CHAPTER IV

Evolution of Money, Barter System & Ancient Banking

Generally people confound the issue by mistaking money for coinage. The coinage system is a comparatively contemporary form of money that was probably pioneered by the Lydians (Turkey) in Asia Minor around the 7th Century B.C. Moreover, it is still uncertain whether the early coins were actually used as money as in the modern times. The history of money may be broadly divided into nine phases; Egypt, Mesopotamia and Greece, the Far East and China, South East Asia and India, the Islamic Lands, the Roman World, Africa and Oceania, Mediaeval Europe, the Early Modern Period and the Modern Period. In fact the Industrial Revolution had made money an omnipresent part of the society (condemned by Marx and Engels).

Barter System : The Barter System is known to be the most primitive mode of transactions as the early people did not possess any form of money to purchase commodities or services. This system was in vogue in our country even during the Rig Vedic period. In olden days when society was in the making man tended to become more social and felt the urge of living together in peace and harmony to make life more livable. But how to procure bare necessaries of daily life like grains, clothes, utensils etc? Necessity always acts as the mother of invention. So a system of exchange of household necessaries i.e. goods, better known as 'barter system' came up. People were engaged in different jobs of production. In a small geographical habitat i.e. village or in a cluster of villages tilling and growing of crops, weaving, making of pots and utensils, chisels and ploughs etc; - all such activities ran within respective clans or groups through generations and thus giving

them opportunities for acquiring expertise in the jobs concerned. But this barter system suffered primarily from two shortcomings e.g. (i) its localized character and (ii) man's variable preference. In absence of fixed measurement or quantum between exchangeable goods the same yardstick could not be made applicable to a greater area and larger sections of people. Quantum of exchanges varied from place to place. Suppose a basketful of rice could fetch one a piece of cloth in a particular place, but the same standard might be unacceptable in another locality. Secondly necessity also varied from man to man at a particular point of time. Suppose a weaver urgently needed a bucket in exchange of a piece of napkin which was the standard practice in the place. But the blacksmith needed no napkin at that time; so he could refuse or alternately bargain for two/three napkins in exchange and thereby became gainer banking on the immediacy of the weaver.

Cow as a Unit of Value : In those days cow was taken as a unit of value. Possessing large number of cows was an indication of wealth and power. That is why the word 'Godhan' ('Go' meaning cows & 'Dhan' – property, both Sanskrit words) finds repetitive references in our literature. Even in the Mahabharata we read of Duryyodhana stealing thousands of cows of King Virata, who claimed to have in possession 500 thousand of cows in his cow sheds, which bore the stamp of his enormous wealth. Livestock was the most common unit of exchange from 9000 B.C. to 6000 B.C. and later agricultural produce too came in its purview. With the increase of demand and production cow posed hurdles in many ways for exchange of value and gold pieces were introduced as replacement. The barter system, which still exists among some communities around the world, denotes the exchange of personal possessions for the value of the desired commodities or services. However, from 1200 B.C. people in China and regions of South East Asia, including India used **Cowry** (a special kind of sea shells)

as a medium of exchange. According to some numismatics Cowry was first introduced almost 4000 years ago. Apart from literature Cowry finds mentions in the writings by historians and tourists like Fa-Hien in the 4th, Hiu-en-Sang in the 7th, Iban Batuta in the 12th, Minhazuddin in the 13th centuries and others. Use of the Cowry became widespread in Africa and prevailed in many parts of the world till the middle of the 20th Century.

Money in Various Forms : The first form of metal money made its appearance in China sometime around the end of the Stone Age in 1000 B.C. The Chinese coins were made from base metals and were normally punctured in the middle so that they could be threaded into a chain.

