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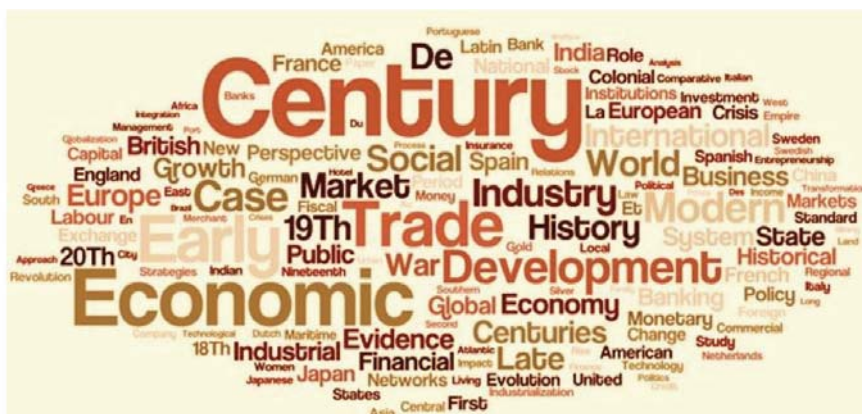


# Economic History Working Papers

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## The Money Doctor Raimundo Fernández Villaverde and the Classical Gold Standard in Spain

Pilar Nogues-Marco



## The Money Doctor *Raimundo Fernández Villaverde* and the Classical Gold Standard in Spain

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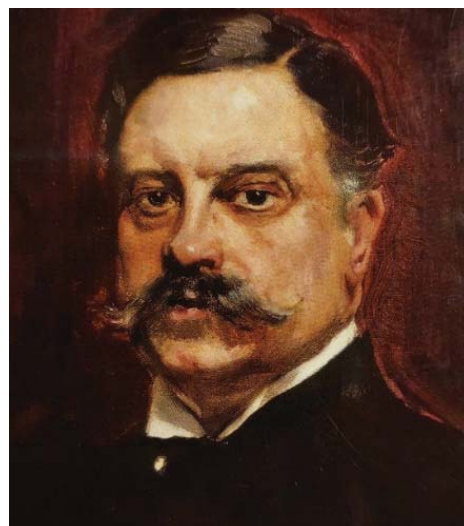
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### Abstract

This paper focuses on the Money Doctor Raimundo Fernández Villaverde, a prominent politician during the Restoration of the Bourbon monarchy in Spain during the Classical Gold Standard period. He reformed the fiscal system and proposed monetary reforms to transition Spain to the Gold Standard after the 1898 Cuban War of Independence.

His monetary reform ultimately failed due to two primary reasons. Firstly, there was a lack of political consensus, as politicians were more inclined to prioritise the distribution of spoils to sustain unstable alliances forged by local political leaders and their clientelist networks, rather than focusing on the development of long-term policies aimed at achieving party political goals. Secondly, the resistance from the Bank of Spain to reduce the circulation of banknotes to deflate the economy, with the aim of preserving its profits as a private institution that distributed dividends to its shareholders, took precedence over its role as the guarantor of exchange rate stability.



Villaverde portrait. Oil painting by Joaquín Sorolla. Madrid (1901). The Congress Palace.

**KEYWORDS:** Money Doctors, Gold Standard, Monetary Orthodoxy, Exchange Rate Stability, Monetary Reform.

**JEL codes:** **B31:** History of Economic Thought. Individuals. **E42:** Monetary Systems. **E58:** Central Banks and Their Policies. **N13:** Monetary Economics. Europe: Pre-1913

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## **1. The Money Doctor *Raimundo Fernández Villaverde*. A Biography within the Spanish Political Regime of Restoration**

The political regime of Spain during the Gold Standard period was a parliamentary monarchy resulting from the Restoration of the Bourbon dynasty (1876-1923). The primary objective of this political regime was to provide stability and overcome the major political turbulences that had occurred during the nineteenth century, which included three civil wars, numerous coups d'état and drastic changes of political regimes. Under this system, both the Crown and the Parliament shared sovereignty. The Parliament was composed of two chambers: the Congress and the Senate. The Congress was elected by citizens possessing the right to vote, consisting of major taxpayers' suffrage until 1890 and universal manhood suffrage from then onwards, albeit characterised by electoral fraud executed by compliant judges and town councillors. The Senate, on the other hand, was comprised of notables, some appointed for life by the Crown, and others elected by the State Corporations to represent the most prestigious religious, intellectual, and military institutions, as well as the major taxpayers.

