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Circumventing credible commitment: Groningen's default and the Dutch Republic's federal escape route, 1666-1761

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Circumventing credible commitment: Groningen's default and the Dutch Republic's federal escape route, 1666-1761

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Abstract: The Dutch Republic is frequently depicted as an early example of a state's credible commitment to debt. Yet these studies tend to overlook the implications of the Republic's federal structure. This paper analyses the default by the province of Groningen during the 1680's, at the expense of its creditors in the province of Holland. It argues that Groningen's unique position within the federation prevented the market to punish the province for its misbehaviour. This was not a carefully thought-out plan, but the coincidental historical outcome of the interaction between creditors and provincial and federal authorities. Ultimately, the creditors resorted to essentially medieval sanctions to enforce a solution.

Keywords: public debt, Dutch history, default, political economy, economic history

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Introduction

A state's credible commitment to debt is supposedly a key factor for various financial revolutions throughout history that formed a basis for modern financial systems and economic growth, due to the protection of property rights.¹ Although a positive link between finance and growth appears to exist, the causal relation between early-modern public finance, financial markets and economic growth remains debated.² Similarly, the widespread notion that institutions that protect property rights fostered growth has been both criticised and elaborated.³ This paper contributes to the debate by analysing the default of the Dutch province of Groningen in the 1680s in relation to the Dutch political institutions and the capital market.

The Dutch Republic is a noteworthy object of study in this respect in several regards. Firstly, the Republic has been portrayed as the first modern economy, not in the last place because of its advanced financial sector.⁴ Secondly, the Dutch Republic's institutional organisation consisted of representative units '*between medieval communes and modern nation-states*', which supposedly simultaneously created agency and improved tax morale.⁵ Thirdly, the Dutch maintained a large public debt with low interest rates, which can be seen as indicator for a modern political economy.⁶ Finally, the Dutch late sixteenth-century financial and tax revolutions financed its struggle

¹ Rousseau and Sylla, 'Financial Revolutions and Economic Growth', 4; North and Weingast, 'Constitutions', 803; Dickson, *Financial Revolution*; Tracy, *A Financial Revolution in the Habsburg Netherlands*; Acemoglu and Robinson, *Why Nations Fail*; Acemoglu, Johnson, and Robinson, 'The Rise of Europe'.

² Fritschy, 'Financial Revolution'; Gelderblom and Jonker, 'Public Finance'; Coffman and Neal, 'Introduction'; Epstein, *Freedom and Growth*; Chilos, 'Risky Institutions'; Dincecco, 'Political Regimes and Sovereign Credit Risk in Europe, 1750-1913'; Dincecco, 'Fiscal Centralization, Limited Government, and Public Revenues in Europe, 1650-1913'; Rousseau and Sylla, 'Financial Revolutions and Economic Growth'; Murphy, 'Demanding "credible Commitment"'; Murphy, *The Origins of English Financial Markets*; Sussman and Yafeh, 'Institutional Reforms, Financial Development and Sovereign Debt'; Buchinsky and Polak, 'Emergence'.

³ Acemoglu and Robinson, *Why Nations Fail*; Sussman and Yafeh, 'Institutional Reforms, Financial Development and Sovereign Debt'; Coffman, Leonard, and Neal, *Questioning Credible Commitment*.

⁴ De Vries and Van der Woude, *The First Modern Economy*; Petram, *The World's First Stock Exchange*; Tracy, *A Financial Revolution in the Habsburg Netherlands*; Van Zanden and Van Leeuwen, 'Persistent but Not Consistent'.

⁵ Van Zanden and Prak, 'Towards'; Prak and Van Zanden, 'The Netherlands and the Polder Model'; Gelderblom, 'Introduction', 3-4; Prak and Van Zanden, 'Tax Morale'.

⁶ Van Zanden and Prak, 'Towards', 140; Dormans, *Het Tekort*; Fritschy, *De Patriotten*; 't Hart, *The Making of a Bourgeois State*; Stasavage, *States of Credit*.

for independence and coincided with its rise as major European power.⁷

Considering these features in the light of 'credible commitment' thesis, sovereign default would seem unlikely in the Dutch Republic.

Yet during the 1680s the province of Groningen defaulted on its creditors in Holland and did not solve the problem until 1761. In the 1660s and early 1670s, the province of Groningen borrowed extensively from creditors in the province of Holland, in the form of redeemable and life annuities. The province had, however, trouble servicing the debt and began running into arrears from 1672. Gradually, an increasing number of annuities remained unpaid. During the 1670s and 1680s, the States of Groningen made irregular payments to creditors in Holland. In an attempt to restructure the debt, the province of Groningen reached an agreement with the possessors of redeemable annuities, in 1686. This was, however, not the case for life annuity holders. The majority of the life annuity holders received no interest payments after 1685, which made the default complete. In spite of requests from creditors and the provincial States of Holland, Groningen refused to pay. Not until the Holland creditors invoked the Law of Reprisal in 1759, the States of Groningen could get away with it. A final agreement to solve the issue was only reached in 1761; the Groningers promised to pay 60% of the unpaid sum of 1.1 million guilders.⁸

To understand how Groningen's temporary deficits evolved into a persistent default, we need to understand the Dutch Republic's institutional organisation and province's position within the federation. This is a vital element of the analysis, because defaulting risk differs for domestic and foreign creditors. By defaulting on the creditors in Holland, Groningen singled out a specific and easy to identify group, which was a common practice in early-modern Europe.⁹ Moreover, creditors living in Holland were not represented in Groningen's assembly, which consisted of people living in Groningen. This deprived them from the credible commitment check on public finance.¹⁰ Therefore, external commitment mechanisms were necessary to

⁷ Israel, *The Dutch Republic*; Fritschy, 'Financial Revolution'; Tracy, *A Financial Revolution in the Habsburg Netherlands*; Gelderblom, 'Introduction'; 't Hart, *The Dutch Wars of Independence*; Epstein, *Freedom and Growth*, 12.

⁸ RHC-Groninger Archieven, inv.nr. 2276: for an impression of the purchasing power of the guilder, please consult: <http://www.iisg.nl/hpw/calculate.php>.

⁹ Velde and Weir, 'Financial Market and Government Debt Policy in France', 5; Drelichman and Voth, 'Serial Defaults, Serial Profits'; Álvarez-Nogal and Chamley, 'Debt Policy under Constraints'.

¹⁰ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 10–11.

credibly commit the province. To mitigate sovereign default risk, the literature emphasised four mechanisms to increase commitment to external debt (re)payments: the role of reputation for future borrowing¹¹, economic spillover effects¹², contingent debts¹³, and sanctions or supersanctions.¹⁴ The use of sanctions had been frequent in the Low Countries during the late middle ages, when the Law of Reprisal provided external creditors with the right to seize or imprison citizens of a defaulting public body – with very disruptive consequences for the economy of the towns involved.¹⁵ Yet, Van der Heijden argued that this form of contract enforcement became extinct during the late 16th century.¹⁶ Perhaps, the disruptive consequences fostered its extinction, while the incorporation of the various provinces into the Dutch federal state might have offered alternatives to overcome the fundamental problem of exchange.¹⁷

This paper maintains that Groningen's credit relation with its creditors in Holland was neither internal nor external, but a mix of both, due to the federal structure. As a result, neither type of commitment mechanism worked. In this institutional twilight zone, the federal government and the Groningen's provincial government – States of Groningen – discovered a common ground that marginalised the Holland creditors. Their interest was subordinated to the interest of Groningen's provincial state and the common cause of the Republic's security. Consequently, this paper adds to the debate about the alleged institutional incompetence of the Dutch Republic as cause of its decline and to the debate about the relation between credible commitment to debt and state formation in general.¹⁸

The paper proceeds as follows. The first section highlights Groningen's position within the institutional structure of the Dutch Republic. Section two discusses the main features of Groningen's public finance. Then, the provincial

¹¹ Tomz, *Reputation and International Cooperation*; Reinhart and Rogoff, *This Time Is Different*; Eaton and Gersovitz, 'Debt with Potential Repudiation'.

¹² Esteves and Jalles, *Like Father like Sons?*; Sandleris, 'Sovereign Defaults'.

¹³ Drelichman and Voth, 'Risk Sharing'; Grossman and Van Huyck, 'Sovereign Debt as a Contingent Claim'.

¹⁴ Mitchener and Weidenmier, 'Supersanctions and Sovereign Debt Repayment'; Oosterlinck, Ureche-Rangau, and Vaslin, 'Waterloo'; Bulow and Rogoff, 'Constant Recontracting'.

¹⁵ Zijlenderdijn, *Medieval Capital Markets*, 63; Greif, *Institutions* calls this collective liability for debt the Community Responsibility System (CRS).

¹⁶ Van der Heijden, *Geldschietters*, 20.

¹⁷ Greif, 'The Fundamental Problem of Exchange'.

¹⁸ Fritschy, *De Patriotten*, 70–73; De Vries, *De Economische Achteruitgang Der Republiek in de Achttiende Eeuw*; Epstein, *Freedom and Growth*, 31.

borrowing behaviour is examined in relation to the capital market before the default. Sections four and five consider the default itself. The former section analyses the character of the default, as piecemeal and unstructured. The latter section scrutinizes Groningen's failed negotiations with Holland life annuity holders. The sixth section summarizes the persistence and eventual resolution of the default in 1761, while emphasising the role of the Dutch Republic's central level – the Generality – in circumventing punishment by the market. Section seven concludes.

Groningen within the Dutch Republic

The Dutch Republic emerged from the Dutch Revolt or Eighty Years' War (1568-1648). The treaty of the Union of Utrecht (1579) stipulated the provinces' mutual relations to organise their common defence. Hence, this document was not designed as a constitution for the Dutch Republic, although it was the only formal document binding the provinces together. The States-General became a congress of delegates from sovereign provinces, with the sole prerogative of deciding about foreign affairs and warfare.¹⁹ These decisions had to be taken unanimously, which in fact granted a right to veto to each province.²⁰ Even though this form of government had disadvantages, such as being time consuming, provincial autonomy formed the essence of the Dutch political system. This section focusses on the position of Groningen within this institutional context.