The silver coins made their first appearance sometime around 500 B.C. in the form of silver. It is believed that the silver coins made their maiden appearance in Lydia or Turkey and their techniques were used repeatedly until they were bettered by the Persian, Greek, Macedonian and Roman Empires. These coins were made from precious and semi-precious metals such as gold, silver and bronze and carried substantial inherent value. In India, during the rule of **Mauryy Dynasty,** i.e. well before the birth of Christ **gold, silver and copper coins** were in use. Gold coin 'Nishka' replaced gold bars. A fixed weight of Nishka came in use, - each weighing 320 Rathis or grains. 'Kahapanas' were copper coins, each weighing 140 grains. During the rule of Satvahanas coins of copper, silver and gold came to be known as 'Kahapanas', 'Karshapanas' and 'Suvarnas' respectively. One Karshapana was equivalent to 80 Rathis ... and so on.

Greek influence spread in our country soon after conquest of a sizable portion by Alexander. **Bi-lingual coins** inscribed in Greek and Brahmi, the language that was much popular in our country at the time, were circulated during the period. The

coins were introduced particularly in the Aryabartya (Northern half of the country). In the Dakshinatya (Southern half) Greek influence was of little existence. Coins that were in vogue during the period in this part of the country were minted by the Pallava rulers.

It is also interesting to note that **earliest record of use of money** was from Mesopotamia (Iraq) some 4500 years ago i.e. 2500 B.C.

The Chinese were first to introduce **leather currency** in 118 B.C.

According to records, the paper money was used in China between the 9th and 15th Century A.D.

Trade and Commerce :

Trade is as old as humanity itself. Long distance commerce is according to some sources at least 1,50,000 years old. It is ten times older than farming. Most types of food and perishables could be only traded locally, preferred were durable goods with large value for a small weight. Since the 17th Century the most common forms have been metal coins, paper notes and book keeping entries. The wide use of cattle as money in primitive times survives in the words like 'pecuniary' (derived from Latin 'pecus', meaning cattle) and 'fee' (derived from Old English 'feoh' and German 'vieh'- both meaning cattle owned).

Discoveries by Archaeological Society of India in the '20's of the 20th century in Harappa of Montgomery district of the Punjab and Mohenjo-daro in Larkana district of Sind show beyond doubt that a highly developed urban economy and discipline was in existence in the 3rd millennium BC. From the finds at the sites it may be inferred that there "must have been frequent communication with places like Rajasthan for copper, steatite and lead; Afghanistan and Baluchistan for copper; Karadagh in North Iran for lead; southern India for gold; Afghanistan for gold and possibly silver also; Hormuz and other islands in the Persian Gulf for hematite and red ochre; Gujarat and Kashmir for amazonite; Tanjore, Kathiwad and Mianwali districts for crystal; Khorasan for turquoise; Badakshan for lapis; Pamirs for jadeite etc. It may thus be assumed that there must have been frequent communication with all these places as well as with the contemporary centres of culture in India and Baluchistan by sea, river and overland. The means used for such communication and trade were boats and country craft, chariots and bullock carts and pack animals such as oxen, buffaloes and goats." ('Indus Valley Civilisation' - Madho Sarup Vats in Cultural Heritage of India - Vol. I). "The means of communication for commercial and cultural contacts between different countries were entirely by land at the beginning...the references in the Rg Veda to 'the treasures of ocean', 'gains of trade', 'ship with a hundred oars', 'shipwreck' etc. clearly show that Vedic Aryans in ancient India knew the ocean and sailed in ships to distant lands ...". ('Cultural Interrelation between India and the Outside World before Asoka' by A D Pusalker. Ibid).

One of the most important **land routes** for the traders was Khyber Pass which was used for commercial intercourse with the west, north and east opening up contacts with Persia, Iraq, Egypt, Greece, Rome, Central Asia, China, Tibet, Burma etc. Indian merchants traded with their counterparts of the south-east and south coast of Arabia, and the Arabian merchants took the Indian goods to Syria and Egypt. It was thus that King Solomon in the 10th century BC got Indian sandal wood, precious stones, ivory, apes and peacocks.