The Restoration was a political system characterized by ensuring the alternance of power between the two main parties: the Conservatives and the Liberals, referred to as the "peaceful alternance" (*turno pacífico*). When the ruling party underwent a process of political attrition or lost the confidence of Parliament, the King would summon the leader of the opposition party to form a new government. Subsequently, this new government would call for elections to secure a sufficient parliamentary majority for stable governance. The alternance of power worked effectively when the incoming party could secure a favourable parliamentary majority in advance, and the outgoing party understood that the relinquishment of power was only temporary.

The party structure consisted of factions formed by local political leaders and their respective clientelist networks. The primary role of the party leader was to maintain cohesion among the different factions of the party by ensuring a balanced distribution of spoils. In cases where satisfactory alliances were not reached, the dissatisfied factions could voice their discontent in Parliament. If a party lost internal cohesion while in government, the King would withdraw his confidence, prompting the opposition to form a new government and organise new elections. Consequently, the distribution of spoils to sustain unstable alliances forged by local political leaders was more important than the elaboration of long-term policies to achieve party political goals (Jacobson and Moreno-Luzón 2000 for an overview).

The Restoration regime witnessed a high degree of political alternance. The position of President of the Government, referred to as Presidency of the Council of Ministers at that time, changed hands 30 times between 1875 and 1913 (see Table 1 for details). However, the number of individuals occupying the Presidency was significantly lower, totalling 17 Presidents during this period, as some Presidents served for multiple alternating terms. For instance, between 1875 and 1902, the Presidency was primarily held by Canovas (Conservative) or Sagasta (Liberal), amounting to nearly 25 years, with only five other individuals briefly holding the position during this period. The party leader needed to possess sufficient charisma to control the party's factions. During the last quarter of the nineteenth century, Canovas and Sagasta were the undisputed leaders. However, internal divisions within their respective parties escalated after their deaths, particularly following Canovas' assassination in 1897. Consequently, the number of individuals occupying the Presidency was higher between 1902 and 1913 than it had been between 1875 and 1902, making the implementation of long-term policies even more challenging at the beginning of the 20th century.

TABLE 1: PRESIDENTS DURING THE RESTORATION, 1875-1913

Number	Date of Crisis	Outgoing President	Party
<b>Reign of Alfonso XII</b>			
01	12-09-1875	Canovas	Conservative
02	02-12-1875	Jovellar	Conservative
03	07-05-1879	Canovas	Conservative
04	09-12-1879	M. Campos	Conservative
05	08-02-1881	Canovas	Conservative
06	13-10-1883	Sagasta	Liberal
07	18-01-1884	Posada Herrera	Liberal
08	27-11-1885	Canovas	Conservative
<b>Regency of Maria Cristina</b>			
09	05-07-1890	Sagasta	Liberal
10	11-12-1892	Canovas	Conservative
11	23-05-1895	Sagasta	Liberal
12	04-10-1897	Canovas	Conservative
13	04-03-1899	Sagasta	Liberal
14	23-10-1900	Silvela	Conservative
15	06-03-1901	Azcarraga	Conservative

Number	Date of Crisis	Outgoing President	Party
<b>Reign of Alfonso XIII</b>			
16	06-12-1902	Sagasta	Liberal
17	20-07-1903	Silvela	Conservative
18	05-12-1903	F. Villaverde	Conservative
19	16-12-1904	Maura	Conservative
20	27-01-1905	Azcarraga	Conservative
21	23-06-1905	F- Villaverde	Conservative
22	01-12-1905	Monero Ríos	Liberal
23	06-07-1906	Moret	Liberal
24	30-11-1906	L. Domínguez	Liberal
25	04-12-1906	Moret	Liberal
26	25-01-1907	Vega Armijo	Liberal
27	21-10-1909	Maura	Conservative
28	09-02-1910	Moret	Liberal
29	14-11-1912	Canalejas	Liberal
30	27-10-1913	Romanones	Liberal

Source: Martorell Linares (2012), p. 144

Additionally, changes in the composition of the cabinet under the same Presidency were common, as governments often resulted from fragile compromises among various party factions. This made the Government even more subject to change than the alternating Presidency. In the same period, from 1874 to 1913, there were a total of 49 Ministers of Finance, resulting in an average tenure of only 10 months (Martínez-Ruiz and Nogues-Marco 2018: 9). This high turnover significantly affected governmental actions, as many governments avoided essential economic reforms to prevent parliamentary rejection, which would lead to the removal of the minister who had championed the proposal and sometimes even the entire Government (Martorell Linares 2012). Villaverde was an exception as he laid the foundation for orthodox monetary reform.