Groningen's history as part of the Dutch Republic began in 1594 with the Treaty of the Reduction (Dutch: *Tractaat van Reductie*). Whereas the countryside of the province (Dutch: *Ommelanden*) had remained loyal to the Revolt, the city of Groningen had returned to the Spanish side. After the Dutch States Army captured the city in 1594, city and countryside were joint as equals into one province, much against the will of the *Ommelanden*. Thereafter, the city and the countryside each held one vote in the provincial assembly: the States of Groningen. This equal power sharing proved an ideal recipe for paralysing decision making, because any disagreement resulted in a

¹⁹ Fruin, *Geschiedenis Der Staatsinstellingen*, 175, 184–185.

²⁰ Ibid., 182.

tied vote.²¹ To overcome such future deadlocks, the Treaty of the Reduction granted the States-General the authority to settle a dispute.²² This provision violated the cherished provincial autonomy and such far-reaching powers by the central authorities created a unique situation within the Dutch Republic.²³

Moreover, the States-General already possessed the right to enforce payments for the common defence of the Dutch Republic, in case of serious arrears. Any defaulting province could even be forced to pay by military means, although this was rare.²⁴ This might seem draconic, but the Generality depended heavily on the provincial contributions to finance army and navy; over 80 per cent of the income came from the provincial coffers and more than 80 per cent of the expenses was intended for the military.²⁵ To remedy the constant quarrels about the contribution to the Generality, the provincial shares in the annual central budget became fixed in 1616, which lasted for almost two centuries.²⁶ Nonetheless, securing income for the Union's defences remained the Generality's major concern throughout the existence of the Dutch Republic.²⁷

In order to secure the regular pay of troops, the States-General could issue loans in expectation of future provincial contributions. During the Eighty Years' War the majority of sums the Generality borrowed was to cover provincial arrears in troop payments.²⁸ Yet, as the Generality's own incomes were but meagre, its credit depended on factors beyond its direct control: 'military solicitors' advanced payments to the troops, the personal credit of the Union's Receiver and provincial contributions.²⁹ The Generality's credit greatly improved during the early seventeenth century, as Holland's credit backed these loans and stood surety for the interest payments.³⁰ The Generality depended, nonetheless, much on the provinces willingness to meet their financial obligations. The Generality's credit would have benefited from

²¹ Formsma, *Historie van Groningen*, 235; Schroor, 'Heroriëntatie', 153–158.

²² Formsma, *Historie van Groningen*, 235, 368; Schroor, 'Heroriëntatie', 153–154.

²³ Waterbolk, 'Staatkundige Geschiedenis', 235.

²⁴ Fruin, *Geschiedenis Der Staatsinstellingen*, 196, 204, 334, 379, 391.

²⁵ 't Hart, *The Dutch Wars of Independence*, 154–155; Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 6–7.

²⁶ 't Hart, *The Making of a Bourgeois State*, 79; Zwitzer, 'Quotenstelsel'.

²⁷ Dormans, *Het Tekort*; Fritschy and Van der Voort, 'From Fragmentation to Unification'; Brandon, *Masters of War*.

²⁸ 't Hart, *The Making of a Bourgeois State*, 170.

²⁹ Ibid., 165–172.

³⁰ Ibid., 167–171; Dormans, *Het Tekort*, 145.

more control over its income, yet the provinces' fiscal autonomy prohibited this.

Eventually, this system of borrowing under the guarantee of the Generality was pushed beyond its limits, between 1691 and 1715. The more than doubling of the Generality debt – from 28.8 million guilders in 1691 to 61.2 million in 1715 – was almost entirely caused by the provinces' inability to provide sufficient funds to pay for the military. Understandably, the provinces had also trouble to find the means to pay interest over the Generality's debt and arrears built swiftly. In 1715, the system collapsed as the provinces' lingering payments led to the closure of the Union's Exchequer office for nine months.³¹ For the remainder of the eighteenth century, the Council of State – as executive committee of the States-General – scarcely issued loans anymore.³²

The 1715 default demonstrated the Generality's dependence on the provincial contributions to the central budget once more. The lack of control over the means to pay the interest to the creditors made the Generality vulnerable to the whims of the provincial governments. Since the provincial sovereignty was an essential feature of the institutional organisation of the Dutch Republic, this could not easily be altered. Groningen was in this regard a special case, due to the Treaty of Reduction from 1594 that granted the States-General extraordinary influence on the provincial administration. This seems to have had a positive influence on the public finance of both province and the Generality. Concerning deficient payments from the other provinces, borrowing on the Generality's account was a second-best option that proved mutually beneficial to all parties, at least, apart from 1715.

Obtaining money from Groningen proved especially difficult, however, even after the Spanish troops were expelled after 1594. Especially the city of Groningen resisted the introduction of new taxes, most notably the 'common means' (Dutch: *gemene middelen*). Since these farmed taxes consisted largely of excises, the city argued that it would be overburdened compared to the countryside. Meanwhile the arrears to the Generality's contributions had risen to 490,000 guilders. The States-General, afraid that the Spanish might again establish a foothold in the north, sent over an embassy in 1600, accompanied by troops to enforce payments. The Generality's military

³¹ Dormans, *Het Tekort*, 145–147.

³² *Ibid.*, 152.

intervention did not stop there; it built a fortress as means of coercion (Dutch: *Dwangburght*) at the city's east gate. This was intended to keep the population in check that had opposed tax reforms, in order to enforce a solution in the provincial disagreement and secure payments to the Union.³³ After imposing higher tariffs on the taxes and convinced of better intentions, the States-General had the fortress dismantled in 1607.³⁴

Eventually, this episode turned-out to have been merely a first intervention in Groningen's provincial politics and public finance. Between 1622 and 1628 the Generality enforced another tax reform, to increase the province's tax revenue.³⁵ Consequently, Groningen's need for the Generality loans decreased after the 1620s, while troops allocated to Groningen's pay role were regularly paid.³⁶ Between 1650 and 1749 the province received no less than thirty-six embassies from the States-General, which concerned either internal conflicts or arrears in payments.³⁷ For instance, in 1726, a Generality-embassy arrived to solve the disputes that had risen about the question how to pay for the arrears on loans the Generality had issued on behalf of Groningen.³⁸ This delegacy repeated the secret advice given by an Groningen internal committee, six years earlier, to sell-off provincial domains.³⁹ Although the provincial government rejected this advice again, it quickly found other solutions that improved the provincial finances.⁴⁰ Sending over an embassy to solve the quarrels was more than justified, since Groningen had paid nothing to service the Generality debt between 1715 and 1725.⁴¹ Hence, the default of the province on its creditors in Holland in 1680s was not the first problem Groningen had in managing its public finance – and certainly not the last.

It is, however, important to note that the States-General interventions proved beneficial. The imposed tax reforms proved effective, which decreased

³³ Schroor, 'Heroriëntatie', 159–160; Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 14–15.

³⁴ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 18.

³⁵ De Bruijn, *Plakaten van Stad En Lande*, 76, 86; Schroor, 'Heroriëntatie', 161–163; Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 15–16, 235–237; Meihuizen, 'Sociaal-Economische Geschiedenis', 303, 325.

³⁶ 't Hart, *The Making of a Bourgeois State*, 170.

³⁷ Boels and Feenstra, 'Regentenheerschappij', 267.

³⁸ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 16, 271–272.

³⁹ Nationaal Archief (hereafter NA) The Hague, Archief van Anthonie van der Heim (1710) 1737-1746, Inv.nr. 524, 17 June 1720.

⁴⁰ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 272–273.

⁴¹ Prak, *The Dutch Republic*, 267.

the risk of unpaid soldiers and the need for loans, whereas the increased tax revenue improved the chances on repayment. In spite of this evident success, the well-protected provincial fiscal autonomy prevented this to happen in other provinces.

Warfare and Public Finance

Warfare formed the single main expense of early-modern states, including the Dutch Republic, to which a mixture of loans and taxes was employed.⁴² This section outlines the major developments of Groningen's provincial finances throughout the time of the Dutch Republic. It maps the overall development of primary income and expenses, to assess the sustainability of Groningen's debts. From the calculated primary government budget balances, periods of primary deficits and surpluses indicate the province's liquidity shortage, subsequent need for borrowing and its ability to pay its creditors. Probing these figures allows for a deeper understanding of the ultimate causes of Groningen's default: whether long-term solvency or short-term liquidity crisis were the real problem for the unpaid creditors in Holland.⁴³ Early-modern states often resorted to default soon after a war had ended, when the debts incurred could not be serviced with tax revenue.⁴⁴ The section begins by framing Groningen's public finance in the context of the Dutch Republic's political history in the years preceding the default.

Despite the Generality's formal responsibility, the costs of warfare affected the provincial finances directly, due to a peculiar system of repartition of military costs. The 1616 fixation of the provincial contributions merely allocated the distribution of the total annual budget administratively. After approving the annual budget, each province individually constituted the actual payments up to the amount it had agreed upon. This implied that most of the consented money did not reach the Generality's coffers, but was spent by the provinces on behalf of the States-General, preferably in their own province. Yet, as Holland paid the lion share of the budget, it also paid for the

⁴² Glete, *War and the State in Early Modern Europe*; 't Hart, *The Dutch Wars of Independence*; Tilly, *Coercion, Capital, and European States, AD 990-1992*; Brewer, *Sinews*; Velde and Weir, 'Financial Market and Government Debt Policy in France', 6.

⁴³ This approach roughly follows the one pursued by: Drelichman and Voth, 'Sustainable Debts'.

⁴⁴ Velde and Weir, 'Financial Market and Government Debt Policy in France', 5; Drelichman and Voth, 'Sustainable Debts'.

upkeep of garrisons in other provinces and tried to exert control there.⁴⁵ Garrisons in fortress and cities' fortifications in the more peripheral provinces had to protect the Republic's core region – Holland, Zeeland and Utrecht.⁴⁶ The city of Groningen formed a vital link in the defence of the northern part the Republic – a position it never failed to mention in case of any discord within the States-General.⁴⁷ Therefore, the increased tax revenues after 1600 were also employed to improve the city's fortifications.⁴⁸



Figure 1: Map of the Dutch Republic around 1650 (Source: M. 't Hart 2014, xiv (reproduced with author's permission)).