Both rivers and seas played very important roles for intra country and inter countries trade. As a result **sea ports and river ports** in the country developed. Simultaneously **some sort of foreign exchange banks** by moneyed mahajans started

their business in the coastal areas. These money lenders also formed guilds and gave loans as per demands of the traders and borrowers. They knew the borrowers intimately and their worth and money lent also got full recovery. Even they started accepting deposits from public, assured safe-keeping of their deposits and gave interest also, as high as 12% per annum at times. These offices remained open for day and night and people in need could knock at their doors at any point of time. So virtually they introduced **24-hour banking.**

Man's search for security and possession of wealth gave him a new taste and meaning of life. Gradually he realized the meaning of money, which he could not eat, or live in it but still he needed it to feed, clothe and house himself. Its omnipotent feature appeared. People out of necessity wanted to add features which would be easy to carry, acceptable universally and convenient as a standard unit of value for purchase of anything.

Banking : The history of banking is closely related to the history of money. But banking transaction probably predates the invention of money. Deposits initially consisted of grain and later other goods including cattle, agricultural implements and eventually precious metals such as gold, in the form of easy-to-carry compressed plates. Temples and palaces were the safest places as depositories as they were constantly attended, guarded and well built. Temples also carried an extra deterrent to thieves and miscreants as sacred places.

The first precursors of banks can be traced as far back as ancient Mesopotamia. Around the year 3300 B.C. the temple of Uruk owned the land it exploited, received offerings and deposits and granted loans to farmers and merchants of livestock and grain.

Banks existed in China in 600 B.C., also in Rome thereafter. In order to facilitate transaction of business **Hundi system** existed in India as far back as in 12th century. In mediaeval Europe banking declined because of unfavourable dictat from the Church. Church disapproved of money-lending for making profits. However, Italy was the centre of Renaissance in mediaeval Europe and hence some important banks also sprang their heads there in 15th and 16th centuries, and they started rendering financial services all over the Mediterranean.

1670 AD saw two mesmerizing wings of modern banking in England; two main instruments for creating wealth - **cheques and Bank-notes** - came into being. **Bank of England** came up in 1694. Walter Bagehot (1826-1877), a noted English writer, efficient banker, expert in shipping business and editor of the 'Economist' gave an interesting account of the birth of the Bank of England, ".... in its origin it was not only a finance company, but a Whig finance company, ... it was founded by a Whig government because it was in a desperate want of money....... In 1694 the credit of William Ill's government was so low in London that it was impossible for it to borrow any large sum; and the evil was the greater, because in consequence of the French war the financial straits of the government were extreme. At last a scheme was hit upon which would relieve their necessities. The plan,' says Macaulay 'was that twelve hundred thousand pounds should be borrowed by the government, on what was then considered as the moderate interest rate of 8 per cent. In order to induce capitalists to advance the money promptly on terms so favourable to the public, the subscribers were to be incorporated by the name of 'The governor and Company of the Bank of England'; they were so incorporated, and the 1200,000 pound was obtained."

".....the government created by the revolution of 1688 could hardly expect to be more trusted with money than its predecessor". Yet the foundation of the Bank became the focal point of London liberalism and rendered inestimable services to the country. However, earliest existence of Bank-notes may

be traced back to China in the 11th century, six centuries earlier than in Europe.

Kolkata may boast of having seen the **first bank in our country** - Hindusthan Bank in 1770. A ground was prepared for subjugation of the country only 13 years prior to the chapter - the Battle of Plassey saw the setting of our independence through defeat of Siraj-Ud-Doullah, – Nawab of Bengal.

Merchant Banking : The first banks were the merchants of the ancient world that made loans to farmers and traders that carried goods between cities. The first record of such activities dates back to around 2000 B.C. in Assyria and Babylonia. Later, in ancient Greece and during the Roman Empire, lenders who were based in temples made loans but also added to important innovations: accepting deposits and changing money. During this period there is similar evidence of the independent development of lending of money in ancient China and separately in ancient India.

The main innovation of **Egyptian Banking** was centralization; the government bank in Alexandria had branches in the most important towns and cities.

