From Bruges to Amsterdam

The Roots of Stock Exchange Trading in the Low Countries

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Since the onset of the present financial crisis, the financial markets have dominated the news, especially since the focus of the crisis has shifted to the sovereign debt of a number of countries in the euro area. Every statement by European politicians or central bankers brings an immediate response from the news media wondering how 'the financial markets' will react. Did yields on Spanish government bonds fall during a speech by European Central Bank president Mario Draghi? If so, his words evidently conveyed hope. Did the euro weaken following the announcement of figures on consumer confidence in the eurozone? That will be a sure sign that confidence has fallen.

A lazy journalist could get away with simply glancing at the share price ticker for an interpretation of the news. And that interpretation would probably not be too far from the truth, because prices are determined by the innumerable transactions of dealers from all over the world, and the way in which all those dealers interpret the news is priced in to those transactions. The most important prices and exchange rates are updated every second of the day – there is always an exchange open somewhere in the world where dollars are being traded for euros. Yet a certain amount of distrust is called for in using price data. Market dealers famously do not always act rationally, and we also know that many transactions are executed by pre-programmed computers – systems which, however clever they may be, cannot be trusted when it comes to interpreting the news.

Price data were already being used as a means of interpreting the news before the arrival of the Internet, when it was not yet possible for enormous quantities of data to be uploaded onto a computer screen within a fraction of a second. In fact, it was already happening more than three centuries ago. In the summer of 1688, Daniel Petit, the English Consul in the Dutch Republic, regularly reported in his correspondence with London the price at which shares in the Dutch East India Company (VOC) were currently being traded. Petit saw a very large fleet being assembled in the Dutch Republic during that summer, but had no idea what its purpose was. Official reports from the Admiralties in the Dutch Republic asserted that the ships were intended to fight piracy in the Mediterranean region, but Petit doubted the truth of these statements: was the fleet not rather large for a pirate mission? To be on the safe side, he kept a close

Antonius Sanderus, *Flandria illustrata,* Coloniae [Amsterdam], 1641-1644, The Stock Exchange square in Bruges

eye on the price of Dutch East India Company shares. If the fleet really was to be deployed against pirates, the share price would hardly respond; however, if the fleet was being readied for war with England – a not implausible notion, given the three recent Anglo-Dutch wars (1652-1654, 1665-1667 and 1672-1674) – the share price would plummet: war with England represented a huge risk for the East India Company, with its richly laden ships making attractive spoils of war.

When the share price suddenly took an enormous dive at the end of August 1688, Petit immediately drew his conclusions and warned his homeland. It was not the fault of Petit that England was unable to prevent the Dutch Stadholder William III from landing at Brixham in Devon, on England's southwest coast, in early November 1688, from where he made haste to London and ascended the throne on 13 February 1689. What Petit was unable to pick up through diplomatic channels, he learned at the stock exchange.

Petit was fortunate that he was based in Amsterdam. In any other city in the late seventeenth century, he would have had to make more effort to determine the reasons for equipping a battle fleet. The Amsterdam exchange was the only one in this period to resemble a modern stock exchange. Traders from all over Europe carried out innumerable transactions there daily. The large exchange building, designed by Hendrick de Keyser, with its rectangular inner courtyard and roofed gallery, was a centre both for trade in commodities and financial transactions. On every day of the week except Sunday, traders could go to the exchange to obtain the latest exchange rates for foreign currencies, the price of East India Company shares, the level of maritime insurance premiums and the price of all manner of commodities. They could also go to the exchange to perform more complex derivatives transactions. If a dealer wished to be sure of securing a consignment of grain from next year's harvest at a fixed price, for example – no problem. Or if he wished to buy an option as a hedge against a fall in the East India Company share price, that too was easily arranged in Amsterdam.

Bills of exchange in Bruges

Daily trading on the exchange was not an Amsterdam invention. That honour goes to another city in the Low Countries: Bruges. From the middle of the fourteenth century, trading in the city took on characteristics which were akin to modern stock exchanges. In and around the inn owned by the Van der Beurse family, situated in what is today Vlamingstraat, traders of many different nationalities came together to perform transactions. Initially the foreign traders left Bruges in the winter, the low season for mediaeval trade, but it was not long before a group of traders settled permanently in the city.