Raimundo Fernández Villaverde, Marquess of Pozo Rubio (a nobility title acquired through marriage), was the Minister of Finance who proposed the fiscal, financial, and monetary reforms to adopt the Gold Standard in Spain after the shock caused by the 1898 Cuban War of Independence. He was born in Madrid in 1848, the son of an academic and politician, he was involved political life from a young age. He graduated in Administrative, Civil and Canon Law in 1868, and later earned a Doctorate in Law. He began his career as a lecturer in the Law School and worked as a lawyer in a law firm. He was a member of the Royal Academy of Jurisprudence and Law from 1869 (serving as its President from 1900 to 1902), a member of the Royal Academy of Moral and Political Sciences from 1888, and a member of the Royal Spanish Academy from 1902.

Villaverde embarked on a long political career within the Conservative Party, serving as a member of Parliament from 1872. He held various positions, including Councillor of Madrid (1875), General Director of Madrid Government (1877), Auditor General of the State Administration (1878), Secretary of the Ministry of Finance (1880), Deputy Secretary of State for Finance (1884), Civil Governor of Madrid (1884), Minister of the Interior (1885) and Minister of Justice (1890). He served as Minister of Finance twice, in 1899 and 1902. During his first term, he implemented a fiscal reform aimed at balancing the fiscal budget, restructuring sovereign debt, and reforming taxation under the Presidency of Silvela, who led the Conservative Party after the assassination of Canovas. Villaverde resigned in 1900 due to significant social resistance to the fiscal reform. His second term lasted only a few months between 1902 and 1903. Finally, between 1900 and 1905, he served as the President of the Congress of Deputies on several occasions and held the Presidency of the Government for two brief periods: from July to December 1903, when he resigned after failing to secure support for the approval of the Budget, and then from January to June 1905, when he was ousted from office by Parliament. In 1903, he proposed a Bill to adopt the Gold Standard in Spain. However, the Bill ultimately failed, and Spain

never adopted the Gold Standard. Villaverde passed away in 1905, just one month after resigning from the Presidency (Comín 2002, Serrano Sanz 2005).

## 2. Monetary Writings of Raimundo Fernández Villaverde

Raimundo Fernández Villaverde's writings primary consisted of speeches delivered in Parliament or academic institutions such as the Royal Academy of Jurisprudence and Law and Royal Academy of Moral and Political Sciences. His work focused on legal and economic topics related to trade, sovereign debt, fiscality and money (for a comprehensive overview on Villaverde's monetary writings, see Sabaté Sort and Serrano Sanz 2006; a list of Villaverde's writings can be found in the section titled "Raimundo Fernández Villaverde's Writings" at the end of this chapter).

His significant contributions to the field on monetary issues included:

- *La cuestión monetaria* [**The Money Issue**] (1890).
- *Sobre el estado anormal de los cambios 1891-1892* [**On the Abnormal State of the Exchange Rates**] (1893).
- *El problema del cambio en España* [**The Problem of Exchange Rates in Spain**] (1901)
- *Proyecto de Ley para regularizar y mejorar el cambio exterior y para procurar el restablecimiento de la circulación y de la libre acuñación de la moneda de oro* [**Bill to Regularise and Improve Foreign Exchange and to Restore the Circulation and Free Minting of Gold Coin**] (1903) (This work was also published in French by the *Economiste Européen*)

Fernández Villaverde's monetary writings aimed to propose solutions for stabilising the exchange rate following two critical currency crises of the period, those of 1891 and 1898 (for detailed information on these currency crises, see Martínez-Ruiz and Nogues-Marco 2014). The first two contributions, "The Money Issue" (1890) and "On the Abnormal State of the Exchange Rates" (1893), were related to the 1891 crisis. "The Money Issue" was a public lecture delivered by Villaverde at the Royal Academy of Moral and Political Sciences (RACMP). "On the Abnormal State of the exchange Rates" was an intervention within a series of discussions on the exchange rate situation organised by Laureano Figuerola -primarily known for being the Minister of Finance who introduced the *peseta* as the Spanish currency in 1868- who was the President of the RACMP at the time. These writings laid the foundations of the Project to Adopt the Gold Standard in 1903, after the currency crash of 1898.

