominent member of the Financial Department of the Government of India, E.F. Harrison, was then visiting Bombay, he seemed to be the perfect choice to head an investigating committee. Frere, wishing not to have the confidence in the bank lost, requested the directors to apply to Lawrence for a committee to review their estimate of the losses set forth in the annual report. The directors complied with the Governor's request, and formed a committee consisting of Harrison, A.J. Hunter, a reputable merchant who had abstained from share speculation, and Dinshaw Manockjee, a wealthy native, also free from the taint of speculation.

On September 8, 1866 these three gentlemen submitted their report to the Governor of Bombay. They were of the opinion that the valuation of June 30, 1866 by the directors

of the Bank of Bombay was fair and had been carried out with care; but they were also of the opinion that a large addition must be made to the estimate of the bank's losses. This addition they said, should be no less than 34.4 lakhs (£344,950).

Frere forwarded the committee's report to the Government of India on September 19, 1866. On October 3 the Government of India telegraphed Bombay asking to see the detailed statement of the bank's account--the statement which the committee had considered "proof of the fairness and care with which [the directors] estimated the position of the bank [on June 30, 1866]." ¹¹ The Government of Bombay asked for this statement at the bank, but Robertson refused to hand it over, replying that the statement "contained information with reference to the committee's estimates which the directors alone could understand, and that the directors therefore considered it unnecessary to forward a copy to Government." ¹² The Government of Bombay took no further steps to obtain a copy of this statement for Lawrence.

Meanwhile Lawrence continued to write Frere, reminding him that the request of July 13, 1866 for a detailed listing of the bank's advances still remained unanswered. Frere,

¹¹ Ibid., p. 220.

¹² Ibid., Summary, p. 43.

disinclined to press the bank for this information, still believing that the bank would suffer a loss of confidence, now felt that the committee report was a sufficient reply. But Lawrence continued to press for detailed information--the discrepancy between the committee report and the annual bank report--rendered this necessary. On October 3 he wrote a letter to the Bombay Government that he felt it was the duty of the Government of India as the largest shareholder in the bank, and as trustee of the treasury balances in their custody to require the full exposition of the bank's affairs.

The reply to the Governor General's letter, dated October 22, 1866, again reiterated the hazards involved if such an inquiry were made and the confidence of the bank lost as a result. Nevertheless Frere did write that he would direct that a statement be prepared and submitted as soon as possible. Then, he added, if the Government of India still was not satisfied, they should select men to make an inquiry into the bank's accounts. Frere obviously felt he was being tormented unnecessarily by Lawrence to furnish detailed information; he complained to Wood:

We have asked the Government of India, if they want more inquiry into the past, to nominate independent commissioners to inquire here; but as nothing has ever been charged against the directors worse than the almost incredible mismanagement, folly, and extravagance from which so many banks have suffered at the same time in their rivalry for custom, and as the directors and

secretary of that day have all left, I hardly see the use of further inquiry.¹³

The statement which Frere promised Lawrence was sent to the Government of India on November 23, 1866. The information it presented was worthless. It listed only advances which exceeded three lakhs which had been overdue on June 30, 1866. It avoided all mention of sums below that amount or any advances that had been renewed (because they were overdue)--most of these were for more than three lakhs. It failed to list both Premchund's great loan of 25 lakhs (for it was not due on June 30, 1866!) and the 19 lakhs due from the Asiatic (the cash credit expired on September 1, 1866). The Royal Commission Report commented that "a more unsatisfactory report could scarcely have been formed."¹⁴

Lawrence certainly acted judiciously from the time he first learned of the bank's difficulties. It was well within the duty of the Government of India as guardian of the public balance in the bank to ascertain the true position of the bank and make any inquiries necessary in forming this opinion. It is actually quite improbable that any of the directors would have resigned if such an inquiry had been instituted,

¹³Ibid., Appendix, Exhibit A195, pp. 79-80.

