Contributions to Economics

Mehmet Baha Karan
Wim Westerman
Jacob Wijngaard

A History of Banks

From the Knights Templar to the Present Era

Springer

Contributions to Economics

The series *Contributions to Economics* provides an outlet for innovative research in all areas of economics. Books published in the series are primarily monographs and multiple author works that present new research results on a clearly defined topic, but contributed volumes and conference proceedings are also considered. All books are published in print and ebook and disseminated and promoted globally. The series and the volumes published in it are indexed by Scopus and ISI (selected volumes).

Mehmet Baha Karan · Wim Westerman ·
Jacob Wijngaard

A History of Banks

From the Knights Templar to the Present Era

Springer

Mehmet Baha Karan
Department of Business Administration
Hacettepe University
Cankaya, Ankara, Türkiye

Wim Westerman
Faculty of Economics and Business
University of Groningen
Groningen, The Netherlands

Jacob Wijngaard
Faculty of Economics and Business
University of Groningen
Groningen, The Netherlands

ISSN 1431-1933 ISSN 2197-7178 (electronic)
Contributions to Economics
ISBN 978-3-031-62296-0 ISBN 978-3-031-62297-7 (eBook)
https://doi.org/10.1007/978-3-031-62297-7

This Springer imprint is published by the registered company Springer Nature Switzerland AG
The registered company address is: Gewerbestrasse 11, 6330 Cham, Switzerland

Preface

Most of this book was originally written by Mehmet Baha Karan and published under the title "Para Banka ve Finansın Sırları: Tapınak Şövalyelerinden Modern Çağlara[1]" (Secrets of Money, Banking and Finance: From the Knights Templar to the Modern Ages) in 2022. He translated the Turkish text 1:1 into English, but felt that it should be taken out of its domestic context and that the cases described should also cover the last 100 years and developed. That is how Wim Westerman and Jacob Wijngaard became to be involved with the book. In the person of Johannes Glaeser, we found an enthusiastic supporter at Springer and this is how the project started. Soon, the authors found out that they could not write a text covering everything and that it would still be interesting to a broad public. Actually, this constraint, while being somewhat painful, helped us to keep on track in terms of both timing and content. We decided to merely focus on the most important banking episodes and to cover the recent period in a condensed way.

Writing is much about rewriting, and this counts even more for the present text. We wanted to agree on every word, despite our differing backgrounds. Mehmet Karan is proud to be from Turkey, and the other two authors are from the Netherlands. Jacob Wijngaard is specialized in supply chain issues and currently finds himself being involved with the design of future monetary systems. Mehmet Karan and Wim Westerman have a corporate finance and financial markets background, and Mehmet Karan also has a strong base of experience in energy finance and economics. Understandably, our political, cultural, and religious backgrounds differ, but perhaps surprisingly our values have much in common. Moreover, the three of us share an interest in case studies and feel that they can help to sketch a general picture. Finally, we agree that facts are first in science and that the reader should decide for herself, but science is by no means value-free, so we should not try to hide our own opinions.

Here it is, our book. If anything, we dedicate it to the people who showed us how decent banking works. We had them in mind, trying to honor them. Having said this, the book is actually written for you in person, whether you are a banker,

[1] Karan, Mehmet Baha. (2022). Para Banka ve Finansın Sırları: Tapınak Şövalyelerinden Modern Çağlara. Scala Publishing. ISBN-13: 9786057110107.

a financial economics or management professional, a policy maker, a student, a lecturer, a researcher, or just a curious individual. If you like to read about the history of banks rather than of banking systems, want to know how banks relate to authorities, are interested in what people actually do rather than in how markets function, and wonder about how the miracle of thousands of years of banking has come around, this book is especially meant for you.

Ankara, Türkiye	Mehmet Baha Karan
Winschoten, The Netherlands	Wim Westerman
Assen, The Netherlands	Jacob Wijngaard
April 2024	

Contents

Chapter 1
Introduction: The Origins and Fundamentals of Banking

1.1 The Magic of Manhattan

At 8:45 a.m. on September 11, 2001, John Murphy, CEO of Oppenheimer Funds, was jogging in Manhattan's Battery Park, as usual, thinking about what he would address at his firm's reorganization meeting that afternoon. Suddenly, he heard an explosion. When he looked up, flames rose from the upper floors at the north tower of the World Trade Center (WTC), one of New York's most symbolic buildings. The first thing that came to his mind was a plane crash. He thought that, fortunately, the plane didn't crash into the South Tower; his office and 598 employees were there. However, just about fifteen minutes later, what he feared would come to pass, and a plane would crash into the South Tower (Argenti, 2002). Little later, other targets, including the Pentagon, would also come under attack. Al-Qaeda terrorists attempted to damage American capitalism by attacking landmark buildings in the Wall Street area and discrediting the financial system. The WTC's Twin Towers symbolized globalization and America's economic power and prosperity. Al-Qaeda hoped that attacking these American symbols would create widespread fear across the country, particularly in the financial markets, and severely weaken the US position in the world community. The United States was not the only country affected by the attacks. It created a snowball effect; stock exchanges, banks, and financial companies worldwide, including the London Stock Exchange, would be closed for a week due to fear of terrorism. The New York Stock Exchange was experiencing a long-term shutdown for the third time. The first occurred at the beginning of the First World War, and the second happened in March 1933, during the Great Depression.

In 2001, while gold prices rose 30%, stocks sharply declined globally in almost every stock market (Makinen, 2002). The attack on 9/11 was a complete disaster. Thousands of people, including many bankers and financial managers, died in this attack. Fortunately, for John Murphy, no Oppenheimer Funds employees were among them. Still, many financial firms, such as Cantor Fitzgerald Securities and Fuji Bank, were not so lucky (Casualties of the September 11, n.d.). John Murphy, who could not

M. B. Karan et al., *A History of Banks*, Contributions to Economics,
https://doi.org/10.1007/978-3-031-62297-7_1

recover from the event's influence for a long time, participated in the documentary film project "Rebirth" for the victims of September 11 ten years later and said that this terrorist attack exemplified the resilience of the human spirit (Stabile, 2011).

