The Liverpool cotton market emerged in the early decades of the nineteenth century to become the largest market supplying the British spinning industry with its raw material. Liverpool had become the largest cotton importing port at the end of the eighteenth century, being supplied by dozens of merchanting firms and with an increasing reliance upon United States cotton (over three quarters of the cotton used by the British industry in the nineteenth century came from the southern United States). The Liverpool market centred around a system of brokers: specialist cotton brokers would sell the merchants' cotton to other brokers who acted for spinners; by the early 1840s there were over one hundred cotton broking firms trading in the Liverpool market, working out of offices in the streets surrounding the Town Hall and Exchange Flags.\(^1\) Because of the centrality of the brokers to the Liverpool marketing system, their organization, the Liverpool Cotton Brokers' Association (which evolved from meetings of brokers which commenced in the first decade of the nineteenth century), came to regulate and govern the market.\(^2\)

The Liverpool cotton market is remarkable in being the first commodity market in Europe to develop futures trading, considerably

\(^1\) Gore's Liverpool directory (1841) states there were 111 cotton-broking firms in 1841.

ahead of the London markets which still trade futures today. By the late nineteenth century, all branches of the British cotton trade—importers, brokers, spinners, and weavers—were widely using the Liverpool futures market. For instance, in January 1912 the Facit Mill Company of Rochdale declared that its policy was to use futures contracts to cover all its supplies, and in the 1890s the Sun Mill Company of Oldham covered half its supplies with futures, while other spinning companies, such as John Hawkins & Sons Ltd, varied the extent to which they covered supplies with Liverpool futures. In 1904 the journal *Cotton* commented that the practice of merchants importing cotton without using Liverpool futures was ‘defunct’. The size of the Liverpool futures market became such that some Liverpool cotton broking firms actually made more money from brokerage on cotton futures than on actual spot cotton itself.

II

Futures are, in a sense, a form of ‘paper currency’ for a commodity. Futures contracts promise delivery of a set quantity of a commodity at some stage in the future. They have various uses. For speculators they are an ideal instrument because one is dealing in ‘promises to supply’ rather than having to handle the bulky physical commodity. For other, more ‘legitimate’ traders, their value is that they can be used to guard against price changes; this is known as ‘hedging’. For instance, when an importer contracts to buy a commodity overseas he can guard himself against the value of this commodity falling while in his possession, by immediately selling futures contracts. When he comes actually to sell the physical commodity, he buys back his futures contracts (at the then current market price). By so

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4 Sun Mill Co. Ltd, minutes, 8 June 1891: J.R.U.L.M., SM/1/3.
7 For instance, the balance sheet of the large Liverpool broking firm of Reynolds & Gibson indicates that in 1913 this firm earned £22,510 from brokerage on futures and only £12,345 from selling actual cotton for importers and £7,748 from buying it for spinners: Reynolds & Gibson, ledger 3B, profit and loss account, 1913: Liv. R.O., Acc. 1216.
doing, he is guarded against price changes. Cotton merchants, brokers, and spinners all came to use this process of hedging to safeguard themselves against a fall in the price of their stock; while holding cotton at sea, in warehouses, or at their mills, they sold futures contracts against them, with the intention of buying these contracts back when they came to sell or spin their actual stock. Many who bought the futures contracts were speculators and hence were not interested in actually having cotton delivered under the futures contracts and were (except in exceptional circumstance) happy to let the seller buy them back. The speculator would, of course, hope that the price of cotton would have risen, so leading to the seller (merchant, spinner, or broker) having to pay more to buy the futures contracts back than they had been worth when they sold them.

A variety of factors can lead to the development of a futures market. The key circumstances are variability to the point of instability in the price of a commodity, uncertainty and lack of information concerning the scale of supply, the ability to specify a standard grade, and the existence of a body able to regulate effectively such a market. With few exceptions, futures markets develop out of existing ‘forward’ markets. To clarify the distinction, a forward market is one in which it is a common practice for specific lots of a commodity to be contracted for before they are available for delivery, as opposed to a futures market, in which contracts are highly standardized and do not refer to a particular cargo.

