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The evolution of financial institutions in the Ottoman Empire, 1600–1914

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I

In recent decades institutions and institutional change have been identified by economists and economic historians as key variables that help explain the widely disparate economic performance of different societies over the last five hundred years. Based on the successful experience of Western Europe and European off-shoots, new institutional economics has argued that long-run economic change is the cumulative consequence of innumerable short-run decisions by political and economic agents that both directly and indirectly shape performance. Economic growth is attained because the underlying framework persistently reinforced incentives for organisations to engage in productive activity. The state is seen as a major player in this context. In the Western European case, as the result of political struggles and alliances, the state and associated institutions moved to provide the appropriate legal framework and incentives.

Institutional economics and economic historians have come to recognise, however, that a society rarely arrives at or creates institutions that are wholly conducive to economic growth. In many cases, institutions have favoured activities that promote redistributive rather than productive activity, that restrict opportunities rather than expand them. Similarly, rather than reinforcing incentives towards productive activity, in most cases states acted as instruments for transferring resources from one group to another, or promoting their own survival at the expense of others. In short, the process of institutional change has not always been favourable to economic growth. Politics and political struggles have played an important role in these unfavourable or less successful outcomes as well.[2]

[1] Earlier versions of this paper were presented at the University of Venice Summer School in Financial History and the Research Division of the Bank of Italy at Rome. I would like to thank Patrick O'Brien, the participants of those meetings, and an anonymous referee of this journal for many helpful comments.

[2] Douglass C. North and Robert P. Thomas, *The Rise of the Western World: a New Economic History* (Cambridge, 1973); Douglass C. North, *Institutions, Institutional Change and Economic Performance* (Cambridge, 1990); Thrain Eggertsson, *Economic Behavior and Institutions* (Cambridge, 1990); more recently, Daron Acemoglu, Simon Johnson and James Robinson, 'The rise of Europe: Atlantic trade, institutional change and economic growth', unpublished manuscript, 2002.

Focusing on the 'rise of the West', institutional economics and economic historians have paid less attention to studying these unsuccessful or less successful cases of institutional change, especially those outside the Western European context. In this study we are interested in examining institutional change of a different type. We will not argue that Ottoman institutions changed before the nineteenth century and came to resemble those that gave rise to capitalism. We will argue, instead, that Ottoman society and Ottoman bureaucracy brought about institutional change in selective areas, in monetary institutions and in public finance, for example, and that such selective institutional change enabled the Ottomans to maintain their rule and the empire over a very considerable period.

The Ottoman Empire stood at the crossroads of intercontinental trade, stretching from the Balkans and the Black Sea region through Anatolia, Syria, Mesopotamia and the Gulf to Egypt and most of the North African coast, for six centuries until World War I. For most of the seventeenth and eighteenth centuries, its population exceeded 30 million (of which the European provinces accounted for half or more; Anatolia and Istanbul for 7 to 8 million, other Asian and North African provinces for another 7 to 8 million) but declined thereafter due to territorial losses.

For most of its six-century existence, the Ottoman Empire is best characterised as a bureaucratic and agrarian empire. The economic institutions and policies of this entity were shaped to a large degree by the priorities and interests of a central bureaucracy. Until recently, Ottoman historiography had depicted an empire in decline after the sixteenth century. In contrast, we will argue that the Ottoman state and society showed considerable ability to reorganise as a way of adapting to changing circumstances in Eurasia from the seventeenth century to the nineteenth century. The central bureaucracy managed to contain the many challenges it faced with its pragmatism and habit of negotiation to co-opt and incorporate into the state the social groups that rebelled against it. These traits enabled the Ottomans to retain power and survive until the modern era, while many of their contemporaries in both Europe and Asia were unable to do so.

The Ottoman state also showed considerable flexibility to adapt not only its military technology but also its fiscal, financial and monetary institutions in response to the changing circumstances. By pragmatism and flexibility we refer here to the willingness of the Ottoman bureaucracy not to be bound in its actions and in the institutions it adopted by specific and rigid rules based on custom, traditions, religion, past behaviour or past enmities.

The Ottomans showed traits of pragmatism and flexibility from the earliest period. Emerging in a highly heterogeneous region populated by Christians and Muslims, Turkish and Greek speakers, the Ottomans' success in western Anatolia and later in the Balkans during the fourteenth and fifteenth centuries owed much to their willingness and ability to adapt to changing conditions, to utilise talent and accept allegiance from many sources, and to make many-sided appeals for support. They were thus able to attract many followers, not only as warriors fighting against the Christians, but also Muslims and Christians fighting for the riches to be gained, the positions and power to be won. The Ottomans also displayed remarkable openness to technological innovation in adapting firearms on a greater scale, more effectively and earlier than the neighbouring states. Similarly, they exhibited a considerable degree of flexibility and pragmatism while expanding the territories under their control. They were prepared to negotiate for the loyalty of local elites whenever the new state was unable to impose full control. They also proved to be quite adept at learning about and borrowing institutions from others. In short, the early Ottoman enterprise was not a religious state in the making, but rather a pragmatic one.[3]

In this article, we will examine the long-term changes in Ottoman fiscal, monetary and financial institutions from this perspective of pragmatism, flexibility and adaptiveness. While such a perspective may provide key insights towards understanding the longevity of the empire, the limitations of this pragmatism need to be equally emphasised. Institutional change did not apply equally to all areas of Ottoman economic life. Moreover, not all types of institutions were affected to the same degree by those changes. Because the central bureaucracy was able to retain its leading position in Ottoman society and politics, the influence of various social groups, not only of landowners but also of merchants, manufacturers and money-changers, over economic matters, and more generally over the policies of the central government, remained limited until the end of the empire. As a result, most of the pragmatism and flexibility were utilised for the defence of the traditional order and its own position in that order. In contrast, institutional changes that threatened the leading position of the central bureaucracy were resisted more forcefully than others. Institutional change thus remained selective and many of the key institutions of the traditional order such as state ownership of land, urban guilds and restrictions on private capital accumulation remained intact until the nineteenth century. These important limitations of Ottoman flexibility, pragmatism and adaptiveness should help provide a more balanced picture regarding not only the ability of the empire to survive through the early modern era but also its disintegration during the nineteenth century, despite the acceleration of institutional changes.

II

For a long time it has been assumed that the use of money in the Balkans and Anatolia was limited to long-distance trade and parts of the urban sector.[4] Recent research has shown, however, that the urban population and some segments of the countryside were already part of the monetary economy by the end of the fifteenth

[3] C. Kafadar, *Between Two Worlds: the Construction of the Ottoman State* (Berkeley, 1995); H. W. Lowry, *The Nature of the Early Ottoman State* (Albany, 2003); and D. Quatert, *The Ottoman Empire, 1700–1922* (Cambridge, 2000), pp. 13–36.

[4] F. Braudel, *Civilization and Capitalism, 15th–18th Century*, vol. III: *The Perspective of the World* (New York, 1984), pp. 471–3.

century. Even more significantly, there occurred a substantial increase in the use of money during the sixteenth century, both because of the increased availability of specie and increasing commercialisation of the rural economy. The evidence for this important development comes from a number of sources. First, recent research has suggested that population growth and urbanisation during the sixteenth century were accompanied by the growth of economic linkages between the urban and rural areas. As a result, there emerged in the Balkans and Anatolia an intensive pattern of periodic markets and market fairs where peasants and larger landholders sold parts of their produce to urban residents. These markets also provided an important opportunity for the nomads to come into contact with both peasants and the urban population. Large sectors of the rural population came to use coinage, especially the small denominations of silver *akçe* and the copper of pilgrims through their participation in these markets.[5]

The annual pilgrimage to Mecca also gave rise to monetisation. A good deal has been written about the importance of Champagne fairs for European economic history. Available evidence indicates that these fairs were dwarfed by the numerous fairs along the pilgrimage routes and particularly by those around Mecca. The Ottoman government ensured the safety of these routes and tried to facilitate the monetary transactions of pilgrim merchants from different corners of Eurasia. The pilgrimage to Mecca also gave rise every year to one of the largest payments and specie flows within the Ottoman Empire. The financing of the caravans including provisioning, payments to tribal leaders *en route* for security and funds carried by tens of thousands of pilgrims – in some years close to 100,000 pilgrims – gave rise to large flows of gold and silver from Egypt, Syria and Anatolia to the Hijaz every year. Even more importantly, the governments in Istanbul and Egypt and the various official, semi-official and private foundations sent large sums every year to support the Holy Cities. In addition, the annual revenues of many small and large pious foundations in Anatolia and some of the largest foundations in Egypt were set aside for the Hijaz. Total remittances by the foundations roughly equalled the amounts sent by the governments in Istanbul and Cairo. From Egypt, some of these net revenues were sent in kind, as cereals. Faroqhi thus estimates that a total of 300,000 to 400,000 *sultanis* or ducats were sent to the Hijaz every year from Istanbul, Anatolia and Egypt combined, in addition to the payments and specie flows arising from the pilgrimage caravans themselves. The funds in cash were sent in gold whenever available, because gold was the preferred specie in the Hijaz.[6]

It has often been assumed that the prohibition of interest in Islam prevented the development of credit, or, at best, imposed rigid obstacles in its way. Similarly, the

[5] S. Faroqhi, 'The early history of Balkan fairs', *Südost-Forschungen*, 37 (1978); S. Faroqhi, 'Sixteenth century periodic markets in various Anatolian sancaks', *Journal of the Economic and Social History of the Orient*, 22 (1979).

