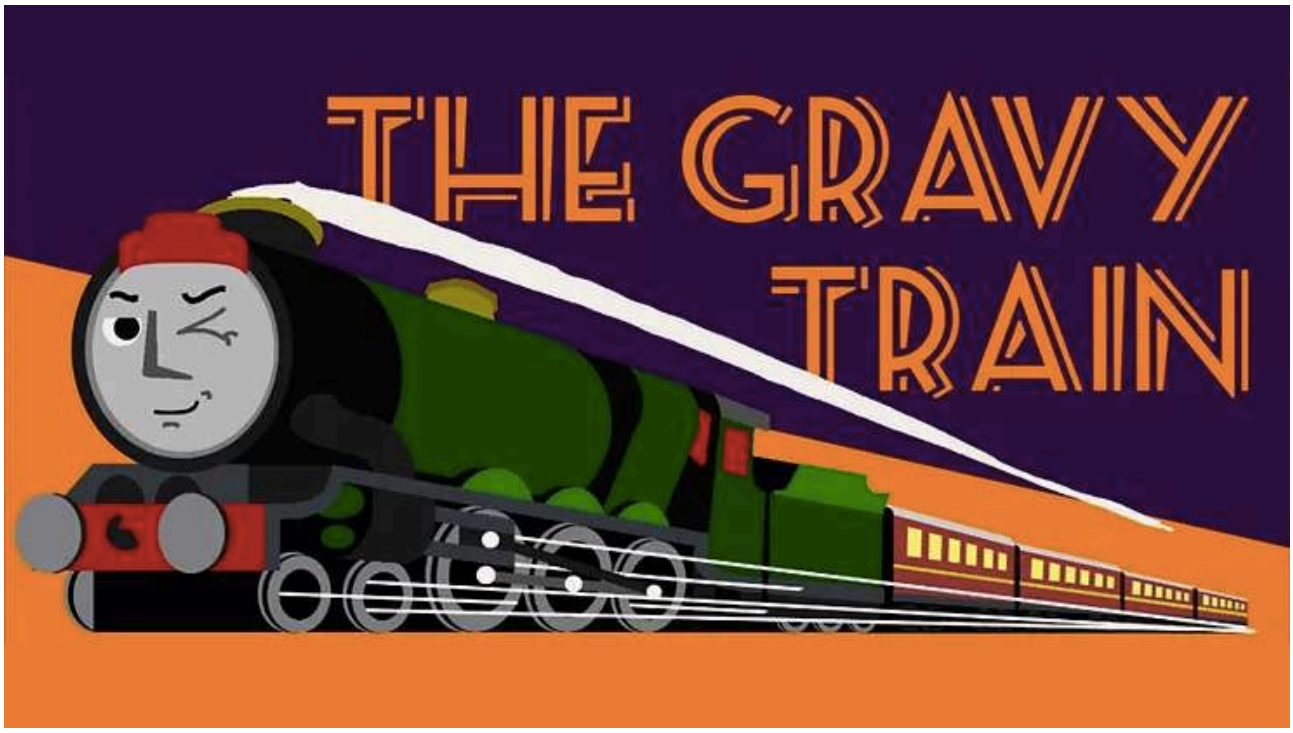
All Aboard The Gravy Train



In a previous newsletter I discussed 'Tulip Mania', which is generally considered the world's first economic bubble, and possibly also the most famous.

However, *arguably the greatest economic bubble in history* (at least when measured by the scale of investment as a proportion of national income), is virtually unknown.

