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BOOK REVIEWS

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Kenneth D. Garbade, **Birth of a Market: The US Treasury Securities Market from the Great War to the Great Depression** (Cambridge, MA: MIT Press, 2012, xii + 393 pp., $50, ISBN 978-0-262-01637-7)

Julia C. Ott, **When Wall Street Met Main Street: The Quest for an Investors' Democracy** (Cambridge, MA: Harvard University Press, 2011, 313 pp., $35.00, ISBN 978-0-674-05065-5)

How do financial markets develop? Do they arise naturally on their own or are they artificially constructed? This is the basic question addressed by two recent works on some specific markets: US Treasuries and retail stocks. Kenneth Garbade, Senior Vice President at the Federal Reserve Bank of New York, addresses the former in *Birth of a Market: The US Treasury Securities Market from the Great War to the Great Depression*, while Julia Ott, Assistant Professor in the History of Capitalism at the Eugene Lang College and the New School for Social Research, takes on the latter in *When Wall Street Met Main Street: The Quest for an Investors' Democracy*.

Garbade has a kind of structuralist view of the matter. The modern bond market, he argues, arose because of and was shaped by the changing nature of the United States public debt. Between 1917 and 1939, the public debt changed from a transitory phenomenon created to fund particular projects or wars that required paying off and specific funding legislation to a permanent institution that required constant management run solely by the Treasury.

With the United States entry into World War I, the public debt ballooned and the traditional method of selling securities at auction was replaced with fixed-price subscriptions. This was done to appeal to the public at large as an effort was made to place war bonds, known as Liberty Loan bonds, among the citizenry. The Treasury then expanded this sales method to financial institutions, abandoning auctions. The speed and complexity of wartime issues also prompted Congress to turn over its debt management responsibilities to the Secretary of the Treasury in the Second Liberty Loan Act. However, Congress retained the right to police the overall debt by setting a debt limit ceiling.

These developments left the Treasury with a large debt and a rather rigid mechanism for managing it. Refunding operations involved almost random entries into the

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market with offers of fixed-price issues that may or may not be welcomed and much churning in the money markets. It also made efforts to manage Treasury cash balances extremely difficult. To overcome these problems, the Treasury slowly reinstituted auctions through a cash management instrument known as the Treasury bill, which provided flexibility, eased sales efforts, and integrated cash and debt management. The Treasury also set up a consistent schedule for refunding operations, providing 'regular and predictable' offerings to the market.

Ott's analysis takes a more discursive turn, arguing that the retail stock market had its origins in an ideological construction of thrift that grew out of World War I bond sales. The idea that the country consisted of a vast sea of potential, small investors (however erroneous) was constructed in the early twentieth century and was wielded as a weapon in support of antitrust legislation: the small investor needed the Government's protection from the NYSE and its like.

This figure of the small investor was appropriated by the Federal Government during World War I and used to sell war bonds and, at the same time, redefine the meaning of citizenship. Instead of grounding citizenship on the holding of real property, the Government machinery behind the Liberty Loans posited citizenship on the purchase of Government securities, which could be held by any class, race, or gender – an investor democracy. As a result, investment became widespread and proof of Americanness.

After the war, large corporations, financial firms, banks and the NYSE took over the small-investor market, smothering the existing Government thrift programme that sold low-denomination securities to the general public. Instead, employee and consumer stock ownership plans were marketed as was the importance of the expert, local stockbroker. At this point, the investor democracy was recast as a popular means to support capitalism through the ownership of corporate stock. In this brave new world, the market became the solution to society's ills, not the cause.

Garbade could learn a thing or two from Ott. While no one can dispute his analysis of the evolution of Treasury debt management during the interwar period as a reaction to changes in the public debt, it does not tell the whole story. Why was the focus of the Treasury only on developing a market targeted at the financial industry? Why were the efforts to popularize the debt abandoned during the 1920s? Garbade does not consider the ideological or political forces shaping Treasury policy, which Ott finds so critical to understanding the period. After spending a decade developing thrift instruments for small investors, the Treasury basically gave the market to the retail financial industry. In fact, except for Savings Bonds, the twentieth century is the story of the exclusion of the small investor from the Treasury securities market and their abandonment to the tender mercies of the for-profit equities market.

And, what pressure did the financial industry bring to bear to shape Treasury policy? Somehow, it helped kill the Government Savings System aimed at small investors in 1924. Also, if we look at the growing size and sophistication of the bond market, it staggers belief to think that the Treasury acted unilaterally in developing that market. Surely, the market makers had more to say to the Treasury than whether or not they approved or disapproved of a Treasury issue after the fact.

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Ott's story of the power of ideology and political economy to shape a market is path breaking and rewrites our understanding of twentieth-century capitalism and finance. However, Ott needs to remember what Garbade takes for granted. There has to be some sort of demand for a market to arise. No amount of advertising, however persuasive or coercive, will bring a market into being if the money is not there for investing. And, evidently, the small investor was there and just waiting for an opportunity to put his or her money to work. Since at least the late nineteenth century, there was a thrift movement in the United States, imported in part from England, leading to the Postal Savings System and Postal Savings bonds. In fact, the targeting of the small investor by the US Government and the creation of a market for low-denomination Treasuries got started during the Civil War and got a major boost during the Spanish–American War. So, the Treasury and the financial industry were pushing against an open door in the 1910s and 1920s.

One would also like to know more about why the financial industry entered the retail sphere. Ott argues that this was a political move to stem the threat of Government regulation of the financial industry by co-opting the investor democracy. But what of the economics, the profits involved? If we follow the money, rather than the rhetoric, is the story the same? Perhaps the actions of the financial industry were primarily those of a grab for fees combined with a marketing campaign that constructed an ideal of the small investor, which, as a side effect, also had political perks for the industry.

So, how do financial markets come to be? Are they the after-effects of economic necessity or institutions created to generate demand? Garbade, the economist, would argue that a financial market arises from a structural need; the politics and agendas of the market makers are immaterial. Meanwhile, Ott, the historian, sees the start of a financial market as the act of designing an artifice not only to generate a new source of profit but also to serve ideological ends. Most likely, the answer lies somewhere in between. A market is shaped (and constantly reshaped) by the dynamic between the sellers and the buyers. And, all sorts of factors come into play here, including economics, politics and ideology. Deciding which is more important probably depends upon if you like your history à la Marx or Hegel.

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Harold James, **Making the European Monetary Union: The Role of the Committee of Central Bank Governors and the Origins of the European Central Bank** (Cambridge, MA, and London: The Belknap Press of Harvard University Press, 2012, 567 pp., ISBN 978-0-674-06683-0)

With Europe' financial crisis, Europe's economic and monetary union is again at the centre of many economic policy debates. The crisis further illustrates the importance of history in understanding the roots of the present situation. This book, which was

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