[6] Suraiya Faroqhi, *Pilgrims and Sultans: the Hajj under the Ottomans 1517–1683* (London and New York, 1994), pp. 74–91, 158–68.

apparent absence of deposit banking and lending by banks has led many observers to conclude that financial institutions and instruments were, by and large, absent in Islamic societies. It is true that a religiously inspired prohibition against usurious transactions was a powerful feature shared around the Mediterranean during the Middle Ages, both by the Islamic world and the Christian West.[7] While the practice of *riba*, the Arabic term for usury and interest, is sharply denounced in a number of passages in the Qur'an and in all subsequent Islamic religious writings, already in the classical era, Islamic law had provided several means by which the anti-usury prohibition could be circumvented just as the same prohibitions were circumvented in Europe in the late medieval period. Various legal fictions, based primarily on the model of the 'double-sale' were, if not enthusiastically endorsed by jurists, at least not declared invalid. Thus, there did not exist an insurmountable barrier against the use of interest-bearing loans for commercial credit.

Neither the Islamic prohibitions against interest and usury nor the absence of formal banking institutions prevented the expansion of credit in Ottoman society. Utilising the Islamic court records, the late Ronald Jennings showed that dense networks of lenders and borrowers flourished in and around the Anatolian cities of Kayseri, Karaman, Amasya and Trabzon during the sixteenth century. Over a twenty-year period which his study covered, he found literally thousands of court cases involving debts. Many members of each family and many women are registered in these records as borrowing and lending to other members of the family as well as to outsiders. These records leave no doubt that the use of credit was widespread among all segments of the urban and even rural society. Most lending and borrowing was on a small scale and interest was regularly charged on credit, in accordance with both Islamic and Ottoman law, with the consent and approval of the court and the *ulema*. In their dealings with the court, the participants felt no need to conceal interest or resort to tricks in order to clear legal hurdles. Annual rates of interest ranged from 10 to 20 per cent.[8]

One important provider of loans in Istanbul, the Balkans and the Anatolian urban centres were the cash *vakifs*, pious foundations established with the explicit purpose of lending their cash assets and using the interest income to fulfill their goals. These endowments began to be approved by the Ottoman courts in the early part of the fifteenth century and had become popular all over Anatolia and the Balkan provinces by the end of the sixteenth century. An interesting development that became more pronounced during the eighteenth century was the increasing allocation of the funds to the trustees of these endowments. The trustees then used the borrowed funds to lend at higher rates of interest to large-scale moneylenders (*sarraf*) at

[7] For a recent discussion of the classical Islamic views on interest, see N. A. Saleh, *Unlawful Gain and Legitimate Profit in Islamic Law: Riba, Gharar and Islamic Banking* (Cambridge, 1988), pp. 9–32.

[8] R. C. Jennings, 'Loans and credit in early 17th century Ottoman judicial records', *Journal of the Economic and Social History of the Orient*, 16 (1973).

Istanbul, who pooled these funds to finance larger ventures, most importantly, long-distance trade and tax farming.[9]

Not surprisingly, a lively debate developed during the sixteenth century within the Ottoman *ulema* regarding whether the cash *vakif* should be considered illegitimate. The cash *vakifs* were opposed by those who believed that only goods with permanent value such as real estate should constitute the assets of a pious foundation and that the cash *vakifs* contravened the Islamic prohibition of interest. The majority of the *ulema*, however, remained eminently pragmatic and the view that anything useful for the community is useful for Islam ultimately prevailed. During the heated debate, Ebusuud Efendi, the prominent, state-appointed religious leader (*Seyhulislam*) of the period, defended the practice from a purely practical point of view, arguing that abolition of interest taking would lead to the collapse of many pious foundations, a situation that would harm the Muslim community.[10]

III

Even though there did not exist an insurmountable barrier to the use of interest-bearing loans for commercial credit, this alternative was not pursued in the medieval Islamic world. Instead, numerous other commercial techniques were developed which played the same role as interest-bearing loans and thus made the use of loans unnecessary. These included a variety of business partnership forms such as *mudaraba* or commenda, credit arrangements, transfers of debt and letters of credit, all of which were sanctioned by religious theory. Long-distance trade was thus financed not by simple credit relations involving interest, but by a variety of Islamic business partnerships, the specifics of which depended on the nature of the risks and the resources provided by the different partners.

Ottoman merchants widely used the varieties of Islamic business partnerships practised in the Islamic world from the classical era.[11] The most frequently used method in the financing of long-distance trade and certain other types of business ventures was the *mudaraba* partnership of classical Islam, in which an investor entrusted his capital or merchandise to an agent who was to trade with it and then return the original amount. The profits were then shared between the principal and the agent according to some pre-determined scheme. Any loss of the capital resulting from the exigencies of travel or the business venture itself were borne exclusively by the principal. The liability of the agent was limited to his time and

[9] M. Çizakça, *A Comparative Evolution of Business Partnerships: the Islamic World and Europe with Specific Reference to the Ottoman Archive* (Leiden, 1996), pp. 131–4.

[10] J. E. Mandaville, 'Usurious piety: the cash waqf controversy in the Ottoman Empire', *International Journal of Middle East Studies*, 10 (1979).

[11] A. L. Udovitch, *Partnership and Profit* (Princeton, 1970), pp. 170–217; and Çizakça, *A Comparative Evolution*, pp. 66–76.

efforts.[12] To a lesser extent the Ottomans also used *mufawada* partnership of the Hanefi school of Islam in which the partners were considered equals in terms of capital, effort, returns and liabilities. In the related *musharaka* or *inan* arrangement, the partners were free to invest different amounts and agree to share the returns and liabilities in unequal but prearranged amounts.

Evidence from Islamic court records on commercial disputes and their resolution until the middle of the nineteenth century indicates that in Anatolia and Istanbul, at least, the Ottoman jurists were well informed about the teachings of medieval Muslim jurists and, in general, adhered closely to the classical Islamic principles in disputes arising from these partnerships. There were some innovations over the centuries; for example, some interesting combinations of *mudaraba* and putting-out activities were developed. On the whole, however, evidence from hundreds of business partnerships indicates that classical Islamic partnership forms not only survived but were applied, with minor exceptions, true to their original forms until the nineteenth century. Çizakça suggests that the continued dominance of small-scale firms or partnerships was probably the most important reason for the limited changes in this area.[13]

One important instrument in the finance of long-distance trade was the *suftaja*, a bill of exchange or letter of credit. The basic purpose of the *suftajas* was to expedite long-distance payments or transfer of funds. In Europe the bill of exchange entailed the initial payment of one type of currency in return for the payment of another type of currency at a different location. In the Geniza documents of medieval Egypt the *suftajas* consistently appeared as involving the repayment of exactly the same type of money to the issuing banker. They were as good as money; the bearer could fully expect to redeem his *suftaja* for cash immediately upon arrival at his destination. The prompt payment was further assured by the government through the imposition of stiff penalties for any delays. *Suftajas* were used widely inside the Ottoman Empire between Anatolia, the Aegean islands, Crimea, Syria, Egypt and also with Iran. Ottoman court documents from fifteenth- and sixteenth-century Bursa, a major centre in long-distance trade, point to the high frequency of the use of *suftajas*. The local judges (*kadis*) were actively involved in the enforcement of the *suftajas* in their various forms.[14] Another type of letter of credit was the *hawala* which was the

[12] In essence, this was identical to the commenda of Europe. For discussions of the Islamic origins of European commenda, see A. L. Udovitch, 'At the origins of the Western commenda: Islam, Israel, Byzantium', *Speculum*, 37 (1962); and E. Ashtor, 'Banking instruments between the Muslim east and the Christian west', *Journal of European Economic History*, 1 (1972) and Çizakça, *A Comparative Evolution*, pp. 10–32.