The WTC was located at the southwestern tip of New York City, Manhattan Island, near the shore of the Hudson River, a few blocks away from Wall Street. The city, particularly Manhattan, is known as the world's cultural, financial, media, and entertainment capital. It also hosts the United Nations headquarters. Also, many multinational media conglomerates are headquartered in Manhattan, and the borough has been the scene of numerous books, movies, and television shows. The Manhattan district has been cited as the economically most powerful city and the world's leading financial and fintech hub. Wall Street is in Manhattan's financial district, symbolizing globalization, high finance, and investment. The Street is home to the New York Stock and Nasdaq exchanges, the undisputed leader worldwide regarding average daily share trading volume and total market capitalization of its listed companies. Hundreds of financial centers' representatives worldwide and all major banks and players in financial markets are located on Wall Street. News agencies such as Bloomberg and Reuters constantly transmit developments on Wall Street to their audiences. Although the WTC is not located on Wall Street, the Twin Towers characterized the power of the finance sector, and an attack on the WTC is an attack on the financial sector.

The term "Wall Street" was originally used to refer to the elite large group of independent brokerages that dominate the US investment industry. But today, it also includes the largest investment and commercial banks, hedge funds, mutual funds, wealth management firms, insurance companies, brokers, currency and commodity traders, and financial institutions. Although many of these organizations are headquartered in other cities such as Chicago, Boston, and San Francisco, the media still refer to the US investment and financial industry as Wall Street. With the increase in the power of the USA after the Second World War, the world's most important financial institutions and stock markets began to take place on Wall Street. While the USA is the most powerful economy in the world, the Federal Reserve Bank has become the world's central bank, with the dollar being the reserve currency. Financial institutions on Wall Street provide various financial services to investors and can reach all countries directly or indirectly. Here, all short-term and long-term monetary transactions can be made, and all transactions that investors will be interested in, from stocks to bonds, from spot transactions to the most complex derivative transactions, can be made in the stock markets where trillions of dollars are traded. So, Wall Street is indeed the center of the Western world. Like the other financial centers, Wall Street has the best commercial and communications infrastructure where people conduct huge volumes of international and domestic trading transactions (Fig. 1.1).

Wall Street, where the slave trade took place in the seventeenth century, takes its name from the wall built by the Dutch in 1653 to protect its colony against English forces. This narrow, short street runs just seven blocks from Broadway to the East River in the southern part of Manhattan in New York. A bull statue placed two blocks south of Wall Street also attracts the attention of visitors. The bull symbolizes a strong stock market in which participants are optimistic and confident (Brooks, 1999). Along with the statue of the bull, the magnificent buildings and the New York

Fig. 1.1 : Wall Street, New York City https://commons.wikimedia.org/wiki/File:Wall_Street,_New_York_City.jpg

Stock Exchange stress the power of the financial sector. These buildings, which are also illuminated at night, bring to mind the phrase "Money never sleeps," as said by Gordon Gekko, the unforgettable character in the movie "Wall Street" (1987) starring Michael Douglas. The impressive skyscrapers in the financial centers are not exclusive to the USA; a similar image is valid for London, Frankfurt, Tokyo, and even Dubai. All these financial centers spread a sense of immunity to its surroundings. It looks as if the world is controlled here. Not only do their buildings stress the power of banks, but the rumors about banks are just as effective. Conspiracy theories claim that they shape world politics; they are behind the scenes in wars, revolutions, and turmoil worldwide. There is a widespread belief that the financial lobby rules the world (Farrell, 2013). Is it really so? How does it work?

The power of the financial world suggested by Wall Street, the City of London, and other financial centers contrasts sharply with the volatility of the financial processes and the fragility of the supporting organizations. Finance and accounting experts know that banks' balance sheets differ entirely from those in the industrial and commercial sectors. Since the financial ratios showing the financial performance of banks are different from the others, banking companies are analyzed separately from companies in other sectors. The specificity of bank financial structures comes from two essential features of banks. Firstly, banks' equity is very low relative to the total assets. While the ratio of a typical company's equity to its total assets is 30–70%, this ratio is as small as 5–10% for banks. Banks' primary source of funds is deposits and loans from other institutions. Banks record such funds as assets and give them to companies as loans. They have to keep some of their assets as cash reserves to meet the cash demands of their customer. When the average maturity of their resources and the average maturity of their assets do not match, a significant jump in interest or exchange rates endangers the bank's life.

Banks are institutions operating with a low capital base, which makes banks very sensitive to financial turmoil. Since a strong wind in the economy can destroy their equity immediately, they are greatly affected by crises in the market and their related non-performing loans. Moreover, since banks trade money, they can quickly lose their equity due to corruption and employee mistakes. Banks sometimes get greedy and self-destruct by entering high-risk business ventures, as Lehman Brothers did in 2008. The second feature of banks is that they have to repay their money when depositors demand it. In other words, the bank can hardly make long-term investments but keep cash reserves to repay the money at any time. In 2023, New York-based Signature Bank went bankrupt when depositors quickly withdrew their money. In banking jargon, this is called a "bank run". In this case, no bank can cover such great demand. All these features make banking more fragile than other sectors.

Banking crises injure not only the banking industry but also the whole economy. The bankruptcy of one bank can lead to a general decrease in the credibility of banks and the spread of this distrust to other banks. Depositors withdraw their money from the distrusted banks and, possibly, out of the country. The spread of such insecurity will cause a collapse in the country and the onset of a significant economic crisis by affecting the country's payment system. So, regulations are required to support the power of the banks and simultaneously prevent them from getting into a very risky position. These regulations support the fragile financial structures of banking, make it difficult for banks to go bankrupt, and ensure the stable functioning of the monetary system. It is a fact that the regulations for banks are stringent and heavy. Since this fragile structure of banks is known, they are subject to national and international regulations not seen in any other sector. Ironically, banks are not free to go bankrupt. The whole society depends on a stable financial system.