So the concept of modern banking also had to pass through different stages of innovation, renovation and improvisation to suit the need of growing demand and pressure of time.

Interest on Capital : Charging of interest on money and services were strictly forbidden or restricted by many of the early religions –

Judaism : – though it criticizes interest earning its interpretations vary. Jews were forbidden to charge interest on loans made to other Jews, but were obliged to charge and accept the same on transactions from non-Jews and others. Exactly the same formulae were applicable in relation to Israelites and non-Israelites too.

Christianity : – describes charging of interest as 'usury' and that is why the same was banned by Christian Churches. Gradually interpretations changed and it was revealed that charging at any rate was banned but imposition of fees for the use of money was very much allowed. Finally with changing times it became allowed by law and universally acceptable.

Islam : – strictly prohibits taking of interest and the Quran is against lending money on interest.

However, **Bank Failures** were also not unknown those days and banks in many countries had to be closed down during the economic crises of the 3rd and 4th centuries A.D.

Gradually over the years modern banking as we know these days came to develop through the journey of the Mediaeval period.

India : In ancient India during the Mauryya Dynasty (321 to 185 B.C.), an instrument called 'Adesha' was in use, which was an order on a banker desiring him to pay the money of the note to a third person, which corresponds to the definition of a Bill of Exchange as we understand it today. During the Buddhist period, there was considerable use of these instruments. Merchants in large towns gave orders to one another akin to present day Letter of Credits.

Banking in the modern sense of the word can be traced to Mediaeval and early Renaissance Italy, to the rich cities in the north such as Florence, Venice and Genoa. The Bardi and Peruzzi families dominated banking in 14th Century Florence, establishing branches in many other parts of Europe. Perhaps the most famous Italian bank was **Medici Bank,** established by Giovanni Medici in 1397.

The development of banking spread through Europe and a number of innovations took place in Amsterdam during the Dutch Republic in the 16th Century and in London in the 17th

Century. By the end of the 16th Century and during the 17th, the trading banking functions of accepting deposits, money lending, money changing and transferring funds were combined with the issuance of bank debt that served as a substitute for gold and silver coins.

New banking practices promoted commercial and industrial growth by providing a safe and convenient means of payment and a money supply more responsive to commercial needs, as well as by discounting business debts. By the end of the 17th century, banking was also becoming important for the funding requirements of the relatively new and combative European States. This would lead on to government regulations and establishment of the first central bank.

Bank of Amsterdam was founded in 1609.

Goldsmiths of London : The main developers of banking in London were the goldsmiths. By promoting acceptance of the receipts as a means of payment, the goldsmiths discovered that they could lend more than the gold and silver they had in hand, a practice that became known as **'Fractional-reserve Banking'.**

Europe : Rothschild family banking business pioneered international high finance during the industrialization of Europe and was instrumental in supporting railways systems across the world and in complex government financing for projects such as the Suez Canal.

Globalization : In the late 18th Century there was a massive growth in the banking industry. Banks played a key role in moving from gold and silver based coinage to paper money, redeemable against the bank's holding. Within the new system of ownership and investment, the State's role as an economic factor grew substantially.

20th Century : During the 20th Century, developments in telecommunications and computing resulting in major changes to the way banks operated and allowed them to dramatically increase in size and geographic spread. The first decade of the 20th Century saw the panic of 1907 in the U.S., which led to numerous runs of banks and the incident became known as the **'bankers' panic'.** During the Crash of 1929 preceding the Great Depression and during first 10 months of 1930, 744 U.S. banks failed. By April 1933, around $7 billion in deposits had been frozen in failed banks or those left unlicensed after the March Bank Holiday.

Gold Standard : In the classical gold standard was a Central Bank of each country expected to hold enough gold in its reserves, while the commercial banks would rely mainly on its bank notes. The American Fed and the Bank of England would be the Central Banks for the whole world (exceptions being France and a few other countries). This system lasted only from 1925 to 1931; the Great Depression of 1929 caused a rise of protectionist policies and foreign exchange controls that chocked the international currency trade. Currencies started fluctuating freely until the end of World War-ll. Actual gold standard was abandoned.