[13] Çizakça, *A Comparative Evolution*, pp. 65–85 and 126–31; also M. Çizakça,'Financing silk trade in the Ottoman Empire: 16th–18th centuries', in Simonett Cavaciocchi (ed.), *La seta in Europa secc. XIII–XX* (Prato, 1993), pp. 711–23.

[14] Udovitch, *Partnership and Profit*, pp. 268–9; Ashtor, 'Banking instruments', pp. 554–62; and H. Sahillioğlu, 'Bursa kadı sicillerinde iç ve dış ödemeler aracı olarak "Kitabü'l-Kadı" ve "Süftece"ler', in O. Okyar and H. Ü. Nalbandoğlu (eds.), *Türkiye İktisat Tarihi Semineri* (Ankara, 1975).

assignation of a fund from a distant source of revenue by a written order. It was used in both state and private transactions to avoid the dangers and delays involved in the transportation of cash.[15]

IV

In the Ottoman monetary system, there existed three levels of coinage: gold, silver and copper. The silver *akçe* until the middle of the seventeenth century and the silver *kurush* (from groschen/piaster) in the eighteenth century were the basic units of account and the leading means of payment in local transactions. The silver content of these units of account changed with the occasional debasements by the government. In contrast, the standards of the gold coins usually remained identical to those of the Venetian ducat and the gold coins of most other states around the Mediterranean. The exchange rate of gold coins, expressed in silver *kurush* and in terms of foreign coins, was determined by the markets, subject to the changes in the silver content of the *kurush*, fluctuations in the gold-silver ratio and a host of other factors. The state encouraged the circulation of gold and silver as well as foreign coinage. The government did not adhere to a legally fixed rate of exchange between the gold and silver coins or a fixed gold-silver ratio around which the face value or the standards of both types of coins would be determined.[16]

This monetary regime might loosely be called bimetallic, since both gold and silver coins were minted and circulated freely. One should be careful, however, about the use of this term and distinguish it from classical bimetallism as practised during the nineteenth century. Under the latter system, a country typically adopted both gold and silver as monetary standards. The relative amounts of the two metals necessary to create the same currency unit, known as the mint ratio or the legal ratio, was specified by the authorities. In other words, the face value of both gold and silver coins was fixed by the government.[17]

In searching for a label for the Ottoman monetary regime, it is more useful to adopt the strict definitions of monometallism and bimetallism used in the nineteenth century. According to these definitions, a monetary regime is characterised as monometallism if there is one standard commodity in terms of which the value of other commodities are measured, even if the circulation may include several metallic and paper elements. The Ottoman regime outlined above certainly fits this definition. The silver *kurush* was the basic unit of account in terms of which the value of all other commodities, including the gold and copper coins, was being measured.

The basic virtue of the Ottoman system was its flexibility. As long as the markets determined the exchange rate of the gold coins and if the official rates at which the

[15] İnalcık emphasizes the use of *hawala* in state transactions. H. İnalcık, 'Hawale', *Encyclopedia of Islam*, second edition, vol. III (Leiden and New York, 1969), pp. 283–5.

[16] S. Pamuk, *A Monetary History of the Ottoman Empire* (Cambridge, 2000), pp. 66–76.

[17] C. P. Kindleberger, *A Financial History of Western Europe*, second edition (Oxford, 1993), pp. 57–63.

government accepted these coins followed the markets closely, neither type of coin was likely to be over or undervalued. For this reason, they were not in danger of disappearing.

The Ottoman government adhered to this framework, with some exceptions, until the nineteenth century. While the practices of medieval and early modern states in Europe and the Near East varied in time and space, the majority pursued a flexible approach similar to that of the Ottomans. One of the most telling examples of Ottoman flexibility concerned the determination of exchange rates between different kinds of coinage. In an environment of frequently recurring shortages of specie, the Ottoman administrators knew that it was essential to attract into the Ottoman lands and maintain in circulation as much coinage and bullion as possible. Their monetary practices were guided more by this concern than any other. They were also aware that the ratio between gold and silver, as well as the value of different types of coins, was subject to fluctuations. Under these conditions, a policy of fixed exchange rates between different coins would have driven the good or undervalued coins out of circulation through the workings of Gresham's law. Instead, the government allowed the local markets to determine not only the exchange rates of the *sultani*, but those for all types of coins, Ottoman and foreign. Local court records show that the *kadıs* relied on these market rates to settle disputes between individuals. In addition, the government announced the official rates at which different coins, gold and silver, would be accepted as payment. Usually, these rates did not diverge significantly from the prevailing market rates for the same coins.

Government policies towards foreign coinage provides another example of flexibility. From the earliest days, the authorities encouraged the circulation of foreign coinage and accepted that as payment. The government also exempted precious metals and foreign currency from import dues. In capitulations or privileges given to merchants of certain European states, the central government exempted them from all customs duties for the foreign coinage they brought. In addition, customs and mint officials were told not to demand that these coins be surrendered to the authorities for the minting of Ottoman coinage. These privileges were eventually extended to the merchants of most European states during the sixteenth century.[18]

V

The evolution of Ottoman fiscal institutions during the eighteenth century provides another good example of the ability of the Ottoman state to contain the challenges it faced with pragmatism, flexibility and negotiation. It sought to co-opt and incorporate into a broad alliance the social groups that challenged its authority.

While loans to kings, princes and governments were part of the regular business of European banking houses in the late medieval and early modern periods, in the Islamic world advances of cash to the rulers and the public treasury were handled

[18] Pamuk, *A Monetary History of the Ottoman Empire*, pp. 63–6, 70–4.

differently. They took the form of tax-farming arrangements in which individuals possessing liquid capital assets advanced cash to the government in return for the right to farm the taxes of a given region or fiscal unit for a fixed period. Tax farming thus dominated the Islamic world from the Mediterranean to the Indian Ocean, from the earliest days through to the early modern period.

From the very beginning, the Ottomans relied on tax farming for the collection of urban taxes. Until late in the sixteenth century, however, the agricultural taxes which constituted the largest part of the tax revenues were collected locally and mostly in kind within the *timar* system. *Sipahis*, state employees who resided in rural areas, were expected to use these revenues to equip and prepare a given number of soldiers for the military campaigns. Until the second half of the sixteenth century, state finances were relatively strong, thanks to the revenues obtained through the rapid territorial expansion of the empire, and the state did not feel the need to increase the revenues collected at the centre. There are some examples, however, of the state engaging in short-term borrowing during the sixteenth century. These services earned the financiers, mostly Jews and Greeks, the inside track on some of the most lucrative tax-farming contracts.[19]

With the changes in military technology during the sixteenth century and the need to maintain larger, permanent armies at the centre, however, pressures increased to collect a larger part of the rural surplus. As a result, the *timar* system began to be abandoned in favour of tax farming and the tax units were auctioned off at Istanbul.[20] The shift away from the *timar* system had been designed to increase the cash receipts at the centre, but the decline of state power *vis-à-vis* the provinces reduced the expected benefits from this change. Bureaucrats in the capital and provincial groups began to share tax-farming revenues with the central government during the seventeenth century.

In the longer term, further deterioration of the state finances increased the pressures on the central government to take greater advantage of the tax-farming system for the purposes of domestic borrowing. The central government thus began to increase the length of the tax-farming contracts from one to three years to three to five years and even longer. In many instances, however, a tax farmer could lose his farm at any time, if a competitor offered to pay a higher amount. The government also demanded an increasingly higher fraction of the auction price of the contract in advance. Tax farming was thus converted to a form of domestic borrowing, with the actual tax revenues being used as collateral by the central government.

Further steps were taken in the same direction with the introduction, in 1695, of the *malikane* system in which the revenue source began to be farmed out on a

[19] Halil Inalcik and Donald Quataert (eds.), *An Economic and Social History of the Ottoman Empire, 1300–1914* (Cambridge, 1994), pp. 212–14.