⁴⁵ 't Hart, *The Making of a Bourgeois State*, 78–86; Zwitzer, 'Quotenstelsel'; Brandon, *Masters of War*, 43.

⁴⁶ 't Hart, *The Making of a Bourgeois State*, 38–39, 81; Schroor, 'Ontwrichting', 255.

⁴⁷ Schroor, 'Heroriëntatie', 157, 172; Schroor, 'Ontwrichting', 255.

⁴⁸ Schroor, *Rurale Metropool*, 214.

The strength of Groningen's defences was severely tested in the two wars with Münster in 1665-1666 and 1672. During the Second Anglo-Dutch War (1665-1667), Bernhard von Galen, prince-bishop of Münster, attacked the Dutch Republic. His troops invaded Drenthe, Overijssel, Gelderland and Groningen in 1665. Although the city of Groningen remained untouched, the Republic's northern defences proved no match for Von Galen's army. External aid was necessary to withstand the bishopric troops; Amsterdam and Zeeland sent troops and ammunition, and a French intervention force eventually caused the bishop to withdraw, only to return seven years later.⁴⁹ In 1672, the Year of Disaster in Dutch historiography, the Republic was attacked by England, France and the bishops of Cologne and Münster.⁵⁰ This time Von Galen's army actually besieged the city of Groningen for more than a month, without taking it.⁵¹ Again troops came from Holland to aid Groningen's defence, while large parts of the countryside were inundated to impede the invading army's progress.⁵² Both invasions and especially the attack on the city in 1672 burdened the provincial finances heavily, since the normal tax revenue could not procure the required money, while military expenses rose vastly.

⁴⁹ Israel, *The Dutch Republic*, 770–772; Waterbolk, 'Staatkundige Geschiedenis', 256–257; Schroor, 'Ontwrichting', 256–257.

⁵⁰ Israel, *The Dutch Republic*, 796 The wars against England and France are better known by their separate names: the Third Anglo-Dutch War (1672-1674), and the Franco-Dutch War (1672-1678).

⁵¹ Schuitema Meijer, 'Stad Groningen'.

⁵² Ibid., 257–259; Schroor, 'Ontwrichting', 257–260.



Figure 2: Siege of Groningen in 1672, by: Jacobus Harrewijn (23 September 1684) (source: Rijksmuseum Amsterdam, object: RP-P-OB-55.449).

Acquiring sufficient income was a recurrent problem for Groningen's government and, consequently, for the Generality. The Generality imposed tax reforms in the 1620s that doubled Groningen's tax revenue to approximately 1 million guilders annually. Despite the increase of taxation, a deficit remained of 17,750 guilders per year, between 1628 and 1664. This can be attributed to the Dutch involvement in the Eighty Years' War until 1648, the First Anglo-Dutch War (1652-1654) and assistance to the Danish in their war against Sweden in 1659 and 1660.⁵³ Deficits soared massively, however, from the two Münster invasions; from 1665 until the end of the Franco-Dutch War (1672-1678), Groningen annually lacked 117,750 guilders. These exceptional deficits incited the province to borrow money on an unprecedented scale, as will be discussed below.

To honour its debt, Groningen needed a primary surplus in the period that followed the loan issues. In the final two decades of the seventeenth

⁵³ Israel, *The Dutch Republic*, 736–738.

century, the province disposed of a surplus, of 154,000 per year. For most of the eighteenth century, a surplus of approximately 70,000 per year remained. This suggests that Groningen could transfer money to its creditors. The War of Spanish Succession (1702-1713) was the major exception to this. During that war the province ran again into huge deficits. Overall, the province had spare money to pay its creditors.⁵⁴

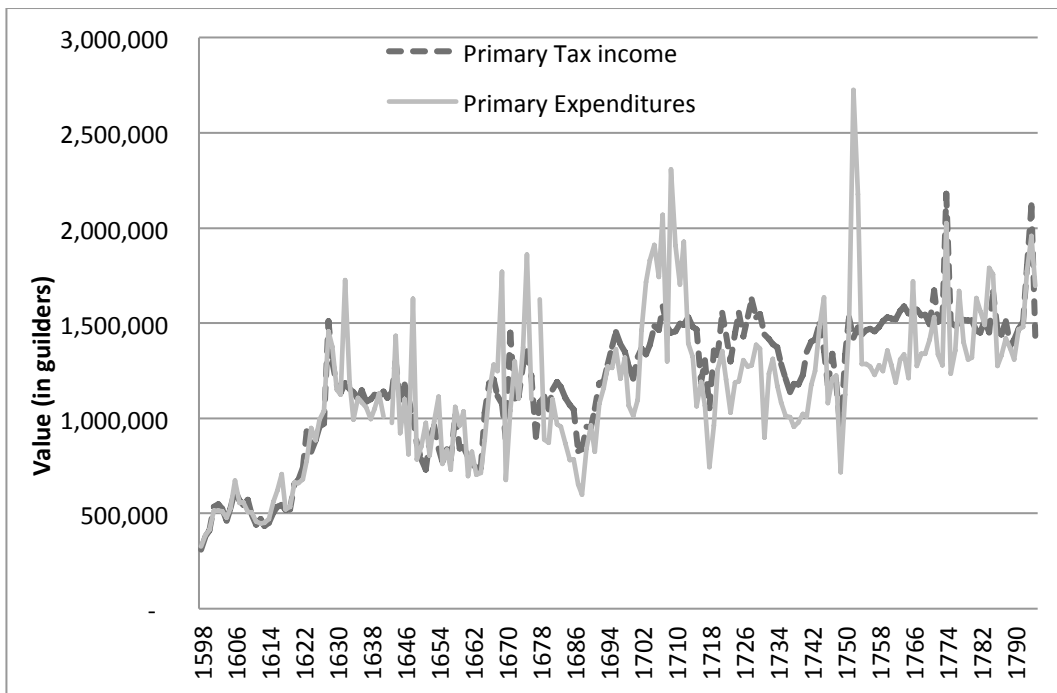


Figure 3: Groningen's primary incomes and expenses (L. Van der Ent and V. Enthoven, 2001, 91-95, 110-119.

The Dutch Republic's diminished warfare in the eighteenth century⁵⁵, resulted in a primary surplus for Groningen's public finance. This suggest that the debt was sustainable in the long-run and the two bishopric invasions caused temporary liquidity problems. Whether Groningen's debt was indeed sustainable can also be derived from the presence of absence of additional borrowing in periods in which it had a primary surplus, which will be analysed in the next section.

⁵⁴ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 91-95, 110-119, 189-193, 294-298, 328, 359-362.

⁵⁵ After the War of Spanish Succession only the War of Austrian Succession (1740-1748) and Fourth Anglo-Dutch War (1780-1784) followed.

Issuing debt

Capital markets play a vital part in smoothing payments by covering liquidity short-falls. Amsterdam was the West-European centre for sovereign borrowing.⁵⁶ However, Groningen did not use that market up to the 1660s for two reasons. Firstly, until the 1620s, Groningen's own creditworthiness was but limited and it relied on the Generality's credit to borrow. Secondly, the increased tax income from the 1620s diminished the need for extensive borrowing. When Groningen entered the Amsterdam capital market in 1665, it was a relative newcomer.⁵⁷ This section argues that when Groningen for the first time relied on the Amsterdam capital market, this turned out a failed experiment.

Figure 4 depicts the amounts the province of Groningen borrowed during the seventeenth and eighteenth centuries. It is clear that until 1665 the province hardly borrowed money to cover its deficits. Until that year the sums issued remained limited to a few ten thousands per year. The total amount of loans since Groningen joined the Union hardly exceeded one million. Groningen, moreover, not borrow any money at all in 26 years between 1620 and 1664. From the 1630s, Groningen probably used temporary arrears on the Generality's budget to smooth payments, as its reliance on the formal credit of the Union diminished.⁵⁸ The relatively small deficits and the alternation of surpluses and deficits allowed for this policy, until 1665.

⁵⁶ Riley, *International Government Finance*; Neal, *The Rise of Financial Capitalism*; Neal, 'How It All Began'; Dehing, *Geld in Amsterdam*, 265–271.

⁵⁷ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 128.

⁵⁸ Ibid., 291, 404 These unpaid/residual sums (Dutch: *restanten*) were common, and were probably mere slow payments as the province prioritised other expenses.

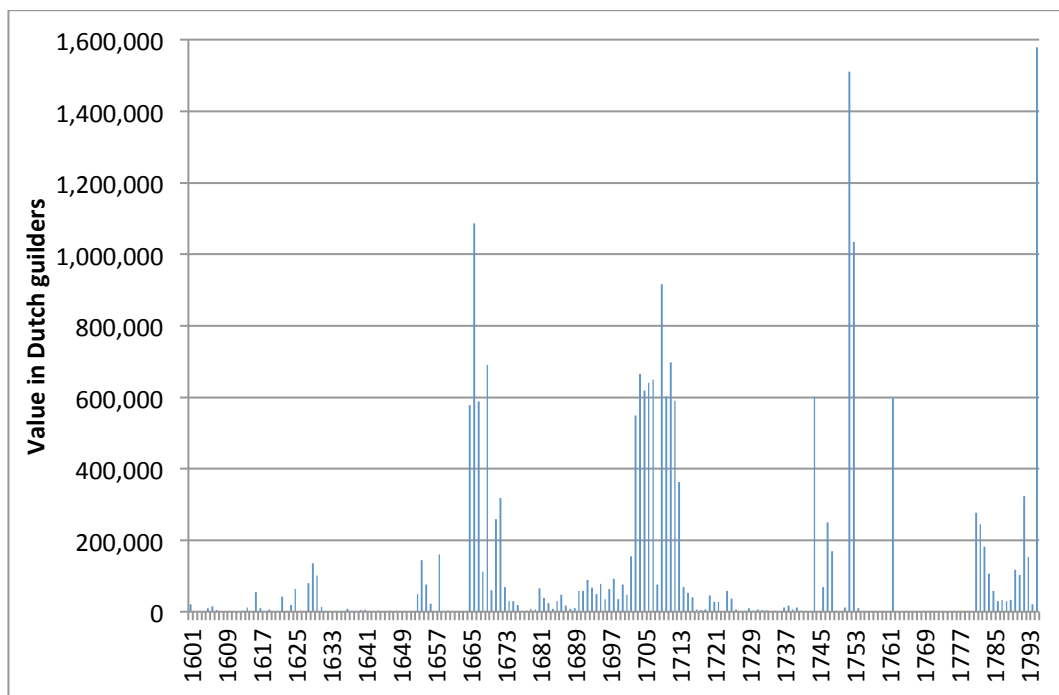


Figure 4: Groningen's loans in amounts in Dutch guilders per year 1594-1795 (source: L. Van der Ent and V. Enthoven, 2001, 110-119).