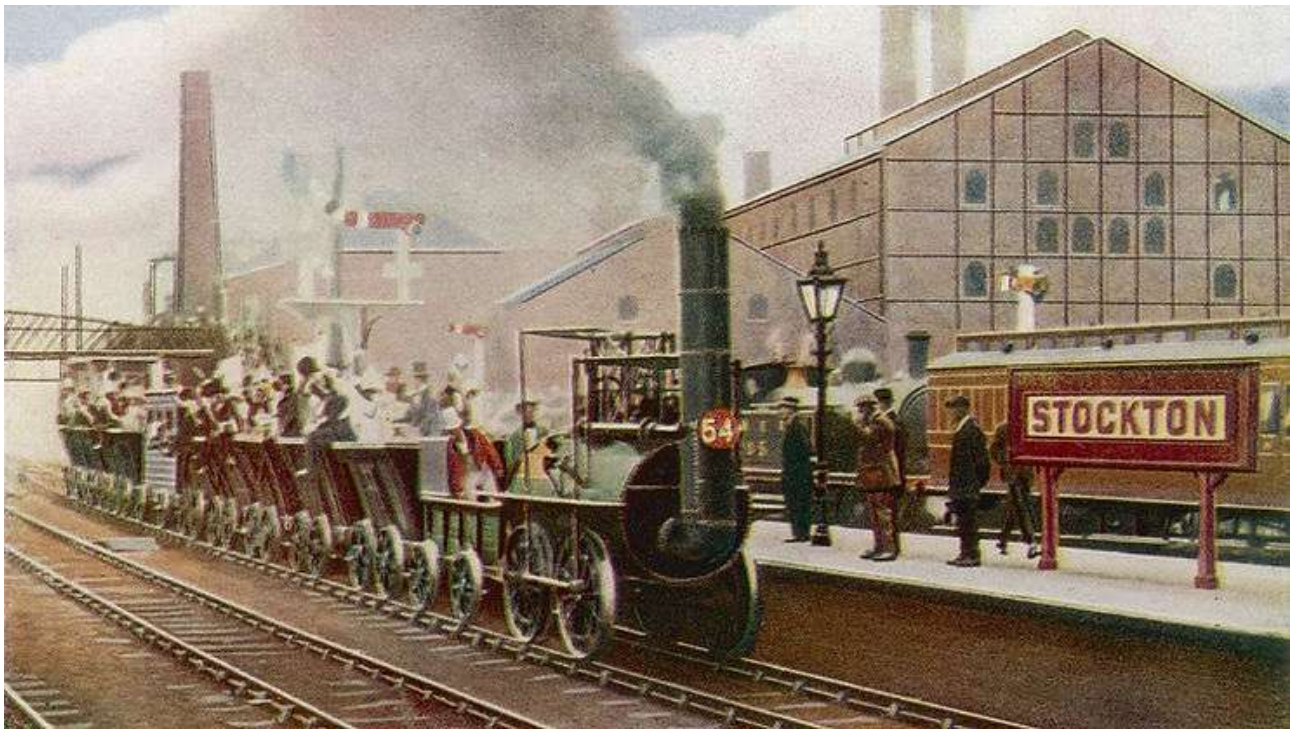
Britain's 'Railway Mania' of the 1840's was, in 2008, described by The Economist magazine as the greatest -ever economic bubble - and who's to argue with The Economist?

It was the advent of steam travel that was the spark to this boom in railway stocks in England, b*ut with investment decisions quickly decoupling from reality, the boom soon became a runaway train which slammed into the buffers in October 1847.*

Building up a Head of Steam

When steam trains first appeared in the 1820s, they were met with widespread hostility. It was feared that they would prevent hens from laying eggs and cattle from grazing, and

that their noxious fumes would blacken the fleeces of sheep. It was even stated that passengers travelling at breakneck speeds of 12.5 mph would be vaporised. (Yes, really!) Notwithstanding such apprehensions, there were two early speculative flurries: the first following the establishment of the 25mile (40km) long Stockton and Darlington Railway in 1825, and the second after the opening of the Liverpool and Manchester Railway six years later.



Yet both of these were fairly short-lived and by the late 1830s, with 2,000 miles of track in place, many felt the national network was complete. Journey times from London to Glasgow had been reduced to 24 hours, prompting the Railway Times to ask: ‘What more could any reasonable man want?’