[20] Linda T. Darling, *Revenue-Raising and Legitimacy: Tax Collection and Finance Administration in the Ottoman Empire, 1560–1660* (Leiden, 1996); H. İnalcık, 'Military and fiscal transformation in the Ottoman Empire, 1600–1700', *Archivum Ottomanicum*, 6 (1980).

life-time basis in return for a large initial fee to be followed by annual payments.[21] One rationale often offered for this system was that, by extending the term of the contract, the state hoped that the tax contractor would take better care of the tax source, most importantly the peasant producers, and try to achieve long-term increases in production. In fact, the *malikane* allowed the state to use tax revenues as collateral and borrow on a longer-term basis. In comparison to the straightforward tax-farming system, it represented an important shift towards longer-term borrowing by the state.

With the extension of their term and the introduction of larger advance payments, the long-term financing of these contracts assumed an even greater importance. The private financiers thus began to play an increasingly important role in the tax collection process. Behind the individual that joined the bidding in the tax-farming auctions, there often existed a partnership that included financiers as well as the agents who intended to organise the tax collection process itself, often by dividing the large initial contract into smaller pieces and finding sub-contractors. Non-Muslims were prohibited from holding most *malikane* contracts but Greeks, Armenians and Jews were very much part of this elite as financiers, brokers and accountants. These arrangements were mostly in the form of an Islamic business partnership involving both Muslims and non-Muslims.[22] Over the course of the eighteenth century, some 1,000 to 2,000 Istanbul-based individuals, together with some 5,000 to 10,000 individuals based in the provinces, as well as innumerable contractors, agents, financiers, accountants and managers controlled an important share of the state's revenues. This grand coalition of Istanbul-based elites and the rising elites in the provinces constituted a semi-privatised but interdependent component of the regime.[23] Many provincials were able to acquire and pass from one generation to the next small and medium-sized *malikane* shares on villages as long as they remained in favour with local administrators or their Istanbul sponsors. For both the well-connected individuals in the capital city and those in the provinces, getting a share of government tax revenues became an activity more lucrative than investing in agriculture, trade or manufacturing.

In the longer term, however, the *malikane* system did not fulfill the expectations of the central government. It actually led to a decline in state revenues because the state was unable to regain control of the revenue sources after the death of the individuals who had purchased them.[24] The central government thus began to experiment with other methods of tax collection and domestic borrowing as state finances came under increasing pressure from the 1770s onwards. After the end of

[21] M. Genç, 'A study of the feasibility of using eighteenth century Ottoman financial records as an indicator of economic activity', in Huri İslamoğlu-İnan (ed.), *The Ottoman Empire and the World Economy* (Cambridge, 1987).

[22] Çizakça, *A Comparative Evolution*, pp. 135–92.

[23] Ariel Salzman, 'An ancien régime revisited: "privatization" and political economy in the eighteenth century Ottoman Empire', *Politics and Society*, 21 (1993).

[24] Genç, 'A study of the feasibility', pp. 354–9.

the war of 1768–74, which had dramatically exposed the military as well as financial weaknesses of the Ottoman system, the financial bureaucracy introduced in 1774 a new and related system of long-term domestic borrowing called *esham*. In this system, the annual net revenues of a tax source were specified in nominal terms. This amount was divided into a large number of shares which were then sold to the public for the lifetime of the buyers. The annual revenues of the source continued to be collected by the tax farmers. The *esham* generally sold for six to seven times the annual net payments, which remained fixed.[25] As the linkage between the annual government payments to *esham* holders and the underlying revenues of the tax source weakened, the *esham* increasingly resembled a life-term annuity quite popular in many European countries of the period.

One motivation for the new system was to broaden the base of state borrowing and reach beyond the limited numbers of large financiers, who tended to dominate the *malikane* auctions, towards a larger pool of small and medium-sized lenders. However, the inability of the state to control or limit sales of the *esham* between individuals, and the difficulties in preventing the heirs of deceased holders from continuing to receive payments, seriously limited the fiscal benefits of this system. During the next half century, the state vacillated between abolishing the *esham* during periods of fiscal stability and expanding it when fiscal pressures mounted and additional funds had to be secured, with little regard for their long-term cost.[26]

In the early part of the nineteenth century, the centre, supported by the new technologies, was able to reassert its power over the provinces. After the central government began to undermine the power of the provincial notables in the 1820s and 1830s, many of the *malikane* contracts were pulled back to the centre and their revenues began to be collected once again by tax farmers. The *malikane* or the life-term tax-farming system was phased out in the 1840s as part of a larger package of administrative and economic reforms. With the same package of centralising reforms, the central government also attempted to eliminate short-term tax farmers. This last step failed, however, due to the administrative limitations of the central government. Short-term tax-farming continued until World War I. Nonetheless, the centralisation of the nineteenth century helped raise the central government's share of the tax revenues from about 2 to 3 per cent of the underlying economy (GDP) in the late eighteenth century to 5 to 6 per cent by the middle of the nineteenth century and to 10 to 12 per cent on the eve of World War I.[27]

The evolution of Ottoman tax collection institutions during the eighteenth century illustrates the state's ability and willingness to reorganise as a way of adapting to changing circumstances, albeit slowly and often with considerable time lags. This

[25] Yavuz Cezar, *Osmanlı Maliyesinde Bunalım ve Değişim Dönemi: XVIII. yy.dan Tanzimat'a Mali Tarih* (Istanbul, 1986), pp. 81–3; also M. Genç, 'Esham', *İslam Ansiklopedisi*, 11 (1995), pp. 376–80.

[26] Cezar, *Osmanlı Maliyesinde Bunalım*, pp. 128–34, 198–200.

[27] Based on series of central government budget documents and author's estimates of per capita income in the Ottoman Empire.

pragmatism and flexibility also provides important clues for understanding the longevity of the empire as well as the key position of the central bureaucracy until the end. In order to remain at the top, the central bureaucracy was thus willing to share the tax revenues with the provincial groups during the seventeenth and eighteenth centuries, until it was able to reassert itself in the nineteenth century.

This trajectory of Ottoman fiscal institutions also suggests that they were willing to borrow or adapt European customs and approaches prior to the nineteenth century. Despite growing research in this area, the causal connections between the evolution of Ottoman institutions of public finance as outlined here, and those in Europe, particularly in France during the seventeenth and eighteenth centuries, have not yet been investigated. The parallels between the two are quite striking, however. It appears that increasing economic and financial integration with Europe during the eighteenth century brought about significant changes in the institutions of public finance. In contrast, changes in the institutions of private finance during this period were limited to those employed by the Europeans and by non-Muslim subjects of the empire.

VI

From the 1770s until the 1840s the Ottoman state finances frequently experienced large budget deficits; these reached their peak during the 1820s and 1830s. In response, the state attempted to increase its control over revenue sources, made use of various forms of internal borrowing, and, when the short-term fiscal pressures mounted, resorted to debasements. The highest rates of debasement in Ottoman history took place during the reign of Sultan Mahmud II (1808–39). The timing and magnitude of these debasements suggest that the government was quite sensitive to the costs of debasements, especially the political opposition they generated amongst the janissaries and other urban groups.

Debasements had an impact on virtually all groups in Ottoman society and, in turn, each group took a position. Most men and women, both urban and rural, were clear about the consequences of different ways of dealing with the coinage, and who gained and who lost. The groups that stood to lose the most from debasements were those who were paid fixed amounts in terms of the unit of account. Most important groups in this category were the employees of the state, the bureaucracy, the *ulema* and especially the janissaries. There existed a large overlap between the guild members and the janissaries after the latter began to moonlight as artisans and shopkeepers in the seventeenth century.

