

# **Decision Taking, Risk Management and Trust in the "periphery": London City bankers and their investments in Greece (1850-1910)**

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## **Introduction: The high-risk Greek loan of 1910**

In 1910, only one year after the Greek Uprising of Goudi which brought Eleftherios Venizelos to power, an international banking syndicate consisting of the National Bank of Greece, several French banks, and the London banks Hambro & Son and Emile Erlanger & Son issued a loan of 150 million drachmas (150 million Francs) in Paris and London. This loan was the first one to be issued after the Greek bankruptcy of 1893 without any guarantee from the International Financial Commission (IFC), which Greece had to accept in 1898 to pay back her foreign debt. Until 1910 all Greek foreign loans were guaranteed by the IFC, because otherwise it would not have been possible for the country to issue on the stock exchanges at acceptable conditions. The 1910 loan was issued only two years before the conflicts in the Balkan regions escalated with the Balkan Wars and WWI, damaging the Greek financial system considerably.

Under these circumstances the question arises as to why the foreign bankers got involved in this obviously high-risk financial transaction. What kind of business connections with Greece did they have? What did their risk management look like? What kind of networks existed? How was confidence between the partners constructed? This paper argues that both London banks became interested in the Greek loan because of their long lasting relationships with the country and because they wanted to keep or develop their reputation as a Greek "house bank". Multiple path dependencies made them open-minded to the idea of providing Greece with fresh money. On the other hand, it was competition between the partners that drove them to increase their risk appetite. The Greek 1910 loan is analyzed as a case study for the risk management of London banks at the beginning of the 20<sup>th</sup> century.

## **Greece's London "House banks"**

In 1909 the Greek government started negotiations for a big foreign loan due to its broker, the Bank of Athens. The Bank of Athens' governor Zafiropoulos Matsas contacted two Lon-

don banks to ask whether they were interested in a Greek loan: Hambro & Son on the one hand, and Emile Erlanger & Son on the other hand. No other London banks were considered. What made these two banks so attractive for the Greek Government? Why did the government count on their willingness to take part in the issue? The history of the relationship between the two banks and the Greek state goes some way to explaining this.

### Hambro & Son

Carl Joachim Hambro started in the eighteenth century as a trader in Hamburg. He then moved to Copenhagen as a protégé of Rothschild. Around 1850 C. J. Hambro & Son had become a member of the first league of British bankers, by then situated in London. Hambro was interested in Mediterranean business, issuing loans for Sardinia and Cavour's struggle for the unification of Italy, but was also active in the USA and Scandinavia. From 1864, Hambro & Son was the most important source of finance for Greece in Britain, due to its good relationship with the royal dynasty and King Georg. This relationship was based on concrete reasons. After the fall of the first Greek King Othon, a native Bavarian, in 1862 a Greek delegation came to London to look for a new king for their country. It was C. J. Hambro who introduced the Greeks to the Danish Prince Wilhelm, who in 1864 became King of Greece. Hambro advanced Wilhelm £10,000 for his enthronement in Athens, without charging interest. As the contract shows, Hambro did not demand any guarantee from the future king but advanced him the money as debt of honor.<sup>1</sup> His agent Count Spounech joined Wilhelm in Greece and was able to announce to his principal not only the prompt repayment of the money, but also the promising economic development of the country. In a letter from Athens Count Spounech pointed out that Georg I. was extraordinarily thankful to Hambro for his confidence and was willing to do him any favor.<sup>2</sup> It is thus not astonishing that Hambro enjoyed a privileged position in Greece as the king's personal banker.

When Greece was re-opened to the international money market in 1879, Hambro energetically entered the new market and participated in 10 of the 13 loans issued to the Greek State between 1879 and 1893. Even if its engagement in Greece only reached its peak in 1920, Hambro & Son was doubtless the most important financier of Greece in Great Britain at the beginning of the twentieth century. Joanna Minoglou-Pepelassis analyzed in detail all of

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<sup>1</sup> See the contract in London Metropolitan Archives.

<sup>2</sup> Count Spounech to Hambro, 30.9./ 12.10.1864, in: London Metropolitan Archives.

