

Toward the Age of Jackson

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The postwar

Financial constraints

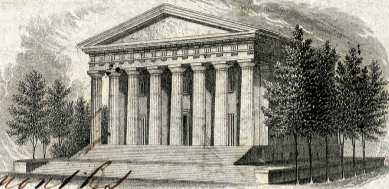
- With no Bank of the United States, government cannot transfer funds across the country and Federalist investors refuse to lend to the government.
- Government is essentially bankrupt. Debt has risen to \$127m in 1815.
- Proliferating state banks suspended specie payment on large amount of notes issued since the demise of the Bank of the United States.
- \$115 million in notes between 1811-15.
- Invest in war bonds.
- When Government begins to default on treasury notes, there are bank runs and notes trading at 70-85% of par.
- Treasury has to rely on depreciated notes to make payments.

No 8895

No 8895

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Seventeen months after date

The Bank of the United States

Promises to pay to *J. W. Fairman*
One Thousand Dollars

in *New York Philadelphia Dec 15th 1840*

at a rate of Cash
Prindley Pres.



THE BANK OF THE UNITED STATES
PROMISES TO PAY TO
ORDER OF
NEW YORK PHILADELPHIA

Printer, Lippitt, Longacre & Co. Phila & New York

A new national bank

- State banks cannot be relied on to help fund the debt.
- Already in 1813, New York and Pennsylvania petition Congress to re-establish a national bank.
- Calhoun proposes to create a national bank in Washington to avoid constitutional issues (Congress has extensive powers regarding the governing of DC).
- Also, Calhoun helps defeat Alexander Dallas' more modest proposal.



RECONSTRUCTING
THE
NATIONAL
BANK
CONTROVERSY

POLITICS & LAW
IN THE
EARLY AMERICAN
REPUBLIC

ERIC LOMAZOFF



Madison changes course

- Madison is now in favor of re-establishing the Bank of the United States. One of few times Madison and Jefferson are at odds.

James Madison, Seventh Annual Message, December 05, 1815

“It is, however, essential to every modification of the finances that the benefits of an uniform national currency should be restored to the community. The absence of the precious metals will, it is believed, be a temporary evil, but until they can again be rendered the general medium of exchange it devolves on the wisdom of Congress to provide a substitute which shall equally engage the confidence and accommodate the wants of the citizens throughout the Union. If the operation of the State banks can not produce this result, the probable operation of a national bank will merit consideration; and if neither of these expedients be deemed effectual it may become necessary to ascertain the terms upon which the notes of the Government (no longer required as an instrument of credit) shall be issued upon motives of general policy as a common medium of circulation..”

- As well, Madison believes the constitutional question had been settled by the precedent of the First Bank.

The Second Bank of the United States

- Initially, Madison cannot get a bill through Congress.
- John Randolph leads the opposition.
- But the Federal Government's financial condition deteriorates and with state banks in trouble the economy deteriorates.
- Need for a more uniform currency and the Second Bank is signed into law in April 10, 1816 and opens its doors January 7, 1817 capitalized at \$35m.
- Depository of federal funds and it can branch in any state.
- The chartering of the Bank represents a large departure in Republican thinking, especially for Madison. But it is the pragmatic solution to the government's fiscal problems.



Manufactures

- The trade disruptions between 1807-1814 gave rise the production of many domestic goods.
- Promotion of infant industries was not the primary goal of the trade policies of Jefferson and Madison.
- Nevertheless they stimulated domestic manufacturing.
- Jefferson assumed the embargo would provide “indirect encouragement” to small domestic manufacturers making the country more economically independent.
- Madison feels the same.
- But he wants to avoid the commercial troubles that plagued the nation and led to war in 1812.
- Become more self-sufficient with less reliance on Great Britain.

A new winning coalition

- A large shift in Democratic-Republican attitudes from those held in the 1790s, when they opposed Hamilton's efforts to support manufacturing.
- Trade policies do more than Hamilton's direct support ever could have done. A bit ironic.
- Manufacturers shift allegiance to the Democratic-Republican party.
- The two political factions pit commercial interests against manufacturing interests.