Mahmud II was well aware of the constraints represented by the janissaries and related urban groups. From the very beginning of his reign, he wanted to replace the janissaries with a Western-style army. During the early years of his long reign, however, he did not have the political support to make this critical move. After the janissaries were finally defeated and the order was abolished in 1826, a major constraint in the way of debasements was lifted. Only two years later, the government began the largest debasement ever in Ottoman history, reducing the specie content of the *kurush* by 79 per cent within a period of four years.[28]

From the perspective of Ottoman economic and monetary history, the nineteenth century was a period quite different from the earlier era. On the one hand, it was characterised by major efforts at Western-style reform aimed at the centralisation of the empire, in administration, education, law and justice as well as economic, fiscal and monetary affairs. On the other hand, it was a period of integration into the world markets and rapid expansion in foreign trade, particularly with Europe. The Ottoman economy was increasingly transformed into an exporter of primary products and an importer of manufactures. The foreign trade of the areas within the 1911 borders of the empire, Macedonia, Anatolia and Syria, increased by about 15 fold between the 1820s and World War I.[29] This process was facilitated by the construction of ports and railroads and the establishment of modern banking institutions, mostly with European capital. As a result, the commercialisation of agriculture proceeded rapidly in Macedonia, western, northeastern and central Anatolia and along the Syrian coast. The rural population was drawn to markets, not only as producers of cash crops, but also as purchasers of imported goods, especially of cotton textiles. These developments substantially increased the demand for, and the use of, money, especially in these more commercialised regions.

For European governments, and especially the British who were concerned about Russian expansionism to the south, the success of Ottoman reforms was considered essential for the territorial integrity of the empire. European governments also believed that rapid expansion of commercial ties with Europe based on the principle of comparative advantage and European direct investment were essential for the development of the Ottoman economy. As a result, they began to exert considerable pressure on the Ottoman government to abandon debasements and establish a more stable monetary system. Bimetallism was proposed as a monetary regime that would bring the Ottoman Empire more in line with the prevailing international trends and help expand both trade and European investment. The European governments also linked Ottoman access to European financial markets to fiscal reform and monetary stability. They made clear that they were ready to provide the technical expertise necessary for this purpose.

Monetary conditions in the Ottoman Empire had assumed crisis proportions by the end of the 1830s. While the government had succeeded in raising short-term revenue from frequent debasements, the resulting inflation created political problems. The production of a large variety of coins since the beginning of the century and the inability of the government to retire the earlier series from circulation had added to the difficulties. These conditions created difficulties both for daily

[28] Pamuk, *A Monetary History of the Ottoman Empire*, pp. 193–200.

[29] C. Issawi, *The Economic History of Turkey, 1800–1914* (Chicago, 1980), chapter 3; and S. Pamuk, *The Ottoman Empire and European Capitalism, 1820–1913: Trade, Investment and Production* (Cambridge, 1987), chapter 1.

transactions and international trade. At the same time, the appeal and use of European coinage had increased especially in international trade and for store of wealth purposes. Under domestic and international pressure, the Ottoman government thus abandoned debasements and embraced bimetallism and stable coinage in 1844. It was hoped that this move would achieve greater price stability and help expand both trade and capital flows between Europe and the Ottoman Empire. The adoption of bimetallism did not mean the end of Ottoman monetary difficulties, however. The expansion of the empire's internal tax base by the commercialisation of peasant agriculture, the extension of cultivation on to unused lands and the development of other forms of primary production such as mining, proceeded only slowly. Moreover, a large fraction of the revenues collected from peasant producers continued to remain in the hands of tax collectors. At the same time, military expenditures continued to mount. Ottoman governments had difficulties balancing the budget and resorted to a variety of methods, both short and long term, to deal with the fiscal problems.

VII

The *sarrafs* of Istanbul were active in the financing of trade and in the guilds during the seventeenth century. In general, they were free to lend with interest. In the closing years of the century, they organised around a guild and began to move their businesses to Galata, a suburb of Istanbul outside the old city walls and across the Golden Horn.[30] While the Jews were not as prominent in moneylending and trade as they had been in the sixteenth century, Greeks and especially the Armenians, often in partnerships of two, emerged as the leading *sarrafs* of the capital city. The Greek financiers often took advantage of the prominence of Greek merchants in maritime trade in the Black Sea and the Balkans to specialise in the financing of international trade.[31] Similarly, the links of the Armenian *sarrafs* to the European commercial and financial networks through the Armenian communities there played an important role in their rise. They also remained well connected to the Ottoman bureaucracy. After Greek independence, the Armenians began to assume even more prominent positions. The leading Armenian *sarrafs* also assumed leading positions within the Armenian community (*millet*) in the Ottoman Empire, often mediating between the community and Ottoman officialdom.[32] In addition, many

[30] The guild of *sarrafs* had a membership of 72 around 1750 and 89 in 1835; A. Şahiner, 'The sarrafs of Istanbul: financiers of the empire', MA dissertation, Boğaziçi University, Department of History (1995), pp. 78–83.

[31] T. Stoianovich, 'The conquering Balkan Orthodox merchant', *The Journal of Economic History*, 20 (1960).

[32] Şahiner, 'The sarrafs of Istanbul', pp. 87–99; O. Jamgocyan, 'Les finances de l'Empire Ottoman et les financiers de Constantinople, 1732–1853', unpublished PhD dissertation, Université de Paris I, Panthéon-Sorbonne (1988), traces the lives and financial affairs of the leading Ottoman *sarrafs* through their correspondence with their European associates, by utilising the European archives.

financiers operated in the provinces, financing trade and the tax collection process just like their counterparts in the capital city.[33]

The Ottoman state had relied on the financiers in the capital for short-term loans and the financing of the tax collection process ever since the sixteenth century. After the shift from short-term tax farming to the long-term *malikane* system, the financing of the large advance payments had assumed even greater importance. The rise of the moneychangers (*sarrafs*) to prominence during the eighteenth century, and their transformation into large financiers known as the Galata bankers during the first half of the nineteenth century, was thus closely related to the financial difficulties of the state and its needs for short- and long-term finance.

On the face of it, the *malikanes* remained almost exclusively in the hands of the Ottoman *askeri* or state class, including palace women. Other social groups were usually not allowed to participate in the auctions. In many instances, however, the *malikanecis* who won the auctions were not involved in the day-to-day operations of the *malikane* after the initial auction. Behind them were often the financiers who loaned the money for the advance payment, arranged the sub-contracting of the tax farm and made the annual payments (*mal*) to the treasury. The net proceeds were then divided between the state, the *malikaneci*, the sub-contractors and the *sarraf*. The original purchasers of the *malikanes* thus turned into absentee owners of the tax farms. Murat Çizakça estimates that the central government received only about one-third of the net or about a quarter of the gross tax receipts under this system.[34]

During the course of the eighteenth century, these absentee purchasers of the *malikanes* began to develop portfolios of *malikane* shares rather than investing their capital in a single tax farm. Investors maintaining shares in as many as 20 to 30 tax farms were frequently observed, although each of them possessed sufficient capital to buy one or more tax farms in their entirety. The motive for this behaviour was risk minimisation through portfolio diversification.[35]

The state needed and encouraged the activities of the *sarrafs*. The growing fiscal difficulties after the 1760s raised their importance as direct lenders. In addition, their connections with the European financial groups enabled them to begin organising in Europe short-term loans to the Ottoman state. Many *sarrafs* also acted as personal financiers to the sultans and many of the leading Ottoman bureaucrats. In the aftermath of the French Revolution, these financiers were also able to replace the European merchants in Istanbul and assume control of important parts of the trade in bills of exchange.[36] From traditional moneylenders and brokers, the sarrafs of Istanbul thus developed into large-scale financiers with well-established international

[33] Genç, 'A study of the feasibility', pp. 347–54; and Çizakça, *A Comparative Evolution*, pp. 169–78.

[34] Çizakça, *A Comparative Evolution*, pp. 165–6; also Salzman, 'An ancien régime revisited', pp. 393–423.

[35] Çizakça, *A Comparative Evolution*, pp. 172–6.

[36] E. Eldem, 'La circulation de la lettre de change entre la France et Constantinople au XVIIIe siècle', in H. Batu and J. L. Bacque-Gremmont (eds.), *L'Empire Ottoman, la république de Turquie et la France* (Istanbul, 1986), pp. 87–97.

connections, forming the embryo of a financial bourgeoisie in Istanbul. In the process they began to be referred to as the Galata bankers, although they did not establish banks until the 1840s.[37]

The leading Armenian members of the guild of *sarrafs* often rose to positions of prominence in the empire, such as master of the imperial mint, during this period. This was at once a powerful and a dangerous position, however. While they were able to assume positions of power and leadership in both the bureaucracy and the Armenian community, many of these *sarrafs* eventually lost their lives, their wealth was confiscated and their families sent into exile after being held responsible for financial or monetary problems such as debasements or the poor quality of coinage. Others lost their offices and even their lives after being accused of enrichment during their public careers.