¹⁴Ibid., Summary, p. 43.

for by the summer of 1866 the directors though still incompetent as bankers, were not involved in speculation as previous directors had been. However by now the position of the Bank of Bombay could no longer be helped, though the ultimate disaster of course could have been lessened somewhat.

In October the Bombay Chamber of Commerce published its annual report. The report declared, "the official year closes amid gloom and depression, after a commercial and banking panic more intense in character and protracted in operation than has hitherto been known in the history of Bombay."¹⁵ The report denied rumors which had hinted that members of the Chamber of Commerce were among promoters of the speculation and said that few if any of the mushroom concerns had ever become members of the Chamber. The verdict of one journalist was included: "there have been commercial panics elsewhere; but probably no community ever went so entirely mad as Bombay did in 1865."¹⁶

Reginald Smith described the year as one filled with great commercial disasters, stagnation of trade, famine and scarcity. He criticized the Bank of Bombay as the worst offender of all, which fostered and spread the speculation

¹⁵Raymond J. F. Sullivan, One Hundred Years of Bombay 1836-1936 (Bombay, 1937), p. 75.

¹⁶Ibid., pp. 76-77.

in spite of repeated warnings from Lord Lawrence.¹⁷

Another contemporary said:

In 1866 when the gains and losses were reckoned up, the fortunes could be counted on the fingers of one's hands while the dead and wounded literally strewn the field of battle.¹⁸

Though surrounded with failures and losses, somehow the Bank of Bombay managed to survive until January 1868. During its final year of existence little happened, for the bank now ruined, was virtually in liquidation. On January 15, 1867 at a special meeting of the shareholders, the capital of the bank was reduced fifty per cent. This meant that the nominal value of a share was now 500 rupees, but as the public confidence in the bank had been lost, shares began to be sold in the market at 250 rupees each.

At this same time John Stuart, a former secretary of the bank under the previous charter, returned to Bombay and became secretary once again. The directors had meanwhile prepared a statement listing all the outstanding debts due the bank and during meetings on January 30 and 31, 1867 concluded that one-half of the bank's capital still remained intact. The directors spent the remainder of the year

¹⁷Reginald Bosworth Smith, Life of Lord Lawrence (New York, 1883), II, pp. 416-417.

¹⁸James Douglas, as quoted in S.D. Mehta, The Cotton Mills of India, op. cit., p. 32.

attempting to realize the assets they claimed the bank had-- their search turned out to be futile. It was an almost impossible task to lay claim to any of the estates of debtors to the bank who had been declared insolvent. This situation occurred because of a poor legislative enactment (Act XXVIII of 1865) which slowed down the processing of these cases to such an extent that only two estates were settled under it by September 1868.

In February 1867 the bank underwent another severe run on its funds, with 1,69,00,000 rupees (£1,690,000) being withdrawn within a few days. The Government of India again came to the bank's rescue by assuring that the bank would be supported with Governmental funds if needed. As in the run of June 1865, the Government's action effectively stopped further withdrawals of deposits.

But as the months went by it became more and more apparent that the debts outstanding to the bank could not be regained. At the general meeting of the shareholders held on August 5, 1867 the directors presented a statement declaring that the last six months of operations had been most unfavorable ones owing to the run on the bank and the undecided claims against insolvent estates. They estimated a loss of capital amounting to one and one-half crore (£1,500,000).

The Bank of Bombay limped along in this deplorable state until at a general meeting of shareholders on January

13, 1868 those present resolved to voluntarily wind up the bank. Stuart, the secretary, was appointed liquidator.

The shareholders, many of whom were Civil Servants both in India and in England who had invested their savings in the bank, were now quick to fix the blame for the bank's failure on the Government of Bombay. The English shareholders brought a charge of corruption against the directors of the bank. Wood accordingly directed Lawrence to appoint a Commission to inquire into the causes of the bank's failure and to issue a report on its findings. The Commission which Lawrence organized consisted of Sir Charles Jackson, a former judge of the Supreme Court of Judicature in Bombay, as President, Major MacLeod Innes, Military Accountant-General with the Government of India, and Maxwell Melville of the Bombay Civil Service. This Commission gathered evidence, first in India (June 29-September 9, 1868), and then in England (November 9-December 11, 1868). Some ninety-six witnesses appeared before the Commission.