Hambro's engagements in Greece until the 1930s.<sup>3</sup> Hambro participated, for example, in the development of the Greek railway system. Shortly before the Greek bankruptcy in 1893, when the difficult financial situation of the country had become obvious to any observer, Hambro was the last one to issue a so-called "funding loan" of £4 Mio for Greece. After the bankruptcy he was the leading figure in the negotiations between the British bondholders and the Greek government, always exerting himself to ensure good conditions for the defaulter. In 1902, 1904 and 1906 Hambro was the first to issue Greek securities again with his participation in a railway loan, even if under the guarantee of the IFC. The first issue failed, but the very successful second and third ones of 1904 and 1906 were interpreted as signs of the economic revival of the country, as well as the resurrection of the confidence of international financial markets after the establishment of the IFC. In 1908 Hambro successfully issued £200,000 of an advance to Greece, a fact that was interpreted by the international press as a further sign of the reestablishment of Greek finances.

So for Hambro & Son the relevance of a 40-year tradition of financing Greek projects and the Greek state cannot be underestimated. Indeed one finds few materials in the British Foreign Office which deal with financial negotiations with Greece where the name of Hambro as broker and intermediary is not mentioned. Seen from the Greek perspective, there were few alternatives to Hambro & Son on the London market.

### Emile Erlanger

But in the case of the 1910 loan, not Hambro but Emile Erlanger & Son was the first London banker contacted by the Greek brokers. The Erlanger family, originally situated in Hedderheim near Frankfurt and later in Frankfurt itself, also had close connections to Greece. Emile Erlanger (born in 1832) was a bill broker in Frankfurt like his father Raphael Erlanger.<sup>4</sup> He became consul-general of Greece in Frankfurt in 1855. Of course we should not overestimate the importance of the consul-general function, which was very popular among Frankfurt bankers at this time, but Erlanger did indeed use his function to initiate business relationships with Greece. Very shortly after his appointment he visited Athens and met with the governor of the National Bank of Greece, Georgios Stavros. He also became acquainted with Stavros' sister-in-law and his niece. In a letter, he thanked Stavros for the

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<sup>3</sup> Minoglou, Ioanna Pepelasis: The rise and fall of the house of Hambros in Greece, 1864-1940, in: Bonin, Hubert (Ed.): Transnational companies. 19<sup>th</sup> and 20<sup>th</sup> century, Paris 2002, p. 401-417.

<sup>4</sup> See documents in the Institut für Stadtgeschichte, Frankfurt.

very pleasant meeting and welcomed any kind of business connection. Indeed, a first business transaction took place in April 1856.<sup>5</sup>

In 1859 Erlanger moved to Paris where he founded his own *maison de banque* with 500,000 francs as capital. He continued the contacts with the National Bank of Greece. In the 1860s these relationships deepened. In Paris he soon became consul-general of Greece again and kept this function for several decades. He organized the contributions of Greece to the universal exhibitions of 1867 and 1878. Maybe anti-Semitic prejudices contributed to his reputation as a ruthless and greedy banker, but on the other hand Erlanger was well known for his widespread philanthropy. After the Franco-Prussian War of 1870, he moved to London. Erlanger was largely engaged in the Mediterranean, especially in Egypt and Tunisia. At the end of the 1890s his relationship with the National Bank of Greece became even closer, and Erlanger intermediated between Greek and French as well as Belgian banks. In 1902, 1904 and 1906 he participated in the abovementioned railway loan with Hambro. At the beginning of the twentieth century, when the currency rate of the drachma improved, Erlanger's relationships with Greece and especially with the National Bank intensified. In June 1901 he thanked Streit, the governor of the National Bank, with warm words for the honor that he had bestowed on them by spending time with Erlanger's son Emile in Florence.

It was not only Erlanger's relationships with Greece that were well established, but also those between Erlanger and Hambro & Son. At the beginning of the 20<sup>th</sup> century Hambro & Son and Erlanger cooperated in many fields, and Everard Hambro used to address Erlanger in his letters very familiarly as 'mon cher Emile'.<sup>6</sup> The possibility of continuing this well-established and faithful cooperation with an investment in Greece, where both British banks were interested in expanding their investments, might have been very attractive for both of them. But was the cooperation the most important motive that attracted them? The correspondence concerning the issuing process gives further insight into their motives and risk management techniques.