The Armenian Düzoğlu family originally controlled some of the foreign trade and manufacturing related tax farms. The management of the imperial mint was given to a member of this family during the reign of Mustafa III (1757–74). Family members retained control of the day-to-day activities of the mint until the 1820s. Their ability to mobilise credit for the state both domestically and abroad was a key reason for the continuation of their appointments to the imperial mint during this difficult period. It is thus clear that thanks to the skills and connections of the Armenian *sarrafs*, the responsibilities of the head of the Istanbul mint went beyond the supply of coinage, to include critical areas of state finances.

Artin Kazaz, who was born into a modest family in eastern Anatolia, took over the imperial mint in the 1820s, upon the dismissal of the last member of the Düzoğlu family. He soon emerged as the key advisor to the sultan in economic affairs and was instrumental in eliminating food shortages in Istanbul during and after the Russian war of 1828–9, by advising the sultan to lift the price ceilings (*narh*). Kazaz also used his connections to obtain short- and medium-term loans for the Ottoman government from private financiers in Europe. At the end of the Russian war, the Ottoman government had agreed to pay the large sum of 400 million *kurush* as reparations.[38] Even though the original amount was subsequently reduced after territorial concessions by the Ottomans and the tsar had decided not to press for the first payment, the Ottoman government was experiencing difficulties in putting together the second instalment. It was at this critical juncture that Kazaz, along with other financiers, succeeded in obtaining short-term loans from Europe.[39] When he died in 1834,

[37] A. Udovitch has referred to the financiers in the medieval Islamic world as 'bankers without banks'. This apt term also characterises the position of the Galata bankers before the 1840s. A. Udovitch, 'Bankers without banks: commerce, banking and society in the Islamic world of the Middle Ages', *Princeton Near East Papers*, No. 30 (Princeton, 1981).

[38] Stanford J. Shaw and Ezel Kuran Shaw, *History of the Ottoman Empire and Modern Turkey*, vol. II, *1808–1975* (Cambridge, 1977), p. 32. Annual revenues of the central government were close to 200 million *kurush* at that time.

[39] Haydar Kazgan, 'İkinci Sultan Mahmut Devrinde Enflasyon ve Darphane Amiri Kazaz Artin', *Toplum ve Bilim*, 11 (1980), pp. 122–5.

the sultan ordered a special funeral ceremony for the man who had provided indispensable services to the state at a very critical juncture.[40]

The growing influence of the *sarrafs* in trade and finance did not go unopposed, however. The growth of imports from Europe in the early part of the nineteenth century created enormous pressures for the declining guilds of the capital city. In addition, the debasements often associated with the Armenian masters of the imperial mint dealt serious blows to the guild membership and the janissaries. Since the seventeenth century, the overlap between the two groups had increased substantially as the soldiers began to rely increasingly on their second jobs to supplement their dwindling military pay. The rising tensions and occasional confrontations between these two groups and the financiers continued until the abolition of the janissaries in 1826.[41]

By the 1840s the ranks of the Galata bankers had expanded considerably to include more Jews and Levantines, Europeans who had settled in the eastern Mediterranean, as well as Greeks and Armenians. The abilities and connections of the Baltazzi, Camondo, Coronio, Eugenides, Mavrocordato, Mısırlıoğlu, Ralli, Zarifi and many other families to organise in Europe short-term loans for the Ottoman state had also grown substantially. In 1847, with the financial support of the government, Th. Baltazzi, from a prominent family of financiers, and J. Alleon, a member of a French banking family that had settled in Turkey during the French Revolution, finally founded Banque de Constantinople, the first bank of the Galata bankers.[42]

The financial power of the Galata bankers reached its peak around mid-century. In the meantime, however, the borrowing needs of the Ottoman state had expanded even faster. As a result, when the Ottoman government decided to turn directly to the European financial markets for its long-term borrowing needs, the Galata bankers began to feel the pressure of the more powerful European banks and bankers who began to open branches or establish banks of their own in the capital city as well as the provinces. The establishment, in 1863, by British and French capital of the Imperial Ottoman Bank, which would act a quasi-central bank for the empire in addition to its commercial operations, further consolidated the position of European capital in the Ottoman financial markets.

Even though they lost their unrivalled position, the Galata bankers were not easily pushed out of state lending or private finance. They entered alliances with European financial groups and opened new banks for lending to the Ottoman government, which continued to rely on them for short-term borrowing in between major bond

[40] Kazgan, 'İkinci Sultan Mahmut devrinde enflasyon', p. 119.

[41] H. Kazgan, *Osmanlıda Avrupa Finans Kapitali* (Istanbul, 1995), pp. 17–19.

[42] Hasan Ferid, *Nakid ve İtibar-ı Mali, 3. Kitab: Bankacılık* (Istanbul: Matbaa-i Amire, H.1334/1918), pp. 26–66; Kazgan, *Osmanlıda Avrupa Finans Kapitali*, p. 20; H. Kazgan, *Osmanlıdan Cumhuriyete Türk Bankacılık Tarihi* (Istanbul, 1997), pp. 25–32; and İ. Tekeli and S. İlkin, *Türkiye Cumhuriyeti Merkez Bankası* (Ankara, 1997), pp. 53–4.

issues in the European financial markets. During the crisis of 1875–81, when the Ottoman government declared a moratorium on debt payments and faced a costly war against Russia in both the Balkans and eastern Anatolia, the Ottoman Bank and the European financial markets refused to make new loans. The government then turned to the Galata bankers for the duration of the crisis. It is interesting that the Galata bankers, all of them Ottoman citizens, adopted a variety of patriotic Ottomanist themes to mobilise support for their centuries-old customer during this difficult period.[43]

VIII

One method of raising fiscal revenue which began to be used in 1840 was the printing and circulation in the Istanbul area of interest-bearing paper money called *kaime*. Since their volume remained limited, the *kaimes* performed reasonably well until 1852. A new phase in the history of the *kaime* began in 1852 when paper money that did not bear any interest was put into circulation for the first time. During the Crimean War large amounts of *kaimes* were printed and the market price expressed in gold liras declined to less than half the nominal value. One gold lira began to exchange for 200–220 *kurush* in *kaimes*. In 1861 a record volume of *kaimes* flooded the markets and the exchange rate against the gold lira plummeted to 400 paper *kurush*. The first experiment in paper money thus resulted, more than a decade after its initiation, in a major wave of inflation. With popular protests and general discontent, the government finally agreed to retire the *kaime* in 1862 with the help of short-term loans obtained from the Imperial Ottoman Bank.[44]

There was one other occasion prior to World War I in which the government resorted to non-convertible paper money. After the Ottoman government declared a moratorium on external debt payments in 1876, it became impossible to borrow from the European financial markets or the Imperial Ottoman Bank. With the Serbian uprising and the outbreak of war with Russia in 1877, the need to raise fiscal revenue became even more urgent. *Kaimes* were issued in both small and large denominations, and were proclaimed legal tender in all parts of the empire. Because of the large volume, however, the exchange rate of the *kaime* declined within two years to 450 *kurush* for the gold lira. They remained in circulation for almost three years and were retired at the end of the decade.[45]

In 1854, during the Crimean War, the Ottoman government began to sell long-term bonds in the European financial markets and this soon became the most

[43] Kazgan, *Osmanlıda Avrupa Finans Kapitali*, pp. 120–2; Tekeli and İlkin, *Merkez Bankası*, pp. 62–9.

[44] Ali Akyıldız, *Osmanlı Finans Sisteminde Dönüm Noktası: Kağıt Para ve Sosyo-Ekonomik Etkileri* (Istanbul, 1995), pp. 50–90; Roderic Davison, 'The first Ottoman experiment with paper money', in Osman Okyar and Halil İnalcık (eds.), *Social and Economic History of Turkey (1071–1920), Papers Presented to the First International Congress on the Social and Economic History of Turkey* (Ankara, 1980); M. Erol, *Osmanlı İmparatorluğu'nda Kağıt Para (Kaime)* (Ankara, 1970), pp. 5–7.