The Liverpool cotton market satisfied all these major preconditions. The Liverpool Cotton Brokers’ Association existed as a potential regulatory body. The uncertainty relating to the supply and price of cotton could place those handling this commodity at risk of financial loss, so that they had a desire to find some mechanism which could guard them against price fluctuations. There is ample documentary evidence of cotton importers in the first half of the nineteenth century incurring losses due to a fall in the price of cotton while in transit or when holding stocks in

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Liverpool. For instance, in 1841 a sharp fall in the price of cotton caused many importers to incur losses, bringing some to the brink of bankruptcy. Early in February 1842 the Liverpool cotton broker and importer George Holt wrote to his cotton shipping agent in New Orleans: ‘Everybody is losing money & have lost it & with it have lost heart, all traders & importers are poorer.’ It is interesting to note that in this crisis the credit normally supplied by banks and brokers to assist in the holding of stocks dried up, no doubt due to their nervousness concerning the serious commercial situation.

A forward market in cotton had developed at Liverpool out of which a futures market could develop. Evidence suggests that forward selling of specific cargoes certainly took place at various points from the early to mid-nineteenth century in Liverpool. For instance, in the period of high prices and speculation during the War of 1812 between Britain and the United States, George Holt’s cotton sales book indicates that he traded various lots of cotton before they were landed in the port. At around the same time the brokers M. & J. Pool were also making forward sales, many months before cotton might be delivered. The firm noted on 15 January 1815 that it had sold fifty bales of American cotton ‘deliverable any time before 1 Aug next, to be equal to sample in Campbell’s hands [another broker] & to be paid for in 10 d[ay]s after our notice [with] . . . good bills on London @ 3 m[onth]s.’ In less hectic times, in the years following the war, this form of trade appears to have been far less common.

Improved knowledge of cotton shipments which developed in the second quarter of the nineteenth century aided the development of forward selling, particularly through the faster mail ships, especially those of the Cunard line. W. F. Machin (who wrote a short history of the Liverpool cotton market) states that these ships in particular

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11 George Holt to John Arrowsmith, 3 Feb. 1842: copy of letter in author’s possession.
15 No forward sales can be found in Holt’s later surviving sales book for 1822–4: Liv. R.O., MD 230/10.
spurred forward selling, but it is difficult to find documentary
evidence either to support or to refute this. The letters of James
Brown, a captain of a Liverpool merchant’s ship, indicate that in the
1840s he was able to provide his employer with plentiful informa-
tion regarding his cotton shipments from New Orleans a consider-
able time before they were landed in Liverpool, so enabling the
merchant to sell in advance if he so wished. For instance, on one
voyage, Croft’s ship arrived in New Orleans in early October 1844
and sailed for Liverpool around 30 November. While in port in
America, Brown wrote five times to Croft in Liverpool advising him
of prices in New Orleans and the amount of cotton he had freighted
the ship with. It is interesting to note in a letter of Brown’s dated 8
October 1843 that he states he is writing it in a hurry so that the
letter can catch the Great Western before it departed for England.
In 1857 a conjunction of high cotton prices, speculation, and the
partial completion of the telegraph to India (permitting knowledge
of shipments of Indian cotton) produced a mini-boom in forward
trading in Liverpool, dampened later in the year by a sharp fall in
prices.

Forward trading of cotton was therefore taking place in the years
before the outbreak of the American Civil War, but seems to have
been most common in times of high prices and speculation. The
logical conclusion that much forward cotton was bought by
speculators is significant, as it is a necessary prerequisite for a
futures market that some market operators are willing to adopt a
‘long’ position, in order to buy the futures contracts put out as
hedges by those holding stocks of actual, spot cotton.

raw cotton annual (1957), 257–69; George Chandler, Liverpool shipping: a short
David Courtney, From forum to futures (London, 1991), 118.
MD 48.
18 Stanley Dumbell, ‘The origin of cotton futures’, in Economic Journal, supple-
ment, historical series (May 1927), 260; Liverpool cotton market reports: Liv. R.O.,
19 For instance, the weeks which are remarked upon as witnessing extensive
forward trading in 1857 are also remarked upon as ones witnessing extensive
The period of extremely high cotton prices and speculation associated with the ‘Cotton Famine’ of the American Civil War, followed by generally falling prices over a period of years, provided the conditions which ingrained forward trading and began the process whereby some forward trading mutated into what we would today recognize as futures trading. The major distinguishing feature between forward contracts and futures contracts is standardization of terms. That is to say, in a futures contract there is a fixed quantity and quality set for the commodity which permits contracts to be bought and sold rapidly between traders who know exactly what it is they are buying and selling (hence, crucially, the market is highly ‘liquid’); only one part of the contract is negotiable—the price.\(^\text{20}\) The other key point is that under futures contracts, the commodity is rarely (if ever) delivered—the contract is bought back at maturity by the seller.\(^\text{21}\)