The Commission performed its duties expeditiously and submitted a comprehensive report on February 10, 1869.¹⁹

¹⁹ Royal Commissions of Inquiry had come into extensive use during the Victorian age. Chosen by the Minister of the Department most concerned, the commissions then worked independently of control by that Department and remained in existence until the work was finished. They exerted considerable influence on the course of British history in the area

It gave six causes for the failure of the bank. First it said that Act X of 1863 removed many restrictions contained in the previous Act and allowed unsafe business transactions.

Secondly the report stated that the powers given under Act X of 1863 had been abused by weak and unprincipled secretaries acting under the influence of a designing native director, Premchund Roychund. Third, the Presidents and directors in the period August 1863 to April 1865 were negligent and,

of colonial practices, parliamentary statutes and social legislation. Hugh McDowall Clokie and J. William Robinson, Royal Commissions of Inquiry (Stanford, 1937), and Harold F. Gosnell, "British Royal Commissions of Inquiry," Political Science Quarterly, XLIX, pp. 84-118. Some commissions, of course, sat for a long time and failing to have a unanimous report, issued a minority report. A poem entitled "Pageant of Parliament" printed in Punch alluded to such reports, it begins:

I saw an old man in the park;
I asked the old man why
He watched the couples after dark;
He made this strange reply: -

"I am the Royal Commission on kissing,
Appointed by Gladstone in '74;
The rest of my colleagues are buried or missing;
Our minutes were lost in the last Great War.
But still I'm a Royal Commission
Which never has made a Report,
And acutely I feel my position,
For it must be a crime (or a tort)
To be such a Royal Commission.
My task I intend to see through,
Though I know, as an old politician,
Not a thing will be done if I do. . . ."

as quoted in Clokie, op. cit., pp. 236-238.

failed to do their duty by omitting to pass byelaws, by not giving proper supervision to bank affairs and to its secretaries, and particularly by failing to ascertain how the business of the bank was being conducted. The Commission listed as the fourth cause the exceptional nature of those prosperous years which should have led the bank officials to exercise more than ordinary vigilance. Fifth, the Presidents and directors were not competent bankers and were incapable of managing such an institution as the Bank of Bombay in difficult times. The absence of sound legal advice and assistance was given as the sixth cause of failure.²⁰

The liquidator's report had been turned in on November 12, 1868, and according to Stuart's estimate the Bank of Bombay had irretrievably lost 1,88,99,331 rupees (~~₹~~1,889,933). This was nearly all the capital of the bank; the few lakhs which remained were turned over to the shareholders. Thus each ruined shareholder received about one hundred rupees for every five hundred rupees (nominal value of each share per January, 1867), which had once been quoted at nearly 3,000 rupees.

²⁰Royal Commission Report, Summary, p. 47.

The bulk of the money, some 25 lakhs, which had been turned over to the shareholders belonged to the balance of the Government of India. The Government of India in January 1868 started a new Bank of Bombay with another 25 lakhs, though this new bank agreed to accept the liability for the whole 50 lakhs. As may be expected there was much criticism for starting up a new bank on the heels of such a disaster.²¹ But the share mania was now over and the economy was making a gradual but firm recovery. Much money had flowed into Bombay during those prosperous days of the American Civil War and much of it had been lost, but some had been applied to sound works which now formed the basis for this renewal. The impract^{is}ability of the numerous schemes which had been launched during the boom period had been demonstrated, and the cotton industry which had weathered the crisis was now seen to be a stable and profitable industry.