The financial hardship of the Münster invasion cannot better be illustrated than by the amount borrowed in these years. In 1665, Groningen's provincial government borrowed 578,050 guilders, the double amount the next year and an additional 558,774 guilders in 1667.⁵⁹ Whereas the total amount of loans obtained prior to 1665 was limited to one million guilders, two times this amount was borrowed in these three years alone.

The States of Groningen issued two types of annuities in the 1660s: redeemable annuities (Dutch: *losrenten*) and life annuities (Dutch: *lijfrenten*). The former paid a fixed annual amount until the issuer reimbursed the principal sum; the latter paid a fixed sum for the remainder of lifetime of the nominee while the principal sum was not to be returned. Life annuities did, thus, technically not result in an outstanding debt, but only a financial obligation to pay the annual sum. Because of this difference the coupons of the life annuities typically yielded 1.5 to 2 times higher interest rates than redeemable annuities.⁶⁰ When Groningen issued both types of annuities, redeemable annuities nominally yielded 4% to 5%, whereas life annuities had

⁵⁹ Ibid., 110-119.

⁶⁰ Dormans, *Het Tekort*, 58-61, 145.

a nominal interest rate of 8% to 10%.⁶¹ Life annuities were consequently considered expensive.⁶²

It is, however, important to notice that the nominal coupons at issuance for life annuities declined for Groningen in this 1660s and early 1670s, which suggests its reputation improved in the Holland capital market. Remarkably, when the States of Groningen offered 9% to investors in Holland in 1669, it simultaneously offered investors in Groningen 10%.⁶³ This could either indicate a lack of trust in Groningen *vis-à-vis* Holland or a lack of funds. Nevertheless, compared to the province of Overijssel, which also was attacked by Münster troops, Groningen's credit performed relatively better still.⁶⁴ Zeeland paid initially lower coupons on life annuities in 1666, but increased these rates to 9% in 1671.⁶⁵ Only the wealthy province of Holland issued life annuities persistently at lower rates in this period.⁶⁶

	Groningen	Overijssel	Holland	Zeeland
1666	10%	10%	8.3%	8.3%
1667	10%	10%	8.3%	
1668	10%		8.3%	
1669	9%		7.1%	
1671	8%	12%	7.1%	9%

Table 1: Nominal yields on life annuities issued in Groningen, Holland and Overijssel 1666-1671 (sources: Groningen: RHC-GA, SvG, inv.nrs. 1888-1894; Holland: GF DI 4 Holland, p. 382; GF DI 1 Overijssel: p. 216; Zeeland: Zeeuws Archief (hereafter: Z.A.), Staten Staten van Zeeland Rekenkamer C (hereafter: RkC), inv.nr. 4510, f.393- 414 and Z.A., 87 Verzameling Verheye v Citters, inv.nr. 125b).

Although the original resolution that approved the issue of the life annuities in Holland is lost, some original life annuities have been preserved.⁶⁷ On 30 March 1666 the States of Groningen decided to issue a life annuity in Amsterdam. It motivated its reliance on lending money by the immediate need for ready cash during this troublesome period (Dutch: *beswaerlijke*

⁶¹ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 285.

⁶² Velde and Weir, 'Financial Market and Government Debt Policy in France'.

⁶³ Regionaal Historisch Centrum Groninger Archieven (hereafter RHC-GA), Archief van de Staten van Stad en Lande, 1594-1798 (hereafter: SvSL), inv.nr. 96, f. 28v, 14 May 1669.

⁶⁴ Fritschy, *Gewestelijke Financiën: Vol. I. Overijssel*, 1:216; Israel, *The Dutch Republic*, 770.

⁶⁵ Zeeuws Archief (hereafter: Z.A.), Staten van Zeeland Rekenkamer C (hereafter: RkC), inv.nr. 4510, f.393- 414 and Z.A., 87 Verzameling Verheye v Citters, inv.nr. 125b.

⁶⁶ Liesker and Fritschy, *Gewestelijke Financiën: Vol. 4. Holland*, 382.

⁶⁷ The resolution books show a hiatus: inv.nr. 13 ends on March 3rd 1666, while inv.nr. 14 continues on February 15th 1667.

tijden).⁶⁸ Although such statements would not necessary have built trust, the regents in Groningen probably tried to signal that the lack of funds was a temporary problem. It simultaneously implied that the funds would be spent on the common cause of the Republic. Moreover, Groningen promised that semi-annual interest payments would be paid in Amsterdam. To this end it pledged all provincial revenue streams, present and future ones, together with all provincial possessions, either within Groningen or beyond its borders. All provincial legal institutions would support this pledge.⁶⁹ Yet this pledge posed a serious risk, since the States of Groningen committed the whole community to the debt, as was the custom under the Law of Reprisal.⁷⁰ Clearly, all provisions were intended to build trust and increase the convenience for the Holland creditors. This increased the chances of a successful issue.

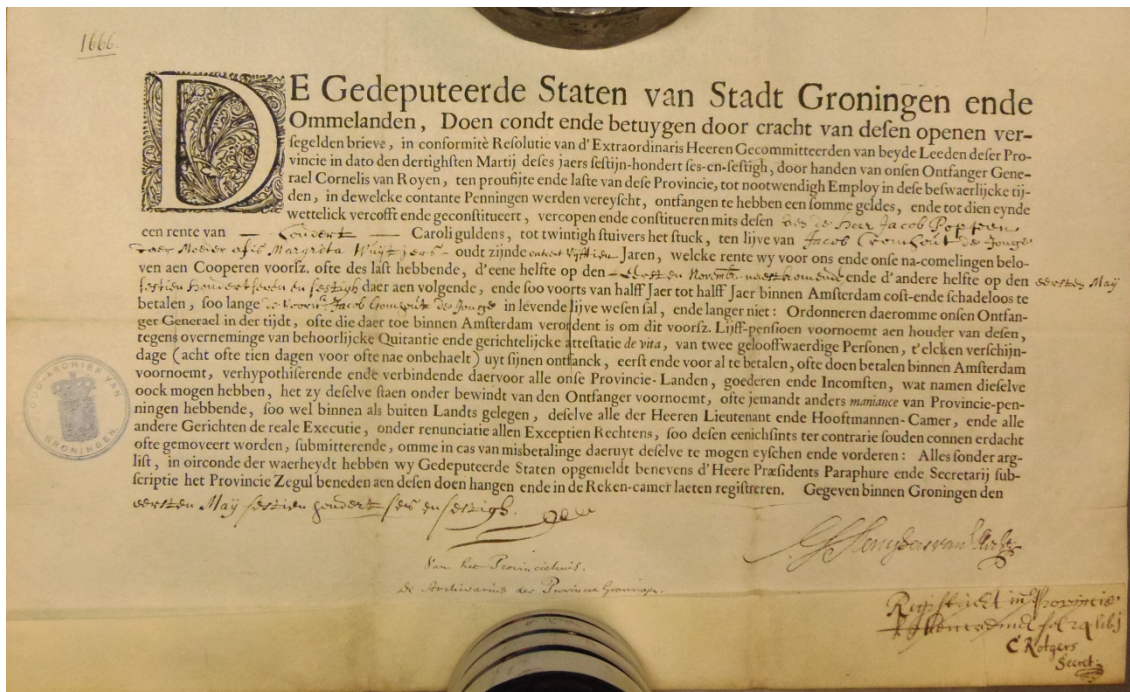


Figure 5: Original contract life annuity 1666 (source: RHC-GA, SvSL, inv.nr. 2698).

⁶⁸ Regionaal Historisch Centrum Groninger Archieven (RHC GrA), 0001 Archief van de Staten van Stad En Lande, 1594-1798, inv.nr. 2698. This refers to the Second Anglo-Dutch War and the first invasion by Von Galen's army.

⁶⁹ Regionaal Historisch Centrum Groninger Archieven (RHC GrA), 0001 Archief van de Staten van Stad En Lande, 1594-1798, inv.nr. 2698.

⁷⁰ Zijlenderdijn, *Medieval Capital Markets*, 83.

In spite of the deficits following the second Münster invasion, the States of Groningen borrowed less than during the first Münster war. The provincial deficit cannot explain the modest provincial borrowing. The province merely borrowed 465,000 guilders throughout the Franco-Dutch War, while the provincial deficit in 1675 alone was larger than that.⁷¹ Probably, there was a supply side problem. The conflict with Britain, France and the German prince-bishops created scarcity of cash in the Dutch Republic.⁷² Furthermore, the provincial credit began to falter, which might have made creditors reluctant in providing additional funds.⁷³

The province's urgent need for money comes forward from the extraordinary measures taken in 1672. Groningen resorted to a 5%-forced loan, levied over 1 per cent of the inhabitant's wealth. Furthermore, the coupon on newly issued life annuities increased from 9 to 10 per cent at the beginning of the year and more later.⁷⁴ The provincial executives (Dutch: *Gedeputeerde Staten*) also forbade the conversion of redeemable annuities into life annuities in 1675.⁷⁵ These measures indicate that the province had much trouble in finding sufficient cash until the war ended 1678.

Peace brought but little improvement for the provincial finance. Interest payments were still overdue in 1680.⁷⁶ After Groningen's arrears evolved into a default in the 1680s – as will be analysed in the next section – the Provincial States had only two options left for borrowing. Firstly, it could rely on the credit of the Generality. It exercised this option especially during the War of Spanish Succession. Secondly, the Provincial States could still borrow money within the borders of its own province, which it also did.⁷⁷ After the War of Spanish Succession the borrowed annual amounts only exceeded the 500,000 guilders of the 1660s in 1744, 1752, 1753 and 1795. Not until the Fourth Anglo-Dutch War (1780-1784) Groningen borrowed outside the

⁷¹ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 91–95, 110–119, 190, 287, 328, 329–362 This included the 1672-forced loan, levied over 1 per cent of the inhabitants wealth.