An old dream gone forever

- Recall the early “republican” vision of a predominantly agricultural community: hard-working, diligent, and economically relatively equal.
- In particular, the U.S. would be a society without the permanent classes of privilege and classes of dependent poor (this vision “forgets” about slavery).
- Vision based on the vast amounts of land yet to be put into productive farming that allows escaping the Malthusian dilemma for at least a century.
- But due to the war and what Madison believes will be insufficient European demand for rapidly growing U.S. agricultural output, he foresees a scenario where prices plummet and the lack of profitability of many farms.
 1. That will lead to idleness and poverty and destroy the republican dream.
 2. An alternative must be found.

The Panic of 1819

- First “modern” financial crisis in the U.S.
- Land and cotton boom of 1818.
- Deep recession that lasts until 1821.
- Role of the Second Bank of the United States?



ANDREW H. BROWNING

**THE PANIC
OF 1819**

THE FIRST GREAT DEPRESSION

A new protectionism

Madison's view of a new economy

- Madison aims to balance the sensitive relationship between demographics, foreign markets, and the U.S. social character.
- He comes to believe that, with good policies (those *not* based on mercantilism), the poverty in European societies can be avoided.
- Madison's new way is to support industry, adopting much of Hamilton's viewpoint.
- Large-scale manufacturing would provide a domestic sector that would demand agricultural products.
- The U.S. economy would now have three legs: agriculture, commerce, and manufacturing.

A move away from free trade

- The earlier Jeffersonian model required free trade, and the years during and before the War of 1812 indicated that was not something to rely on.
- After 1814, the focus is on building a more balanced economy that will provide greater insulation from Europe.
- The lure of cheap land would place a floor on the wages that manufacturers could offer (reservation wage or outside option), avoiding the worst excesses of the British Industrial Revolution.
- Madison remains optimistic that institutional arrangements can be created to let the U.S. avoid the corruption and poverty of Europe.

A new Report on Manufactures

- In Secretary of the Treasury Gallatin's April 10, 1815, *Report on Manufactures*, he argued that bounties were the best vehicle for supporting exporters as high tariffs would tax the consumer and divert capital from its most profitable uses.
- This echoes Hamilton, who argued that tariffs were inefficient because they raised prices but importantly benefitted both efficient and inefficient producers.
- Gallatin recommends that Government create a stock of investment money for loans to new manufacturers in the range of \$5-\$20 million.
- Idea goes nowhere in Congress.

Madison's proposal

- Contrary to Gallatin's advice, Madison proposes high tariffs in his December 1815 address to Congress.
- Applauds the growth in manufacturing due to disruption of trade with Great Britain.
- A change that Madison believes is justified given the policies of European belligerents. "How far it may be expedient to guard the infancy of this improvement in the distribution of labor by regulations of the commercial tariff is a subject which cannot fail to suggest itself to your patriotic reflections."
- But there are tradeoffs. Industries involved in exporting, such as shipbuilding, suffered, while import-competing industries benefitted.
- Further, the gain to import-competing industries was largely reversed after the war.

Jefferson's change of heart

- The change in Democratic-Republican philosophy is summarized by Jefferson: “I have not formerly been an advocate for great manufactories. I doubted whether our labor, employed in agriculture, and aided by spontaneous energies of the earth, would not procure more than we could make ourselves of other necessaries. But other considerations entering into the question, have settled my doubts.”
- Within the thirty years that have elapsed [since the publication of Notes on Virginia], how circumstances have changed. To be independent for the comforts of life we must fabricate them ourselves. We must now place the manufacturer by side of the agriculturalist...Experience has taught me that manufacturers are now as necessary to our independence as to our comfort.”
- Now commerce and agriculture are joined by the interest of manufacturers.