Bretton Woods System : A new system was designed in 1944 in Bretton Woods (New Hampshire, U.S.) to make the production of bank notes even more flexible. The gold reserves of the whole world should be concentrated in a single pool; the Fed would redeem its notes while all others would keep the U.S. dollar as reserve. In order to reduce dependency on the Fed and to make it politically acceptable, **two arms of the USA were extended** – The International Monetary Fund (IMF) and the World Bank, both two influenced the introduction of new bank notes. They would supply short term (IMF) and long term (WB) credit to member states in trouble, primarily the Board Members. They survived the collapse of Bretton Woods. The growth of inflation, the main purpose of the

Bretton Woods was so successful, that the Fed eventually ran out of gold and had to suspend its payments in 1971. That was the end of the so called gold standard and its variants.

The Paper Standard : After the lust to gold was broken, a large number of paper currencies was created. Every country could set its monetary policies as it desired and their exchange rates fluctuated widely. Many states floated bonds in other currencies than their own, like in the Europe or in US Dollar. This way came 'Dollarization'. And the international paper currency - the Yen, Dollar and newly the Euro are dominating the international scene.

1980's Deregulation & Globalization : Global banking and capital market services proliferated during the 1980s after deregulation of financial markets in a number of countries. In 1986 'Big Bang' in London allowing banks to access capital markets in new ways, which led to significant changes to the way bank operated and accessed capital. It also introduced a trend where retail banks started to acquire investment banks and stock brokers creating universal bank that offered a wide range of banking services.

21st Century : The consolidation was accomplished through acquisitions which grew in size over this period and there were many of them. The first decade of the century also saw substantial extension of the technical innovation in banking over the previous thirty years and witnessed a major shift away from traditional banking to internet banking.

Major Events in Banking History :

- 1602 – First joint-stock company, the Dutch East India Company founded.
- 1602 – The Amsterdam Stock Exchange was established by the Dutch East India Company for dealings in its printed stocks and bonds.

- 1609 – The Amsterdamsche Wisselbank (Amsterdam Exchange Bank) was founded.
- 1694 – The Bank of England was set up to supply money to the King.
- 1695 – The Parliament of Scotland formed the Bank of Scotland.
- 1717 – Master of the Royal Mint Sir Isaac Newton established a new mint ratio between silver and gold that had the effect of driving silver out of circulation (bimetalism)and putting Britain on a gold standard.
- 1781 – The Bank of North America was founded by the Continental Congress.
- 1791 – The First Bank of the United States was a bank chartered by the United States Congress. The charter was for 20 years.
- 1800 – Rothschild family founds Euro wide banking.
- 1913 – The Federal Reserve Act created the Federal Reserve System, the central banking system of the United States of America, and granted it the legal authority to issue legal tender.
- 1930-33 – In the wake of the Wall Street Crash of 1929. 9,000 banks closed, wiping out a third of the money supply in the United States.
- 1933 – Executive Order 6102 signed by U.S. President Franklin D. Roosevelt forbade ownership of Gold Coin, Gold Bullion, and Gold Certificates by U.S. citizens beyond a certain amount, effectively ending the convertibility of US dollars into gold.
- 1971 – The Nixon Shock was a series of economic measures taken by U.S. President Richard Nixon which cancelled the direct convertibility of the United States dollar to gold by foreign nations. This essentially ended the existing Bretton Woods system of international financial exchange.

- 1986 – The “Big Bang” (deregulation of London financial markets) served as a catalyst to reaffirm London’s position as a global centre of world banking.
- 2007 – Start of the Late-2000s financial crisis that saw a credit crunch that led to the failure and bail-out of a large number of’the world’s biggest banks.
- 2008 – Washington Mutual collapses. It was the largest bank failure in history.