Some forward selling began almost as soon as the American Civil War broke out,\(^\text{22}\) but it commenced in earnest in 1863, particularly in the autumn, with the price of spot cotton between three and four times the pre-war level. Speculation was spurred by recovering demand for cotton goods from the key Indian market, which had been somewhat glutted with goods around the start of the war. It should be noted that at this stage the forward selling was generally in Indian cotton due to the shortage of the American article, aided by the telegraph communication with the subcontinent. Forward prices for cotton began to be quoted regularly in the Liverpool trade press in late 1863.\(^\text{23}\) The forward market in Liverpool moved a step closer to a futures market as individuals began to make contracts when


\(^{21}\) Futures markets, ed. Goss, 28.

\(^{22}\) Gore's General Advertiser, 26 Sept. 1861.

they were not in possession of actual cotton, in other words not referring to specific shipments and acting as what we would call 'bears'. The commencement of this was also noted as taking place in 1863, by the broking firm of Smith, Edwards & Co. The forward market became what might be termed 'institutionalized' in the same year through the Liverpool Cotton Brokers' Association producing a standard form of contract for traders to use for forward sales, though exactly when or under quite what circumstances is unclear because the minute books of the Association have not survived for this period. There was a reduction in forward trading caused by sharp falls in the price of cotton in the late summer of 1864 (sparked by the raising of the discount rate and rumours of peace in America), but forward trading had become firmly established as a permanent feature in the Liverpool market and continued after the close of the conflict.

The reason for the continued extensive use of forward selling in the years following the American Civil War was the difficult market conditions which Liverpool cotton merchants faced. From the end of the American Civil War and into the 1870s, the international price of cotton steadily fell. This was because of the recovery of the United States after the disruption of the war to its previous level of cotton production. Gradually, year on year, the United States recovered a little more, supplies of cotton increased, and prices fell. Merchants importing cotton were therefore at serious and prolonged risk of the value of their cotton stock falling between the date they purchased it in the United States and when they came to sell it in the Liverpool market. The Liverpool merchant Thomas Bower Forwood warned his son, William Bower Forwood, in August 1866: 'the most dangerous trade you can go into is cotton, and it will be so for years to come'. Hence there existed good reason for importers to try to guard themselves against price falls by making forward sales as soon as they had made their purchases in America. Speculators and others purchased the forward-sold cotton either to safeguard their future supply or in the hope of profiting if the price of cotton did rise while in transit.

25 The contract was reproduced and discussed in The Times, 12 Nov. 1863, p. 6.
One of the major agents leading to an expansion of forward trading and the further advance towards a futures market was the development of telegraph links with the United States, with the cable between Britain and the United States coming into operation in 1866. The cable was very quickly put to use for transferring information relating to cotton across the Atlantic. Information regarding shipments from the United States to Liverpool could be relayed in a fraction of the time taken by ship, and a similar speed was possible in orders of cotton from Liverpool to the United States.

The notion of specifying a standard quality in contracts appears to have emerged around 1866, and this innovation is usually attributed to the cotton broker John Rew. One of the key problems with forward selling of cotton was uncertainty regarding the exact quality of the cotton. Rew therefore made his contracts on the basis of ‘middling’ quality; the value of any actual cotton delivered would be established in relation to the price of this quality, providing the cotton was delivered, rather than the contract being bought back. Forward prices began to be regularly quoted in the Liverpool trade press, using the ‘basis middling’ clause, towards the close of 1866.