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<sup>5</sup> See the correspondence between Erlanger and Stavros in the Historical Archives of the Greek National Bank.

<sup>6</sup> See their correspondence in: London Metropolitan Archives, MS 19108.

### **The 1910 loan and its pre-negotiations: the bankers and their deliberations**

Even before the Greek Uprising of Goudi in 1909 the Greek government had initiated new negotiations about an international loan. It was extraordinary that the Greek government did not use the National Bank of Greece as broker in this question, but rather the quite young Bank of Athens (founded in 1893). It was Bank of Athens' director Matsas who contacted Banque de l'Union Parisienne on the one hand and Erlanger on the other hand – the Greek government in any case wanted an international syndicate to set limits to French demands for a *tied loan*, bound to Greek orders for the French armaments industry. What were the first reactions like? Erlanger did not react enthusiastically, but referred to the very disadvantageous political situation in the Balkans. However he did not refuse. Instead he insisted that parts of a possible loan should be earmarked not for armaments but for productive spending – Erlanger was thinking primarily of the railway line from Piraeus to Larissa, in which he himself had invested largely and which was in urgent need of fresh capital.<sup>7</sup> But on the other hand Erlanger realized that the French and British governments would only agree if part of the money were to be spent on ordering armaments from France and Great Britain. He saw clearly that he could not count on the IFC to help with guarantees again, but that this new loan must be emitted independently by Greece. On this basis Erlanger was the one who contacted Eric Hambro.<sup>8</sup> Obviously he wanted to split the risk, but also to benefit from Hambro's good reputation in Greek business. However, Hambro's reaction displayed even greater distrust. His argument reveals much about his risk management. Hambro did not want to participate in any loan without the National Bank of Greece, with whom he had conducted business in Greece for decades and who he knew to be a very reliable partner. Even the very high commission to which Erlanger aspired (4.5%) was not able to resolve all of Hambro's doubts. In his opinion the fact that the National Bank was not included was an alarm signal which was not to be ignored.

The letters between Eric Hambro and his father and partner give more insight into the deliberations of the bankers behind the curtain. Everard Hambro insisted upon the participation of the National Bank of Greece in any Greek business. Without its participation or even leadership he considered any loan too risky and dangerous for the good reputation of Hambro. He also discussed the reasons why Erlanger, in contrast, was willing to take part even with-

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<sup>7</sup> Correspondence Erlanger to Matsas in: London Metropolitan Archives, MS 19108.

<sup>8</sup> See their correspondence in: London Metropolitan Archives, MS 19108.

out the National Bank: *I further think it would be wrong for us to use our influence to try and make it [the loan] go, whatever the profit may be. As far as Erlanger is concerned he is simply trying to get commissions. His thoughts are only to make money. We have so far looked at business from another point of view, and that is probably why the two names stand in a different category.*<sup>9</sup> As Monika Pohle-Fraser pointed out in her publications about the risk management of German and French banks, the accusing of a competitor with a higher risk appetite of being an irresponsible speculator was a quite common way to legitimize one's own risk awareness in the 19<sup>th</sup> century.<sup>10</sup> The Hambro's second director Robert Heriot agreed with Everard's point of view. He pointed out that a Greek loan, bound especially to armament orders, would be disastrous for Hambro's reputation if the British press were to pick up the topic. Eric Hambro listened to his advisors and wrote a telegram to the National Bank of Greece: *We have now been told that you did not wish to participate or take the lead, and therefore we also have declined to have anything to do with it.*<sup>11</sup>