In an economy without banking, there are no intermediary activities, and the wheels of the whole economy will stop. Therefore, laws often prohibit the spreading of negative news or rumors about banks. Even mentioning such a possibility may harm a country's economy. In addition, banks conduct close business transactions with so-called near-banks, mutual fund partnerships, insurance companies, and even stock exchange organizations. A climate of insecurity can have pervasive consequences on them. For this reason, the asset-based interests of banks on their "reputation," "fame," and "wealth" have been deemed necessary to be specially protected

(Saritas, 2010). The financial system is delicate and needs protection because we depend on it.

There is some bitter irony in this: the destruction of the WTC was an attack on the heart of the financial system; it had a terrible impact, but the financial system itself recovered soon, while seven years later it appeared that the system almost destroyed itself. While regulations protect banks from bankruptcy, they can also reduce their profits by chaining their activities. So, banks tried to stretch these chains and circumvent or even eliminate them. That fueled the growth of banks and the economy, but made the system more fragile and vulnerable to shocks. Toward the end of 2007, many banks in the US came to the edge of bankruptcy. Timothy Geithner was president of the Federal Reserve Bank of New York then, and hence the supervisor of many of the big New York banks, e.g., Citibank (see Chap. 10). He saw how they had stretched the regulations and how that had caused the problems. In September 2008, Lehman Brothers collapsed because of too heavy involvement in the subprime mortgage crisis, causing a wave of new problems. It brought the system to the brink of a total meltdown, notwithstanding the involvement of the Fed and Treasury. In his memoirs, Geithner (2015) describes how he concluded that most of the banks were "too big to fail" and that the best way to proceed was to do whatever was possible to save them, also the banks that behaved irresponsibly. Even replacement of the bank management was not possible because it would create too much turmoil. That was what happened. Geithner was first involved as President of the New York Fed and from 2009 as Secretary of the Treasury.

If a bank has come to the edge of bankruptcy, central banks lend to save that institution; if this support is insufficient, the Treasury can directly intervene to the rescue. Banks may cover the losses with the people's taxes. The book "Too Big to Fail" by Andrew Ross Sorkin, describing the 2008 financial crisis and the collapse of Lehman Brothers, reveals the discourses between Wall Street CEOs and government officials. This book, later filmed, describes how the public had to bear the losses of poorly managed banks (Sorkin, 2009).

1.2 What Are the Tasks of Modern Banks

For a flourishing society, it is necessary to be able to settle and pay transactions. We need money for that, only bartering is very inconvenient. There are three types of money, coins, produced and issued by the Mint, banknotes issued by the Central Bank, and bank money, i.e., demand deposits, organized by the banks (Galbraith, 2017). Bank money is the most common form of money, certainly for the larger transactions. Banks create money while doing their regular business of taking deposits and making loans. For example, when you get a loan to buy a car, the bank opens an account for you, and money that did not exist before is deposited into your account. The amount deposited into this new account is the new money created by the bank. The cash amount will increase when you pay with this money by depositing it into the car dealer's bank account. When the car dealer uses this money to repay his debts, the amount will grow again. There is a well-known anecdote about this. John comes to a town hotel as a tourist and likes the room shown to him; he pays a 100-dollar deposit to the hotelier to keep the room for a few hours. Then, John leaves the hotel to consult his friends who are waiting nearby. When the hotel owner receives the money, he transfers it to the account of the greengrocer, whom he has owed money for a while. When the greengrocer sees the $100 in his statement, he pays the wholesaler in the primary vegetable market. The wholesaler happily takes the money and pays the prostitute he was with before, and the prostitute deposits her debt to the hotel's bank account. A few hours later, John returns to the hotel and demands his $100 deposit back, saying his friends prefer another hotel. The hotelier pays John the $100 credited to his account. Although the hotelier could not earn money at the end of this transaction, everyone in the town paid their debts due to the money created. When this process is done continuously by all banks, the amount of money made in the country will increase. When this situation comes to the point where the value of the money decreases, the Central Bank will step in. To stop the money supply that creates inflation, it takes the excess cash from the system by selling treasury bills to the market with an appropriate interest rate. If the liquidity in the market is insufficient, the Central Bank does the opposite of this process; that is, it gives cash to the market by purchasing back the treasury bills it sold before.

According to a famous professor at Harvard University, John Kenneth Galbraith, the money creation process of banks is so simple that even the mind does not accept it. Bankers love to use jargon such as letters of credit, forwards, and swaps that the ordinary person may not understand. They probably feel that people respect terms they do not understand and that it contributes to the image of a magic, powerful, unassailable, and trustworthy financial system. Professor Galbraith has been telling an anecdote about George W. Ball, a lawyer who started as a banking associate at Lehman Brothers in the 1960s. After seeing the profession's appeal, he said, "Why hasn't anyone told me about banking before?" (Galbraith, 2017).

Banks and other financial corporations provide a range of financial services: money transfer, foreign exchange, lending and borrowing, insurance, and trade in financial products. And there are many different financial products. Some follow right away from the execution of real transactions; others are intended to hedge the risk of real transactions. For all these transactions, it holds that intermediate parties temporarily possess the assets involved. That is why the whole system is threatened by uncertainty. If such a party goes bankrupt during the transaction, it leads to severe losses for the other parties. The transactions are halted because of the threat. Even a normal bank payment is not completely instantaneous and risky, therefore. Suppose actor **A**, with a deposit from bank A, wants to pay actor **B**, with a deposit from bank B. Then bank B may receive the money just before it goes bankrupt, blocking the further transfer. Geithner (2015) refers to the use of Repo's to organize daytime credit for security trading. A Repo is a repurchase agreement. The borrower sells some securities contracting that they can repurchase them at the end of the day, and they do that day after day. But what if there is a threat that the borrower is bankrupt during the day? The whole system stops if there is a broad risk of bankruptcy. It is very common for a third party to service this repeated sale and repurchase, but that makes the whole situation even more sensitive to bankruptcy risks. Regulations are necessary to limit that risk. The government has to establish and maintain those regulations.