Jefferson's late age doubts

- However, later in life it appears that Jefferson became increasingly alarmed and believes there was a Hamiltonian conspiracy afoot.
- Fear of corruption led by conniving aristocrats under the command of Chief Justice John Marshall.
- He opposes Henry Clay's American System.
- "Solemn Declaration and Protest," December 24, 1825: usurpation of power by the federal government might lead to the rupture of the Union. He believes this would be bad but not a great calamity.
- Drew McCoy: "Jefferson's frantic retreat to a sectional, narrowly agrarian out-look was fueled by a mixture of fear, bitterness, and paranoia."

The tariff, I

- Reiterating, Madison and the Republicans do not want the new industries to disappear with renewed competition from Great Britain.
- Congress approves, and the Madison administration enacts the first truly protective tariff in U.S. history setting off many trade policy battles in the decades to come.
- Trade policy debate shifts from securing neutral trading rights to whether import duties should be used to protect domestic producers from foreign competition rather than to set them only as high as necessary to secure the needed revenue.
- With the end of the War, staple producers see large volumes of trade return and sharp price rises for their goods.
 - Exports surge, but imports increase even more.
 - These imports were subject to duties averaging 49%, but even that could not stem the pent up demand for British manufactured goods.

The tariff, II

- Customs duties are large enough to enable the government to start paying down wartime debts.
- Imports are a shock to the fledgling domestic mfg. sector.
 - Especially devastating to producers of iron, cotton, and woolen goods.
 - Import prices fall 28% from 1814 to 1816.
 - Set off numerous bankruptcies.
 - Britain accused of dumping its goods.
- The effects of increased trade are anticipated.
- Madison requested Congress to consider “means to preserve and promote the manufactures which have sprung into existence...”

The tariff, III

- Enacting the tariff is politically easy since the Federalist party has collapsed.
- Since high wartime duties are not set to expire until 1816, there is no need for any legislation in 1815.
- Madison also maintains the belief that a liberal trade policy could only be adopted if other nations reciprocated.
- “experience teaches that so many circumstances must concur in introducing and maturing manufacturing establishments...”
- Because the war gave a “powerful impulse to manufacturing”, there was good reason to think that if they were given protection domestic manufacturers would be safe against occasional competitors and be a source of wealth.

The tariff, IV

- In 1816, Treasury Secretary Alexander Dallas proposes a new tariff schedule. The tariffs should be sufficient to pay down the debt incurred during the war, and satisfy three other main objectives:
- Promote commerce, agriculture, and industry.
- Difficult as their interests were competing.
- Farmers want low tariffs and manufacturers high ones.
- Commercial interests want policies that increase trade.
- Dallas points out that the country had recently been almost entirely cut off from foreign supplies such as weapons, munitions, clothing, and a range of goods.
- Jeopardizes the country's security.
- Manufacturing needed for the independence of the country.

The tariff, V

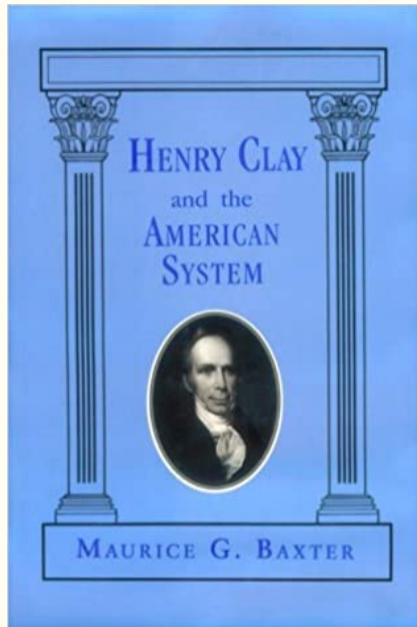
- Dallas places manufactures into 3 broad categories.
 - Those firmly established: cabinets, hats, iron castings, muskets, window glass....
 - Those recently and partially established, but in the longer run with help will succeed: cotton and woolen goods, iron manufacturers, spirits...
 - Those that barely exist such as finer cottons and linens, silk, chinaware and other glass products.
- Strangely, the tariff schedule is highest on the first set of goods and lowest on the last.
 - On the first set the supply of goods would not be endangered by high tariffs since we produce those goods.
 - Third deserve no support. Policy is one of protection not creation.