But Erlanger continued negotiations in direct contact with Banque de l'Union Parisienne.<sup>12</sup> In spring 1909 he managed to produce a joint offer to the Greek government with only 2.5% commission this time. Armament orders to the British and French industry were planned in proportions related to the extent to which banks of these two nations participated in the syndicate. After the settlement was nearly finished, Erlanger asked Hambro a second time to participate. Did Hambro really not want to take part, not even from the second line? Hambro remained critical: *We think we are better go ahead*, he wrote in a telegram.<sup>13</sup> But he did not send it. In the telegram he did send, he on the contrary agreed to take over £800,000. As the reason for changing his mind he mentioned his wish to provide the Greek government with fresh money for the debt service of former loans. But in a visibly sheepish letter to the Greek National Bank Erich's father Everard mentioned another reason for the decision: *That they [his son and his partner] think that in view of future Greek business not leaving us we had better consent to issue it, and that they have done so. I must confess that I am sorry that the Greek Government have been able to make the contract, and this in the interest of Greece herself, for it seems to me the security they now quote is very nearly the*

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<sup>9</sup> Everard to Eric Hambro, 29.2.1909, in: London Metropolitan Archives, MS 19108.

<sup>10</sup> Pohle, Monika: Risk, information and noise: risk perception and risk management of French and German banks during the nineteenth century, in: *Financial History Review* 2 (1995) 2, 25-39.

<sup>11</sup> Hambro to Streit, 8.3.09, in: London Metropolitan Archives, MS 19108.

<sup>12</sup> *Affaire emprunt grec*, extrait du registre des délibérations du Conseil d'administration, 13.3.1909, in: Société Générale CN254.

<sup>13</sup> Draft of telegram by Eric Hambro, 9.3.09, in: London Metropolitan Archives, MS 19108.

*last that they have to offer, and that the money could have been more profitably used than in the increase of their navy and army, which I suppose is the purpose of the Loan.*<sup>14</sup> The fear of losing market shares to the competition seemed to be the most important reason for the acceptance. The paternalistic attitude towards the Greek government and attempts to prevent it from spending money irresponsibly had to be subordinated to these deliberations.

In any case the project did not succeed this time, because the Greek government refused any tied loan bound to armament orders to the French industry. Erlanger was in high dudgeon and tried to save at least a smaller version of the project, but inner Greek turbulence prevented his plans from even being discussed in the Greek parliament.

In spring 1910, after the coming to power of Elefterios Venizelos as the white hope of international policy, the project was reconsidered. The new syndicate consisted of the Bank of Athens, National Bank, Banque de l'Union Parisienne, Comptoir National d'Escompte, Société Générale, Hambro and Erlanger – Hambro's wishes were broadly catered for with a wide splitting of risk between a couple of well-reputed international banks, including the Greek National Bank. The question of an involvement of the IFC, be it in managing the loan or in giving part of its surplus as guarantee, was discussed in detail this time. The bankers finally decided not to count on the IFC because its decision would take too long due to the contradictory interests of the powers involved. Furthermore, the bankers felt that it was not worth waiting for its decision as even the IFC was not an unquestionable guarantee if Greece should fail again. At least the surplus of the IFC counted to the loan's guarantees.<sup>15</sup> An advance of 40 million drachmas was very successfully issued in November 1910, as was the main loan of 150 million drachmas in June 1911. The profit of the syndicate was calculated at 2.9%, an amount quite common for the customs of the time.<sup>16</sup>

## **Conclusion**

Due to the uncertain political and financial situation of the country the Greek loan of 1910 was a very risky issue for the London bankers involved. The risk premiums offered by Greece were not high enough to explain the investment decisions of the bankers. In this situation only bankers came into question that had very longstanding business relationships with Greece. Due to path dependencies to older investment projects they had a strong self-

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<sup>14</sup> Everard Hambro to Streit, 12.3.09, in: London Metropolitan Archives, MS 19108.

<sup>15</sup> Obligation Générale, in: BNP, 11-DFOM-221-846.

<sup>16</sup> Notice de Emprunt Grec 4% 1910, 23.5.1911, in: Société Generale, CN255.

interest in providing the Greek government with money. On the other hand the cooperation of reliable and well-known partners in Greece and abroad was an important tool for the bankers to split the risk among solid shoulders. But when the going gets tough these considerations could be crowded out by the anxiety of losing market leadership to the competition in a “peripheral” market. In this case, all available instruments were used to avoid being driven out and the risk appetite had to rise.