The last two contributions, "The Problem of Exchange Rate in Spain" (1901) and "Bill to Regularise and Improve Foreign Exchange and to Restore the Circulation and Free Minting of Gold Coin" (1903),



were focused on providing solutions to the stability of the exchange rate after the crisis of 1898. These writings included policy recommendations, with the later explicitly proposing the adoption of the Gold Standard in Spain. Fernández Villaverde's monetary writings exhibited a high level of rigor and technical competence. Indeed, in late 19<sup>th</sup> and early 20<sup>th</sup> century Spain, the monetary issue was one of the topics of discussion among highly competent experts with extensive information and technical expertise (Sabaté Sort and Serrano Sanz 2001). The following sections will delve into each crisis, focusing on the issue that Fernandez Villaverde aimed to address, the underlying causes of the problem, and his policy recommendations.

### 3. The currency crisis of 1891

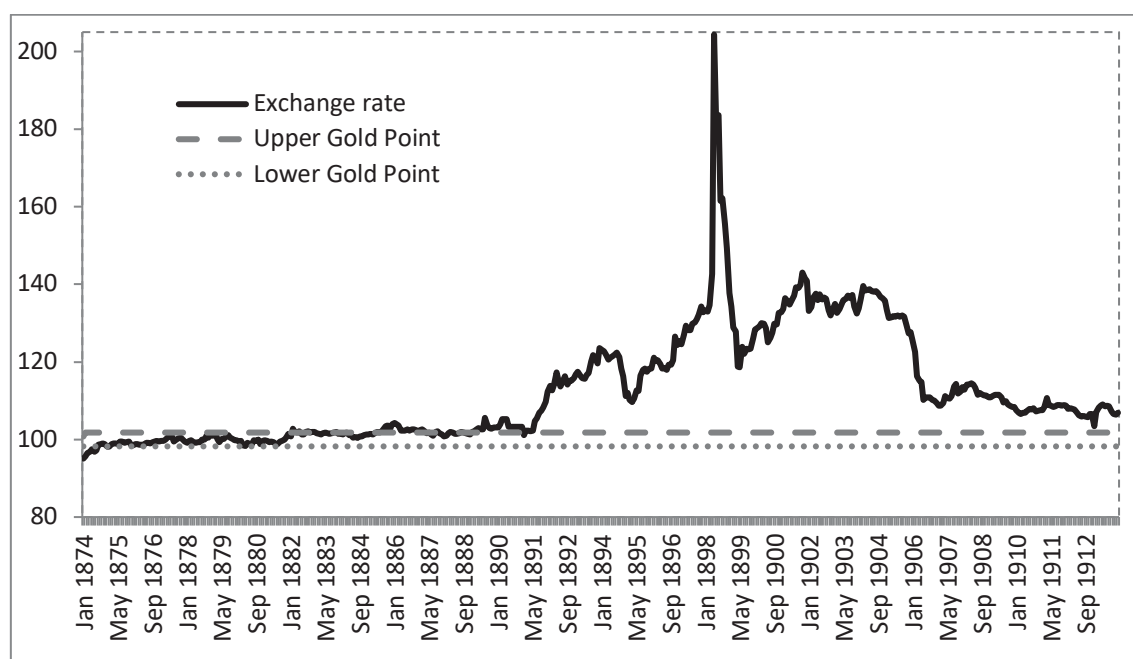
Spain maintained a *de iure* bimetallic monetary system throughout the entire Gold Standard period, although it effectively transitioned into a *de facto* silver monometallic system. The Spanish Government introduced the *peseta* in 1868, aligning its gold-silver ratio with the 1:15.5 bimetallic official ratio established by the bimetallic bloc of the Latin Monetary Union in 1865. The Spanish exchange rate remained within the gold-points -experiencing only a few short-lived breaks- until the currency crisis of 1891 (see Figure 1; Martínez-Ruiz and Nogues-Marco 2014 for an overview). The pressure on the exchange rate in 1891 originated from the panic triggered by the bankruptcy of the Baring Brothers in London in November 1890 (Kindleberger 1978). This event violently disrupted the international capital market, with a significant impact on Spain (Sardà 1948, Tedde de Lorca 1974). The panic erupted during a challenging period for the Bank of Spain as it was negotiating with the Government for the extension of its issuing privilege. The years preceding the Baring crisis had already been unfavourable to the *peseta*'s exchange rate, which had depreciated due to increased demand for foreign bills to service foreign sovereign debt (which included the regular interest payment plus debt amortization). During this period, the silver reserve of the Bank of Spain saw a significant decline, decreasing by 60% between 1888 and 1890. However, the gold reserve suffered only a minor reduction because the Bank had gradually ceased the conversion of banknotes to gold between the mid-1880s and 1890 (Martinez-Ruiz and Nogues-Marco 2014: 31).