We will describe several banking episodes in this book, starting with the Knights Templar in this chapter and finishing with Citibank and the Financial crisis of 2008 in the last two chapters. The tensions between the government, on the one hand, and banks or other financial intermediaries, on the other hand, are an essential element in the context of all these banking episodes. This field of tension changed dramatically between the Middle Ages, the age of the Knights Templars, and 2008, the start of the financial crisis, but the heavy interdependence remains. We give an impression of the development of banking through the ages and provide also attention to this field of tension between banks and governments.

1.3 Banking from the Ancient to Medieval Times

1.3.1 Roman Banking

The history of banking goes back further than the Middle Ages. To stress this, we give an impression of banking during the Roman period. The Mediterranean region was the most important trade center of the ancient times. From 700 BC to the first centuries AD, the Mediterranean experienced steady economic growth, particularly maritime trade. Economic activity in this period was dazzling; it could only be reached in the early modern era. While very different peoples belonging to other religions, cultures, races, or tribes lived in the regions on this trade route connecting the East and the West, the trade of goods and money developed. With the conquests of Alexander the Great, trade became even more open in the Mediterranean world. In the eastern sea basin, Greek became the language of international trade, as Latin would in the western one (Curtin, 1984). The power of the Roman Republic and later the Roman Empire brought the stability (the Pax Romana) necessary for the trade to develop. As Thomas Hobbes wrote in 1631, "*If a covenant be made, wherein neither of the parties performs presently, but trust one another; in the condition of mere nature... upon any reasonable suspicion, it is void: but if there be a common power set over them both, with right and force sufficient to compel performance, it is not void. For he that performeth first, has no assurance the other will perform after; the bonds of words are too weak to bridle men's ambition, avarice, anger, and other passions, without the fear of some coercive power*." (Farrell, 1984).

A single state's unification of the Mediterranean Basin ameliorated economic conditions in practical ways: monetary and metrological systems were standardized, removing costly trade barriers. Legal rules were also standardized, which held the potential for an even more significant transaction-cost-reducing effect.

The first bankers, who took deposits from customers and used some money to make loans, were known as 'trapezites' in Athens in the second half of the fifth century. The word denoted that their work was "trapeza" (literally 'table'). Similar professionals first settled in the Forum in Rome between 318 and 310 BC (Andreau, 1999).

Millett (1991) categorizes financial loans and transactions in the fourth century BC Greece into three groups: (a) non-profit interest-free loans based on personal and social relationships; (b) loans and transactions made for some fee but only occasionally carried out by anyone without any financial expertise, i.e., non-professional interest-only loans; (c) 'professional money lending'. According to Millett, the last category falls into two groups. The first group includes transactions carried out by specialized financiers, who in some cases were profit-seeking and competent businessmen, but not practicing any urban profession, e.g., members of the elite who lent part of their wealth at interest to generate income or increase their inheritance; the second group includes professional men, moneylenders/bankers (trapezites and argentarii in Rome), merchants and wholesalers, who also engaged in financial business. Millett believes that the practice of free lending was widespread in Athens and was based on relationships of kinship, neighborhood, and civic solidarity (Andreau, 1999).

In Rome, bankers carried out the following activities: the assaying of coins; foreign exchange; the raising of credit and the collection of money at auctions; the taking of deposits, which formed the basis of bank accounts and the payments made by moneylenders/bankers; the advancement of loans; and all other transactions arising from the above. Verboven (2020) documents the existence of banker guilds in Rome and Ostia from the second and third centuries (AD) onwards. Rome had four banking-type professions: Argentarii, Nummularii, Coactores, and Coactores Argentarii. Argentarii were free citizens, independent of the state, and belonged to a guild that accepted a limited number of new members. There were also slaves who were argentarii, mainly belonging to the imperial family. But most of these argentarii slaves were goldsmiths or silversmiths, not bankers or coin assayers. The primary function of the Argentarii was deposit banking. They regularly attended auction sales to advance credit to buyers. Nummularii limited themselves to assaying coins and changing money. Subsequently, they became deposit bankers, like the Argentarii. By the middle of the second century (BC), a third group of professionals emerged. These were called Coactores. These were not bankers, but private buyers who received commissions on the sums they held for their clients. Finally, a fourth profession emerged in the first century (BC), the Coactores Argentarii, who were buyers, moneylenders/bankers. None of these bankers were women. Probably the profession of Argentarius was officially forbidden to women (Andreau, 1999).

There were two differences between Italy (Rome) and the non-Latin-speaking states, like Greece. In the Greek world, professional bankers were never regularly involved in auctions. Auctions were held in Greece, and buyers were free to borrow money to pay sellers for their purchases, however, trapezites did not take part in these sales. The second difference concerns the geographical distribution of these professions. While the Latin-speaking world adopted Italian tradition and seems to have been relatively homogeneous in this respect, regional peculiarities are striking in the Greek part of the Empire, especially in Egypt and Palestine.

No argentarii were documented in Italy after the early years of the third century (AD). With this disappearance, the word argentarius, used alone, came to be used for a different profession, the silversmith. Later, these silversmiths, known as argentarii, began to carry out money exchange and banking transactions (Andreau, 1999).

In Greco-Roman antiquity, especially in Italy, it was very common to sell goods at auction. All kinds of goods were auctioned in ports, fairs, wholesale and retail markets, at harvest times, as were estates, slaves, etc. Announcing an auction was a good way to advertise a sale. It was useful after a death, when heirs wanted to sell their jointly owned inheritance. Collateral for those who could not pay their debts was also sold at auctions. Cicero's correspondence gives several examples of auctions following a death in the family. It was the crier, the praeco, who presided over such auctions and gave the objects to the highest bidders. At auctions, there were money buyers (coactores), who did not lend money but received a commission for taking the money from the buyers and passing it on to the sellers. Where both seller and buyer were constantly on the move (as with itinerant merchants and absentee landowners), the services of a buyer became even more indispensable. A buyer was officially responsible for keeping detailed records (tabulae auctionariae or auctionales) of these auctions, noting dates, detailed descriptions of the objects sold, prices, and the names of sellers and buyers (Andreau, 1999).