⁷² Gelderblom and Jonker, 'Public Finance', 18.

⁷³ Groningen merely paid 1.5 years of interest to Holland creditors between 1672 and 1680. RHC-GA, SvG, inv.nr. 1457, f. 605r-605v, 17/7 August 1680.

⁷⁴ RHC-GA, SvSL, inv.nr. 1896, f. 682r.

⁷⁵ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 284, 287.

⁷⁶ Groningen merely paid 1.5 years of interest to Holland creditors between 1672 and 1680. RHC-GA, SvG, inv.nr. 1457, f. 605r-605v, 17/7 August 1680.

⁷⁷ Van der Ent and Enthoven, *Gewestelijke Financiën: Vol. 3 Groningen*, 128.

provincial borders.⁷⁸ By that time, the conflict over the unpaid interest to the creditors in Holland was solved.⁷⁹ For most of the eighteenth century Groningen refrained itself from the capital market. Additional loans to service its debt were thus unnecessary. This indicates that Groningen's debt was sustainable in the long-run.

Quantitative analysis of Groningen's default

This section analyses how Groningen's arrears turned into a default, based on quantitative materials. It is based on archival research into the records of the final settlement of the dispute in 1760-1761. The next section complements this with an analysis of the negotiations with the creditors. The former section analyses what happened, the latter section examines how and why.

Default was a common phenomenon in early-modern Europe. Although the magnitude of these other cases differ, they offer valuable theoretical insights for this case. Early-modern sovereign defaults are often explained as excess of absolutist regimes. Unbound by representative assemblies monarchs overspent the budget and consequently defaulted.⁸⁰ Yet the Dutch Republic was no absolutist state and possessed representatives assemblies.

Recent research offers a more nuanced alternative interpretation for early-modern sovereign defaults. Velde and Weir argued for eighteenth century France that the defaults were part of a system to manage the debt. Persistent interest payments would ruin the state's public finance.⁸¹ More recently, Drelichman and Voth argued that Philip II of Spain 'priced-in' the defaulting risk, which was thus paid in advance to compensate creditors for a future default.⁸² Therefore, the sovereign defaults were neither total nor random: a specific asset was targeted.⁸³ The creditors knew beforehand to expect a default and anticipated to that by requesting a higher coupon for only a specific part of the debt. Consequently, assets with the highest yields,

⁷⁸ Ibid.

⁷⁹ Heeres, 'Holland Contra Groningen'; Loosjes and Wagenaar, *Vaderlandsche Historie*, 23:140–141; Kok, *Vaderlandsch Woordenboek*, XVIII:667.

⁸⁰ Acemoglu and Robinson, *Why Nations Fail*; Stasavage, *States of Credit*; North and Weingast, 'Constitutions'.

⁸¹ Velde and Weir, 'Financial Market and Government Debt Policy in France'.

⁸² Drelichman and Voth, 'Serial Defaults, Serial Profits'.

⁸³ Velde and Weir, 'Financial Market and Government Debt Policy in France', 5.

mostly higher coupons that had been paid for a longer period of time, formed the most likely target for a default. Thereafter, creditors and debtor entered into renegotiations to quickly reach an agreement to allow for future lending and borrowing. In their interpretation, sovereign default was used as an instrument to restructure public finance and was consequently part of a deliberate policy, or even a system in itself to manage public finance.⁸⁴ It was thus neither sheer inability to manage its public finance nor a deliberate violation of the creditors' property rights by absolutist kings.

Superficially, Groningen's default on creditors in Holland resembled those by early-modern Spain and France in several respects. The default was neither total nor random and a specific high coupon asset was targeted. A more thorough scrutiny shows that Groningen's case significantly differed. A clear strategy behind the default seems absent. The argument of excessive coupons as justification for the default was not invoked before the 1750s. On the contrary, the picture that emerges is that of a troubled government whose control over its finances crumbled under its hands. Arrears then gradually slid into a default. Attempts to restructure failed, when arrears increased, for the creditors were unprepared to accept significant haircuts.

The quantitative analysis shows three characteristics of Groningen's defaults. Firstly, the default was gradual and piecemeal, which suggests that arrears slowly evolved into a default. Secondly, until 1716 at least one life annuity was paid, implying that there was no total moratorium on these assets. Thirdly, the default was randomly distributed within the group of Holland life annuity holders. This seemingly unstructured default sequence indicates defaulting risk was not priced-in. Before turning to the analysis, a few remarks must be made about the nature and limitations of the source.

When the default was finally settled, a list was drawn up of the old life annuities. A first remark is that only those that possessed the asset for at least 15 years were eligible to the settlement.⁸⁵ Hence, not all life annuities that still circulated are taken into account. Nevertheless, the claims presented in the register are probably representative for the general development, since this is a random sample on which the States of Groningen could not exercise any influence. This 1761-list of claims lists a total of 338 annuities, which

⁸⁴ Velde and Weir, 'Financial Market and Government Debt Policy in France'; Drelichman and Voth, 'Serial Defaults, Serial Profits'.

⁸⁵ NA), Provinciale Resoluties, inv.nr. 715, pp.1279-1285, provincial resolution of the States of Holland and West-Friesland 1761.

equals approximately half of the sold annuities between 1666 and 1672.⁸⁶ The list contains the names of the buyers and nominees, the original date the life annuity was bought, the date each of the nominees had deceased and had received their last interest payment, the amounts of annual interest and the total sum of unpaid interest between the last instalment paid and nominees death.⁸⁷ Based on this information, the following analysis could be made on the development of the default in the 1680s.

Year of last paid instalment	Year of purchase						Grand Total
	1666	1667	1668	1669	1671	1672	
1681						5.00%	0.30%
1682			2.78%	0.61%			0.59%
1683		6.06%		3.07%			2.66%
1684	59.57%	51.52%	50.00%	47.85%	50.00%	35.00%	49.70%
1685	17.02%	21.21%	25.00%	32.52%	16.67%	25.00%	26.63%
1686	4.26%	10.61%	8.33%	4.91%		15.00%	6.80%
1687	2.13%	6.06%	2.78%	4.29%		5.00%	4.14%
1688	10.64%	3.03%	8.33%	3.07%	16.67%		4.73%
1689				1.23%			0.59%
1690						5.00%	0.30%
1692		1.52%		1.23%	16.67%	5.00%	1.48%
1693	4.26%						0.59%
1695				0.61%			0.30%
1696				0.61%			0.30%
1701			2.78%				0.30%
1704						5.00%	0.30%
1716	2.13%						0.30%
Grand Total	100%	100%	100%	100%	100%	100%	100%

Table 2: Defaults in proportion per year of purchase: (Source: RHC-GrA, SvSL, inv.nr. 2276.)

The earliest dates that creditors obtained the last regular instalment are those of 1681. This might have been caused by missed collection dates or other common irregularities in payments. There was a clear concentration of final payments in 1684 and 1685: almost 50% of the creditors received interest for the last time in 1684 and another 26% in 1685. Between 1683 and 1688,

⁸⁶ RHC-GA, SvSL, inv.nrs. 1890, 1891, 1892, 1894, 1896, 2276. Between 1666 and 1672, 749 life annuities were sold in Holland.

⁸⁷ The arrears or default, thus, began after half a year after the last paid instalment. It still provides a fair indication of the progress of the default.

95% of the creditors had received their last regular instalment. Yet some creditors received money for a longer period and one even as late as 1716. This pattern shows that the halt of interest payments was no universal default on all Holland's life annuities at once. Rather, the province withheld payments bit by bit, until gradually all arrears turned into a default. This interpretation is consistent with the picture emerging from the analysis of Groningen's public finances discussed in the previous section: a pitiable financial situation with insufficient money to temporarily pay all expenses.

The unequal distribution of the final payments also suggests that Groningen was able to play the creditors against each other. Or from the creditors' perspective, that it was unable to coordinate action against the province of Groningen. Moreover, Groningen, could always rely on the credit of the States-General to avoid punishment by the market. Furthermore, as the next section will demonstrate, Groningen negotiated a solution with the redeemable annuity holders in Holland, which also worsened the bargaining power of the life annuity holders.

The second characteristic of Groningen's default is the random distribution of defaults within the group of life annuity holders. Although Groningen eventually singled out the life annuity holders in Holland, a clear strategy of targeting specific creditors seems absent. This conclusion is based on the comparison between the purchasing date and the defaulting date. If Groningen followed the rationale of first repudiating its most expensive loans, we would expect the life annuities issued in 1666, 1667 and 1668 to be defaulted upon first. These annuities yielded 10% annually, whereas those issued in 1669 returned 9%, 8% for the ones from 1671 and those issued in 1672 between 9% and 10%. Hence, the 1666 annuities would have been the first logical target for a default, since these had had the highest yields: these were paid the longest and had the highest coupons. However, such a deliberate policy in the default was absent if we plot the default years against the purchasing years. The patterns of the separate purchasing years basically follow the general pattern of the default; very few final payments before 1684, the majority concentrated in 1684, followed by 1685. This indicates that clear policy in targeting specific life annuities among those issued in Holland was absent.

Finally, the apparently unstructured nature of the default implies that Groningen did not use the excuse that risk was priced-in to differentiate

among the creditors; those with higher coupons were not structurally earlier defaulted upon than others. This was also clear from the brief comparison with other provinces issuing life annuities in the Dutch Republic, in the previous section. Groningen's offered coupon of 8% to 10% appears not excessive. Indeed, the States of Groningen only began to invoke this argument when the creditors from Holland started to increase pressure in the 1750s. In 1759 the States of Groningen claimed that the creditors had received their interest for 20 years, which allegedly had yielded the creditors a profit on top of the recovery of the original investment.⁸⁸

Archival data from 1761 allow us to test this claim. Life annuities returned a nett loss in the first years after they were purchased, because the purchase amount was not be returned for life annuities. Hence, the nett cumulative return of a life annuity is equal to the number of years the instalment is paid times the annual coupon minus the original purchasing sum. For instance, to recoup the investment of a 10%-life annuity an investor had to receive 10 years of interest payments; the break-even point was 10 years.⁸⁹ Only a minority of the investors received the claimed 20 years of interest payments: only 16 out of 338 annuities equalled or exceeded 20 years. On average Groningen did not live up to the contractual obligations for more than 16 years and 10 months. The remaining 95% of the life annuities received payments for 11 to 20 years, which meant that these creditors recouped their investment, but earned considerable less than claimed.