In an attempt to uphold the stability of the exchange rate, the Bank of Spain increased interest rates from 4% to 5% in 1891 and later from 5% to 5.5% in 1892 (Martinez-Ruiz and Nogues-Marco 2014: 31). Nevertheless, the rise in the interest rate did not lead to a reduction in the money supply. This was due to the simultaneous increase in the quantity of banknotes in circulation, as the issuing ceiling doubled from 750 to 1,500 million *pesetas* under the Law of July 1891, a law negotiated between the



Government and the Bank of Spain (Martín-Aceña *et al.* 2012: 163). Subsequently, starting in August 1891, the Bank of Spain ceased actively defending the stability of the *peseta*, prioritising its own profitability over monetary stability (Martínez-Ruiz and Nogues-Marco 2018, Martín-Aceña *et al.* 2020). As a result, the exchange rate began to float just a few days after the Bank of Spain renewed its national issuing monopoly for a 30-year period.

FIGURE 1. MONTHLY EXCHANGE RATE 1874-1913, PTAS/£ (% OFFICIAL PARITY)



**Sources:** Martínez-Ruiz and Nogues-Marco (2018: 17). Author's calculations. Exchange rate: *Boletín de cotización oficial del Colegio de agentes de cambio de la Bolsa de Madrid 1874-1913*, Biblioteca de la Bolsa de Madrid. From 1874 to Dec 1887 the exchange rate in Madrid on London was quoted at 3 months. I have converted the 3-month exchange rate to the spot exchange rate (see Flandreau *et al.* 2009; I have used London market interest rates collected from *The Economist* to calculate the spot exchange rate). Official gold parity between Spain and England was 25.20 ptas/£. Shipping costs has been extracted from *Actas de la Junta Consultiva de la Moneda, 1876-1888*. Archivo del Ministerio de Hacienda, Book 22859, pp. 273-278, 08/08/1877.

**Note:** Estimated gold cost is 1.78% (shipping cost from Madrid to London, via Santander), similar to the gold cost reported by Esteves, Reis and Ferramosca (2009) for the case of Lisbon-London (1.5%).

The writing *La cuestión monetaria* [The money issue] (1890) and *Sobre el estado anormal de los cambios 1891-1892* [On the abnormal state of the exchange rates] (1893) aimed at searching solutions to stabilise the exchange rate. *La cuestión monetaria* [The money issue] was writing in January 1890, that is, before the Barings bankruptcy at the end of that year. Therefore, the exchange rate situation was not so turbulent yet. Villaverde reviewed the world monetary landscape, which was being debated between gold monometalism and bimetallism. He analysed the policies of relevant countries such as Great Britain, the United States, France, and Germany to outline the theoretical possibilities for Spain

to stabilise the exchange rate, as well as the practical challenges involved. The first theoretical possibility was to re-establish the official gold-silver parity of 1:15.5, which was unfeasible in practice due to significant differences between the official and market gold-silver ratios at that time. The second option was to remain in bimetallism but defining a new official bimetallic ratio based on updated market prices. The third option was to demonetize silver and adopt the Gold Standard. Villaverde acknowledged that these last two solutions for exchange rate stability, whether it be bimetallism adopting a new official ratio in line with updated gold and silver market prices or gold monometalism, were unfeasible in practice at the time due to "the sacrifices the change of monetary regime would have imposed on the Treasury" (Fernández Villaverde 1890a: 216). Therefore, his recommendation was a "wait-and-see monetary policy" (*política monetaria expectante*), while also advising against exacerbating the situation with new silver coinage. Additionally, he emphasised the imperative need for the Bank of Spain to have a solid gold reserve to meet the requirements of international trade.