It would probably be correct to describe the years between 1865 and 1873 as ones of flux in the Liverpool forward market, with contracts apparently being put to different uses. In this state of flux, a gradual separation took place between on the one hand those transactions involving the sale of specific lots of cotton from a variety of sources, which would normally be delivered, and on the other special contracts for American cotton which did not refer to specific shipments, were made on the basis of a standard quality, and, generally, would be bought back at maturity by the seller. The first surviving rules for forward contracts in the records of the Liverpool Cotton Brokers’ Association are from 1867. Rule 2 states that ‘In all cases when the terms are by ship or ships, or for shipment before a specified date, the name of the ship or ships . . . must be given to the buying Broker’. This would seem to imply that the

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28 See, for instance, the ‘telegraphic cotton report’ in Gore’s General Advertiser, 27 Sept. 1866.
29 Todd, Marketing of cotton, 67–8; Machin ‘Cotton market’, 302–4; Auguste Bruckert, Cotton pamphlet (Liverpool, 1911), 9–10.
30 See, for instance, Gore’s General Advertiser, 20 Dec. 1866.
contract could be used for a sale on the lines of, say, 250 bales on a particular ship leaving New Orleans in a named month. On the other hand, the sale might not involve the naming of ships, and simply state a date of future delivery; in other words, it might not refer to actual cotton, and hence it approximated to a futures contract. Indeed, the minutes of the Brokers' Association seem to suggest strongly that although there was only one standard printed Association contract, sales could be of two distinct types. For instance, the broker Edgar Musgrove in August 1867 referred to 'purchases for arrival or future delivery' [emphasis added], and yet there was only one form of standard contract in use. Rules from January 1871 make a similar distinction. In March 1871 the President of the Association referred to 'delivery contracts' which specified 'middling American from any ports'. It would therefore seem likely that contracts could be made for future delivery in the late 1860s, or not long after, which did not refer to specific shipments but simply promised to supply a specific quantity by a set date on the basis of one quality; in other words, approximating closely to a fully developed futures contract. The coming of age of the Liverpool cotton futures market arrived with the adoption of a separate contract for 'future delivery' in 1873. Indeed, a guide to the Liverpool market published forty years later goes as far as to state that “Trading in “Cotton Futures” was commenced in 1873.” This contract specified the delivery of one hundred bales of American cotton in a fixed month on the basis of middling quality; although, of course, the contract would usually be bought back by the seller rather than the cotton actually being delivered.

It will be noted that futures contracts only developed (at this stage at least) for United States cotton. For success a futures market requires ‘liquidity’, in other words a market large enough to allow contracts to be bought and sold quickly and easily. Although various types of cotton were sold at Liverpool besides American, it will be remembered that this type dominated the market. Hence, the market for American cotton was far broader and more liquid, and it should therefore not come as a surprise that it was in this type of cotton that standardized futures contracts developed first.

32 Ibid. 16 Aug. 1867.
33 Rules relating to cotton sold to arrive (Jan. 1871), rule 2: printed insert in Liv. R.O., 380 COT 1/5.
34 Bruckert, Cotton pamphlet, 9.
The mature Liverpool futures contracts could be employed by members of the cotton trade in differing ways. An importer with stocks of cotton in transit to Liverpool, or stored prior to being sold, would use futures to guard against price falls. If the price of cotton fell, an importer might find that the cotton he owned could only be sold for less than he had paid for it. To counter this, the importer would sell futures contracts. In other words, he would sell promises to deliver cotton at some date in the future. If the price of cotton fell, he would be selling his actual stock of cotton at a loss, but could buy back his futures contracts for less than he had sold them for, hence mitigating the loss on the actual spot cotton by a profit on the futures contract.

This process of hedging with futures required skill and judgement. If a holder of cotton stocks sold too many futures contracts against his stock, he could wipe out all his profit or even make a loss. Hence, importers might decide to hedge only a portion of their holdings with sales of futures. Alternatively, they might sell futures contracts promising delivery at a distant date. These distant date contracts could then be employed to cover several cargoes, being bought back only if the price of cotton did fall.35

It was not only importers who traded futures. Spinners made considerable use of the market. If a cotton spinner held a large stock of cotton, he, like an importer, was exposed to the risk of its value falling if the price of cotton declined. Spinners would therefore cover their stocks by selling futures at Liverpool. The price of spun cotton yarn was closely linked to the price of the raw material. Hence, if a spinner held stocks of unsold yarn, he could also cover a proportion of this by selling futures.36

If a spinner made a contract to spin yarn he might not be able to find the exact type of raw cotton necessary immediately. By the time it was available, the price of cotton might have risen, so upsetting the calculation he had made when quoting the price of finished yarn to the buyer. To avoid this, the spinner could buy futures at Liverpool the moment he struck a yarn contract, knowing that if the price of cotton did subsequently rise, so pushing up the price of the raw cotton he needed, this would be offset by a rise in the value of the futures contracts he held.37