⁸⁸ Heeres, 'Holland Contra Groningen', 189.

⁸⁹ 10 years * 10% = 100%

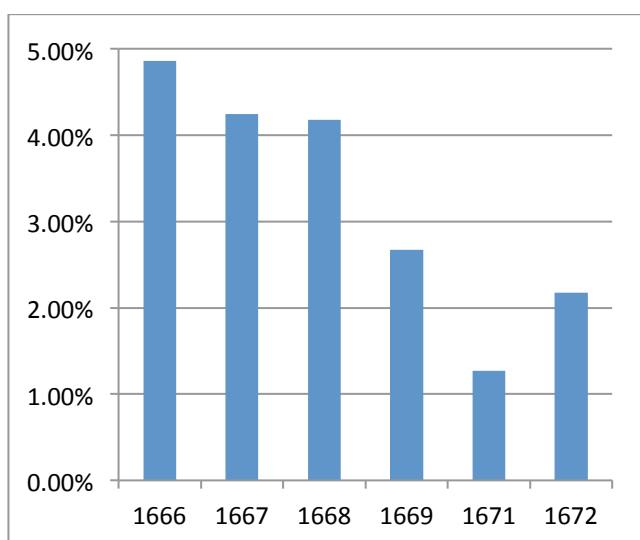


Figure 6: Annualized returns on investment in Groningen life annuities, per issuance year (Source: RHC-GA, SvSL, inv.rn. 2276).

Given these data on the actual duration of the contracts, it is unlikely that risk was indeed priced-in. If the risk was priced-in, the creditors would have been compensated sufficiently in advance by excessive interest rates. The returns, however, provide little support to this claim. Assessing the possible excessive compensation requires both the returns on these life annuities and alternative risk-free assets, as a measure of opportunity costs. To begin with the latter, a loan collateralized by a VOC-share might be considered one of the safest assets. This risk-free asset yielded 3.5 per cent in 1677 to 2.5 per cent in 1683.⁹⁰ To first provide an indication of the additional profitability in case of sovereign default, the short-term lending to Philip II of Spain is informative, as these assets were targeted in his defaults. After a default this asset yielded an additional revenue of 3.16 per cent on top the opportunity costs of a 7.14 per cent, making a total of 10.3 per cent profit.⁹¹ Similarly, alternative expensive debt instruments in eighteenth-century France yielded up to 3.5 percentage points more than life annuities that returned 5.24 to 10 per cent.⁹² For Groningen, the average annual return on investment was a mere 3.4%, after deducting the purchasing sum of the life annuities that was not to be returned. Within the group there are large differences per year of purchase. Annuities issued in the three years that offered an annual interest rate of 10% nominally, eventual yielded 4.9% to 4.2%. Yet those issued at 9% in 1669

⁹⁰ Gelderblom and Jonker, 'Public Finance', 20.

⁹¹ Drellichman and Voth, 'Serial Defaults, Serial Profits', 14.

⁹² Velde and Weir, 'Financial Market and Government Debt Policy in France', 33.

and 8% in 1671 returned 2.7% and 1.25% respectively. Buyers of annuities in 1672, who were offered 9% to 10% nominal interest rate, yielded 2.2% eventually. If Groningen had offered a reasonable compensation in advance, the effective yield had to have been at least 3 per cent more than the 2.5 per cent opportunity costs: a 5.5 per cent yield. If the buyers of life annuities also factored death risk, the coupon should have been even higher. Clearly, Groningen offered the investors too little to compensate a future default.

Groningen's default on the life annuity holders in Holland unmistakably differed from the Spanish and French defaults. The default risk in the Groningen case appears not to have been priced-in to the nominal coupon of the asset. More importantly, those defaults were the result of premeditated decisions, which seems not to have been the case for Groningen.⁹³ Whereas the other defaults, were the result of deliberate decisions and policy, Groningen appears to have fiddled its financial affairs.

Failed negotiations with life annuity holders

The impression of Groningen's gradual default, evolving from arrears that grew out of control, is corroborated by this section's analysis of the provincial correspondence and decisions in the 1670s to 1680s. The first signs of financial difficulties appeared already during the late 1660s and early 1670s. The Generality was the first victim of Groningen's liquidity problems; in September 1668 the States of Groningen decided to repudiate all payments on Generality debts incurred prior to 1665, the year that Groningen began to borrow on an unprecedented scale.⁹⁴ The Council of State reacted as before by sending an embassy over. Its reaction to a default could be easily coordinated, as the Generality was the sole creditor that fell victim.⁹⁵ Although this could be interpreted as fitting the pattern of a notoriously complicated relation with the States-General, creditors might have observed this with suspicion.

Meanwhile, Groningen's provincial government tried to maintain trust by stipulating the prompt and neat payment of redeemable and life annuities

⁹³ Drelichman and Voth, 'Serial Defaults, Serial Profits'; Velde and Weir, 'Financial Market and Government Debt Policy in France'.

⁹⁴ RHC-GA, SvSL, inv.nr. 96, f. 21r, 16 September 1668

⁹⁵ NA, Raad van State: Extra Aanwinsten 1904 XII, inv.nr. 23c,

in Amsterdam in 1671.⁹⁶ Neat payment seems already to have become problematic. Four months after this stipulation, the States of Groningen allowed the auditing committee to dispose of the unpaid interest in Holland, by the former provincial receiver.⁹⁷ Hence, when Groningen issued another loan in 1672, the creditors already witnessed inaccurate interest payments, which might have incited them to require a higher risk premium.

The difficulties with the sale of the life annuities in 1672 might indicate that the market must have begun to doubt Groningen's ability or willingness to pay debts to others as well. Whereas in the previous years the provincial administration managed to issue these securities against decreasing interest rates, the provincial government raised its offer to 9%-coupons, because the market did not buy 8%-coupon life annuities.⁹⁸ In January, the province decided to issue life annuities at 9 or 10 per cent at most, in Holland and in Groningen.⁹⁹ It was, however, stipulated that this offer was to be kept secret; probably because it would reveal the province's despair for funds. Such an instruction is consistent with the findings of Gelderblom and Jonker, who argued that the local tax receivers in Holland had considerable bargaining power *vis-à-vis* the investors and played one against the other by rationing information.¹⁰⁰ From February to April, the States of Groningen managed to issue 48,000 guilders worth of 10% life annuities in Holland.¹⁰¹ Soon, however, creditors would uncover Groningen's deteriorating financial health.

The actual semi-annual interest payments were conducted by a local agent, by the name of Christoffel Indisraven. This merchant not only ran Groningen's affairs with the Amsterdam capital market, but also performed other services, such as the purchase of fuses from a fuse maker in Utrecht.¹⁰² Afterwards he could reclaim expenses, suggesting that he advanced expenses on Groningen's behalf.¹⁰³ Presumably, he also could advance interest payments, although the total amounts would have exceeded his purse. In any case he did not advance the total arrears that began to arise from 1672. Between April 1672 and 1680 the creditors in Holland merely received one

⁹⁶ RHC-GA, SvSL, inv.nr. 96, f. 41v, 15 April 1671

⁹⁷ RHC-GA, SvSL, inv.nr. 96, f. 41v, 26 August 1671

⁹⁸ RHC-GA, SvSL, inv.nr. 96, f. 41v, 9/19 January 1672

⁹⁹ RHC-GA, SvSL, inv.nr. 96, f. 41v, 18 January 1672

¹⁰⁰ Gelderblom and Jonker, 'Public Finance', 9.

¹⁰¹ RHC-GA, SvSL, inv.nr. 1896, f. 672r-681r.

¹⁰² Het Utrechts Archief (hereafter: HUA), Notarissen in de stad Utrecht 1560-1905, inv.nr. U083b009, notarial deed nr. 10, 20 February 1684.

¹⁰³ RHC-GA, SvSL, inv.nr. 96, f. 121r, 2 June 1681.

and a half years' of interest.¹⁰⁴ This suggests that April 1672 formed the last regular instalment paid during that period.

The scanty interest payments were probably war related. The province suffered from the siege of July and August of 1672.¹⁰⁵ After Von Galen retreated, the States of Groningen turned once again to the Amsterdam capital market. In September the Groningers offered life annuities, differentiated by age of the nominees, ranging from 10% to 33.3% per year.¹⁰⁶ This overly generous offer did yield Groningen another 93,000 guilders.¹⁰⁷ The absurdly high coupons probably reflects the combination of increased demand for capital due to the war and the high defaulting risk for Groningen.

The scanty payments between 1672 and 1680 were probably also the result of the prioritised payments to the military. In 1673, the States of Groningen stipulated that interest payments came second after the troops were paid, favouring those that had matured the longest time ago.¹⁰⁸ The meagre payments suggest that there was but little left for the creditors.

In 1677, the States-General mediated in another conflict between the city and the *Ommelanden*. In exchange for more autonomy over legal, administrative and financial matters, the Generality demanded at least two months of payment to the soldiers. The States-General simultaneously urged the States of Groningen to pay at least one year of interest to the creditors in Holland.¹⁰⁹ This diplomatic pressure had effect. In March 1678, the States of Groningen assumed the writings of the States-General and agreed to the resumption of payments of the redeemable and life annuities in Holland.¹¹⁰ It

¹⁰⁴ RHC-GA, SvSL, inv.nr. 1457, f. 605r-605v, 17/7 August 1680.

¹⁰⁵ Schuitema Meijer, 'Stad Groningen'.

¹⁰⁶ RHC-GA, SvSL, inv.nr. 1896, f. 682r.

10.0%	1-20 years
10.5%	20-30 years
11.1%	30-40 years
11.8%	40-45 years
12.5%	45-50 years
13.3%	50-55 years
14.8%	55-60 years
16.7%	60-65 years
20.0%	65-70 years
25.0%	70-75 years
33.3%	75 years and older

¹⁰⁷ RHC-GA, SvSL, inv.nr. 1896, f. 682r-685r.