Trading at the Bruges inn, the name of which still lives on in several languages as the name for the stock exchange (Dutch – *beurs*, German – *Börse*, French – *bourse*), was a marked contrast to the way in which international trade had been organised up to that point. Until the fourteenth century, long-distance trade in Europe took place mainly overland. Merchants from northern and southern Europe came together at annual fairs, the biggest and best known

The Stock Exchange in Antwerp

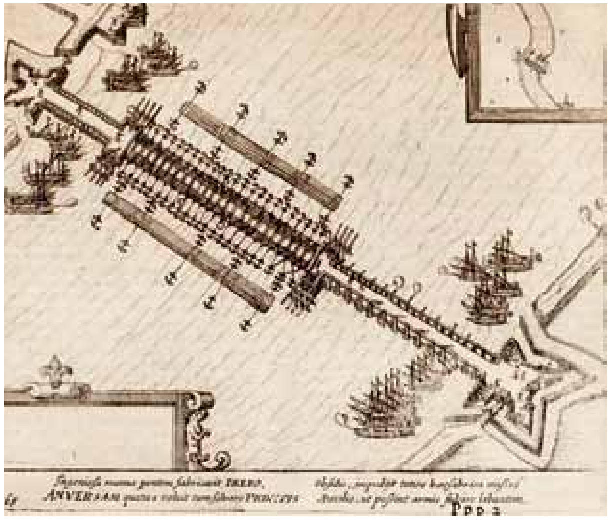
of which were in the Champagne region of northern France. The concentration in one place of merchants from every corner of Europe made these fairs highly suited to international trade. However, during the fourteenth century the political situation in Europe became unstable – among other things, this was the era of the Hundred Years War (1337-1453). Land-based trade became risky and therefore expensive. Merchants increasingly preferred transport by sea.

In this situation, Bruges was in the ideal position to grow into Europe's principal trading centre: it was close to the sea, had long played a pivotal role in the northern European Hanseatic trading network and had a hinterland in Flanders and Brabant where cloth was produced for export, making it an attractive place for Castilian wool traders to set up business. It was not long before Italian merchants also began to see that Bruges was the ideal city from which to export luxury goods from southern Europe and to import cloth from northern Europe. The level of commercial activity in Bruges grew at lightning pace, and was of course not limited to the trade in goods. Italian bankers followed in the wake of the merchants and introduced their financial techniques to the north. Bruges grew into a centre of the trade in bills of exchange, the primary means of payment for international transactions. And in contrast to the annual fairs, trade in Bruges took place every day, summer and winter.

Antwerp as a world city

Bruges remained the principal trading centre in Europe for around 150 years, but in the sixteenth century lost its primacy to Antwerp. Bruges had lost its appeal, partly because of the silting up of the harbour and the waning importance of the Hanseatic League. At the same time, Antwerp succeeded in attracting merchants by imposing less stringent regulations. Antwerp grew into an even bigger trading centre than Bruges had been – so big, in fact, that the city administration decided to build an exchange, just behind one of the most important streets in the city, the Meir. Where merchants in Bruges had been forced to do their deals in a family inn and in the square that fronted it, and in Antwerp had initially traded in a row of adjacent houses, for the first time they now had their own building, specially designed for commercial trade.

Midway through the sixteenth century, Antwerp was a world city by early modern standards, but later things went decidedly downhill, and to make matters worse the city became a political football of the opposing sides in the Dutch Revolt. In the 1570s, Antwerp had taken the side of the rebels, who were demanding that the Spanish King Philip II allow them a degree of freedom of conscience and some influence over the administration of the Low Countries. However, the King was naturally not about to allow Antwerp, the largest city in the Low Countries, to slip through his fingers without a murmur, and in 1584 he laid siege to the city. The siege lasted almost fourteen months before, on 17 August 1585, the city surrendered to Alexander Farnese, later Duke of Parma. The long siege was disastrous for Antwerp trade, but it was the rebels who really sounded the death knell. They controlled the area around the mouth of the Scheldt, the river linking Antwerp to the sea, and closed it off to all shipping to Antwerp. It would be well into the nineteenth century before the Scheldt opened again, but by then, of course, international trade had long since moved on to a new location.