The writing *Sobre el estado anormal de los cambios 1891-1892* [On the abnormal state of the exchange rates] (1893) was a brief intervention within a series of discussions on the exchange rate in which Villaverde reiterated the same points he had already developed in *La cuestión monetaria* [The money issue] (January 1890). He acknowledged that the difference between the official bimetallic ratio and the market ratio had been causing gold to flow out (or hoarding) for more than ten years. He criticised the Government for continuing to mint silver, a policy that was very tempting for the Government due to the profit margin between the official and market price of silver. He recognized that servicing foreign sovereign debt was an obstacle to exchange rate stability because it exerted pressure towards the depreciation of the exchange rate due to the demand for foreign bills. He lamented that the Bank of Spain did not intervene more actively in defending the exchange rate through ordinary means, primarily through interest rate increases and the use of the gold reserve to convert banknotes, which he considered as "services that the bank is called to provide" (Fernández Villaverde 1903: 562). It should be noted that, legally, the Bank's reserve was composed of both gold and silver since the country was *de jure* bimetallic. In other words, the Law of 1874 did not distinguish between gold and silver reserves, as bimetallism was fully operational in Spain at that time. The new Law of 1891 only required having half of the reserve in gold, but it is at the discretion of the Bank of Spain to exchange banknotes for either gold or silver because the system remained *de iure* bimetallic, even though *de facto* gold was no longer in circulation in the country, and the Bank of Spain had the legal right not to convert banknotes for gold but only for silver (see Martín-Aceña et al. 2012: 163 on the banknotes issuing regulations). In summary, Villaverde's recommendations pointed towards a path of gradual exchange rate stabilisation, or at the very least, towards actions by the Government and the

Bank of Spain that would not worsen the exchange rate situation further. However, neither the Government nor the Bank heeded these recommendations and the exchange rate situation deteriorated, as we will see with the next currency crisis.

#### 4. The currency crisis of 1898

The second key episode is the currency crash of 1898. After 1895, money creation largely financed the Spanish-American War, which led to a sharp depreciation of the exchange rate. In 1898, the *peseta* experienced the highest level of depreciation in 1898 (see Figure 1; Martínez-Ruiz and Nogues-Marco 2014 for an overview). The direct cost of the colonial wars is estimated to have exceeded 3,000 million *pesetas* between 1895 and 1899, with the total public expenditure being approximately 4,600 million *pesetas*. This amount represents half of the annual GDP at that time (the estimation of the war cost can be found in Tedde de Lorca 1985: 245 and Maluquer de Motes 2008: 365; GDP data in Prados de la Escosura 2003).

The depreciation of the *peseta* made servicing foreign sovereign debt increasingly burdensome. Faced with the impossibility of guaranteeing debt service, the Government implemented a Law in May 1898, which required a sworn statement (*affidavit*), which meant that foreign sovereign debt bonds held by foreigners would continue to be paid in gold, while those held by Spaniards would be paid in *pesetas* with the option to convert them into domestic debt in exchange for a bonus. The Ministry of Finance provided a one-year window for foreign sovereign debt holders to go to overseas Treasury offices to stamp the foreign sovereign debt bonds upon proving foreign nationality (Martínez-Ruiz and Nogues-Marco 2014: 33). It was estimated that half of the Spanish foreign debt was held by nationals (Martínez-Mendez 2005, chapter 8: 2). Paying the foreign sovereign debt held by nationals in silver, rather than gold, substantially reduced the debt burden in the short term in the extraordinary context of the 1898 crisis.

When the war ended, the volume of domestic sovereign debt had significantly increased, in addition to the colonial debt that Spain had acquired through the Paris Treaty in December 1898, which marked the conclusion of the Spanish-American War. In 1899, the total sovereign debt reached 118% of GDP, placing a heavy financial burden on the budget. The debt crisis, triggered by the war and subsequent defeat, required a comprehensive fiscal reform designed to stabilise the exchange rate with the main person responsible being the new Minister of Finance, Raimundo Fernández-Villaverde. He implemented the reform based on a tax overhaul and a sovereign debt restructuring plan, intended

not only to eliminate the fiscal deficit but also to cease its monetization in order to mitigate its impact on the depreciation of the Spanish exchange rate (Férrnandez Villaverde 1901, 1903).

Fiscal orthodoxy was achieved through a consolidation process that involved cutting public expenditures, introducing new taxes, and raising the existing ones. This tax reform aimed to generate revenue and modernise the tax system (Comín and Martorell 1999, Comín 2002, Pan-Montojo 2015). Consequently, starting from 1902, the fiscal budget consistently recorded surpluses for nearly a decade. However, despite fiscal austerity and the sovereign debt restructuring plan, orthodox monetary policy was not fully realized.