36 Todd, Marketing of cotton, 76, 109, 111.
37 Ibid.
A central feature of all modern futures markets is a clearing house. The clearing house exists to deal with the closing out of contracts, assessing who owes what to whom when contracts are bought back, and overseeing the physical delivery of a commodity in the unusual event that it is actually produced under a futures contract. Of vital importance in a futures market is a system of 'margins'. Under a futures contract, because a commodity is not set to be delivered until some date in the future, it does not have to be paid for by the buyer, or bought back by the seller, until the contract reaches maturity. Anyone, therefore, could enter the market, buying or selling huge numbers of contracts without having to provide any money, and potentially trading far beyond his means. Such a situation is a charter for rampant speculation and instability due to the likelihood of rash traders falling bankrupt when contracts matured. Under a margins system, payments are exchanged regularly between buyers and sellers of contracts between the date when the contract is entered into and the supposed date of delivery, depending upon whether the value of the commodity in the contract has moved in favour or against the buyer and seller; this ensures that those without adequate means will fail early should the market move against them, before building up a large interest in the market, or be deterred from entering the market in the first place. Margin systems are administered by clearing houses. 38

The Liverpool cotton market is remarkable for, on the one hand, developing a clearing house at a very early stage and, on the other, not introducing a margins system until comparatively late—and after considerable destabilizing speculation. The reason for this apparent contradiction lies largely with the broking membership of the Liverpool Cotton Brokers' Association—the body which regulated the market—which was keen to protect its own financial interests.

The establishment of a clearing house at Liverpool came quickly upon the adoption of a separate contract for futures trading. Confusion appears to have attended the closing of futures at the end of the months specified in the contracts. This was because contracts had been sold and resold from trader to trader, often

38 Futures markets, ed. Goss, 34; Williams, Function of futures markets, 14.
many times, and delays ensued as declarations of cotton were handed on, invoices made, etc. Those who had lost by a transaction appear to have deliberately delayed making payment or handing the contract on.\textsuperscript{39} The cotton broker Joseph Morgan therefore suggested to the Liverpool Cotton Brokers' Association in the spring of 1873 that it should create a special clearing house to oversee the swift closing out of contracts. Despite some opposition from brokers who feared such an institution would facilitate information about their own firms' business becoming known, the clearing house was established for a trial period. Essentially, it simply required all futures contracts falling due in a particular month to be presented in one place on one day, overseen by a special committee of the Brokers' Association. This worked well, and the experiment was repeated; by June 1873 a permanent home for the clearing house was being sought.\textsuperscript{40} The first clearing house for commodities, not only in Britain but anywhere in the world, had been created. Within a couple of years, the Clearing House had its own printed rules, premises, and an elected committee, subject to the Brokers' Association, which oversaw the clearing and settled disputes. All futures contracts had to pass through it, and any broking firm could be fined if it did not send a representative to a clearing involving contracts to which it was party.\textsuperscript{41}

Despite the pioneering development of the Clearing House, the development of a system of margins at Liverpool took a surprisingly long time, even though there was considerable and early disquiet on this subject. The first evidence of concern in Liverpool regarding the extent and standing of forward trading can be found as early as 1863. The broking firm of Smith, Edwards & Co. commented at the end of the year: 'The system of business in use gives boundless facilities to the operations of speculators without capital, and it cannot be doubted that if a great breakdown in the market occurred immense confusion would follow.'\textsuperscript{42} The brokers Ellison & Heywood argued at the same time that using forward sales 'men of

\textsuperscript{41} Liverpool Cotton Brokers' Association, \textit{Constitution, rules, and regulations of the clearing house for arrival and delivery contracts} (Liverpool, 1876): copy in Bodleian Library, Oxford, 1784 e. 18 (1).
limited capital and others of no means whatever' were able to operate in the market, and that should prices fall, they would never be able to fulfil their engagements; something needed to be done to put the market upon a sounder footing.\(^{43}\) Other brokers and merchants echoed these sentiments.\(^{44}\)