The tariff, VI

- On middle set, just enough for domestic producers to meet foreign competition on equal terms. Duties in the 20-33 and 1/3% range.
- High tariffs should be temporary. Future advantages will outweigh current costs.
- For the first time the tariff debate focuses on protection.
 - Henry Clay: “The revenue was only an incidental consideration...”
 - Ways and Means Committee reflecting the southern views of its Chairman, William Lowndes, marks down many of the suggested duties.
 - Debate exposes the sectional differences. Low tariff south, high tariff Mid-Atlantic, divided New England.

Henry Clay's American System

- Greatest proponent of the tariff is Henry Clay: national security requires reducing the U.S. dependence on critical supplies.
- Also, Clay believes there will be broad economic benefits.
- Clearly articulated on Henry Clay's speech on the Senate, February 2, 3, and 6, 1832.
- Four pillars:
 1. High tariff to protect U.S. industries and generate revenue for the federal government.
 2. High public land prices to generate federal revenue.
 3. Defend the Second Bank of the United States to stabilize the currency and rein in risky state and local banks.
 4. Internal improvements (such as roads and canals) to knit the nation together and be financed by the tariff and land sales.



Opposition in the South

- John Randolph of Virginia denounces tariffs as a way of promoting northern manufacturing at the expense of southern agriculture.
- After recent events, the South could not oppose a moderately protective tariff because of concerns for national defense.
- The lack of supplies had hampered the war effort.
- Bill passes with strong support from Pennsylvania, New England (cotton textiles), and a split South (strong anti-British sentiment).
- However, as time passes by, the South will become solidly anti-tariff: Ordinance of Nullification by South Carolina in 1833.
- As late as 1860, James Buchanan vetoes S. 416, the Homestead Act, June 22, 1860, and an appropriation to deepening the channel over the St. Clair flats, in Michigan.

To the Senate of the United States.

I return, with my objections,
to the Senate, in which it originated, the Bill
entitled "An Act to secure Homesteads to
actual settlers on the public domain and for
other purposes," presented to me on the 20th
instant.

This Bill gives to every citizen of the
United States "who is the head of a family" and
to every person of foreign birth residing in the
Country who has declared his intention to become
a citizen, though he may not be the head of
a family, the privilege of appropriating to
himself one hundred and sixty acres of
Government land, of settling and residing
upon it for five years, and should his
residence continue until the end of this
period he shall then receive a patent ~~xxx~~
on the payment of twenty five cents
per acre, or one-fifth of the present

- Ironically protectionism originates in the Madison administration.
- However not an infant industries policy. These industries are those that arose as a byproduct of trade policies designed to hurt countries belligerent to U.S. commercial interests.
- These industrial interests then argue for protection.

Internal improvements

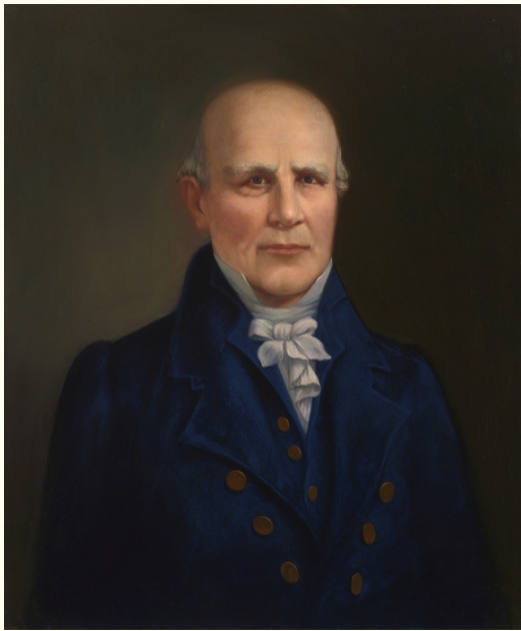
An infrastructure plan

- The final piece of the Madisonian program is internal improvements through the establishment of roads and canals.
- Economic benefits of improved transportation.
- Political benefits in “binding together the various parts of our political confederacy.”
- Importantly, however, Madison believes that doing so will require a constitutional amendment.
- Fourteenth Congress extremely capable and inclined toward strong government.
- Led by Henry Clay and John Calhoun.