The New Bank of Bombay, Limited, as the reconstructed bank was named, began with a capital fixed at one crore of rupees (£1,000,000) divided into 20,000 shares of 500 rupees apiece. A prospectus was issued and subscription was invited from the shareholders of the old Bank and the public for the first issue of 10,000 shares at par. The limitations in the

²¹Times, February 7, 1868, p. 10.

charter of the earlier period were reimposed and under prudent management the new bank prospered once again. The Presidency Banks Act of 1876 took over the governing of the new Bank of Bombay along with the Presidency Banks of Bengal and Madras. The Government thereupon ceased to be a shareholder in the bank. In 1921 these three banks were amalgamated as the Imperial Bank of India.

The new bank prospered because it had learned two important lessons from the downfall of the Old Bank of Bombay. First it learned that certain rules had to be imposed on the bank's business and these rules must be strictly followed by the board of directors. Secondly the relation between the Government of India and the bank was revealed to be unsound as well as misleading.²²

The ascendancy which Premchund Roychund attained in the bank could never have been attained but for the defects in the constitution of the bank. These defects had arisen almost entirely from the dangerous relationship to the State which the bank enjoyed. The bank had seemingly been a state institution, though everything possible had been done to deprive the State of even the smallest effective control. The Government had held one-third of the shares of the bank, they appointed one-third of the directors, they banked with

²²Economist, July 3, 1869, pp. 773-774.

it exclusively, they twice stepped forward to save it from ruin by promising advances from the Treasury, and most of all they appeared to assume an almost direct responsibility by passing the Legislative Act (Act X of 1863) defining its operation. The public and the shareholders observing this, naturally looked upon the bank as a State department certain to be safe and requiring little attention on their part. Thus little attention was paid to the directors who became a self-renewing body, and who studiously neglected to fulfill their duty to the Bank.

But the Government's liability for the bank was absolutely illusory. The Government owned shares exactly as the other shareholders owned them. The charter (Act X of 1863) on which the bank operated had been drawn up by the directors of the bank and it contained clauses neither intended or known of by the Government, one of which (granting advances on personal security) ultimately destroyed the bank.

The entire legal constitution of the bank had thus been altered by the bank's officers who seemingly acted under the Government which had accepted their charter without any inquiry or alteration. The powers to lend money were supposed to be regulated by the board of directors on which the Government directors sat. But these Government directors were outnumbered two to one and furthermore they were '

officials who previously had had no acquaintance with banking. Everyone eventually lost from such an arrangement: the Government, because it felt duty bound to support the bank in time of danger, and the shareholders, who believed that the bank could not fail since the State was watching over it. The new Bank of Bombay, Limited, however, was much the better for the lessons learned and was able to avoid the path to failure experienced by its predecessor.

CHAPTER V

CONCLUSION

The blockade of the southern American ports during the American Civil War caused the textile industry of England to look elsewhere for cotton supplies. They found at Bombay an enterprising group of merchants who, at the prospect of large monetary rewards, eagerly attempted to fill a large portion of Lancashire's demands. The subsequent flow of funds into Bombay had a great impact upon the small island. Its economy, which previously had been governed by the monsoon season, now made its first large-scale contact with world trade. Up to this time Indian cotton had mostly been ignored due to its poor quality and the uncertain delivery schedules caused by the lack of internal communications and long voyages around Africa. The sudden and real demand for cotton during the Civil War caused these problems to be partly surmounted or discounted. Sir Bartle Frere, the Governor of Bombay, introduced legislation to raise the standard of Indian cotton and prevent adulteration to the bales. The subsequently passed Cotton Frauds Act helped realize Frere's aim. Railroad lines were built and communications with the cotton growing districts were speeded up.

The cotton growing districts of India certainly benefited from the demand for their crop, but the island of Bombay felt the largest impact of the times. Being an island, its position was peculiar. Already crowded, the island experienced a large influx of people who wished to share the wealth being accumulated there. Frere, characterized by many, including Lord Lawrence, as too free a spender of Government funds, launched upon a massive reconstruction effort in the city. Older portions of the town including the fort were leveled and new Government buildings and housing areas erected. But this was not sufficient to meet the needs of the growing population and commercial activities. Thus the notorious land reclamation companies which grew up during this period were really an obvious outgrowth of the situation. They were for the most part based on a sound need--they were designed to fulfill port and warehouse demands as well as living areas. Unfortunately, once the large amounts of money flowing into Bombay could no longer find sound investments, the reclamation companies fell into the hands of speculators and their shares began to sell for prices inconsistent with good business judgement. And so when the cotton market collapsed, the reclamation companies received the death-blow as well, since the capital which backed them had been carelessly placed in unsound financial companies.