The study of epigraphic records reveals the regular presence of private bankers in urban environments and marketplaces, some of whom were involved in auctions linked to the sale of specific goods. Examples from the city of Rome include a group of coactores and argentarii who dealt with fish auctions. However, professional bankers were rarely involved in the financial affairs of members of the socio-economic elite, such as the auctions of manors and patrimonial goods reported in Cicero's Correspondence. The receipts of the tabulae ceratae of L. Caecilius Iucundus (reign of Tiberius and Nero) found in Pompeii in 1875 represent the most revealing testimony to Roman professional bankers preserved. The coactor argentarius participated in organizing auctions, opened deposits, and provided loans to buyers (Morcillo, 2008).

Argentarii, coactores argentarii and (later) nummularii accepted deposits. One of the most essential activities of bankers was lending. Bankers were not averse to lending beyond a fraction of the funds entrusted to them. Sometimes, by special authorization, they also managed properties for their clients. Almost all we know about loans made during this period is when their repayments were due. They were due in a few months or, at most, a year. When a client was involved in a lawsuit, a banker's account book was required by law to be produced, even if it did not involve the banker personally (Andreau, 1999).

Credit for auction sales was very important for the argentarii, but banking in ancient Rome was more than that. The banker did not only lend his own money, but also some of the money he received from his customers. Once the customer deposited his money with the banker, he could leave it on deposit, withdraw it at any time, or ask the banker to pay him with it. For instance, according to Andreau (1999), the bankers applied interest on some of these deposits. There is no documentation on the interest rate charged. However, it is clear that bankers profit from their banking by charging a lower interest rate on customer deposits than they do on loans to those in need. A customer could withdraw his deposit all at once or little by little. He could also visit the bank with one of his creditors and ask the banker to pay him or—in some cases—send his creditor to the bank himself. In the latter case, the customer would give the banker a payment order and the creditor, if not recognized by the banker, would come to the bank with some kind of token by which he could be recognized. One type of deposit was a sealed deposit, also known as a regular deposit. These deposits, sometimes in the form of coins, sometimes in the form of goods or documents, had to be returned to their owners untouched by the person who accepted them as deposits. The depositor did not have the right to use the money or object or to earn a return by investing it. Such a deposit was kept in a sealed sack. When a text mentions the delivery of money in a sack to a person (in sacculo dare), it usually means the delivery of a sealed deposit. The point is that while there is no doubt that argentarii, coactores argentarii, and (later) nummularii accepted unsealed deposits, it is not certain that jurists recognized the existence of an irregular deposit contract to support this financial practice. Many legal historians believe that no such contract existed in the second and third centuries and that a deposit in a bank was legally recognized as a loan. Although some evidences indicate that the first traces of deposit banking date back to the Middle Ages, there is no consensus among historians on this issue. A few check-like practices have been found in the eastern Mediterranean. There are also examples of money transfers from one customer to another.

Apart from the bankers described above, four other groups in ancient Rome were engaged in finance. These were the entrepreneurs, usurers, high-interest moneylenders, and merchant-financiers. The entrepreneurs had strong social relationships. They were not only very socially mobile but also technically and professionally mobile. Their financial situation and cultural background allowed them to avoid any profession other than large-scale wholesaler or ship-owner. Their active lives were, therefore, much more flexible and versatile than those of professional bankers. Some had an inheritance that consisted partly of real estate and partly of movable assets. They managed the money of senators and nobles, looking for the best way to manage their inheritance. They adopted a profit strategy and took risks to succeed in their speculations. In private finance, they openly practiced lending practices, using both their funds and those of their friends and contacts. Moneylenders, on the other hand, included commercial financiers. They operated as both wholesalers and financiers, lending to merchants. There is limited information about high-interest lenders. Four wall inscriptions testify to their presence in Pompeii. The fourth category, merchant-financiers, mostly financed a one-way or round trip with a commercial loan, usually between a moneylender and a wholesaler or a ship-owner (Andreau, 1999).

In 1959, a building was discovered about 160 m south of the Stabiae Gate in Pompeii. The writing tablets in this building constitute the third major group of tablets found in towns in the Vesuvian region. They are known as either the Agro Murecine tablets, or the Murecine (the name of the place where they were found) tablets, or the Sulpicii archive, as the Sulpicii, a group of businessmen from Puteoli, guarded them. These tablets undoubtedly constitute examples of commercial loans granted in connection with activities in the port of Puteoli. The findings indicate they were involved as an intermediary in a maritime loan. The evidence is strong enough to dispel all doubts. Secondly, the Murecine tablets show that the Emperor's entourage and the retinue of some senators deposited money through the financiers of Puteoli. These investments are indicated in the Sulpicii archive. Several imperial slaves or freedmen lent money to Sulpicii or merchants in Puteoli. The Murejine tablets provide information about the role played by the warehouses where the collateral for these loans would be kept, as well as about the private grain trade. Thirdly, the tablets are concerned with the security of loans and the legal means of securing this security. If the money lent was not repaid, the creditor could put the property he had pledged as collateral or up for sale and cover his expenses from the price paid at the sale. If the sale proceeds exceeded the debt amount, he would transfer the excess to the debtor. The loan agreement would include the possibility of an auction, which would provide ample publicity for the sale (Andreau, 1999).

1.3.2 From Rome Until the Crusades

With the official acceptance of Christianity by the Roman Empire in 379 AD, religious pressures started on those who traded money in exchange for interest, and banking activities gradually disappeared. However, some still exchanged money with interest, primarily the Jews. Since Christians were banned from usury during this period, Jews became indispensable as moneylenders. While they could not lend money at interest to other Jews because of their religion, they could lend money to those of other faiths. They, therefore, filled a critical gap in the financial system. They provided much-needed capital for businesses and personal loans. They also performed banking practices such as deposit banking, currency exchange, and issuing of promissory notes. In addition, Jews traded various goods in local and interstate commerce. They were vital in establishing trade routes along the Silk Road, linking Europe to the eastern countries.