Nonetheless, by the early 1840s, speculative interest in the railways was beginning to pick up again. Much of the earlier opposition had diminished and most could now see the benefits of steam travel compared to other modes of transport. Queen Victoria made her first train trip in 1842, following which railways became quite the rage.

Investors fawned upon railway companies, lured by their highly desirable dividend promises, encouraging lobbyists and promoters to rush through plans for new lines and issue new share subscriptions. These sold instantly, and commanded huge premiums, even for the most dubious of projects.

Railway schemes were typically projected in the following way. Advertisements for a new company would flood the newspapers, including a list of ‘committeemen’ (company trustees) and the promise of a 10% dividend. If the subscription went well, the committeemen would retain a large share allocation, creating a scarcity, and then get their friends in the railway press to ‘puff’ the stock, whereupon they would sell it at a premium.

Although the committeemen were billed as upstanding members of the local community, they were often, according to The Times newspaper, ‘the most notorious scamps and swindlers’, whose sole interest was personal gain. Many politicians were also in on the game, acting as committeemen and hawking their parliamentary votes in return for shares.

Emergency Announcements

Some public figures, notably Alexander Baring and William Gladstone, urged caution and called in parliament for tighter regulation but their appeals fell upon deaf ears. This was hardly surprising, given that most MPs were in on the game. Prime Minister Sir Robert Peel refused to intervene, believing that the previous year’s Bank Act (which stipulated that notes must be fully convertible) had prevented all undue speculation.

However, the speculation continued and reached fever pitch by summer 1845. By June there were twelve schemes coming before Parliament each week alongside plans for over 8,000 miles of new track. The whole country was consumed with railway mania and speculative fervour pervaded all sections of society.

Running Out of Steam

As the summer wore on, the railways began to lose their gloss. It was becoming increasingly clear that many people had speculated far beyond their means and were in no position to meet the capital calls that were now being made. For example, a parliamentary report found that two brothers who had subscribed for £37,500 of stock were the 'sons of a charwoman living in a garret off a guinea a week'. (In 21st century English; 'sons of a cleaner, living in a small dismal attic room with a salary of £1.05 per week)

There was also growing evidence of fraud, lovingly exposed by The Economist and The Times. Both publications, (despite carrying dozens of railway advertisements!), began to launch blistering tirades against the railway companies and the cynicism of their investors.

By early October, shares were beginning to decline as investors were forced to liquidate stock to meet the calls; on 14 October, a failed speculator shot himself in Hyde Park, crystallising investors' apprehensions. To cap it all came the news of the Irish potato famine. So when the Bank of England raised interest rates by 0.5% a few days later, share premiums evaporated and there was an 'avalanche' in prices, with the shares of the Great Western, Britain's largest operator, 'down 40% from their August peak'.

Off the Rails

Britain's railway investors reaped a bitter crop that autumn, not unlike Ireland's potato farmers. The unfortunate speculator, in like manner, finds that on one hand, we hear of potatoes being thrown to the cattle; on the other, we have rumours of speculators having "gone all to the dogs".'

Given the crushing burden of the continued share calls, the government passed a dissolution act allowing railway companies to be dissolved if at least 75% of shareholders agreed. Yet despite the act, declining share prices and growing despondency, railway building continued.

