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Public debts and financial markets in renaissance Italy: between choice and coercion

(very preliminary paper)

At first sight a sharp difference among early renaissance Italian governments turns out: the means by which they fund their deficit. On the one hand there are communal cities and republics, which raise money from citizens through the system of forced or voluntary loans; there are, on the other, princes and lords who exploit services of bankers and merchants. These two different systems of borrowing bring about important financial and political aspects. In this paper I will examine the main features that characterize the two mechanisms of indebtedness and the implications concerning the emergence of a true financial market connected with state bonds.

The cities

As far as we know, the first loan to a urban government was on a voluntary basis. Compelled by urgent - usually military - needs, the commune called for the wealthiest citizens to lend a given sum by committing itself to pay back in short time. The social area of lenders was composed of merchants, bankers, Jews and sometimes foreigners. The government usually granted fiscal or domain revenues as mortgages. This practice took place as early as the mid-12th century, while the communes took up the whole sovereignty on fiscal rights, traditionally held by bishops and feudal lords.

The availability of voluntary loans, though, did not prove to be adequate for the growing financial needs of communes, which were relentlessly engaged in the territorial and economic expansion. Governments thus started requesting forced loans along with the voluntary ones. The system relied on fiscal documents (*estimi* and *catasti*) that determined the amount of wealth or income of all citizens. According to these registers the government assigned the amount each citizen was to lend. Also in this case it was a short-term loan with, usually, a modest interest rate. This system considerably enlarged the social area of lenders; all the citizens, apart from the poorest ranks, were requested to put money into the commune's coffers. Likewise the Jewish community was obliged to lend to the government. Although the government debt was characterized by the participation of city dwellers, it nevertheless is worth noting that in some cases subject communities were involved in the system. In 1287 in Siena, for example, where the *presta generalis* was imposed on both the capital city and the rural communities. In 1371 the same occurred in Lucca. During the second half of the 15th century Venice also, albeit seldom, raised forced loans from the subject cities. Like the voluntary loans, the forced loans were conceived as short-term loans, guaranteed on fiscal revenues that also assured interest payments.

Principalities

As far as the *signorie*, the state of the church and the kingdom of Naples are concerned, the picture is very different. The mechanism of borrowing first relied on the money freely provided from merchants, bankers, courtesans, and foreigners. We may paradoxically argue that a primary market existed in the princely states, whereas instead a ‘public’ debt similar to that of the city-states did not exist. A primary market, however, very peculiar, which should be defined as a personal market. Lenders to princes usually were merchants and bankers whose business in the country were conspicuous. Thus, no wonder to meet the bank Strozzi largely involved in managing state finance in Aragonese Naples; or the Medici, who lend to the duke of Milan. Lending to the lord and commercial activity intertwined constituting a mechanism extremely advantageous to lenders, as long as the debtor kept his promises. Along with these persons, whom we may call credit specialists, we find around the prince also nobles and officers, who wish to get or to enhance their political role through lending activity. They willingly lend, sometimes even at no interest, counting on princely benevolence in order to get privileges, offices and advantages. Such a mechanism in some way recalls the cronyism evocated by Root with regard to ancient regime France. The king stands at the centre of a system of relations that, if well exploited, allow to get enormous political and economic advantages. This system, however, calls for high costs, due to the great uncertainty pervading the relations between creditors and king. The latter, in fact, is not bound to any rule and can repudiate his commitments almost with no consequences. This sharp asymmetry of course brings about costly loans. It is usual that loans to princes be much dearer than those obtained by urban governments. In the mid-15th century, the Aragonese crown at Naples, for example, paid an interest rate of 24%, while in Florence interest on short-term loans usually did not exceed 12-14%.