First, there were also Syrian and Greek merchants, but these turned their attention to the Eastern Roman Empire, and the Jewish merchants expanded their activities and dominated international trade with the Middle East (Jewish Virtual Library, n.d.). The concentration of Jews in trade and banking was a combination of push and pull. They were pushed from other areas, not being allowed to own land or become a member of guilds, but they were also pulled to such work because, in that way, they could use their lead in education. It was also more profitable (Botticini & Eckstein, 2003).

The Western Roman Empire collapsed in 476 AD. During the rule of the Merovingian kings (from 481), the Jews probably collected taxes and made advances on revenues to high officials, but they had to hide their activities due to Church pressure. The most powerful state in Western Europe after the collapse of the Western Roman Empire was the Holy Roman Empire under Charlemagne in the early ninth century and developing before. Charlemagne was rather tolerant with respect to Jewish contributions to economic development. It was a matter of pragmatism. They depended on the Jews for contacts with the Middle-Eastern trade centers. During the Carolingian dynasty, the Jews spread further over Western Europe, with the Rhineland as basis. A special community of Jews associated with the trade with the East is the community of the Radhanites. The travels of the Radhanites are described by a contemporary Muslim official from Iran (Ibn Khordadbeh, around 870). He wrote that there were four trade routes, from the Rhone valley all the way to China's east coast, and that they traded in slaves, furs, silk and swords (going east), cinnamon and other spices, and camphor (going west) (Radhanite, n.d.). There was only a fragmented legal framework for the role of the Radhanites. It relied mainly on their reputation.

1.3.3 Trust, Reputation and the Maghribi Merchants

There is another community of Jewish merchants that has been used extensively in the literature to investigate how it was possible to develop international trade in medieval times, when there was no integrated legal system. Trust in their dependability was provided by their reputation. Maintaining this reputation was also important for the community that provided the services, e.g., the Radhanites (early medieval Jewish merchants) and the Maghribi. Maghribi Jews were ethnic Jews who had traditionally lived in the Maghreb region of North Africa (al-Maghrib, Arabic for "the west") under Arab rule during the Middle Ages (yadvashem.org, n.d.). It was for these communities a very rational policy to develop and protect this reputation. At that time, there was great uncertainty about trade between countries, the duration of the ship's voyage, the conditions of the arrival of the goods, and the price; it was not clear which goods would be sold at what cost for example, the journey from Egypt to Sicily could take 13–50 days, and ships did not always reach their destination. The goods inside the vessels were not well protected and were often damaged in transit, and there was always the possibility that the ship's captain could extort the goods. If merchants did the shipment themselves, their business would suffer as they would be on boats or on the road for months. Therefore, merchants had to work with intermediaries. However, these intermediaries had to be reliable and reputable. They could confiscate the merchants' goods and not pay them. It was impossible to rely on the countries' laws in the trade carried out in such a large area. There was no legal mechanism to enforce the implementation of the contracts with intermediaries. The only thing one could do was to believe in their intermediaries and trust them. Over time, the intermediaries understood that their reputation was much more valuable than the money made in the short run. If this reputation were lost, no one would give them goods or cash for their trade (Buckley & Nixon, 2009).

Around AD 1055, Abun ben Zedaka, a Maghribi merchant living in Jerusalem, was an intermediary for African trade. Although successful, it turned out that he was probably overly ambitious or embezzling the other Maghribi merchant's money to meet a need. When the corruption was learned by other Maghribi merchants with whom he was doing business, he faced a considerable backlash. Those around him and the merchants with whom he did business in Sicily stopped trading with him. No one, not even his friends, could conduct a commercial transaction. Because this person was doing dishonest things as an intermediary, no one wanted to share the responsibility of their business by doing business with him. It would also not put any pressure on the intermediary. In particular, the sanction excluded a dishonest intermediary from that market. Where the law could not protect traders, the only thing to rely on was the community's or diaspora's rules. These rules were also tried to strengthen the merchants' reputations. Thus, nobody would work with Zedaka, as no one would want to sacrifice the lucrative mutual partnerships (Greif, 1993). Undoubtedly, economic sanctions were significant for this mechanism to work. Everyone would make money together, or all would be on their own. Avner Greif's work suggests that complex social networks and diasporas can create reputation-based enforcement mechanisms if formal rules do not work. These unique contractual enforcement mechanisms replaced a proper legal system. Greif's research showed that other institutions, like diasporas, besides courts and the rule of law, can support economic growth. Interestingly, Edwards and Ogilvie (2008) challenged Greif's views and argued that Maghribi traders had no more 'collectivist' cultural beliefs than their European counterparts. However, Greif (2008), on the other hand, challenged their argument by defending her views with some evidence.

Organization theory predicts that when cooperation leads to efficiency gains that the market and the legal system fail to capture, "private order" economic institutions will be established. Since agents were employed by Maghreb merchants and "trust" prevailed in agency relations, it is plausible that they would have established a "private order" institution. Reputation in repeated contractual relationships could provide the basis for such an economic institution. Theoretically, two types of reputation mechanisms can be distinguished in relation to agency relationships. The first allows an agent to signal that he is trustworthy because he fears God or because he has internalized the ideology of honesty. The second mechanism allows an agent to determine in advance that it is most profitable to be honest. The merchant, knowing this mechanism, will be able to trust the agent. Relations of diasporas rely upon the second mechanism and improve reputation among the merchants (Greif, 1989).