[45] Akyıldız, *Kağıt Para*, pp. 91–174; Erol, *Osmanlı İmparatorluğu'nda*, pp. 15–27.

important means of dealing with the recurring budgetary difficulties. In the early stages of this process, the Ottoman government was supported by its British counterpart and wartime ally, which guaranteed the first bond issue against the Ottoman annual receipts from the Egyptian tribute. In the following two decades, the Ottoman government borrowed large sums in London, Paris, Vienna and elsewhere under increasingly unfavourable terms. The net proceeds of these issues were directed almost entirely towards current expenditures, however. Only a small fraction was spent on infrastructure investment and on increasing the capacity to pay back. By the second half of the 1860s, Ottoman finances had deteriorated to the point where new bond issues had become necessary to maintain the debt payments. A moratorium was in sight but the financial markets kept the process going, lured by the unusually high rates of return.[46]

After the financial crises of 1873 led to the cessation of overseas lending by the European financial markets, the government was forced to declare in 1875–6 a moratorium on its outstanding debt, which stood at more than 200 million pounds sterling. After protracted negotiations, the Ottoman Public Debt Administration (OPDA) was established in 1881 to exercise European control over parts of Ottoman finances and ensure orderly payments on the outstanding debt, whose nominal value was reduced by approximately half during the negotiations.

In the same negotiations for debt resettlement, the nature of the new Ottoman monetary regime was also discussed. Following the lead of many European states during the 1870s, and under pressure from European interests, especially those of the creditors as represented by the OPDA and the Imperial Ottoman Bank, the Ottoman government moved away from the bimetallic system in 1881. The link between silver and gold was severed and gold was accepted as the standard for Ottoman currency. The government also decided to limit the supply of silver coinage. At the same time, however, the economy continued to rely heavily on silver for most daily transactions. The government did not have the reserves and financial strength to redeem the existing silver stock and move to a fully fledged gold standard. Receiving primary support from gold and partial support from silver, the Ottoman currency system thus became another example of the 'limping' standard (*topal mikyas*). Gold was at the centre of relations with the world economy, while silver fluctuated according to supply and demand in internal commerce. The *kurush* or piaster remained the basic unit of account for most daily transactions. In many ways, the emerging system was a compromise between the preferences of European interests and the realities of a low-income, agrarian country.

For the following three decades until the outbreak of World War I, a sizeable share of government revenues was controlled by the OPDA and applied to debt payments. This control and the regular payments on the debt were quite reassuring

[46] Christopher Clay, *Gold for the Sultan: Western Bankers and Ottoman Finance, 1856–1881* (London, 2000); for an earlier treatment, see D. C. Blaisdell, *European Financial Control in the Ottoman Empire* (New York, 1929).

for the European financial markets. As a result, the Ottoman government was able to resume borrowing towards the end of the century. With the rise in military spending, both external borrowing and the annual payments on the outstanding debt gained momentum after the turn of the century. The almost permanent search for new loans led, in turn, to new dependencies and complications in Ottoman foreign policy. On the eve of World War I, the volume of annual borrowing as well as the outstanding external debt had once again reached the unusually high proportions witnessed in the 1870s.

It may be useful to consider the long-term balance sheet for the mid-nineteenth-century regime change from debasements to stable currency and external borrowing. Relative monetary stability, rapid expansion of foreign trade and European direct investment should appear on the positive side. The annual rate of growth of Ottoman foreign trade averaged close to 5 per cent in real terms during the nineteenth century. There is also some evidence for economic growth in the period before World War I, which can be linked to the growing commercialisation of the Ottoman economy.[47] Monetary stability undoubtedly contributed to economic growth. At the same time, however, the default of 1875–6, the establishment of the Ottoman Public Debt Administration and the surrender of some of the leading sources of revenue to the European creditors in 1881 also suggest that the Ottomans paid a heavy price for borrowing large amounts from abroad before putting their fiscal house in order.

IX

Greater economic and financial integration with Europe meant that banks began to be established in the Ottoman Empire for the first time in the 1840s. Part of the demand for them came from the growth of trade with Europe and the financial needs of the merchants. In fact, the first bank to begin operations in the Ottoman Empire was the Commercial Bank of Smyrna which had been founded in London in 1844 by a group of English merchants to meet the growing needs of European and other merchants in the Izmir region. The bank was forced to close down during the financial crisis of 1847.[48]

For most of the banks established before the 1880s, however, lending to the state remained the more important part of their operations. The first bank to be established in the Ottoman Empire was Banque de Constantinople (Dersaadet Bankası), founded in 1847 with a capital of 200,000 pounds. The bank was to provide short-term loans to the government and stabilise the exchange rate of the Ottoman paper currency. The initiative and capital for the bank came from two of the leading

[47] Vedat Eldem, *Osmanlı Imparatorluğu'nun Iktisadi Şartları Hakkinda Bir Tetkik* (Istanbul, 1970), pp. 302–9; Osman Okyar, 'A new look at the problem of economic growth in the Ottoman Empire, 1800–1914', *The Journal of European Economic History*, 16 (1987).

[48] R. Kasaba, 'İzmir Ticaret Bankası', *Tarih ve Toplum*, 43 (1987), pp. 57–60.

Galata bankers. Because of the expansion in the volume of paper currency, however, the bank could not prevent the deterioration of the exchange rate for long. Due to the mounting losses and the inability of the state to continue to provide financial support for its activities, the bank was forced to close in 1852.[49]

Government efforts to establish another bank for its financial and monetary needs soon led to the formation of the Ottoman Bank by a British group in 1856, in the aftermath of the Crimean War. The bank obtained a royal charter in Britain and was founded in London with a capital of 500,000 pounds, but the centre of its operations was located in Istanbul. It was given permission to open branches in other cities of the empire, except in Egypt.

The continuing fiscal difficulties of the government soon forced it to seek a more powerful European institution. In 1863, the British owners of the Ottoman Bank were joined by a French financial group who took a 50 per cent share in the new Imperial Ottoman Bank. The new bank was managed by committees in London and Paris which directed the day-to-day administration in Istanbul. An important characteristic of the Imperial Ottoman Bank was its double nature, as a private Franco-British bank as well as a state bank at Istanbul. The bank was entrusted with most of the transactions of the state Treasury, in return for the obligation to provide certain short-term loans to the state. It agreed to help the state in withdrawing the existing paper currency and debased coinage from circulation. The Imperial Ottoman Bank also had a privileged position in the servicing of the external debt. Most payments of the Ottoman state on its outstanding external debt were handled by the Bank, which was to charge one per cent commission for this service. Finally, the Ottoman government promised not to issue any paper currency and the bank was granted the monopoly of issuing gold-backed banknotes. The Bank thus enjoyed unique financial and monetary privileges and was in a good position to derive maximum benefits from these circumstances.[50]

Until the middle of the 1870s, the continuing fiscal difficulties of the Ottoman government and the popularity of the high-interest Ottoman bond issues in the European financial markets made lending to the Ottoman state a very lucrative business. The Galata bankers tried to obtain a share of this market by forming alliances with British, French and Austrian financial groups and establishing a number of banks in the capital city. In addition to providing short-term loans of their own, these institutions played the role of intermediaries between the purchasers of Ottoman bonds and the Ottoman state, earning commission and interest from each

[49] Edhem Eldem, *A History of the Ottoman Bank* (Istanbul, 1999), pp. 29–126; A. du Velay, *Essai sur l'histoire financière de la Turquie* (Paris, 1903), pp. 126–9.