¹⁰⁸ RHC-GA, SvSL, inv.nr. 96, f. 55r, 7 March 1673

¹⁰⁹ NA, Raad van State: Extra Aanwinsten 1904 XII, 17-18, 1 June 1677.

¹¹⁰ RHC-GA, SvSL, inv.nr. 96, f. 75v, 2 March 1678.

still took over a month to sign the order to pay the troops and the Holland creditors.¹¹¹

In 1680, the States of Groningen took a more active attitude towards the Holland debt. It established a committee, in March, to explore the possibilities to convert arrears into new debt and to reduce the interest on redeemable annuities from 5% to 4%.¹¹² On the same day, it established another committee that had to take care for Holland debt that was purchased.¹¹³ On 25 June that same year, the States decided to pay one semi-annual instalment on the first of July and another three months later.¹¹⁴ On the 21st of August, it took a series of decisions concerning the life and redeemable annuities. First, it designated certain taxes to fund the debt to pay the interest payments on life and redeemable annuities. This was the result of negotiations between the States of Groningen and "*gentlemen from Holland*" (Dutch: *Hollandsche Heeren*).¹¹⁵ Second, to reassert its seriousness on this matter, the States ordered the tax receiver to use this money for these payments, under the penalty of losing his office, even if other provincial public bodies would urge him to spend the money differently.¹¹⁶ Third, copies of these decisions were to be sent to the provincial government of Holland, together with the instruction to Indisraven. This instruction was the, fourth decision; the States summoned Indisraven immediately to Groningen to obtain the amount for the first instalment.¹¹⁷

In an address of September 1680, Indisraven wrote to the States of Groningen that the majority and most important creditors were prepared to accept the restructuring proposal of 25 June. This proposal was to convert the arrears into new debt and reduce the interest on redeemable annuities from 5 per cent to 4 per cent. On the condition that a semi-annual instalment was paid immediately and all future instalments would be promptly paid.¹¹⁸ Indisraven argued that if the States would not pay the creditors, no one in Holland would lend a penny to Groningen anymore.¹¹⁹ This was the

¹¹¹ RHC-GA, SvSL, inv.nr. 96, f. 76r, 27 April 1678.

¹¹² RHC-GA, SvSL, inv.nr. 96, f. 110r, 20 March 1680.

¹¹³ RHC-GA, SvSL, inv.nr. 96, f. 110r, 20 March 1680.

¹¹⁴ RHC-GA, SvSL, inv.nr. 96, f. 112r, 25 June 1680.

¹¹⁵ RHC-GA, SvSL, inv.nr. 96, f. 114v, 21 August 1680.

¹¹⁶ RHC-GA, SvSL, inv.nr. 96, f. 114v, 21 Augustus 1680.

¹¹⁷ RHC-GA, SvSL, inv.nr. 96, f. 114v, 21 August 1680; f. 115r, 21 August 1680.

¹¹⁸ RHC-GA, SvSL, inv.nr. 1457, f. 605r-605v, 27 September 1680, f. 615v-616r.

¹¹⁹ RHC-GA, SvSL, inv.nr. 1457, f. 605r-605v, 27 September 1680, f. 618v-619r.

consequence of Groningen's scanty payments in the previous years: it had merely paid one and a half years' of interest to creditors in Holland since 1672.¹²⁰ The proposed conversion of arrears into new debt, seems to have applied to all annuities, redeemable and life annuities alike.

Next spring, the States stipulated that Indisraven should receive an additional sum to pay the creditors, that was not exceed 10,000 guilders.¹²¹ In June 1681, the States of Groningen offered a conversion of redeemable annuities that were in arrears into 8 per cent life annuities.¹²² Together with the aforementioned attempts to convert arrears into new debt, the provincial government seems to have tried to restructure the debt in various ways. This was probably ineffective as negotiations with Holland creditors continued while arrears accrued.

In early 1683, matters began to turn for the worse. From that moment the States received complaints, transmitted by Indisraven, that creditors in Holland received unequal payments.¹²³ A certain Gerhardt Block acted as representative of creditors in Holland and would report in writing to Indisraven.¹²⁴ In June, two delegates, Bothenius and Piccard, hastened to Amsterdam to pay another semi-annual instalment on life and redeemable annuities.¹²⁵ These defective payments and the *ad hoc* committee to Holland rather seem to have been temporary makeshifts that lacked a clear policy to tighten the screws on external creditors.

In the two following years, 1684 and 1685, most of the life annuity holders received their final instalments. These partial and irregular payments might be interpreted as part of these ongoing renegotiations with the Holland creditors. Following the advice of the Generality, a number of creditors agreed in February 1686 to a reduction of 25 per cent on its redeemable annuities.¹²⁶ The States also continued to try to buy up annuities, both redeemable and life annuities, in Holland.¹²⁷ These securities, probably, sold below par, due to Groningen's bad payment behaviour. Buying these annuities through the

¹²⁰ RHC-GA, SvSL, inv.nr. 1457, f. 605r-605v, 17/7 August 1680.

¹²¹ RHC-GA, SvSL, inv.nr. 96, f. 114v, 21 August 1680; RHC-GA, SvSL, f. 115r, 22 April 1681.

¹²² RHC-GA, SvSL, inv.nr. 96, f. 120r, 1 June 1681 / RHC-GA, SvSL, inv.nr. 96, f. 120v, 2 June 1681.

¹²³ RHC-GA, SvSL, inv.nr. 96, f. 156v, 6 January 1683; RHC-GA, SvSL, inv.nr. 96, f. 157v, 28 February 1683; RHC-GA, SvSL, inv.nr. 96, f. 158r, 1 March 1683; RHC-GA, SvSL, inv.nr. 96, f.159r, 3 March 1683.

¹²⁴ RHC-GA, SvSL, inv.nr. 96, f. 158r, 1 March 1683; f.159r, 3 March 1683.

¹²⁵ RHC-GA, SvSL, inv.nr. 96, f. 164v, 22 June 1683.

¹²⁶ RHC-GA, SvSL, inv.nr. 96, f. 196v, 25 February 1686; f. 199r, 26 February 1686.

¹²⁷ RHC-GA, SvSL, inv.nr. 96, f. 110r, 20 March 1680; f. 196v, 25 February 1686.

secondary market was consequently cheaper than reimbursing the creditors at face value. The dismissal of Indisraven as broker for Groningen, in the same month is presumably best explained from the perspective of these renegotiations. The States of Groningen dismissed him because of continued payments to creditors in Holland.¹²⁸ If the States of Groningen wanted to pressure the creditors, it would withhold interest payments. If Indisraven then still paid these creditors, that strategy would have had little effect. In spite of his dismissal, Indisraven, reappears twice to receive instalments, in 1688 and 1689, destined for interest payments on both life and redeemable annuities.¹²⁹ This reaffirms the impression of increasing arrears that gradually evolved into a default that was seemingly random within the group of life annuity holders, whereas the redeemable annuity holders stroke a bargain with Groningen's government.

Unable to reach a collective agreement, the States of Groningen continued to work around the life annuity holders, using the secondary market. Besides these direct purchases, mentioned in 1680 and 1686, it explicitly allowed – encouraged – inhabitants of Groningen to buy up Groningen public securities in Holland. The inhabitants could then reinvest this in return for 6 per cent life annuities, at a nominee that was inhabitant of Groningen.¹³⁰ The practice of re-trading public bonds to the domestic market has previously been described as an instrument for creditors to mitigate the effects of a default.¹³¹ This case demonstrates that the defaulter could use the secondary market as well to help solving its problems. It moreover shows that the secondary market for public debt within the Dutch Republic was already well-developed.

The States of Groningen's preparedness to renegotiate was still not limited to the redeemable annuity holders. In 1689, the province negotiated a contract with Christoff count of Rantzow concerning his four life annuities. A lump sum of 20,000 guilders was paid to compensate for the unpaid interest of 16,000 guilders that had accumulated between 1678 and 1689. The payments of this redemption money were to be made in three equal instalments: one immediately, the other two through the office of Hendrik Staats and sons in Amsterdam. If the remaining two payments were too late,

¹²⁸ RHC-GA, SvSL, inv.nr. 96, f. 196v, 25 February 1686; f. 200v, 27 February 1686.

¹²⁹ RHC-GA, SvSL, inv.nr. 96, f. 238v, 3 March 1688; f. 259r, 20 October 1689.

¹³⁰ RHC-GA, SvSL, inv.nr. 96, f.237r, 2 March 1688; f. 239r, 3 March 1688.

¹³¹ Broner, Martin, and Ventura, 'Sovereign Risk'.

the entire arrangement would be void. In that case the previous payment should be considered as partial redemption on the arrears, whereas the interest was to be paid according to the original conditions of the life annuities contract with priority in Amsterdam. The case is even more interesting because king-*stadtholder* William III of Orange, was one of the nominees of the life annuities.¹³² The question remains whether this count of Rantzow bought this asset as agent of William, or that it was allowed to nominate third parties as happened in late eighteenth-century France.¹³³ Nonetheless, individual renegotiating was possible, but did not lead to an agreement between Holland's life annuity holders and the States of Groningen.

Perhaps, the trouble was that the conditions and prospects within this group of creditors varied more than for the redeemable annuity holders. This larger variation was the result of the design of the asset, since the expected returns depended on the life expectancy of each individual nominee. Hence, it might have been the case that the nature of the life annuity caused too much heterogeneity to reach a solution that would satisfy all life annuity holders equally.

It was not preordained that the life annuity holders eventually fell victim to an outright repudiation of payments. For a while, both life annuity holders and possessors of redeemable annuities suffered from the postponed payments, that resulted from liquidity problems. Whereas the latter managed to bargain a deal, the former did not. Although the creditors in Holland as a group were targeted, the differentiation between redeemable annuity holders and life annuity holders was the outcome of a renegotiation process and not a premeditated plan. The redeemable annuity holders accepted an interest reduction in return for a resumption of payment, the large majority of the life annuity holders did not receive a penny for the next 75 years to come. Consequently, this case demonstrates why coordinating punishment proves so difficult for bondholders.¹³⁴ It, moreover, seems that the remarkable result of this partial default was a regression in the functioning of free financial markets for public debt; prior to the default capital freely flowed to Groningen, thereafter Groningen depended on the Generality's credit.