In the first decade of the eleventh century, Samhun ben Da'ud, a leading merchant in Tunis, sent a long letter to his business partner Joseph ben Awkal of Fustat. The letter is a historical document that reflects the merchants' awareness of the importance of the implied contract in governing their relationship. In this document, Joseph makes this clear when he makes his future dealings with Samhun dependent on her track record: "If you conduct my business properly, I will send you goods." The linking of future relationships to past behavior, i.e., the essence of reputation mechanisms, is well captured in this example. According to this letter, Joseph believed that Samhun was not sending his revenues on time and subsequently imposed economic sanctions by not providing him with agency services (Greif, 1989).

The diaspora connection enabled traders to reduce the transaction costs associated with agency relationships by reducing the wage premium that had to be paid to keep an intermediary honest and the cost of not working through intermediaries in relationships previously known to be short-lived. The traders' shared religious-ethnic origins created natural boundaries for the diaspora and gave credibility to its own traders and intermediaries. On the other hand, it motivated them to preserve their distinct identity within the Jewish world (Greif, 1989).

1.4 Banking in Medieval Times and the Knights Templar

From the third to the eleventh century, the church's prohibition of interest was quite effective and a significant institutional structure couldn't emerge in Europe except for individual money exchange or secret usury activities. However, the beginning of the Crusades created a significant change in Europe and the Middle East and increased the need for banking. This gap was to be filled by an organization that no one expected at the time. This organization was the Knights Templar.

The idea of the crusades began with the rise in self-confidence of the Christian world. The threat of more Moorish victories in Spain and France was gone and the invasion of Vikings and Huns had ended. But there were new threats form the East. The Seljuk Turks defeated the Byzantine army in Anatolia at the battle of Manzikert (1071) and continued their advance from the east. Pilgrimage to the Holy Land was complicated and dangerous. The Byzantine emperor Alexios I, who had established a good political relationship with the Pope, responded to Pope Urban II's appeal for his support. The Pope's aim was not only to capture Jerusalem by defeating the Muslims but also to control the "Heretical" Eastern Christians who did not adopt Catholic thought and to unite the Christian world under the Papacy. The Crusades were the largest and most comprehensive military campaigns of the Middle Ages and took place in a historical period of religious bigotry, greed, and poverty. In total, eight major Crusades were organized between 1096 and 1291. These bloody, violent, and often brutal conflicts were crucial to world history. They strengthened the position of European Christians for the first time, making them essential players in the territorial struggle in the Middle East. During these expeditions, tens of thousands of Europeans went to the Middle East, wars took place, and lands and cities changed hands. Beyond being a series of religious expeditions between Christians and Muslims to secure control of the holy places, this series of wars had significant cultural, sociological, and economic consequences. It began in 1099 when Christian armies conquered Jerusalem during the First Crusade and took it from Muslim control. Thus, groups of pilgrims from all over Western Europe began to visit the Holy Land. These pilgrims included soldiers, nobles, knights, and various groups of unarmed people who wanted to fulfill their religious duties. However, in the conditions of the time, it was not easy to reach the Middle East from Europe; the roads passed through lands inhabited by Muslim countries and peoples. Moreover, pilgrims traveled among deserters, and bandit groups, and many of them were robbed and killed during their journey. Thus, a number of problems related to the safety and health of Christian pilgrims arose during this period.

The Order of the Knights Templar was founded in 1118 by a French knight, Hugues de Payens, to protect the pilgrims who wanted to visit Jerusalem during the Crusades. They gained the support of the Pope as a religious order. The Templars got their name from their headquarters on the Temple Mount of Solomon in Jerusalem. Next to the Templars, there were the Knights Hospitaller and the Teutonic Knights, together the three great Masters or Houses. They played essential roles in logistics, health, and war issues in the Crusades. Each of these left their mark on history with different characteristics. However, the Knights Templar, the Crusaders' most important military and logistics power, established the first bank-like institutional organization in history.

Hugues de Payens, together with eight knights, with the support of Baldwin II, the ruler of Jerusalem, established a headquarters on the Temple Mount, where the Temple of Solomon was located. The knights quickly gained the official approval of the Catholic Church and the support of Bernard of Clairvaux, a prominent abbot, thanks to their demonstrated skills. When the Order started, the Templars were nothing more than a group of poor monks, but they became a powerful organization as their support grew. In his order rule, Bernard of Clairvaux described these warring men as monk warriors, calling them "*Knights of Christ*". The Templars and other Orders initially considered their mission to fight to protect pilgrims in the Holy Land. They said they would carry out this task by adhering to the three traditional vows of the Church known as poverty, chastity, and obedience like other orders. While maintaining them, the Templars would also take up arms and stand up to the threats posed by the infidels. In Bernard's words, "*They would have to be gentler than the lambs, but tougher than the lions.*" (Bellitto, 2017).

With the support of Bernard, the Templars gained land in many areas all over the world (Fig. 1.2). The most essential lands held by the Templars were in France, given by the King of France. They had also established a network of land and property in Ireland, England, Spain, Portugal, Italy, Hungary, Germany, and even as far as Cyprus. The Templars were skilled, resourceful people. The Order managed their holdings to maximize income and became excessively cash-rich and property-rich. By the thirteenth century, they had also developed the skills to move their wealth around in their territory. We know that during the Fifth Crusade from 1213 to 1221, the Pope used the Templars as tax collectors to reach different regions. Templars owned large tracts of land in Europe and the Middle East, were involved in manufacturing and import/export, and maintained a fleet of ships. The Templars operated a large logistics organization that grew in Europe to sustain the warriors in the Holy Land. It is estimated that at its peak, the order had 9,000 estates from Syria to Scotland; it also controlled ports and had a vast fort that served as its financial center just outside the walls of Paris (Wu, 2019).

The Knights Templar organization served as a military force in Europe and the Middle East for nearly two hundred years. At the Battle of Montgisard in 1177, they proved that a small force could defeat a much larger enemy under the right conditions. On the other hand, they became increasingly involved in logistics and finance operations (Fig. 1.3).