A system whereby buyers of contracts paid a deposit into a separate bank account was put forward by some merchants and cotton broking firms, including Ellison & Heywood, and Smith, Edwards & Co.\(^{45}\) However, the objections raised were several. It was suggested that a deposits system was impractical, given the need for new bank accounts to be opened and closed, perhaps quickly if contracts were resold. Speculators (who bought the forward contracts) argued that the selling merchants should also be required to make deposits, for it was contended that sellers embarked upon bear selling and hence ‘gambled’ as much as the so-called speculators. In addition, it was stated that a deposit system would lock up too much capital. A meeting of Liverpool cotton brokers discussed the idea; a merchant commented that while the brokers did not challenge the justice of the proposed reform, ‘refuge was taken in the alleged impracticability of the measure proposed’, though the merchant suspected that the loss of the ‘gambling clientele’ (and their brokerage payments) in fact gave rise to the brokers’ reluctance. The merchant went on to warn that if nothing was done a commercial crisis greater than 1847 or 1857 was in prospect.\(^{46}\)

In fact, the following year, 1864, witnessed something of a crisis in this emerging market. A sharp downturn in the price of cotton in the early autumn brought panic and numerous bankruptcies; market commentators noted that the rampant and insecure forward trading of those with limited means had greatly exacerbated the crisis in the market.\(^{47}\) Despite this salutary lesson, no action was taken. The lack of action on the part of the Liverpool Cotton

\(^{43}\) Circular of Ellison & Heywood, reprinted in *Economist*, 20 Feb. 1864, supplement, p. 27.

\(^{44}\) Anonymous letter in *The Times*, 12 Nov. 1863, p. 6; 11 Dec. 1863, p. 4.


Brokers’ Association on the question of margins indicates one of the weaknesses this early body had in acting as the regulatory body for the developing futures market. It was not a body encompassing all concerned with the market, but only the brokers. Specifically, the merchants and spinners were not members. Hence while merchants, and later spinners, desired at different times to see the creation of a margins payments system, the interests of the brokers could and did prevent this: the more forward and futures trading there was, the more brokerage they would earn on these transactions. If a broker traded a contract for an individual who went bankrupt, the most he could lose was a brokerage payment, so long as he had not extended any credit to the person concerned.

Over the next two decades, proposals for deposit and margins systems were put forward but not adopted, for instance in 1870 and 1877, and a system of optional deposits was endorsed in 1870 but appears not to have been used. Comments at brokers’ meetings highlighted a number of objections, similar to those voiced in 1863, with one important concern being a desire on the part of a group of the brokers not to limit the extent of the market. Interestingly, some of the more conservative brokers opposed schemes because they believed they would in some way aid speculation; quite how, is not clear. Other cotton brokers (particularly those with slender resources) who imported cotton and hedged it using futures did not wish to see their capital tied up; this latter issue affected some merchants who, hence, also opposed a margins system.48

Pressure for change built up outside the market. Observers were shocked by the possibilities which the lack of a deposit system permitted. The Porcupine, a satirical Liverpool publication, declared as early as 1870: ‘An American, fresh over from the other side, with scarce enough credit at home to buy “a suit of clothes,” can promenade our [Exchange] Flags within four-and-twenty hours after his arrival the owner of some thousand bales of cotton.’ The author recommended a deposit system on the model of that already used in the New York cotton market, but suspected that brokers wished to maintain their incomes at the level of the price-inflated

48 Liv. R.O., 380 COT 1/5 (30 Sept., 7, 14, 28 Oct. 1870); 380 COT 1/10 (13 Apr. 1877); letter of Thomas Holder, 1 Oct. 1870 inserted in ibid. 380 COT 1/5; American Chamber of Commerce in Liverpool, minutes, 12, 31 Oct. 1870: Liv. R.O., 380 AME 3; Ellison, Cotton trade, 292–3; Porcupine, 28 May 1870, p. 88.
Civil War and were hence keen not to reduce speculation. Other commentators argued in a similar vein.

The facility which futures gave to speculators led spinners to propose, in 1881 at a joint meeting with the Brokers’ Association, the adoption of a monthly settlement of ‘differences’ or margins between buyers and sellers of futures. The brokers stated that they were, in fact, willing to adopt the payment of differences and were keenly looking into it, though how representative of the majority in the Association the deputation’s views were is open to question, given the earlier opposition from brokers to such a move. They also stated that in the past, spinners who were already making use of futures had objected to this. (Evidence for this is hard to find, although it is possible that some spinners using futures might have objected because it would tie up capital.) The brokers also stated that there were problems in designing a system which did not place ‘very serious difficulties in the way of legitimate business’ (no doubt the importing activities of brokers and brokerage income). The spinners left the meeting feeling dissatisfied.