The sudden wealth caused by the cotton sales led to the growth and expansion of unsound financial companies. Just as the reclamation companies grew out of a need for increased land, the financial companies too fulfilled the need for a place of investment for the profits of the cotton trade. The Bank of Bombay figured prominently in the rise of these institutions by lending them large sums of money. Some of the Bank of Bombay's directors and officials were dishonest men out to make fortunes in the speculative market, others were simply lazy victims of their own lack of knowledge of sound banking procedures. The Government of India still, suffering the effects of the Mutiny, was weak and unfortunately followed to some extent a laissez-faire attitude towards the economic activity. During the height of the boom period, many Government officials resigned and returned to England because the cost of living had risen to such a degree that the civil servants' salaries barely covered living expenses. Others quit to join the staffs of the newly founded bubble enterprises. With fewer men to govern such an expanding community, Frere cannot unconditionally be blamed for the economic disaster which followed the termination of the American Civil War.

Frere tried vigilantly under questioning by the Royal Commission of Inquiry to vindicate his part in the calamity. Certainly he deserves partial blame for what happened, but

perhaps such strong words as "supineness and inaction" which one of the Commissioners used to characterize his actions should not have been uttered. Frere had previously served as a Government official in Calcutta and had welcomed the post of Governor of Bombay. He meant well; he hoped to transform Bombay into a prosperous, beautiful city. He worked hard and long and suffered many illnesses and separations from his family. Unfortunately he lacked discretion and spent too much money for building projects at just the wrong time, and promoted the reclamations and growth of cotton, while not watching the financial side of the city with adequate caution. Even when prompted by Sir Charles Wood to look into the affairs of the Bank of Bombay, Frere was too sanguine in his belief that the Bank would somehow work things out on its own. Then too his hostility with Calcutta over the Government of India's criticism of his liberal spending policies, and their powers to check his acts led him to ignore repeated requests by Lawrence for information regarding the Bank of Bombay. It is doubtful however that even if their warnings which came after considerable damage had already been done had been heeded, that the Bank could have survived the massive failures which befell men and companies in Bombay.

In the long run Bombay was better as a result of the economic disaster. Frere's building projects created a new,

forward looking city--modern day Bombay dates from his governorship. The demand for cotton had given an impetus to improve the quality of Indian cotton and had forced an improvement of communications with the interior of India. Some of the money which the cotton trade had brought into Bombay went to good use; cotton mills were built, old portions of the city were renovated and public works and government buildings considerably improved. In addition the Lancashire manufacturers found that trade with India had enhanced the quality of the Indian staple and thus helped their industry. They formerly had feared the Indian mills as competition but now realized that the cotton mills in Bombay were not a threat to their business. When the crisis was over the Bombay merchants and cotton spinners found they had a good base for the future, and this industry has thrived up to the present time.

Surely the speculative mania had its disruptive effects, but both Indian and Englishmen suffered equally. Kipling's maxim of a later decade that, "East is east, and west is west and never the twain shall meet,"¹ proved erroneous in this situation. All classes of Indians and

¹Rudyard Kipling, "The Ballad of East and West" (1889), British Literature (ed. Spencer, Houghton, Barrows), vol. 2 (Boston, 1952), pp. 872-874.

Englishmen had invested in and organized the speculative schemes, so neither could be condemned entirely for misjudgment. Thus both could start afresh with no injurious burden of blame. Even Premchund Roychund suffered no recriminations for his part in the mania--and amassed yet another fortune before his death in the early 1900's. A lesson had been learned from the disaster and Indians as well as Englishmen took care not to cause a similar situation in the future.

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