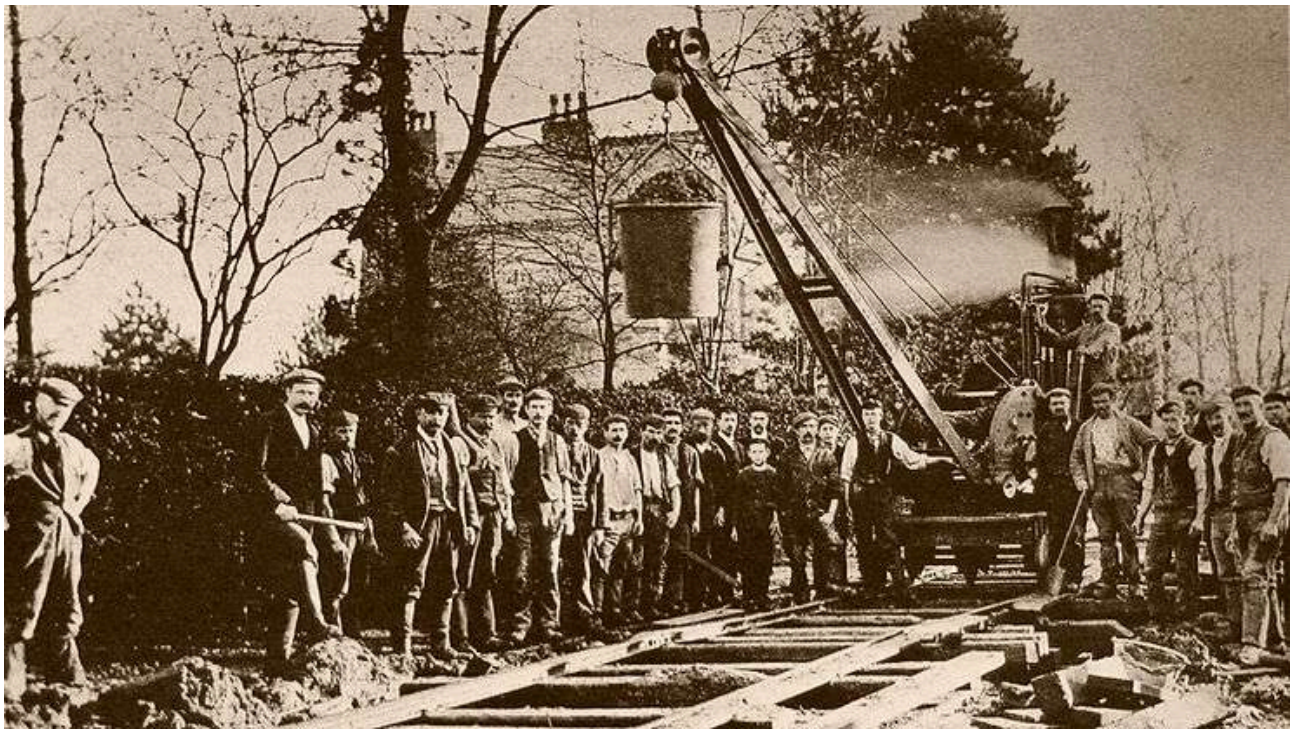
By summer of 1846, bankruptcies were at an all-time high and Britain was mired in economic gloom, with middle-class families in particular suffering. Entire families were ruined.

Panic Stations

By early October 1847, the Bank of England's bullion reserves had fallen to dangerously low levels, reaching crisis point on Monday 17th. October.

The following day, four major banks failed and by the end of the so-called 'week of terror', the Bank of England had such low reserves that another run would have been fatal. On Saturday 23rd. October, a group of prominent financiers visited Downing Street and begged the Prime Minister to suspend the Bank Act (i.e. the full convertibility of banknotes) which was causing such misery in the City. Two days later, their request was granted and the crisis rapidly dissipated.

However, Railway Mania was not entirely negative. As well as Britain being left with a first rate transport system, the high amount of railroad construction provided employment for hundreds of thousands of Irish navvies desperate for work during the potato famine.



As we all know, financial bubbles of different sizes continue to this day, with maybe the most recent being the Gamestop, Reddit-fueled, price surge that was similar with one person trying to get an advantage over the next person in line.

Of course, the difference these days is that todays' internet-based gravy train runs much faster and falls much quicker than any gravy train of the 1840s. So beware getting on whatever will be the next gravy train arriving at platform number 2!