Funding debt and the emergence of the financial market

Beginning from the second half of the 13th century some governments acknowledged it was impossible to return the principal being borrowed, and decided to fund their debt. In 1262 Venice and in 1274 Genoa consolidated their debts; by mid-14th century they were followed by Florence, Pisa, Siena, and Lucca. Even if sometimes reimbursements were undertaken, government creditors gave up all hope to get their money back. The institutionalisation of the debt also brings about an important process of socialisation of the debt. Through brokers and speculators bonds circulate throughout almost all social environments, from the great merchants to the humble artisans. It is also worth noting that the resort to forced loans increased and at the same time *estimi* and tax records were fully exploited. Citizens thus became true lenders-taxpayers rather than lenders-investors. It is useful to stress this aspect, which sheds a particular light on the indebtedness mechanism of Italian renaissance cities. Actually a structural change occurred. As long as state finance was not under severe and extended pressure the system represented a ‘moneylender’s paradise’. Principals were paid back in relative short time and interest was paid regularly. But growing and endless expenses provoked huge holes of the budgets: indebtedness thus became a regular tool, which led almost naturally to funding.
The pace of indebtedness is shown in Table 1.

Table 1. *The growth of state debts 1350-1500*
(Tons of silver)

	Venice	Genoa	Florence
1350	41		14
1375	118		43
1400	147	104	102
1425	234		149
1450		183	
1475		170	130
1500	420	192	150

Source: author's database

The performances of these cities can better be evaluated by comparing them with data concerning the European great powers, which are available for the mid-17th century.

Table 2. *Per capita indebtedness*
(Kg of Silver)

	Venice	Genoa	Florence	Holland	Castile	France
1350	0.2		0.2			
1400	1.7	2.1	2.8			
1450		3				
1500	4.1	2.7	3.0			
1600	0.1	5.4				
1650	1.7	3.6	0.5	1.7	0.6	0.4

Source: J. Macdonald, *A free nation deep in debt* (New York 2003), p. 152; and author's database

These figures confirm how political and above all economic power of major Italian city-states relied on the exploitation of capital-intensive resources. It also is worth noting that the amount of indebtedness considerably increased although the demographic decline beginning from the mid-14th century.

As far as the working of the market in northern Italy, some common features stand out. Bond market is vivid and involves large sectors of population. Brokers take up a central role in order to meet sellers and buyers, they fix the market price and so lead market behaviours; transactions must be registered from the government offices managing the debt.

Yet there are significant differences. The Florentine government, particularly in the 15th century, appointed prominent citizens – bankers and merchants – charged to raise short-term loans. These loans were to be paid back through the yield of forced loans. In Genoa and Venice instead there is no evident trace of intermediaries between government and lenders. Venetian bankers were asked to anticipate money for state agencies and to make payments on behalf of the government, but it does not seem they were engaged to find lenders.

Bondholders and market

First of all, the citizens enlisted in the tax registers, and particularly those enlisted above a given assessed property value. Lending to the commune was considered a dutiful act, such as servicing in the urban militia. So the resort to forced loans was not criticized– albeit initially- but represented a manifest choice aiming at limiting direct taxation. The continuous resort to borrowing, however, raised resentment and unrest.

As far as foreigners are concerned, communal rules usually prohibited foreigners to purchase government bonds. They could buy them only upon government authorization. In case of need governments, nevertheless, granted citizenship to whom willing invest in urban debt, and sometimes they were promised a higher interest than the usual one. Norms on foreigners were quite flexible and did not limit foreign capital supply. At any rate, the foreign presence among bondholders seems to have been a limited phenomenon: by the early 15th century about one tenth of the Florentine debt was held by foreigners. The decision to invest In foreign debt depended more on the creditworthiness of the government than on the return of its bonds. Unlike some Italian princely states, such as Milan and the papal state, and German cities, the urban governments of Venice, Florence, and Genoa succeeded in raising enormous amounts of money from their citizens and very seldom borrowed from foreigners.