The deadlock was broken by the activity of an American speculator, Morris Ranger. Through buying up futures contracts he managed to corner the Liverpool market in 1879, attempted it in 1880, managed to do so again in 1881, and fell spectacularly bankrupt in 1883 with estimated debts in Liverpool of £400,000. In the process, his speculations had forced up the price of the industry’s raw material, to the considerable discomfort and anger of the spinners. The remarkable point was that Ranger had been to all intents and purposes bankrupt long before he finally declared the fact publicly in October 1883; the lack of a system of margins in Liverpool had permitted him to continue trading as he tried to extricate himself from his losses, while in fact storing up mounting losses for the date when he could continue to trade no longer.

In Liverpool the extremity of the situation was clearly identified

49 Porcupine, 28 May 1870, p. 88.
as the result of a lack of a margins system and it was reported that, in consequence, support in the market for adopting a margins system similar to that used in New York was gaining ground.\textsuperscript{53} Despite this, opposition still existed among the brokers. Many did not wish to see a possible contraction of the futures market (it should perhaps be noted that one source states that Ranger paid no less than the enormous sum of £330,000 to brokers in Liverpool from September 1878 to his collapse in 1883).\textsuperscript{54}

A group of about sixty Liverpool brokers keen to avoid the dangers of the existing situation began a Settlement Association for paying margins on a voluntary basis in December 1882, independent of the Liverpool Cotton Association (which had now succeeded the old Brokers' Association). Every two weeks a special committee established the ruling price of futures, with cash being transferred between members of the Settlement Association depending upon whether prices for futures had moved in their favour or against them. The Settlement Association ran independently for two years, during which time the practicality of the system was demonstrated. According to one source, members of the Settlement Association attracted more futures business because settlements gave greater security. At the end of this two-year period, the new Liverpool Cotton Association (a body which admitted merchants to full membership and spinners to associate membership) adopted the scheme officially, but even at this stage the proviso that it was only voluntary remained, although the vast majority used it—no doubt bearing in mind the Ranger episode and the success of the Settlement Association.\textsuperscript{55}

It should be noted that while the margins system may have limited the ability of some to speculate and the extent to which some others could trade in futures, it did not eradicate the prospect of either major speculations or damaging bankruptcies caused by the collapse of leading speculators in futures. For instance there were large speculations in Liverpool centred around one William Steenstrand in the period 1888–90. By the time he became bankrupt in the autumn of 1890, his losses amounted to some £200,000. One

\textsuperscript{53} The Times, 1 Oct. 1881, p. 9; 6 Oct. 1881, p. 4; 31 Oct. 1883, pp. 5, 9; 1 Nov. 1883, p. 10; 2 Nov. 1883, p. 10; 3 Nov. 1883, p. 7; 23 Nov. 1883, p. 7; Liverpool Echo, 28 Oct. 1929.

\textsuperscript{54} The Times, 23 Nov. 1883, p. 7.

\textsuperscript{55} Ibid.; Ellison, Cotton trade, 294–6; Muir, Cotton futures, 22–3.
suspects that Steenstrand’s financial backers helped pay his margins until his losses became unsustainable. While a margins system might remove the prospect of a speculator without capital dislocating the market, a speculator or group of speculators with their own resources or ample credit could still disrupt it.

V

An important feature of a futures market is the existence of a centralized trading location (conventionally a ‘pit’) where buyers and sellers can find each other quickly and trade rapidly and competitively. A central point at which the futures market could operate in Liverpool emerged spontaneously, but it took over thirty years for a purpose-built exchange to be erected. The place in Liverpool which was the first home of the developing futures market was Exchange Flags; this was an open area behind Liverpool Town Hall surrounded by buildings built to a plan similar to the original Royal Exchange in London. It had been common for merchants and brokers to congregate in this area near the Town Hall since the eighteenth century. Most cotton brokers had their offices in the Exchange Buildings themselves or in the surrounding streets. Because this open area was public, it was possible for bystanders to watch the ‘top-hatted cotton men striking deals’. Poor weather naturally hindered the market, and snowball fights between traders were not unknown. The problem with inclement weather led to various proposals for indoor accommodation for the market and several nearby locations were suggested in the 1870s and 1880s, but for reasons ranging from expense to unsuitability no solution was reached. It was the spread of the telephone towards