The exchange rate did not converge with gold parity because sterilisation prevented deflation, despite fiscal discipline. The Government reimbursed a substantial portion of the Treasury loans held in the Bank of Spain's portfolio. However, the quantity of banknotes in circulation was not proportionally reduced due to the sterilisation carried out by the Bank of Spain. Instead of reducing banknotes in circulation, public earning assets were offset by increasing silver reserves and private earning assets (Martínez-Ruiz and Nogues-Marco 2018: 6). In his essay *El problema del cambio en España* [The Problem of Exchange Rates in Spain] (1901), Villaverde pointed out that it was among the duties of the Bank of Spain as a privileged issuing bank to "exercise its functions as a regulator of currency circulation, provide assistance to the State in monetary reform, offer to commerce the highly important service of moderating the exchange rate premium and combating its fluctuations, counteracting speculation, rather than participating in it and seeking its benefits" (Férrnández Villaverde 1901a: 272). Villaverde emphasized "the conviction of a manifest and already unavoidable need for greater means of action by the Ministry of Finance over the Bank of Spain for everything related to the plan for the reform of fiduciary and metallic circulation, aimed at improving international exchange. It undoubtedly must include among Bank's duties, the abstention from any profit on the exchange rate, whose trade should be for that institution, not a business, but a service" (Férrnández Villaverde 1901a: 273-274). He proposed raising the discount rate to reduce the quantity of banknotes in circulation and decreasing loans secured by sovereign debt to prevent the Bank of Spain from replacing the reduction of public earning assets achieved through fiscal reform with an increase in private earning assets instead of reducing banknotes in circulation.

Villaverde also strongly advocated for the prohibition of silver coinage by law. He recalled the three theoretical solutions he had proposed in his 1890 speech (*La cuestión monetaria* [The Money Issue]) and argued that by 1901, the only possible solution was the most costly and slowest but the only secure one: the gradual restoration of gold circulation with the gradual demonetization of silver (Férrnández Villaverde 1901a: 281).

Two years later, Villaverde proposed the *Proyecto de Ley para regularizar y mejorar el cambio exterior y para procurar el restablecimiento de la circulación y de la libre acuñación de la moneda de oro* [Bill to Regularise and Improve Foreign Exchange and to Restore the Circulation and Free Minting of Gold Coin] (1903), bill that was also published in French by the *Economiste Européen*. This Bill began with a lengthy review of the exchange rate situation in Spain, followed by a description of the monetary policy measures adopted by Austria-Hungary, Russia, Japan, France, Italy, and Greece. Finally, it outlined concrete proposals for adopting the Gold Standard, including:

1. Currency Exchange Office: The proposal suggested the creation of a currency exchange office under the direct control of the Ministry of Finance. This office would handle the buying and selling of bills of exchange and gold exclusively. The Bank of Spain would require consent from the currency exchange office to conduct these operations (Article 3).

2. Management of the Currency Exchange Office: The Ministry of Finance would appoint a person to manage the currency exchange office, either from the Bank of Spain or externally, based on the Ministry's trust (Article 4). The operations of the exchange office would be oriented towards the public interest, and its accounts would be completely separate from the Bank of Spain's accounts (Article 4).

3. Funding for the Currency Exchange Office: To support the operations of the currency exchange office, a fund would be established. This fund would primarily be funded by the surplus from customs duties, savings from exchange rate stabilisation on foreign Treasury obligations, and an advance on the revenue from the Almadén mercury mines (Article 8).

4. Demonetization of Silver: The proposal suggested the gradual demonetization of silver, with the losses incurred in the process charged to the fund for the currency exchange office's operations (Article 10).

5. Conversion of Banknotes into Gold: The Bank of Spain would be required to convert banknotes into gold (Article 11).

6. Regulation of Domestic Debt: There would be regulations on the maximum issuance of sovereign domestic debt for a four-year period, with subsequent actions to be determined based on market conditions (Article 12).

7. Interest Rate Control: The Bank of Spain would not be able to lower the discount rate or interest on loans without authorization from the Ministry of Finance, and these rates could not fall below the yield of sovereign debt (Article 13).

8. Reducing Circulation of Banknotes: The Ministry of Finance, in agreement with the Bank of Spain, reserved the right to take measures to reduce the circulation of banknotes resulting from the Treasury's debt repayment to the Bank (Article 14).

9. Monitoring Commission: A commission would be established to monitor all operations related to foreign exchange and currency circulation in Spain. This commission would be required to submit an annual written report to the Parliament (Article 15).

10. Trade Policy and Clearinghouses: The Government would negotiate trade treaties to promote domestic production and exports (Article 15). It would also encourage the establishment of clearinghouses for securities, bonds, and credit instruments in Spanish main commercial markets to stimulate domestic trade and economic development (Article 16).