Parma's bridge over the Scheldt in 1584, built of ships. The bridge closed the access to Antwerp and was the beginning of the end for the city

Share dealing in Amsterdam

That location was Amsterdam, a city which in the sixteenth century derived its success principally from trade with the Baltic region, and which during the Dutch Revolt had responded best to shifts in the trade flows in northwestern Europe. Within a short space of time, Amsterdam grew into a hub of trade routes, just as Bruges and Antwerp had done before it, and found it had struck gold. Henceforth, ships no longer sailed to the Baltic laden with worthless ballast in order to return with their holds full of grain and timber, but instead carrying luxury goods imported from southern Europe on the outward voyage. International merchants flocked to the city and the city walls reverberated from the number of commercial transactions. The city administration, though, apparently needed a little time to realise fully what was going on in its city. It was not until 1607 that the city fathers gave instructions for the building of an exchange, at a time when London and Rotterdam – cities which, not entirely without justification, saw an important role in international trade for themselves – had long had such a building. The design of all these exchange buildings was greatly inspired by their Antwerp predecessor: with their open inner courtyards and roofed galleries, they all resembled a walled market square.

Until 1611, when Hendrick de Keyser's *beurs* was taken into use, trade in Amsterdam was an open-air affair. Initially it took place in Warmoesstraat, the most important street linking the port and the Dam, Amsterdam's central square. On busy days, this narrow street was sometimes so full of traders that it was impossible to walk through it. For this reason, in 1561 the city administration designated the Nieuwe Brug – the most northerly bridge over Damrak, situated right on the IJ, the sea inlet which formed Amsterdam's natural harbour – as the new location for trade. In good weather this was an excellent spot, but when the weather was bad, with a raw wind blowing across the IJ making it feel bone-chillingly cold, the merchants were completely unprotected. On such days, they returned to the Warmoesstraat, where they found shelter under the awnings of the shops. So, when it was raining or cold they still blocked all commercial activity in this little street. To resolve this problem, in 1586 the merchant community was given permission to use Sint Olofskapel (St. Olof's Chapel), a stone's throw from the Nieuwe Brug. The Chapel had stood empty since 1578, the year in which Amsterdam sided with the rebels and embraced Protestantism, and was owned by the city. Now it became Amsterdam's first exchange building.

Today the average tourist in Amsterdam walks past the Nieuwe Brug and Sint Olofskapel without a second glance. That is a pity, because history was written here. These are the places where for the first time in world history, trading in an exchange was extended to include the trade in shares. These were the same shares which in 1688 warned Daniel Petit of the preparations for war with England: shares in the Dutch East India Company (VOC). Like Amsterdam's success in international trade, the VOC was a child of the Dutch Revolt. As a result of the war with Spain, the rebellious regions, later united to form the

Jacob van der Ulft, The Dam, Amsterdam, 1659. Gouache on paper. Musée Condé, Chantilly

Dutch Republic, dared to break the Treaty of Tordesillas. Under this Treaty, signed in 1494 and sealed by Pope Alexander VI, Spain and Portugal divided the known world between themselves. Spain received America, apart from part of present-day Brazil, while Asia and Africa were for Portugal. Other countries had not signed this Treaty, but the papal seal of approval meant that it could

Claes Jansz. Visscher, 1612, *Stock Exchange Amsterdam.* City Archives, Amsterdam

not simply be ignored without compunction. And since Spain and Portugal were the two most powerful nations on earth at that time, no one considered infringing the Treaty and risking war as a result. But once the rebellious regions of the Low Countries had become embroiled in war with Spain for other reasons in the sixteenth century, they had nothing more to lose. They scented their opportunity for a share in the lucrative long-distance trade.

As luck would have it, from 1580 Portugal fell under the power of the Spanish crown. As a result, the rebelling regions of the Low Countries, and later the Dutch Republic, were effectively catapulted into war against Portugal. This offered opportunities to send expeditions to the crown jewel of the Iberian colonies, the East Indies, and specifically the Moluccas, where under the Treaty of Tordesillas only Portugal was permitted to trade.

The VOC and the birth of share dealing

The first Dutch ships set sail for the East Indies in 1595. The vessels were owned by the Compagnie van Verre (lit.: long-distance company), a privately owned company which had raised the capital needed to build the fleet by recruiting investors. This expedition was not especially successful, but it did demonstrate that it was possible to trade with the Indies without being overcome by the Portuguese. The initiative accordingly mushroomed and in the years that followed dozens of ships, owned by a variety of companies, set sail from the Dutch Republic to the East Indies.

All these companies were in fierce competition with each other. The States-General, the supreme authority of the Dutch Republic, was not happy with this situation, feeling it would be better for the country's economy if they were to compete with Portugal instead of with each other. Moreover, a strong, united company could also come in very useful in the war.