Although data on bondholders are scarce, it seems that many citizens held government annuities. One can estimate that, between the late 14th and the early 15th century, one Florentine in every six was a creditor of the government. Genoa presents a similar situation. By 1500 one citizen in seven enjoyed returns from the government debt.

As previously said, the consolidation of the debt started the secondary market of state bonds. The trade changed the profile of state creditors. In 15th-century Florence one can see an increasing concentration of shares among a few households. According to the data of the *catasto*, in 1427 the Gini concentration index for government shareholders is 89.7, while that for the total wealth is 78.7.

In the principalities the size of the credit market was very restricted; it was actually controlled by crown creditors and their credits – as far as we know – did not circulate in the secondary market. In the second half of the 15th century an innovation, however, emerged in Rome. Along with the loans provided by banker and merchants, the pope raised money by selling some offices. The mechanism was simple: the lender purchased an office at a certain fee (i.e. the principal) and the government paid him interest through a life salary. In many case the holder could also make his office inheritable and marketable, by paying a fee. It is important to point out that the buyer did not any administrative function but received a salary. Offices and shares of them were traded on the secondary market.

A sharp difference, thus, turns out by comparing the credit markets in the cities, on the one hand, and in the principalities, on the other. In the latter personal connections exist; while in the former we can speak of a market characterized by prevailing impersonal relations. Creditors are supposed to enjoy the same rights and to face the same risks.

Why should citizens freely lend to the government? The forced loans system actually eluded a crucial point, that is the lack of robust constraints that compelled urban governments to meet their obligations with creditors. It does not mean, however, that governments were not concerned with financial markets. Venetian and Florentine rules shoed themselves particularly alert in government bond market. It is not surprising indeed: many rulers were both sellers and buyers of state credits. Along with the fiscal capacity of the major city-states (mainly Venice and Genoa), which drew substantial financial resources from the international trade in order to pay the debt service, the pillar of the credibility of urban governments was the role of rulers as debt investors. In Florence in 1427 4 % of households held about two thirds of the government credits. Many patrician families, trust funds, and charitable institutions enjoyed conspicuous income from state annuities. So, it would be very difficult the government defaulted. It is, moreover, worth pointing out that throughout the phase of political and economic expansion (from the 12th through the early 15th centuries) a large consent supported the financial policy of the major urban governments. The money paid for forced loans actually was regarded as a sort of investment for both the whole city and particular interests (merchants, artisans, politicians...). A huge network supported the aggressive policy of mercantile cities such as Venice, Genoa and Florence.

The system allowed urban governments to limit the cost of borrowing. Like in other European places, in Italy the interest rate decreased throughout the late middle ages. Table 3 presents some data.

Table 3. *Interest rates on government loans, 1290-1500*

	Florence	Siena	Genoa	Venice
1290-99	10	20		5
1300-09	8	15		5
1310-19		17		5
1320-29	8,7	14,9		5
1330-39	13	12,9		5
1340-49	7,5	9,2	10	5
1350-59	15	8,7	10	5
1360-69	12,5		10	5
1370-79			8	5
1380-89	5		8,7	4
1390-99			9	4
1400-09	5		6,2	4
1410-19				4
1420-29				3,7
1430-39	3,75			2,8
1440-49	3,4		4	2,2
1450-59			4	2
1460-69			3,6	2
1470-79	3,25			1,8
1480-89	3			1,8
1490-99	2,25			1,8

Source: author's database

Urban rules succeeded in paying lesser their loans than lords did. The latter had to pay short-term loans at an interest of 15-20%, due to the uncertainty of their commitments. The economic environment of the cities provided a great deal of capitals to be invested; the fiscal system proved to be relatively effective; a mix of popular consent and groups interest created a favourable atmosphere. As long as the elements of the mechanism worked well, the system also enjoyed a good reputation; but when military and financial troubles emerged, the (forced) lenders had to be transformed in tax-payers. In the end, however, from trade of government bonds, arrears claims, overdue interest, discounted payments, a significant financial market arose.