In summary, Villaverde's Bill aimed at adopting the Gold Standard in Spain was a multifaceted package that included: (a) very specific measures in monetary policy designed to wrest control from the Bank of Spain, which, in his view, had completely neglected its responsibility to stabilise the exchange rate; (b) some guidelines for fiscal policy regarding sovereign debt issuance over a four-year period, while leaving future decisions in fiscal policy open; (c) much less precise directions in trade policy, reflecting Villaverde's perspective that exchange rate stability was primarily a monetary issue rather than a balance of payments issue.

## **5. Conclusion. The Failure of Villaverde's Monetary Reform to Adopt the Gold Standard in the Context of the Deflationary Debate for Interpreting the Monetary Crisis**

Spain did not adopt the Gold Standard. According to Raimundo Fernández Villaverde, the depreciation of the peseta had been a consequence of the increased money supply, mainly in the form of banknotes, resulting from the financing of wars through the direct monetization of the fiscal deficit by the Bank of Spain (Fernández Villaverde 1901, 1903). This is why Villaverde implemented fiscal reform that successfully led to fiscal orthodoxy after the 1898 Cuban War of Independence. However, the exchange rate did not converge with gold parity primary because the Bank of Spain's policies of sterilisation prevented deflation, despite fiscal discipline (Martínez-Ruiz and Nogues-Marco 2018).

Villaverde did not contemplate the possibility of adhering to the Gold Standard with a depreciated exchange rate due to concerns about the credibility of a depreciated currency. Hence, deflation was a necessary condition for him to adopt the Gold Standard. Therefore, he conceived the Gold Standard as a contingent rule: only in case of well-understood emergencies, such as a war, financial crisis or trade shock, would temporary departures from the rule be permitted, assuming that convertibility of the national currency into gold would be restored once the emergency passed. The rule was contingent in the sense that investors understood that the suspension would last only for the duration of the emergency plus some period of adjustment, and afterwards, the Government would adopt the

deflationary policies necessary to resume payments at the original parity between the currency and gold (Bordo and Kydland 1995).

The interpretation of the causes of exchange rate depreciation, as well as the need to deflate the economy to adhere to the Gold Standard, was shared by other renowned monetarist economists, such as Eduardo Sanz Escartín (1905), who was also a member of the Conservative Party, along with the most well-known representatives of the French *école libérale*, such as Edmond Théry (1899, 1901). However, the Bank of Spain resisted reducing banknotes in circulation. The negotiation process between the Government and the Bank was intense. According to *The Economist* "the board of directors [of the bank of Spain] had a hard fight with the finance ministers, who were backed by public opinion, by commercial and financial circles, by the press, and even by the opposition statesmen and ex-ministers of finance in the Parliament (The Economist, "The Report of the Bank of Spain for 1902", April 4, 1903, issue 3110, pp. 605-606). The Bank of Spain prevailed over the Government, and the circulation of banknotes was not reduced to deflate the economy. In this regard, Martínez-Ruiz and Nogues-Marco (2018) calculated the relative power of the Bank of Spain and the Government, concluding that the Bank of Spain gained power during the Restoration, while the Government lost power, making it impossible for the Government to compel the Bank to deflate the economy. As a result, the Bank of Spain prioritised its primary goal of profitability as a private institution over the public good of monetary stability.

Circles close to the Bank of Spain argued that monetary contraction would negatively impact economic growth and advocated for measures aimed at improving the balance of payments. These measures included productivity gains, export promotion, interest rate reductions to stimulate private activity, attracting foreign direct investment, or promoting foreign tourism as solutions to exchange rate stabilisation (see Maluquer de Motes 1997 for an overview). For instance, Fariña Cisneros (1901: 279), who served as Sub-governor of the Bank of Spain between 1884 and 1903, warned of the dangers of economic crises caused by monetary contractions. He argued that costs, wages, and prices would need to adjust downward in a highly challenging process. Similarly, Jiménez Rodríguez, Director of the Bank of Spain in Palma de Mallorca and recipient of the prestigious Conde de Toreno award from the Royal Academy of Moral and Political Sciences for his Critical Study of the Monetary Crisis, also opposed the reduction of banknotes. He protected the interests of the Bank of Spain and proposed adopting the gold standard without deflating the economy, relinquishing the historical parity of the *peseta*, and acknowledging the effective 25% depreciation in the exchange rate (Jiménez y Rodríguez 2005: 309). Ultimately, no measures were adopted, and Spain never adhered to the Classical Gold Standard.



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