That united company, the VOC, was formed in 1602. It acquired a monopoly on trade from the Dutch Republic with the East Indies. In exchange, the VOC was

Philipp von Zesen, Picture of the city of Amsterdam. New bridge

expected to represent the interests of the Republic in the East Indies. In practice, this meant that the VOC had to take on the war against the Portuguese in Asia.

The VOC also raised its initial capital from private investors. Unlike its predecessors, however, the East India Company organised a public subscription. 'All residents of these Countries', declares the 10th article of the deed of incorporation, 'may participate in this Company.'

The offering was a great success. In Amsterdam 1,143 persons subscribed for more than 3.5 million Dutch guilders. Naturally, they hoped that they would earn a return on their investment, but for many this was not the only reason for subscribing to the Company's initial capital. The VOC was not simply a company which would send ships to the East Indies to bring back spices. The VOC was more than that: it was a prestige project for the Republic. The idea that the young Republic could be supported by investing in the VOC also played a role - it was still only 21 years since the States-General had renounced Philip II as their King, and in 1602 the Republic was not even recognised internationally as a sovereign state.

In addition to the public subscription, there was another way in which the VOC set itself apart from its predecessors. The Company not only had to steal away as many spices as possible from under the noses of the Portuguese, but also had to ensure that the Dutch presence in the Indies would be a lasting one. The VOC built forts at strategic locations and actively engaged in the battle with the Portuguese. In view of this, the VOC was incorporated for a period of 21 years – a very long time compared with the average of three to four years for which its forerunners had been in business. The authorities realised that investors might hesitate to tie up their money for so long, and the first page of the subscription register accordingly included an additional provision: 'Reassignments or transfers [of shares] may be effected by the bookkeeper of this Chamber.' In other words, subscribed capital could be transferred to someone else! For investors, this provision meant that they did not need to wait until the VOC was wound up before being able to recover the capital they had contributed. They could simply sell on their share before that time. This would go down in the annals of world history as the start of share dealing.

Emanuel de Witte, *Interior of the Stock Exchange in Amsterdam,* 1653. Oil on panel, 49 cm x 47,5 cm. Museum Boijmans van Beuningen, Rotterdam

The first transactions date from the moment when, a few months after the subscription register had been closed, the VOC asked its investors to pay the first instalment of the capital to which they had subscribed. One investor, Jan Allertsz., realised that he did not have enough money to pay this first instalment. He sold his share and so became the person who performed the first ever share transaction. After Allertsz. came more – many more – transactions. And because most of the shareholders were merchants, the share dealing took place in the same locations where the merchants had become accustomed to performing their goods transactions and settling their bills of exchange: Nieuwe Brug (New bridge) and Sint Olofskapel.

Naked short sellers and repos

The red tape that accompanied share transactions – shares had to be officially transferred from the seller's account to the buyer's account in the VOC books, something for which transaction fees also had to be paid – quickly took traders in search of simpler ways of dealing in shares. In 1607, just five years after the founding of the Company, forward contracts ('futures') for the delivery of shares were already being concluded. This was the beginning of derivatives trading – trading in contracts which were associated with shares and the stock market, but in which no shares were traded directly. This trade took off rapidly. As early as 1608, a group of merchants sold large numbers of forward contracts for the delivery of VOC shares which they did not even possess. Their intention was to engineer a fall in the share price and to generate profit from this. Today, they would be called naked short sellers. A few years later, share dealers began trading 'repos': they pledged shares to lenders as collateral for loans which were used to buy those same shares. Investing in this way – using borrowed money – meant that even people with little capital could acquire large positions in VOC shares. Finally, from the middle of the seventeenth century onwards, a lively trade in options got under way. Around this time, the community of share dealers had become quite large and diverse, with speculators on the one hand and on the other investors hoping for a positive return in the longer term. This meant that there was a ready market for the transfer of risks, something for which the option is a very suitable instrument. Long-term investors were only too keen to transfer their risks in respect of short-term price fluctuations to speculators, who conversely were willing to take on those risks.

Three centuries after the start of daily exchange trading in Bruges, the Amsterdam exchange had taken on much of the élan of Wall Street today. The trade in futures, options and repos was the bread and butter of Amsterdam traders. One only had to step inside the exchange, or to accost a broker, to learn the latest exchange rate in any number of foreign cities. And there was another similarity with today's world, in that the exchange regularly played host to a crisis. Where wars were the agents of those crises in the seventeenth century, in the eighteenth century the crises were taking place in the exchange itself. So the Low Countries were present at the birth of all facets of modern stock market trading. ■

Translated by Julian Ross