- Old line republicans like John Randolph view themselves as standing for party's original principles and look at Madison's proposals with suspicion.
- Also, linked with slavery..

Nathaniel Macon (1757-1837), Letter in 1818

"If Congress can establish banks, make roads and canals, whether they can free all the Slaves in the U.S."



Opposition

- The old guard equate the program with that of the Federalists.
- But there are distinct differences.
- Unlike Hamilton, the debt is viewed to be a temporary means to finance national defense and infrastructure.
- Madison's tariff is primarily protective and designed to make country immune from British commercial and naval interests.
- Hamilton's outlook was Atlanticist, Madison's continentalist.
- The program was also intended to powerfully cement the Union together.

Congressional action

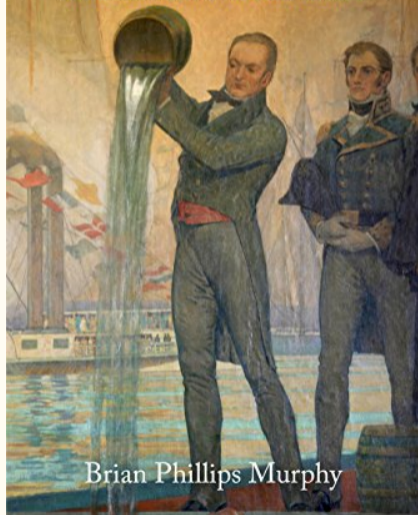
- Progress is made on internal improvements.
- Appropriate \$100,000 to build a national road that will eventually link Baltimore and St. Louis. Madison signs.
- Clay and Calhoun proposed to use the \$1.5 million bonus owed by the Second Bank along with the government's share of the dividends to be earmarked for roads and canals: "Let us conquer space." (Calhoun)
- Opposed in New England and the South, who have little to gain and supported in the mid-Atlantic and West who have a lot to gain. Bill passes 86-84.
- On March 3, 1817, on his last day in office, Madison vetoes the bill: he believes Constitution could not be stretched that far (although he is in favor of a constitutional amendment to allow for internal improvements).

The reaction to Madison's veto

- Madison wants an amendment.
- Also, Madison was suspicious of the type of funding created in the so called "Bonus Bill". It was an invitation to corruption and he refers an integrated national plan.
- Madison's veto stuns Clay and Calhoun.
- They consider Madison's position impractical. Implied the need for an amendment every time some power was called into question. Amending is tedious and protracted.
- Madison chooses theoretical consistency over practicality.
- Most voters agree with him: they are suspicious of grand national plans.

BUILDING THE EMPIRE STATE

POLITICAL ECONOMY IN THE EARLY REPUBLIC



Brian Phillips Murphy

Consequences

- From an economic standpoint, Madison's veto is a missed opportunity.
- The Democratic-Republican alternative to the Hamiltonian program follows a rather circuitous route:
 1. From a policy promoting small farms to an energetic industrial policy.
 2. From a disdain for finance to the reauthorization of a national bank.
 3. From a low tax small government to one considerably more vigorous and unafraid to provide funding for broad projects.
 4. From local economies to creating policies that will economically and politically unify the nation.
- Quite a road. Laid the path for Clay's American System.

A coda

The Confederate Constitution

- The issue of the protective tariffs and internal improvements were one of the main cleavages between democrats and whigs from the 1830s to the Civil War.
- We have an interesting example in the Confederate Constitution.
- Democrats controlled the Constitutional Convention at Montgomery during February and March 1861 (democrats control 5 states vs. 2 controlled by whigs; vote by states).
- Democrats impose their majority.
- Both a protective tariff and federal funding for internal improvements (with a small exception) are prohibited by the new Constitution due to amendments tabled by Robert Rhett (1800-1876).