The success of the Templars depended heavily on their institutional structure as a multinational order of Christian monks maintaining high values. The members were highly reliable, reputable, creative, and flexible. Underlying the success of the Knights Templar was the rapidly growing trade in Europe and the Middle East due to

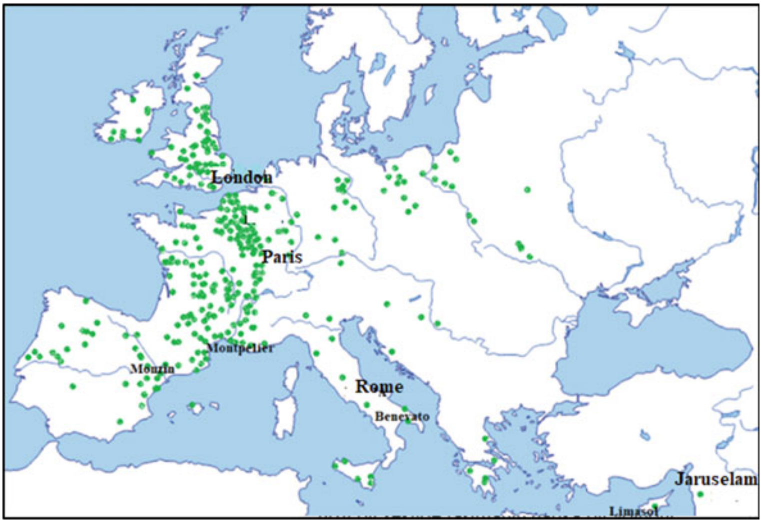

Fig. 1.2 Templar bases in Europe. *Source* It is redrawn by the author. https://en.wikipedia.org/wiki/List_of_Knights_Templar_sites#/media/File:Templerorden_in_Europa_1300.png

the crusades to the Holy Country of Palestine. The Templars were a critical institution that kept a social balance between kings and people. They inspired modern banking with corporate insights far beyond their contemporaries, leaving significant traces for 200 years.

This issue is especially evident in the relationship with the Church as an institution that carries out financial transactions. The Knights Templar were not affiliated with any country; their only link was to the Pope and the Church. They attached great importance to their relationship with them. Since the Templars were religious people, they tried to live up to their vows, paid attention to the relationship between worldly and spiritual affairs, and tried to act morally. Their relations with the Popes were excellent until their last days. In the latter's eyes, they were the guardians of Christianity. They especially cared about staying away from interest and usury, which the Church forbade. However, we know that not using interest in banking and money matters was not technically easy, and this issue was also very delicate for the Church. Therefore, the Templars needed more pragmatic interpretations. They had easy access to these comments and they discovered banking practices similar to Islamic finance methods used today to obtain the Pope's indulgence. While the Church was against the practice of interest, the Western and Eastern Churches' practices differed. In the East, moderately controlled lending was considered better than too strict control with no effect, especially for commercial ventures. In the Byzantine Empire at the beginning of the tenth century, Leo VI allowed lending with interest no higher than about 6% for most loans, and loans for high-risk commercial ventures were even allowed at 12% (Maniatis, 2016). Since the Templars in the West also developed other ways to cover the cost of the debt, they were not at odds with the

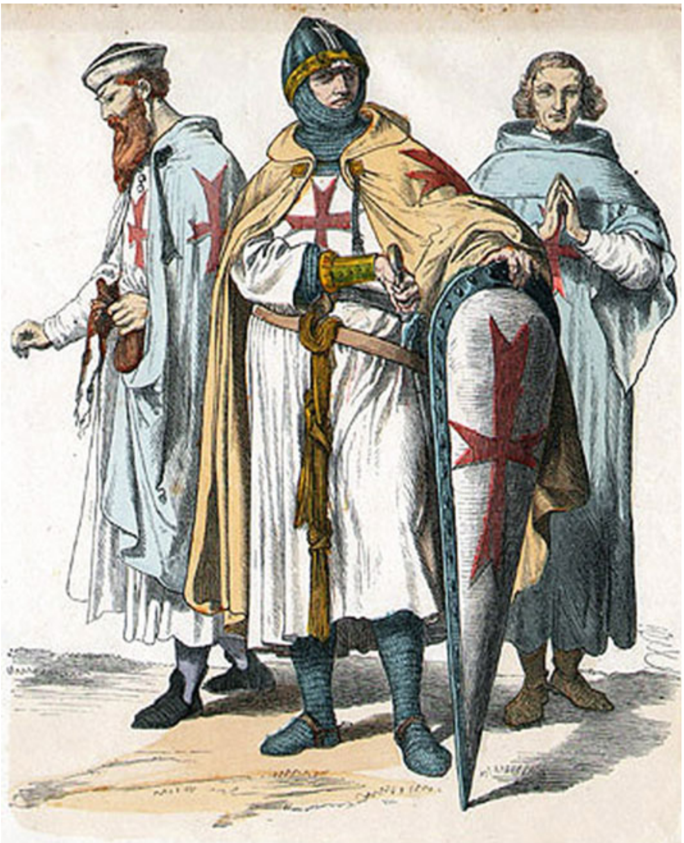

Fig. 1.3 Knight Templars (11–12th Centuries) https://commons.wikimedia.org/wiki/File:Knights-templar.jpg

Church. For example, some Templar loans in the South of France included a clause in the loan agreement that if the coin lost value between the time the loan was granted and the time of repayment, the borrower had to add a fixed amount to compensate the lender. Since the fixed sum would remain the same no matter how much the coin depreciated, an interest charge was likely embedded in this fixed sum. Again, if the land was pledged as collateral for the debt, the terms of the loan could stipulate that the produce from the land was not included in the repayment of the debt, but was an extra for the lender (Nicholson, 2014).

The Templars showed a similar flexible behavior while working with kings, especially the Kings of France. They met their special requests, lent them money, and rushed to the aid of the Kings, stretching their principles. In 1148, when King Louis VII of France arrived in Jerusalem, having lost most of his army and all of his treasury in a disastrous land crusade, the Knights Templar lent him so much cash to cover his expenses during his stay in the Holy Land that it brought the Order to the brink