[50] A. Autheman, *La Banque Impériale Ottomane* (Paris, 1996), pp. 1–32; J. Thobie, 'European banks in the Middle East', in Rondo Cameron and V. I. Bovykin (eds.), *International Banking 1870–1914* (Oxford, 1991), p. 407; C. Clay, 'The bank notes of the Imperial Ottoman Bank, 1863–1867', *New Perspectives on Turkey*, 9 (1993); also A. Billiotti, *La Banque Impériale Ottomane* (Paris, 1909); and A. du Velay, *Essai sur l'histoire financière.*

transaction. Conditions were particularly favourable, the commissions amounting to between 10 and 12 per cent of the sums actually gathered.[51]

Although originally a Franco-British bank, the Imperial Ottoman Bank became more than 80 per cent French in the 1880s and the Paris Committee soon became the real decision-making body in its Ottoman affairs. The bank maintained its primacy in the market for Ottoman bonds until World War I. During this later period, however, its commercial and investment banking activities became increasingly more prominent. It developed an extensive network in the Ottoman Empire consisting of eighty establishments (branches and sub-branches) as well as others in Egypt and Cyprus. The Bank also supported and to some extent coordinated the activities of French capital groups, not only in the floatation of Ottoman bond issues but also in various direct investment projects, such as railways, ports, utilities, mining and insurance companies. In contrast, European direct investment in agriculture and manufacturing remained limited until World War I. As British capital and financial groups began to scale down their interests and investments in the Ottoman Empire after 1880, German groups, spearheaded by the Deutsche Bank, emerged as the main rival of French capital in these activities.[52]

After 1899 an intense competition developed between European commercial banks, both large and small, as many of them rushed to open branches in the Ottoman Empire. These banks aimed at drawing deposits from local customers to finance trade and agriculture. Most favourable conditions were offered to those possessing savings, to merchants, traders and local notables, as much to attract their deposits as to respond to their need for credit. While the Imperial Ottoman Bank was in a better position than any of its competitors, the new banks were also engaged in commercial operations, discounting commercial paper, offering terms of payment on bills of exchange.[53]

In addition to banks or branches of banks established by European capital, domestic groups founded a small number of regional banks in the 1880s. Numbers of Ottoman banks founded with domestic capital increased significantly after 1910 as a result of the policies of the Young Turk government that promoted the development of domestic capital and a Muslim-Turkish bourgeoisie. Four banks in Istanbul and two in Anatolia were established with the initiative and capital of domestic groups before World War I. These efforts reached a new stage with the establishment of the Osmanlı Itibar-ı Milli Bankası (Ottoman National Credit Bank) with a capital of 4 million lira in early 1917. It was hoped that this bank would play an important role in national economic development. There were also plans to convert

[51] Thobie, 'European banks', pp. 407–8, Tekeli and İlkin, *Merkez Bankası*, pp. 62–9.

[52] Eldem, *Ottoman Bank*, pp. 275–304; Thobie, 'European banks', pp. 413–37; Autheman, *La Banque*, chapters 6–11.

[53] Thobie, 'European banks', pp. 421–5; C. Clay, 'The origins of modern banking in the Levant: the development of a branch network by the Imperial Ottoman Bank, 1890–1914', *International Journal of Middle East Studies*, 26 (1994).

this institution into a state bank and let it assume the functions of the Imperial Ottoman Bank after the expiration of the latter's privileges in 1925.[54]

The most important domestic bank of the long nineteenth century, however, was the Agricultural Bank (Ziraat Bankası) established by the state in 1888 to support agricultural development through the extension of low-interest credit to cultivators. The origins of this institution went back to the Memleket Sandığı (regional fund) and the Menafi Sandığı (fund for public improvement) systems originated by the reformist governor Midhat Pasha in the Balkans during the 1860s and later duplicated throughout the empire. In an effort to make its facilities more widely available, the bank established more than 400 branches, more than any other financial institution. Although the bank as a credit institution could not meet the full needs of cultivators, it initiated an alternative to the high rates demanded by the traditional moneylenders. As one of the few indigenous banks in the empire, it was an important part of government organised efforts to finance economic development from domestic savings.[55]

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Institutions and institutional change have been identified by economists and economic historians as key variables that help explain the widely disparate economic performance of different societies over the last five hundred years. Based on the successful experience of Western Europe and European off-shoots, new institutional economics has argued that long-run economic growth is attained because the underlying framework persistently reinforced incentives for organisations to engage in productive activity.

Institutional economics and economic historians recognise, however, that a society rarely arrives at or creates institutions that are wholly conducive to economic growth. While focusing on the 'rise of the West', institutional economics and economic historians have paid less attention to studying unsuccessful or less successful cases of institutional change, especially those outside the Western European context. This study offers an alternative perspective.

For most of its 600-year existence, the Ottoman Empire, its economic institutions and policies were shaped to a large degree by the priorities and interests of a central bureaucracy. The influence of various social groups, not only of landowners, but also of merchants and moneychangers, over the policies of the central government, remained limited. Despite the general trend towards decentralisation of the empire during the seventeenth and eighteenth centuries, merchants and domestic

[54] Z. Toprak, *Türkiye'de Milli İktisat 1908–1918* (Ankara,1982), pp. 137–49; Tekeli and İlkin, *Merkez Bankası*, pp. 136–61.

[55] Donald Quataert, 'Dilemma of development: the Agricultural Bank and agricultural reform in Ottoman Turkey, 1888–1908', *International Journal of Middle East Studies,* 6 (1975), pp. 210–27; Y. S. Atasagun, *Türkiye Cumhuriyeti Ziraat Bankası 1888–1939* (Istanbul, 1939).

producers, who were the leading proponents and actual developers of mercantilist policies in Europe, never became powerful enough to exert sufficient pressure on the Ottoman government to change or even modify these traditional policies.

Nonetheless, the Ottoman state and society showed considerable ability to reorganise as a way of adapting to changing circumstances from the seventeenth century to the nineteenth century. With its pragmatism, flexibility and habit of negotiation, the bureaucracy managed to contain many challenges, both internal and external, and succeeded in maintaining a traditional order. Pragmatism, flexibility, willingness to negotiate, and ability to adapt their institutions to changing circumstances, were traits that enabled the Ottomans to retain power while managing a transition to modern centralism in a period when many of their contemporaries in both Europe and Asia were unable to do so. Ultimately, however, pragmatism and flexibility characterised their response, and change was allowed only as far as necessary for the defence of the traditional order.

Institutional change did not apply equally to all areas of Ottoman economic life. Moreover, not all types of institutions were affected to the same degree by these changes. Because the central bureaucracy was able to retain its leading position in Ottoman society and politics, the influence of various social groups, not only of landowners but also of merchants, manufacturers and money changers over economic matters, and more generally over the policies of the central government, remained limited until the end of the empire. As a result, most of the pragmatism and flexibility was utilised by the central bureaucracy for the defence of the traditional order and its own position in that order. In contrast, institutional changes that threatened the leading position of the central bureaucracy were resisted more forcefully than others. Institutional change thus remained selective and many of the key institutions of the traditional order, such as state ownership of land, urban guilds and restrictions on private capital accumulations, remained intact until the nineteenth century.

This article has examined the long-term changes in the Ottoman financial, fiscal and monetary institutions from this perspective of pragmatism, flexibility and willingness to change in defence of a traditional order. Ottoman institutions of private and public finance retained their Islamic lineage and remained mostly uninfluenced by the developments in Europe until the end of the seventeenth century. Money was used widely both by the urban and rural population. Neither the Islamic prohibitions against interest and usury nor the absence of formal banking institutions prevented the expansion of credit in Ottoman society. The Ottoman government relied on tax farming during this period for both tax collection and short-term borrowing purposes, as had been the practice of most Islamic states.

European institutions of both private and public finance began to grow in influence during the eighteenth century. The evolution of Ottoman institutions of public finance during the period 1650 to 1840, from short-term tax farming to lifetime tax farms to government borrowing with tax revenues as collateral and finally to government bonds, was especially remarkable. The striking similarities between this trajectory of Ottoman institutions and the evolution of the European institutions of public finance, especially those of *ancien régime* France, need further scrutiny from historians.

With the onset of the Ottoman reform movement called *Tanzimat* and greater economic interaction with Europe during the nineteenth century, institutional change accelerated. Ottomans adopted a variety of modern fiscal, monetary and financial institutions up to the First World War. They struggled to centralise tax collection and increase revenue. The attempt, in the 1840s, to replace tax farming with direct state collection of agricultural and other taxes was not successful, however. Attempts were also made to move towards a more stable monetary regime. Debasements were abandoned in favour of bimetallism during the 1840s and the Gold Standard after 1880. The local financiers began to be replaced by modern banks, both European and Ottoman. The Ottoman economy also attracted substantial amounts of European direct investment until World War I, mostly in railroads, ports and other infrastructure. A stock exchange was opened in Istanbul in 1873.

Rising military expenditures and the mounting costs of centralising reform during the nineteenth century can all be viewed as the rising costs associated with keeping the disintegrating empire together. The budget deficits were financed mostly with debasements until the 1840s. After the Ottomans decided to embrace bimetallism and stable coinage, only one alternative remained for the finance of budget deficits: external borrowing. Ottoman borrowing in the European financial markets after 1854 led to a default in the 1870s and partial control of state finances by European creditors. Despite experimentation with different fiscal strategies, the inability to bring state finances under control during the nineteenth century thus proved to be the major, if not fatal, weakness of the Ottomans.

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