¹³² RHC-GA, SvSL, inv.nr. 2700.

¹³³ Velde and Weir, 'Financial Market and Government Debt Policy in France', 31.

¹³⁴ Tomz, *Reputation and International Cooperation*, 196–219.

Ending a remarkably persistent default

Finally, compared to other public defaults, Groningen's default persisted for remarkable long period. Since creditors barred defaulting states from new loans until the old debts were restructured, a state in default could not issue anew on the capital market. Consequently, credit rationing confined the duration of the default to the moment the defaulter needed to borrow money again, mostly within a few years.¹³⁵ So, why did it take so long before the creditors in Holland reached an understanding?

This section summarizes the process and attempts to solve the issue before 1761. Part of the persistence of the default can be attributed to the changing attitude of the Generality. Whereas the Generality stood for the rights of the unpaid creditors in Holland during the 1670s, it shielded Groningen from the unpaid life annuity holders in the eighteenth century. This question relates to the question of the presumed eighteenth-century Dutch institutional impotence.

The Generality's interest in the province lay in Groningen's importance for the Dutch common defence system. In November 1687, the States of Groningen replied to the Generality that the maintenance of its fortifications could only be paid for by the import of money from outside the provincial borders. It, meanwhile, withheld its payments to the Receiver-General of Union until the other provinces had paid their contributions, as a lever.¹³⁶ Seven months later, Groningen attached the condition to issue a loan for the maintenance of the fortress on the Republic's border, in exchange for Groningen's approval to the building of 36 new warships.¹³⁷ In turn, the Council of State sent over an embassy to discuss this matter.¹³⁸ Without Groningen, the Dutch defences in the north would have been severely weakened. Hence, there was a clear mutual interest between the Generality and the Groningen provincial administration to maintain the border fortress in good condition.

¹³⁵ Ibid., 53–54; Reinhart and Rogoff, *This Time Is Different*, 80–81; Drelichman and Voth, 'Serial Defaults, Serial Profits'.

¹³⁶ RHC-GA, SvSL, inv.nr. 96, f. 233v, 18 November 1687.

¹³⁷ RHC-GA, SvSL, inv.nr. 96, f. 242v, 26 June 1688.

¹³⁸ RHC-GA, SvSL, inv.nr. 96, f. 243v, 27 July 1688.

On the other hand, the States-General protected Groningen against harsh actions by the life annuity holders. However, whereas fully sovereign borrowers had to come to terms with the market in order to issue new debt, Groningen was offered an escape route by borrowing under guarantee of the States-General. This made credit rationing an ineffective means for contract enforcement, for Groningen did not need the free market to obtain the loan. This also made the States-General Groningen's main creditor, who assured that it received prioritized payments. This becomes clear from the report by the aforementioned generality-commission, in 1726. It declared that Groningen was already burdened enough by paying the Generality's debts and interest and could not pay others.¹³⁹ The States of Holland, nonetheless, repeatedly and fruitlessly admonished the States of Groningen to come to terms with the creditors, during the 1730s.¹⁴⁰ In 1739, it delivered an ultimatum to its Groningen counterparts that was due in May the next year.¹⁴¹ However, the outbreak of the War of Austrian Succession in 1740 halted Holland's pressure, since internal harmony was required during this international conflict.¹⁴² Negotiations and mediation by *stadtholder* William IV after the war also remained without effect.¹⁴³

The default was only ended when the creditors in Holland invoked the 'medieval' Law of Reprisal. In October of 1759, the States of Holland allowed the creditors to seize ships and goods of Groningen's inhabitants in Holland.¹⁴⁴ The creditors argued that if Groningen could pay other bills, it also could them. By adding that all Groningen's inhabitants were liable for their provincial debt, it clearly invoked the Law of Reprisal.¹⁴⁵ Remarkably, in the middle of the conflict the Generality granted a safeguard against the seizing by Holland's creditors for money designated for the payment of Generality's debts and interest.¹⁴⁶ Again, the protection of the Generality's interest always prevailed over those of the private creditors. Eventually, the States-General mediated an agreement that granted a compensation to the heirs of the

¹³⁹ Loosjes and Wagenaar, *Vaderlandsche Historie*, 23:139–140; Heeres, 'Holland Contra Groningen', 188.

¹⁴⁰ Loosjes and Wagenaar, *Vaderlandsche Historie*, 23:139–140; Heeres, 'Holland Contra Groningen', 175–176, 183, 192.

¹⁴¹ NA, Raad van State: Extra Aanwinsten 1904 XII, inv.nr. 23c.

¹⁴² Loosjes and Wagenaar, *Vaderlandsche Historie*, 23:140.

¹⁴³ Heeres, 'Holland Contra Groningen', 183, 192.

¹⁴⁴ *Ibid.*, 184–185.

¹⁴⁵ *Ibid.*, 182–183.

¹⁴⁶ Loosjes and Wagenaar, *Vaderlandsche Historie*, 23:142–143.

annuity holders of 10% cash, 50% in 2.5% bonds, in October 1760.¹⁴⁷ Hence, both the persistence and solution of the default depended on the Generality's mediating position between creditor's and defaulter.

Conclusion

The case of Groningen's default casts doubt on the widespread notion that credible commitment to debt was an essential part of the Dutch Republic's state finance. It demonstrates that credible commitment to debt would be pushed aside if one could come away relatively unharmed. The States of Groningen discovered, along the process of renegotiation its arrears, that the Generality offered an escape route. This escape was the trade-off of diminished fiscal autonomy in return for access to the capital market via the States-General. This allowed the Groningers to circumvent the capital markets punishment for a default, such as credit rationing or higher interest rates charged.

However, Groningen's default was no premeditated plan. It rather was the outcome of the interaction between the creditors, the States of Groningen and the Generality. This explains the evolution from arrears that turned into a gradual and piecemeal default and eventually an outright repudiation of the debt. When urged so by the States-General in the late 1670s, the States of Groningen attempted to pay the interest in arrears. The temporary make-shifts and *ad hoc* money transfers in the 1680s, indicate attempts to restructure the debt. In accordance with the Generality's advice, the States of Groningen reached an agreement with the redeemable annuity holders. This left the life annuity holders on their own. Consequently, they fell victim to increasing arrears that gradually evolved into a default. The outright repudiation of that share of the debt, only followed from the protection the Generality offered to the States of Groningen.

The States-General allowed Groningen's default to persist, for two reasons. First, it needed to securing its own income. To foot the bill, it depended heavily on the provincial contributions. A failure to pay the military was dangerous and its own revenue stream but small. Issuing debt on behalf of the provinces helped to smooth its liquidity shortages. It, therefore,

¹⁴⁷ Heeres, 'Holland Contra Groningen', 190–197.

granted Groningen the possibility to borrow under its guarantee. Moreover, it exercised large control over Groningen's public finance and prioritized its own income, over all other expenses. This was the result of the far-reaching powers assigned by the 1594 Treaty of Reduction. This solution was mutually beneficial for the province and the Generality, but detrimental to the creditors in Holland.

Second, Groningen formed an important link in the Republic's defences. Upkeep of the fortresses at the Republic's border was important, as became clear from the two invasions by the bishop of Münster in 1665 and 1672. Groningen's military victory in 1672 came at the price of an extraordinary financial burden, including a forced loan and arrears to its creditors. The States of Holland acknowledged Groningen's military importance and also subordinated the creditors' interests to the greater good of internal harmony in time of warfare. But when the Republic could keep aloof during the Seven Years' War (1756-1763), Groningen's military position proved a less important argument.

To force Groningen to pay its old debts, the Holland creditors resorted to the 'medieval' Law of Reprisal. This was the result of the absence of centralized juridical institutions. It shows that the Dutch Republic remained fragmented federal state that made internal contract enforcement problematic. Yet, for its survival as independent state, this was apparently not necessary. Private interests were subordinated to the Greater Good of common security, while sufficient money could be raised to finance this.

Data Appendix

	Primary Income	Primary Expenditure	Subtotal: Primary Govt. balance	Interest & Redemptions	Loans	Total Balance
1594-1600	306.750	-265.750	41.000	0	0	41.000
1601-1610	539.750	-535.000	4.750	0	13.000	17.750
1611-1620	508.000	-544.250	-36.250	-3.000	17.000	-22.250
1621-1630	996.500	-997.000	-500	-38.000	73.000	34.500
1631-1640	1.128.250	-1.145.500	-17.250	-28.000	7.000	-38.250
1641-1650	1.073.000	-1.057.750	15.250	-19.000	4.000	250
1651-1660	852.000	-926.250	-74.250	-26.000	76.000	-24.250
1661-1670	954.250	-993.500	-39.250	-175.000	514.000	299.750
1671-1680	1.167.500	-1.240.500	-73.000	-180.000	74.000	-179.000
1681-1690	1.030.250	-851.500	178.750	-207.000	31.000	2.750
1691-1700	1.276.750	-1.156.750	120.000	-221.000	64.000	-37.000
1701-1710	1.433.250	-1.734.000	-300.750	-220.000	486.000	-34.750
1711-1720	1.370.250	-1.263.500	106.750	-297.000	188.000	-2.250
1721-1730	1.496.000	-1.258.500	237.500	-260.000	18.000	-4.500
1731-1740	1.283.750	-1.067.500	216.250	-237.000	7.000	-13.750
1741-1750	1.297.750	-1.190.750	107.000	-200.000	156.000	63.000
1751-1760	1.479.000	-1.532.750	-53.750	-204.000	642.000	384.250
1761-1770	1.546.250	-1.341.000	205.250	-217.000	0	-11.750
1771-1780	1.591.250	-1.446.250	145.000	-132.000	0	13.000
1781-1790	1.475.500	-1.493.500	-18.000	-125.000	111.000	-32.000
1791-1795	1.665.750	-1.675.000	-9.250	-167.000	435.000	258.750

Table 3: Groningen's Income and expenditures per decade (source: L. Van der Ent and V. Enthoven, 2001, p. 91–95, 128, 110–119, 189–193, 294–298, 328, 359–362).

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