57 Machin, ‘Cotton market’, 186–8; Liverpool Echo, 28 Oct. 1929; John Mortimer, Cotton: from field to factory (Manchester, 1894), 57–8.
58 Machin, ‘Cotton market’, 189; Sir William B. Forwood, Recollections of a busy life (Liverpool, 1910), 44.
the end of the century which finally forced the Cotton Association to provide an indoor cotton exchange, because brokers wanted to use this new device to keep in touch with their clients.\textsuperscript{60}

Initially, a nearby building, Brown’s Buildings, was rented, with a large central room for futures trading, space for the offices of the Liverpool Cotton Association and the Clearing House, and telephone provision; the futures market opened here in 1896.\textsuperscript{61} This move proved to be something of a mistake—Brown’s Buildings was too small and telephone provision did not prove adequate.\textsuperscript{62} As early as 1901 investigations began into providing a new exchange. Various proposals were discussed, but it was finally decided to erect a purpose-built cotton exchange—no doubt bearing in mind the problems that had resulted from trying to convert an existing building. The site chosen was to the north of Exchange Flags, on Old Hall Street, despite objections that it was too far from Exchange Flags, where many traders had their offices.\textsuperscript{63}

The new cotton exchange was planned on a grand scale, with an imposing classical façade. Inside there was a large central trading floor for the futures market, ample office provision for the Liverpool Cotton Association and the Clearing House, cable company offices, many telephones, and offices which could be rented by cotton trading firms.\textsuperscript{64} The Cotton Exchange cost a massive £367,000 to erect, almost three times the projected cost; it was financed by loans from the Bank of England and the issuing of debenture stock by the Cotton Association. Trading in futures finally commenced in this location at the start of 1907, some forty years after the market had begun to emerge.\textsuperscript{65}

\textsuperscript{60} \textit{Liverpool Echo}, 28 Oct. 1929.

\textsuperscript{61} Liv. R.O., 380 COT 5/3 (29 Nov. 1895; 2 Nov. 1896; 8 Nov. 1897; 6 Sept. 1899); 380 COT 5/5 (18 July 1906).

\textsuperscript{62} Ibid. 380 COT 5/3 (2 Nov. 1896; 14 May 1900; 3 July 1901).


\textsuperscript{64} For descriptions of the Cotton Exchange: Anon., \textit{World cotton conference} (Liverpool, 1921), 10, 12, 14, 16, 18–21 (copy in Liv. R.O., H942.7212 COT); \textit{The Builder}, 9 July 1904, pp. 42–3; \textit{Times textile numbers}, p. 249; Weld & Co., \textit{Bolsa de algodon de Liverpool} (Liverpool, 1910), p. 5.

\textsuperscript{65} Liv. R.O., 380 COT 6/5 (1 Apr. 1903); 380 COT 6/6 (16 Nov. 1906); \textit{World cotton conference}, 9.
In conclusion, Liverpool developed Europe’s first futures market, and the foundations of this were laid in the early decades of the nineteenth century. Fluctuations in the price of cotton gave those holding stocks a strong motive to find some mechanism whereby they could safeguard themselves against a fall in their value. In addition, the practice of selling specific lots of cotton in advance of delivery had been experimented with during the same period. The emergence of the Liverpool Cotton Brokers’ Association as a body governing the Liverpool market provided an institution which had the potential to regulate a futures market and to devise contracts. The period of the American Civil War and its aftermath produced high prices and rampant speculation, followed by a period of declining prices which led to the mutation of forward sales into highly standardized futures contracts. The Liverpool Cotton Brokers’ Association played an important role in advancing the market by producing standard contracts, evolving trading rules, and establishing a clearing house. However, due to its desire to protect the interests of its members, it was slow to develop a much needed system of margins, the lack of which permitted rash speculation in cotton. Only after the foundation of the more inclusive Liverpool Cotton Association in 1882 was a margins system adopted. It also took time for a modern location to be established for the market, with Liverpool’s futures traders still forming their market in the open air until as late as the 1890s.